

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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 23, 2012

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 0-21154

CREE, INC.

(Exact name of registrant as specified in its charter)

North Carolina

(State or other jurisdiction of incorporation or
organization)

56-1572719

(I.R.S. Employer Identification No.)

**4600 Silicon Drive
Durham, North Carolina**

(Address of principal executive offices)

27703

(Zip Code)

(919) 407-5300

(Registrant's telephone number, including area code)

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares outstanding of the registrant's common stock, par value \$0.00125 per share, as of October 10, 2012, was 116,283,450.

CREE, INC.
FORM 10-Q

For the Quarterly Period Ended September 23, 2012

INDEX

Description	Page No.
<u>PART I - FINANCIAL INFORMATION</u>	
Item 1. Financial Statements	3
Consolidated Balance Sheets as of September 23, 2012 (unaudited) and June 24, 2012	3
Consolidated Statements of Income for the three months ended September 23, 2012 (unaudited) and September 25, 2011 (unaudited)	3
Consolidated Statements of Comprehensive Income for the three months ended September 23, 2012 (unaudited) and September 25, 2011 (unaudited)	4
Consolidated Statements of Cash Flow for the three months ended September 23, 2012 (unaudited) and September 25, 2011 (unaudited)	4
Notes to Consolidated Financial Statements (unaudited)	5
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	6
Item 3. Quantitative and Qualitative Disclosures About Market Risk	15
Item 4. Controls and Procedures	15
<u>PART II – OTHER INFORMATION</u>	
Item 1. Legal Proceedings	16
Item 1A. Risk Factors	16
Item 2. Unregistered Sale of Equity Securities and Use of Proceeds	16
Item 3. Defaults Upon Senior Securities	16
Item 4. Mine Safety Disclosures	17
Item 5. Other Information	17
Item 6. Exhibits	17
<u>SIGNATURE</u>	18

PART I - FINANCIAL INFORMATION**Item 1. Financial Statements****CREE, INC.
CONSOLIDATED BALANCE SHEETS**

	September 23, 2012 (unaudited)	June 24, 2012
(Thousands, except par value)		
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 163,852	\$ 178,885
Short-term investments	652,432	565,628
Total cash, cash equivalents, and short-term investments	816,284	744,513
Accounts receivable, net	162,287	152,258
Inventories	179,678	188,849
Deferred income taxes	21,773	21,744
Prepaid expenses and other current assets	60,223	56,917
Total current assets	1,240,245	1,164,281
Property and equipment, net	566,138	582,461
Intangible assets, net	371,994	376,075
Goodwill	616,345	616,345
Other assets	7,920	8,336
Total assets	\$ 2,802,642	\$ 2,747,498
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable, trade	\$ 87,520	\$ 78,873
Accrued salaries and wages	37,361	29,837
Income taxes payable	9,647	3,834
Other current liabilities	40,425	36,633
Total current liabilities	174,953	149,177
Long-term liabilities:		
Deferred income taxes	15,719	15,609
Other long-term liabilities	19,995	22,695
Total long-term liabilities	35,714	38,304
Commitments and contingencies (Note 11)		
Shareholders' equity:		
Preferred stock, par value \$0.01; 3000 shares authorized at September 23, 2012 and June 24, 2012; none issued and outstanding	—	—
Common stock, par value \$0.00125; 200,000 shares authorized at September 23, 2012 and June 24, 2012; 116,280 and 115,906 shares issued and outstanding at September 23, 2012 and June 24, 2012, respectively	144	144
Additional paid-in-capital	1,876,622	1,861,502
Accumulated other comprehensive income, net of taxes	11,848	11,133
Retained earnings	703,361	687,238
Total shareholders' equity	2,591,975	2,560,017
Total liabilities and shareholders' equity	\$ 2,802,642	\$ 2,747,498

The accompanying notes are an integral part of the consolidated financial statements.

**CREE, INC.
(UNAUDITED)
CONSOLIDATED STATEMENTS OF INCOME**

	Three Months Ended	
	September 23, 2012	September 25, 2011
(Thousands, except per share amounts)		
Revenue, net	\$ 315,753	\$ 268,980
Cost of revenue, net	199,704	170,952
Gross profit	116,049	98,028
Operating expenses:		

Research and development	37,547	34,402
Sales, general and administrative	52,645	45,539
Amortization of acquisition-related intangibles	7,670	3,925
Loss on disposal or impairment of long-lived assets	898	775
Total operating expenses	98,760	84,641
Operating income	17,289	13,387
Non-operating income:		
Other non-operating income, net	1,593	974
Interest income, net	1,792	1,969
Income from operations before income taxes	20,674	16,330
Income tax expense	4,551	3,511
Net income	\$ 16,123	\$ 12,819
Earnings per share:		
Basic net income per share	\$ 0.14	\$ 0.11
Diluted net income per share	\$ 0.14	\$ 0.11
Shares used in per share calculation:		
Basic	115,539	111,866
Diluted	115,960	112,543

The accompanying notes are an integral part of the consolidated financial statements.

CREE, INC.
(UNAUDITED)
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended	
	September 23, 2012	September 25, 2011
	(In thousands)	
Net income	\$ 16,123	\$ 12,819
Other comprehensive income:		
Currency translation gain, net of tax expense of \$110 and \$197, respectively	182	323
Net unrealized gain (loss) on available-for-sale securities, net of tax (expense) benefit of (\$323) and \$661, respectively	533	(1,092)
Other comprehensive income	715	(769)
Comprehensive income	<u>\$ 16,838</u>	<u>\$ 12,050</u>

The accompanying notes are an integral part of the consolidated financial statements.

CREE, INC.
(UNAUDITED)
CONSOLIDATED STATEMENTS OF CASH FLOW

	Three Months Ended	
	September 23, 2012	September 25, 2011
	(In thousands)	
Cash flows from operating activities:		
Net income	\$ 16,123	\$ 12,819
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	36,474	32,128
Stock-based compensation	12,485	11,440
Excess tax benefit from share-based payment arrangements	(42)	(261)
Loss on disposal or impairment of long-lived assets	898	775
Amortization of premium/discount on investments	2,264	1,922
Changes in operating assets and liabilities:		
Accounts receivable	(10,054)	(21,725)
Inventories	9,002	12,431
Prepaid expenses and other assets	(3,030)	1,811
Accounts payable, trade	9,680	(13,708)
Accrued salaries and wages and other liabilities	11,886	4,013
Net cash provided by operating activities	<u>85,686</u>	<u>41,645</u>
Cash flows from investing activities:		
Purchases of property and equipment	(12,597)	(33,962)
Purchases of investments	(179,601)	(80,874)
Proceeds from maturities of investments	78,504	42,590
Proceeds from sale of property and equipment	47	2
Proceeds from sale of available-for-sale investments	12,886	236,518
Purchase of Ruud Lighting, net of cash acquired	—	(456,008)
Purchases of patent and licensing rights	(5,548)	(4,159)
Net cash used in investing activities	<u>(106,309)</u>	<u>(295,893)</u>
Cash flows from financing activities:		
Net proceeds from issuance of common stock	5,286	2,094
Excess tax benefit from share-based payment arrangements	42	261
Net cash provided by financing activities	<u>5,328</u>	<u>2,355</u>
Effects of foreign exchange changes on cash and cash equivalents	262	468
Net decrease in cash and cash equivalents	<u>(15,033)</u>	<u>(251,425)</u>
Cash and cash equivalents:		
Beginning of period	178,885	390,598
End of period	<u>\$ 163,852</u>	<u>\$ 139,173</u>

The accompanying notes are an integral part of the consolidated financial statements.

CREE, INC.
(UNAUDITED)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Basis of Presentation and Changes in Significant Accounting Policies

Overview

Cree, Inc. (the "Company") is a leading innovator of lighting-class light emitting diode (LED) products, lighting products and semiconductor products for power and radio-frequency (RF) applications. The Company's products are targeted for applications such as indoor and outdoor lighting, video displays, transportation, electronic signs and signals, power supplies, solar inverters and wireless systems.

The Company develops and manufactures semiconductor materials and devices primarily based on silicon carbide (SiC), gallium nitride (GaN) and related compounds. The physical and electronic properties of SiC and GaN offer technical advantages over traditional silicon, gallium arsenide (GaAs) and other materials used for electronic and opto-electronic applications.

The Company's LED products consist of LED components, LED chips, and SiC wafers. As LED technology improves, the Company believes the potential market for LED lighting will continue to expand. The Company's success in selling LED products depends upon the ability to offer innovative products and its ability to enable its customers to develop and market LED based products that successfully compete and drive LED adoption against traditional lighting products.

The Company's lighting products consist of both LED and traditional lighting systems. The Company designs, manufactures and sells lighting systems for indoor and outdoor applications, with a primary focus on LED lighting systems for the commercial and industrial markets. The Company also uses its LED systems expertise to accelerate LED lighting adoption and expand the market for its LED components.

In addition, the Company develops, manufactures and sells power and RF devices. The Company's power products are made from SiC and provide faster switching speeds than comparable silicon-based power devices for a given power level. The Company's RF devices are made from GaN and produce higher power densities as compared to silicon or gallium arsenide.

The majority of the Company's products are manufactured at its production facilities located in North Carolina, Wisconsin, and China. The Company also uses contract manufacturers for certain aspects of product fabrication, assembly and packaging. The Company operates research and development facilities in North Carolina, California, Wisconsin, and China.

The Company currently operates its business as three reportable segments:

- LED Products
- Lighting Products
- Power and RF Products

Basis of Presentation

The consolidated balance sheet at September 23, 2012, the consolidated statements of income for the three months ended September 23, 2012 and September 25, 2011, the consolidated statements of comprehensive income for the three months ended September 23, 2012 and September 25, 2011, and the consolidated statements of cash flows for the three months ended September 23, 2012 and September 25, 2011 (collectively, the "consolidated financial statements") have been prepared by the Company and have not been audited. In the opinion of management, all normal and recurring adjustments necessary to present fairly the consolidated financial position, results of operations and cash flows at September 23, 2012, and for all periods presented, have been made. The consolidated balance sheet at June 24, 2012 has been derived from the audited financial statements as of that date.

Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") have been condensed or omitted. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended June 24, 2012 ("fiscal 2012"). The results of operations for the three months ended September 23, 2012 are not necessarily indicative of the operating results that may be attained for the entire fiscal year ending June 30, 2013 ("fiscal 2013").

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual amounts could differ materially from those estimates.

Certain fiscal 2012 amounts in the accompanying consolidated financial statements have been reclassified to conform to the fiscal 2013 presentation. These reclassifications had no effect on previously reported consolidated net income or shareholders' equity.

Recently Adopted Accounting Pronouncements

Presentation of Comprehensive Income

In June 2011, the Financial Accounting Standards Board ("FASB") issued new guidance concerning the presentation of total comprehensive income and its components. Under this guidance, an entity has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. This guidance also requires an entity to present on the face of the financial statements reclassification adjustments from other comprehensive income to net income. In December 2011, the FASB issued an accounting standards update that deferred the presentation requirement for other comprehensive income reclassifications on the face of the financial statements. This guidance, as amended, became effective for the Company beginning in the first quarter of fiscal 2013. The Company's adoption of the new accounting guidance did not have a significant impact on its consolidated financial statements.

Note 2. Acquisitions

On August 17, 2011, the Company entered into a Stock Purchase Agreement with all of the shareholders of Ruud Lighting, Inc. ("Ruud Lighting"). Pursuant to the terms of the Stock Purchase Agreement and concurrently with the execution of the Stock Purchase Agreement, the Company acquired all of the outstanding share capital of Ruud Lighting in exchange for consideration consisting of 6.1 million shares of the Company's common stock valued at approximately \$211.0 million and \$372.2 million cash, subject to certain post-closing adjustments. The acquisition allows the Company to expand its product portfolio into outdoor LED lighting.

Prior to the Company completing its acquisition of Ruud Lighting, Ruud Lighting completed the re-acquisition of its e-conolight business by purchasing all of the membership interests of E-conolight LLC ("E-conolight"). Ruud Lighting previously sold its e-conolight business in March 2010 and had been providing operational services to E-conolight since that date. In connection with the stock purchase transaction with Ruud Lighting, the Company funded Ruud Lighting's re-acquisition of E-conolight and repaid Ruud Lighting's outstanding debt in the aggregate amount of approximately \$85.0 million.

Following the acquisition, the Company recorded certain post-closing purchase price adjustments resulting in a \$2.3 million reduction to the purchase price and a total purchase price of approximately \$666.0 million.

The Company incurred total transaction costs related to the acquisition of approximately \$3.6 million, of which, \$3.1 million were expensed in the first quarter of fiscal 2012 in accordance with U.S. GAAP. Ruud Lighting is included in the Lighting Products segment.

The amounts of revenue and net income of Ruud Lighting in the Company's Consolidated Statements of Income from and including August 17, 2011 to September 25, 2011 are as follows (in thousands, except per share data):

	Amounts	
Revenue	\$	22,343
Loss from operations		(522)
Net loss		(664)
Basic net loss per share	\$	(0.01)
Diluted net loss per share	\$	(0.01)

The following unaudited pro forma information presents a summary of the Company's consolidated results of operations as if the Ruud Lighting transaction occurred at the beginning of the fiscal year for the period presented (in thousands, except per share data):

	Three Months Ended	
	September 25, 2011	
Revenue	\$	299,312
Income from operations		8,788
Net income		8,853
Earnings per share, basic	\$	0.08
Earnings per share, diluted	\$	0.08

The total revenue for Ruud Lighting included in the pro forma table above was \$53.8 million for the three months ended September 25, 2011.

Note 3. Financial Statement Details

Accounts Receivable, net

The following table presents a summary of the components of accounts receivable, net (in thousands):

	September 23, 2012	June 24, 2012
Billed trade receivables	\$ 184,504	\$ 173,145
Unbilled contract receivables	1,561	1,576
	186,065	174,721
Allowance for sales returns, discounts, and other incentives	(21,921)	(20,681)
Allowance for bad debts	(1,857)	(1,782)
Total accounts receivable, net	\$ 162,287	\$ 152,258

Inventories

The following table presents a summary of the components of inventories (in thousands):

	September 23, 2012	June 24, 2012
Raw material	\$ 55,826	\$ 57,618
Work-in-progress	68,126	74,241
Finished goods	55,726	56,990
Total inventories	\$ 179,678	\$ 188,849

Note 4. Investments

Short-term investments consist of high grade municipal and corporate bonds and other debt securities. The Company classifies its marketable securities as available-for-sale based upon management's determination that the underlying cash invested in these securities is available for operations as necessary.

The following tables provide a summary of marketable investments by type (in thousands):

	September 23, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Municipal bonds	\$ 237,007	\$ 1,936	\$ (24)	\$ 238,919
Corporate bonds	142,437	2,573	(7)	145,003
Certificates of deposit	185,000	—	—	185,000
U.S. agency securities	72,759	515	(2)	73,272
Non-U.S. government securities	10,214	25	(1)	10,238
Total	\$ 647,417	\$ 5,049	\$ (34)	\$ 652,432

	June 24, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Municipal bonds	\$ 209,626	\$ 2,036	\$ (58)	\$ 211,604
Corporate bonds	144,942	1,848	(123)	146,667
Certificates of deposit	130,000	—	—	130,000
U.S. agency securities	68,156	450	(7)	68,599

Non-U.S. government securities	8,746	15	(3)	8,758
Total	\$ 561,470	\$ 4,349	\$ (191)	\$ 565,628

The following tables present the gross unrealized losses and estimated fair value of the Company's investment securities, aggregated by investment type and length of time that individual investments securities have been in a continuous unrealized loss position (in thousands):

	September 23, 2012					
	Less than 12 Months		Greater than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Municipal bonds	\$ 33,121	\$ (24)	\$ —	\$ —	\$ 33,121	\$ (24)
Corporate bonds	15,850	(7)	—	—	15,850	(7)
U.S. agency securities	3,013	(2)	—	—	3,013	(2)
Non-U.S. government securities	3,037	(1)	—	—	3,037	(1)
Total	\$ 55,021	\$ (34)	\$ —	\$ —	\$ 55,021	\$ (34)
Number of securities with an unrealized loss		22		—		22

	June 24, 2012					
	Less than 12 Months		Greater than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Municipal bonds	\$ 30,102	\$ (58)	\$ —	\$ —	\$ 30,102	\$ (58)
Corporate bonds	30,550	(123)	—	—	30,550	(123)
U.S. agency securities	3,014	(7)	—	—	3,014	(7)
Non-U.S. government securities	1,543	(3)	—	—	1,543	(3)
Total	\$ 65,209	\$ (191)	\$ —	\$ —	\$ 65,209	\$ (191)
Number of securities with an unrealized loss		33		—		33

The contractual maturities of marketable investments at September 23, 2012 were as follows (in thousands):

	September 23, 2012				
	Within One Year	After One, Within Five Years	After Five, Within Ten Years	After Ten Years	Total
Municipal bonds	\$ 109,450	\$ 129,469	\$ —	\$ —	\$ 238,919
Corporate bonds	40,096	104,907	—	—	145,003
Certificates of deposit	185,000	—	—	—	185,000
U.S. agency securities	29,334	43,938	—	—	73,272
Non-U.S. government securities	4,541	5,697	—	—	10,238
Total	\$ 368,421	\$ 284,011	\$ —	\$ —	\$ 652,432

Note 5. Fair Value of Financial Instruments

Under U.S. GAAP, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., "the exit price") in an orderly transaction between market participants at the measurement date. In determining fair value, the Company uses various valuation approaches, including quoted market prices and discounted cash flows. U.S. GAAP also establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available.

Observable inputs are obtained from independent sources and can be validated by a third party, whereas, unobservable inputs reflect assumptions regarding what a third party would use in pricing an asset or liability. The fair value hierarchy is categorized into three levels based on the reliability of inputs as follows:

- Level 1 - Valuations based on quoted prices in active markets for identical instruments that the Company is able to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.
- Level 2 - Valuations based on quoted prices in active markets for instruments that are similar, or quoted prices in markets that are not active for identical or similar instruments, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.
- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The financial assets for which the Company performs recurring fair value remeasurements are cash equivalents and short-term investments. As of September 23, 2012, financial assets utilizing Level 1 inputs included money market funds. Financial assets utilizing Level 2 inputs included certificates of deposit, corporate bonds and municipal bonds, U.S. agency securities and non-U.S. government securities. Level 2 assets are valued using a third-party pricing services consensus price which is a weighted average price based on multiple sources. These sources determine prices utilizing market income models which factor in, where applicable, transactions of similar assets in active markets, transactions of identical assets in infrequent markets, interest rates, bond or

credit default swap spreads and volatility. The Company does not have any financial assets requiring the use of Level 3 inputs. There were no transfers between Level 1 and Level 2 during the three months ended September 23, 2012.

The following table sets forth financial instruments carried at fair value within the U.S. GAAP hierarchy and using the lowest level of input (in thousands):

	September 23, 2012				June 24, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets:								
Cash equivalents								
Municipal bonds	—	—	—	—	—	3,000	—	3,000
Money market funds	4,864	—	—	4,864	31,318	—	—	31,318
Total cash equivalents	4,864	—	—	4,864	31,318	3,000	—	34,318
Short-term investments								
Municipal bonds	—	238,919	—	238,919	—	211,604	—	211,604
Corporate bonds	—	145,003	—	145,003	—	146,667	—	146,667
Certificates of deposit	—	185,000	—	185,000	—	130,000	—	130,000
U.S. agency securities	—	73,272	—	73,272	—	68,599	—	68,599
Non-U.S. government securities	—	10,238	—	10,238	—	8,758	—	8,758
Total short-term investments	—	652,432	—	652,432	—	565,628	—	565,628
Total assets	\$ 4,864	\$ 652,432	\$ —	\$ 657,296	\$ 31,318	\$ 568,628	\$ —	\$ 599,946

The Company utilizes specific identification in computing realized gains and losses on the sale of investments. Realized gains from the sale of investments for the three months ended September 23, 2012 of approximately \$28 thousand are included in “Other non-operating income, net” and unrealized gains and losses are included as a separate component of equity, net of tax, unless the loss is determined to be “other-than-temporary.”

The Company evaluates its investments for possible impairment or a decline in fair value below cost basis that is deemed to be “other-than-temporary” on a periodic basis. It considers such factors as the length of time and extent to which fair value has been below cost basis, the financial condition of the investee, and its ability and intent to hold the investment for a period of time that may be sufficient for an anticipated recovery in market value.

Note 6. Intangible Assets

The following table presents the components of intangible assets, net (in thousands):

	September 23, 2012	June 24, 2012
Customer relationships	\$ 137,440	\$ 137,440
Developed technology	147,710	147,710
In-process research and development	15,050	15,050
Non-compete agreements	10,244	10,244
Trade names	83,400	83,400
Patent and license rights	102,733	97,812
Intangible assets, gross	\$ 496,577	\$ 491,656
Accumulated amortization	(124,583)	(115,581)
Intangible assets, net	\$ 371,994	\$ 376,075

Total amortization expense, including the amortization of acquisition related intangibles, patents and license rights, recognized during the three months ended September 23, 2012 was \$9.2 million. For the three months ended September 25, 2011, total amortization expense, including the amortization of acquisition related intangibles, patents and license rights, was \$5.3 million.

Total annual amortization expense of intangible assets is estimated to be as follows (in thousands):

Fiscal Year Ending	
June 30, 2013	\$ 37,032
June 29, 2014	34,908
June 28, 2015	31,937
June 26, 2016	31,638
June 25, 2017	29,658

Note 7. Shareholders' Equity

As of September 23, 2012, the Company is authorized by the Board of Directors to repurchase shares of its common stock having an aggregate purchase price not exceeding \$200.0 million for all purchases from June 14, 2012 through the June 30, 2013 expiration of the program. During the three months ended September 23, 2012, there were no repurchases of common stock by the Company under the repurchase program.

Note 8. Earnings Per Share

The following presents the computation of basic earnings per share (in thousands, except per share data):

	Three Months Ended	
	September 23, 2012	September 25, 2011
Basic:		
Net income	\$ 16,123	\$ 12,819
Weighted average common shares	115,539	111,866
Basic earnings per share	\$ 0.14	\$ 0.11

The following computation reconciles the differences between the basic and diluted earnings per share presentations (in thousands, except per share data):

	Three Months Ended	
	September 23, 2012	September 25, 2011
Diluted:		
Net income	\$ 16,123	\$ 12,819
Weighted average common shares - basic	115,539	111,866
Dilutive effect of stock options, unvested shares and ESPP purchase rights	421	677
Weighted average common shares - diluted	115,960	112,543
Diluted earnings per share	\$ 0.14	\$ 0.11

Potential common shares that would have the effect of increasing diluted earnings per share are considered to be antidilutive and as such, these shares are not included in calculating diluted earnings per share. For the three months ended September 23, 2012 and September 25, 2011, there were 8.4 million and 5.3 million, respectively, of potential common shares not included in the calculation of diluted earnings per share because their effect was antidilutive.

Note 9. Stock-Based Compensation

The Company currently has one equity-based compensation plan from which stock-based compensation awards can be granted to employees and directors. In addition, the Company has plans that have been terminated as to future grants, but under which options are currently outstanding.

During the first quarter of fiscal 2013, the Company initiated grants of performance-based stock option and stock unit awards. The compensation expense for an award with a performance condition is based on the probable outcome of that performance condition. Compensation expense is recognized if the Company believes it is probable that the performance condition will be achieved and is adjusted for subsequent changes in the estimate or actual outcome. As with non-performance based awards, compensation expense is recognized over the vesting period. The vesting period runs from the date of grant to the expected date that the performance objective is likely to be achieved.

The Company also has an Employee Stock Purchase Plan ("ESPP") that provides employees with the opportunity to purchase the Company's common stock at a discount. The ESPP was amended in the second quarter of fiscal 2012 to increase the six-month participation period to a twelve-month participation period, divided into two equal six-month purchase periods, and to provide for a look-back feature. At the end of each six-month period, employees purchase the Company's common stock through the ESPP at 15% less than the fair market value of the common stock on the first day of the twelve-month participation period or the purchase date, whichever is lower. The plan amendment also provides for an automatic reset feature to start participants on a new twelve-month participation period if the share value declines during the first six-month purchase period.

Stock Option Awards

The following table summarizes outstanding option awards as of September 23, 2012, and changes during the three months then ended (shares in thousands):

	Number of Shares	Weighted-Average Exercise Price
Outstanding at June 24, 2012	8,800	\$ 36.71
Granted	3,103	27.73
Exercised	(221)	23.91
Forfeited or expired	(147)	40.11
Outstanding at September 23, 2012	11,535	\$ 34.50

Restricted Stock and Stock Unit Awards

A summary of nonvested shares of restricted stock and stock unit awards outstanding under the Company's 2004 Long-Term Incentive Compensation Plan as of September 23, 2012, and changes during the three months then ended, follows (shares in thousands):

	Number of Shares/Units	Weighted- Average Grant- Date Fair Value
Nonvested at June 24, 2012	517	\$ 37.41
Granted	313	27.77
Vested	(179)	34.98
Nonvested at September 23, 2012	651	\$ 33.44

Stock-Based Compensation Valuation and Expense

The Company accounts for its employee stock-based compensation plan using the fair value method. The fair value method requires the Company to estimate the grant date fair value of its stock-based awards and amortize this fair value to compensation expense over the requisite service period or vesting term.

To estimate the fair value of the Company's stock option awards, the Company currently uses the Black-Scholes option-pricing model. The determination of the fair value of stock-based payment awards on the date of grant using an option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of complex and subjective variables. These variables include the expected stock price volatility over the term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate and expected dividends. Due to the inherent limitations of option-valuation models available today, including future events that are unpredictable and the estimation process utilized in determining the valuation of the stock-based awards, the ultimate value realized by award holders may vary significantly from the amounts expensed in the Company's financial statements.

For restricted stock and stock unit awards, grant date fair value is based upon the market price of the Company's common stock on the date of the grant. This fair value is then amortized to compensation expense over the requisite service period or vesting term.

Stock-based compensation expense is reduced by estimated forfeitures such that expense is recognized only for those stock-based awards that are expected to vest. A forfeiture rate is estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from initial estimates.

Total stock-based compensation expense was as follows (in thousands):

<u>Income Statement Classification</u>	Three Months Ended	
	September 23, 2012	September 25, 2011
Cost of goods sold	\$ 2,284	\$ 1,714
Research and development	3,056	2,428
Sales, general and administrative	7,145	7,298
Total operating expenses	10,201	9,726
Total	<u>\$ 12,485</u>	<u>\$ 11,440</u>

Note 10. Income Taxes

The variation between the Company's effective income tax rate and the U.S. statutory rate of 35 percent is due to a percentage of the Company's projected income for the full year being derived from international locations with lower tax rates than the U.S. and the impact of tax credits available in the current year.

U.S. GAAP requires a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is cumulatively more than 50 percent likely to be realized upon ultimate settlement.

As of June 24, 2012, the Company's liability for unrecognized tax benefits was \$4.4 million. During the three months ended September 23, 2012, there were no changes to the amount of unrecognized tax benefits. As a result, the total liability for unrecognized tax benefits as of September 23, 2012 was \$4.4 million. If any portion of this \$4.4 million is recognized, the Company will then include that portion in the computation of its effective tax rate. Although the ultimate timing of the resolution and/or closure of audits is highly uncertain, the Company believes it is reasonably possible that approximately \$2.2 million of gross unrecognized tax benefits will change in the next 12 months as a result of pending audit settlements or statute requirements.

The Company files U.S. federal, U.S. state, and foreign tax returns. For U.S. federal purposes, the Company is generally no longer subject to tax examinations for fiscal years ended June 29, 2009 and prior. For U.S. state tax returns, the Company is generally no longer subject to tax examinations for fiscal years prior to 2009. For foreign purposes, the Company is generally no longer subject to examination for tax periods 2002 and prior. Certain carryforward tax attributes generated in prior years remain subject to examination and adjustment. The Company is currently under inquiry by the Hong Kong Inland Revenue Department for the fiscal year ended June 29, 2008 through the fiscal year ended June 27, 2010.

Note 11. Commitments and Contingencies

Warranties

The following table summarizes the changes in the Company's product warranty liabilities (in thousands):

Balance at June 24, 2012	\$ 5,513
Warranties accrued in current period	626
Changes in estimates for pre-existing warranties	549
Expenditures	(707)
Balance at September 23, 2012	<u>\$ 5,981</u>

Product warranties are estimated and recognized at the time the Company recognizes revenue. The warranty periods range from ninety days to ten years. The Company estimates these warranty liabilities as a percentage of revenue, based on historical knowledge of warranty costs and expected future warranty costs. The Company evaluates its warranty reserve on a quarterly basis. If actual product failure rates materially differ from the Company's estimates, revisions to the estimated warranty liability are recognized in the period in which they are determined.

Litigation

The Company is a party to various legal proceedings, including those described in the Company's Annual Report on Form 10-K for fiscal 2012 as updated below for any material changes. Unless otherwise indicated, the potential losses for claims against the Company in these matters are not reasonably estimable.

Cooper Lighting Litigation

In addition to the previously disclosed litigation with Cooper Lighting, Cooper Lighting, LLC filed a complaint for patent infringement against Cree, Inc. and Ruud Lighting, Inc. in the U.S. District Court for the Northern District of Georgia on September 7, 2012. The complaint seeks injunctive relief and damages for infringement of one U.S. patent owned by Cooper Lighting, LLC: No. 8,210,722, entitled "LED Device for Wide Beam Generation."

Note 12. Reportable Segments

The Company's three operating and reportable segments include:

- LED Products
- Lighting Products
- Power and RF Products

Reportable Segments Description

The Company's LED Products segment includes LED chips, LED components, and SiC wafers. The Company's Lighting Products segment consists of both LED and traditional lighting systems, with its primary focus on LED lighting. The Company's Power and RF Products segment includes power devices and RF devices.

Financial Results by Reportable Segment

The following table reflects the results of the Company's reportable segments as reviewed by the Chief Operating Decision Maker (CODM) for the first quarter of fiscal 2013 and the first quarter of fiscal 2012. The Company's CODM is the Chief Executive Officer.

The Company uses substantially the same accounting policies to derive the segment results reported below as those used in the Company's consolidated financial statements.

The Company's CODM does not review inter-segment revenue when evaluating segment performance and allocating resources to each segment. Thus, inter-segment revenue is not included in the segment revenues presented in the following table. As such, total segment revenue in the table below is equal to the Company's consolidated revenue.

The Company's CODM reviews gross profit as the lowest and only level of segment profit. As such, all items below gross profit on the income statement must be included to reconcile the consolidated gross profit presented in the following table to the Company's consolidated income before taxes.

In order to determine gross profit for each reportable segment, the Company allocates direct costs and indirect costs to each segment's cost of sales. The Company allocates indirect costs, such as employee benefits for manufacturing employees, shared facilities services, information technology, purchasing, and customer service, when the costs are identifiable and beneficial to the reportable segment. The Company allocates these indirect costs based on a reasonable measure of utilization that considers the specific facts and circumstances of the costs being allocated.

Unallocated costs in the table below are not reviewed by the CODM when evaluating segment performance and allocating resources to each segment. These unallocated costs include variable compensation costs for manufacturing employees consisting primarily of stock-based compensation, expenses for profit sharing and quarterly or annual incentive plans, matching contributions under the Company's 401(k) plan, and acquisition related costs.

	Three Months Ended	
	September 23, 2012	September 25, 2011
Revenue	(In thousands)	
LED Products	\$ 187,547	\$ 196,778
Lighting Products	108,073	51,673
Power and RF Products	20,133	20,529
Total Revenue	\$ 315,753	\$ 268,980
Gross Profit		
LED Products	75,467	77,760
Lighting Products	34,100	15,950
Power and RF Products	10,422	8,742
Total Segment Gross Profit	119,989	102,452
Unallocated Costs	(3,940)	(4,424)
Consolidated Gross Profit	\$ 116,049	\$ 98,028

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

Information set forth in this Quarterly Report on Form 10-Q contains various "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). All information contained in this report relative to future markets for our products and trends in and anticipated levels of revenue, gross margins and expenses, as well as other statements containing words such as "believe," "project," "may," "will," "anticipate," "target," "plan," "estimate," "expect" and "intend" and other similar expressions constitute forward-looking statements. These forward-looking statements are subject to business, economic and other risks and uncertainties, both known and unknown, and actual results may differ materially from those contained in the forward-looking statements. Any forward-looking statements we make are as of the date made, and except as required under the U.S. federal securities laws and the rules and regulations of the Securities and Exchange Commission (the "SEC"), we have no duty to update them if our views later change. These forward-looking statements should not be relied upon as representing our views as of any date subsequent to the date of this Quarterly Report. Examples of risks and uncertainties that could

cause actual results to differ materially from historical performance and any forward-looking statements include, but are not limited to, those described in “Risk Factors” in Part II, Item 1A of this Quarterly Report.

The following discussion is designed to provide a better understanding of our unaudited consolidated financial statements, including a brief discussion of our business and products, key factors that impacted our performance, and a summary of our operating results. The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in Part I, Item 1 of this Quarterly Report on Form 10-Q, and the consolidated financial statements and notes thereto and Management’s Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended June 24, 2012. Historical results and percentage relationships among any amounts in the financial statements are not necessarily indicative of trends in operating results for any future periods.

Overview

Cree, Inc. (Cree, we, our, or us) is a leading innovator of lighting-class light emitting diode (LED) products, lighting products and semiconductor products for power and radio-frequency (RF) applications. Our products are targeted for applications such as indoor and outdoor lighting, video displays, transportation, electronic signs and signals, power supplies, solar inverters and wireless systems.

We develop and manufacture semiconductor materials and devices primarily based on silicon carbide (SiC), gallium nitride (GaN) and related compounds. In many cases the physical and electronic properties of SiC and GaN offer technical advantages

over traditional silicon, gallium arsenide (GaAs) and other materials used for electronic and opto-electronic applications.

Our LED products consist of LED components, LED chips, and SiC wafers. As LED technology improves, we believe the potential market for LED lighting will continue to expand. Our success in selling LED products depends upon our ability to offer innovative products and our ability to enable our customers to develop and market LED based products that successfully compete and drive LED adoption against traditional lighting products.

Our lighting products consist of both LED and traditional lighting systems. We design, manufacture and sell lighting systems for indoor and outdoor applications, with our primary focus on LED lighting systems for the commercial and industrial markets.

In addition, we develop, manufacture and sell power and RF devices. Our power products are made from SiC and provide faster switching speeds than comparable silicon-based power devices for a given power level. Our RF devices are made from GaN and produce higher power densities as compared to silicon or gallium arsenide.

The majority of our products are manufactured at our production facilities located in North Carolina, Wisconsin, and China. We also use contract manufacturers for certain aspects of product fabrication, assembly and packaging. We operate research and development facilities in North Carolina, California, Wisconsin, India, and China.

Reportable Segments

We have three reportable segments:

- LED Products
- Lighting Products
- Power and RF Products

Reportable segments are components of an entity that have separate financial data that the entity's Chief Operating Decision Maker (CODM) regularly reviews when allocating resources and assessing performance. Our CODM is the Chief Executive Officer.

Industry Dynamics and Trends

There are a number of industry factors that affect our business which include, among others:

- *Overall Demand for Products and Applications using LEDs.* Our potential for growth depends significantly on the adoption of LEDs within the general lighting market and our ability to affect this rate of adoption. Although LED lighting has grown in recent years, adoption of LEDs for general lighting is relatively new, still limited, and faces significant challenges before widespread adoption. Demand also fluctuates based on various market cycles, a continuously evolving LED industry supply chain, and demand dynamics in the market. These uncertainties make demand difficult to forecast for us and our customers.
- *Intense and Constantly Evolving Competitive Environment.* Competition in the LED and lighting industry is intense. Many companies have made significant investments in LED development and production equipment. Traditional lighting companies and new entrants are investing in LED based lighting products as LED adoption has gained momentum. Product pricing pressures exist as market participants often undertake pricing strategies to gain or protect market share, increase the utilization of their production capacity and open new applications to LED based solutions. To remain competitive, market participants must continuously increase product performance and reduce costs. To address these competitive pressures, we have invested in R&D activities to support new product development to deliver higher levels of performance and lower costs to differentiate our products in the market.
- *Technological Innovation and Advancement.* Innovations and advancements in LED technology continue to expand the potential commercial application of LEDs particularly in the general illumination market. However, new technologies or standards could emerge, or improvements could be made in existing technologies, that could reduce or limit the demand for LEDs in certain markets.
- *Regulatory Actions Concerning Energy Efficiency.* Many countries have already instituted or have announced plans to institute government regulations and programs designed to encourage or mandate increased energy efficiency, even in some cases banning forms of incandescent lighting, which are advancing the adoption of more energy efficient lighting solutions such as LEDs. While this trend is generally positive, these regulations are affected by changing political priorities which can modify or limit the effectiveness of these new regulations.

- *Intellectual Property Issues.* Market participants rely on patented and non-patented proprietary information relating to product development, manufacturing capabilities and other core competencies of their business. Protection of intellectual property is critical. Therefore, steps such as additional patent applications, confidentiality and non-disclosure agreements, as well as other security measures are generally taken. To enforce or protect intellectual property rights, litigation or threatened litigation commonly occurs.

Financial Results of the First Quarter Fiscal 2013

The following is a summary of our financial results for the three months ended September 23, 2012:

- Revenues increased to \$315.8 million in the first quarter of fiscal 2013 from \$306.8 million in the fourth quarter of fiscal 2012.
- Gross margins improved to 36.8% in the first quarter of fiscal 2013 from 34.8% in the fourth quarter of fiscal 2012.
- Operating income was \$17.3 million in the first quarter of fiscal 2013 compared to \$8.7 million in the fourth quarter of fiscal 2012. Net income per diluted share was \$0.14 compared to \$0.09 for the fourth quarter of fiscal 2012.
- Inventory decreased to \$179.7 million at September 23, 2012 compared to \$188.8 million at June 24, 2012.
- We spent \$12.6 million on purchases of property and equipment during the three months ended September 23, 2012 compared to \$19.8 million during the three months ended June 24, 2012.
- Combined cash, cash equivalents and marketable investments increased to \$816.3 million at September 23, 2012 compared to \$744.5 million at June 24, 2012.

Business Outlook

We project that the markets for our products will remain highly competitive during fiscal 2013. We anticipate focusing on the following key areas, among others, in response to this competitive environment:

- *Accelerate adoption of LED lighting.* We continue to work to develop new LED lighting systems to increase the lumens per dollar, which brings LED lighting closer to price parity with conventional technology and reduces the payback time for the customer. We are focused on delivering best-in-class products for key lighting categories and expanding our sales channels to build the Cree brand and access more customers.
- *Grow LED component sales through product innovation.* We are working to leverage our SC³ Technology™ next generation LED platform into a range of new LED component products that are targeted to deliver more lumens per dollar to the customer. We are also developing component and module products targeted to simplify our customers' product designs and reduce their time to market.
- *Leverage technology leadership in Power and RF to open new applications for these products.* In the power product line, we are working with our customers to combine our SiC MOSFET and Schottky diodes technology to enable power modules for solar, uninterruptable power supplies (UPS) and motor control applications. In the RF product line, we are developing GaN based products to access new military applications and some commercial platforms.
- *Translate product innovation into revenue and profit growth.* We target incremental improvement from factory cost reductions, process improvements and lower cost new product designs.

Results of Operations

The following table sets forth certain consolidated statement of income data for the periods indicated:

(in thousands, except per share amounts and percentages)	Three Months Ended			
	September 23, 2012		September 25, 2011	
	Dollars	% of Revenue	Dollars	% of Revenue
Revenue, net	\$ 315,753	100%	\$ 268,980	100%
Cost of revenue, net	199,704	63%	170,952	64%
Gross profit	116,049	37%	98,028	36%
Research and development	37,547	12%	34,402	13%
Sales, general and administrative	52,645	17%	45,539	17%
Amortization of acquisition-related intangibles	7,670	2%	3,925	1%
Loss on disposal or impairment of long-lived assets	898	—%	775	—%
Operating income	17,289	6%	13,387	5%
Other non-operating income, net	1,593	—%	974	—%
Interest income, net	1,792	—%	1,969	1%
Income from operations before income taxes	20,674	6%	16,330	6%
Income tax expense	4,551	1%	3,511	1%
Net income	16,123	5%	12,819	5%
Diluted earnings per share	\$ 0.14		\$ 0.11	

Revenues

Revenues for the three months ended September 23, 2012 and September 25, 2011 were comprised of the following (in thousands, except percentages):

	Three Months Ended			
	September 23, 2012	September 25, 2011	Change	
LED Products	\$ 187,547	\$ 196,778	\$ (9,231)	(5)%
<i>Percent of revenue</i>	60%	73%		
Lighting Products	108,073	51,673	56,400	109 %
<i>Percent of revenue</i>	34%	19%		
Power and RF Products	20,133	20,529	(396)	(2)%
<i>Percent of revenue</i>	6%	8%		
Total revenue	\$ 315,753	\$ 268,980	\$ 46,773	17 %

Our consolidated revenue increased 17% to \$315.8 million in the first quarter of fiscal 2013 from \$269.0 million in the first quarter of fiscal 2012. This year over year increase is due primarily to recognition of revenues from the Ruud Lighting acquisition for a full quarter in addition to increased sales of our existing products.

LED Products Segment Revenue

LED Products revenue represents the largest portion of our revenue with approximately 60% and 73% of our total revenues for the first quarter of fiscal 2013 and fiscal 2012, respectively.

LED Products revenue decreased approximately 5% to \$187.5 million in the first quarter of fiscal 2013 from \$196.8 million in the first quarter of fiscal 2012, primarily due to a decline in blended average selling price (ASP) despite increased unit sales of LED products. The ASP decreased by approximately 5% in the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 due to downward pricing pressure for LED components partially offset by changes in product mix.

Lighting Products Segment Revenue

Lighting Products revenue represents approximately 34% and 19% of our total revenues for the first quarter of fiscal 2013 and fiscal 2012, respectively.

Lighting Products revenue increased approximately 109% to \$108.1 million in the first quarter of fiscal 2013 from \$51.7 million in the first quarter of fiscal 2012. The increase was due to recognizing a full quarter of sales in fiscal 2013 for products acquired from Ruud Lighting and an increase in the sales of our indoor LED lighting products. The ASP for our lighting products decreased by approximately 2% in the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 due to product mix.

Power and RF Products Segment Revenue

Power and RF Products revenue represents approximately 6% and 8% of our total revenues for the first quarter of fiscal 2013 and fiscal 2012, respectively.

Power and RF Products revenue decreased approximately 2% to \$20.1 million in the first quarter of fiscal 2013 from \$20.5 million in the first quarter of fiscal 2012. The ASP for our power and RF products decreased by approximately 12% in the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 due to a change in product mix.

Unallocated Revenue

All of our revenue is allocated to our reportable segments. Our CODM does not review inter-segment revenue when evaluating performance and allocating resources to each segment, and inter-segment revenue is not included in the segment revenues presented above. As such, total segment revenue in the table above is equal to our consolidated revenue.

Gross Profit and Gross Margin

Gross Profit and Gross Margin for the three months ended September 23, 2012 and September 25, 2011 were comprised of the following (in thousands, except percentages):

	Three Months Ended			
	September 23, 2012	September 25, 2011	Change	
LED Products gross profit	\$ 75,467	\$ 77,760	\$ (2,293)	(3)%
LED Products gross margin	40.2%	39.5%		
Lighting Products gross profit	34,100	15,950	18,150	114 %
Lighting Products gross margin	31.6%	30.9%		
Power and RF Products gross profit	10,422	8,742	1,680	19 %
Power and RF Products gross margin	51.8%	42.6%		
Unallocated costs	(3,940)	(4,424)	484	(11)%
Consolidated gross profit	\$ 116,049	\$ 98,028	\$ 18,021	18 %
Consolidated gross margin	37%	36%		

Our consolidated gross profit increased 18% to \$116.0 million in the first quarter of fiscal 2013 from \$98.0 million in the first quarter of fiscal 2012. Our consolidated gross margin increased to 37% in the first quarter of fiscal 2013 from 36% in the first quarter of fiscal 2012. The quarter over quarter consolidated gross margin increases were due to the increases realized by all our segments, as discussed further below.

LED Products Segment Gross Profit and Gross Margin

LED Products gross profit decreased approximately 3% to \$75.5 million in the first quarter of fiscal 2013 from \$77.8 million in the first quarter of fiscal 2012 and LED Products gross margin increased to 40.2% in the first quarter of fiscal 2013 from 39.5% in the first quarter of fiscal 2012. LED Products gross margin increased due to better factory execution, realization of cost reduction initiatives and the introduction of lower cost products, which all offset the decline in ASPs.

Lighting Products Segment Gross Profit and Gross Margin

Lighting Products gross profit increased approximately 114% to \$34.1 million in the first quarter of fiscal 2013 from \$16.0 million in the first quarter of fiscal 2012. In the first quarter of fiscal 2013, Lighting Products gross margin increased to 31.6%

from 30.9% in the first quarter of fiscal 2012. Lighting Products gross profit increased due to increased sales volumes of products acquired from Ruud Lighting and gross margins increased due to manufacturing cost reductions and lower cost new product designs.

Power and RF Products Segment Gross Profit and Gross Margin

Power and RF Products gross profit increased approximately 19% to \$10.4 million in the first quarter of fiscal 2013 from \$8.7 million in the first quarter of fiscal 2012. In the first quarter of fiscal 2013, Power and RF Products gross margin increased to 51.8% from 42.6% in the first quarter of fiscal 2012. Gross profit and gross margin increased due to production yield improvements, increased factory utilization and conversion to lower cost products.

Unallocated Costs

Unallocated costs were \$3.9 million and \$4.4 million in the first quarter of fiscal 2013 and 2012, respectively. These costs are for manufacturing employees, consisting primarily of stock-based compensation, expenses for profit sharing and quarterly or annual incentive plans, matching contributions under our 401(k) plan and acquisition related costs. These costs are not allocated to the reportable segments' gross profit because our CODM does not review them regularly when evaluating segment performance and allocating resources. For further information on the allocation of costs to segment gross profit, refer to Note 12, "Reportable Segments," in our consolidated financial statements included in Item 1 of this Quarterly Report.

Research and Development

Research and development expenses include costs associated with the development of new products, enhancements of existing products and general technology research. These costs consist primarily of employee salaries and related compensation costs, occupancy costs, consulting costs and the cost of development equipment and supplies.

The following sets forth our research and development expenses in dollars and as a percentage of revenues (in thousands, except percentages):

	Three Months Ended			
	September 23, 2012	September 25, 2011	Change	
Research and development	\$ 37,547	\$ 34,402	\$ 3,145	9%
<i>Percent of revenues</i>	12%	13%		

Research and development expenses in the first quarter of fiscal 2013 increased 9% to \$37.5 million from \$34.4 million in the first quarter of fiscal 2012. These increases were primarily due to increased spending on research and development activities focused on new LED chips, LED components, LED lighting products, power and RF products and the incremental research and development expense due to the Ruud Lighting acquisition. Our research and development expenses vary significantly from quarter to quarter based on a number of factors, including: the timing of new product introductions, timing of expenditures and the number and nature of our ongoing research and development activities. However, we anticipate that in general our research and development expenses will continue to increase over time to support future growth.

Sales, General and Administrative

Sales, general and administrative expenses are composed primarily of costs associated with our sales and marketing personnel and our executive and administrative personnel (for example, finance, human resources, information technology and legal) and consist of 1) salaries and related compensation costs, 2) consulting and other professional services (such as litigation and other outside legal counsel fees, audit and other compliance costs), 3) facilities and insurance costs, and 4) travel and other costs. The following table sets forth our sales, general and administrative expenses in dollars and as a percentage of revenues (in thousands, except percentages):

	Three Months Ended			
	September 23, 2012	September 25, 2011	Change	
Sales, general and administrative	\$ 52,645	\$ 45,539	\$ 7,106	16%
<i>Percent of revenues</i>	17%	17%		

Sales, general and administrative expenses in the first quarter of fiscal 2013 increased 16% to \$52.6 million from \$45.5 million in the first quarter of fiscal 2012. The increase in sales, general and administrative expenses for the first quarter of fiscal 2013 is primarily due to an increase in spending on sales and marketing for lighting products, including commissions and trade shows, as we continue to expand our direct sales resources and channels and invest in building and promoting the Cree brands. Additionally, the increase included incremental sales, general and administrative expenses for the full quarter from the Ruud Lighting acquisition, as well as personnel additions during fiscal 2012 to support our growth which were partially offset by decreased legal costs.

Amortization of Acquisition Related Intangibles

As a result of our acquisitions, we have recognized various intangible assets that require amortization, including customer relationships and developed technologies. During fiscal 2012, we acquired Ruud Lighting, resulting in \$206.0 million of amortizable intangible assets consisting of developed technology, customer relationships, trade names, in-process research and development, and non-compete agreements. During fiscal 2008, we acquired LLF, resulting in \$41.2 million of amortizable intangible assets. These intangible assets are principally composed of developed technology that specifically relates to technologies underlying the development of LED lighting products for the general illumination market. During fiscal 2007, we acquired INTRINSIC Semiconductor Corporation and COTCO Luminant Device Limited (now Cree Hong Kong Limited) (COTCO), resulting in \$63.7 million of amortizable intangible assets principally composed of customer relationships and developed technology.

Amortization of intangible assets related to our acquisitions is as follows (in thousands, except percentages):

	Three Months Ended				
	September 23, 2012	September 25, 2011	Change		
INTRINSIC	\$ 186	\$ 186	\$ —	— %	
COTCO	1,041	1,264	(223)	(18)%	
LLF	750	750	—	— %	
Ruud Lighting	5,731	1,725	4,006	232 %	
Total	\$ 7,708	\$ 3,925	\$ 3,783	96 %	

Loss on Disposal or Impairment of Long-Lived Assets

We operate a capital intensive business. As such, we dispose of a certain level of our equipment in the normal course of business as our production processes change due to production improvement initiatives or product mix changes. Due to the risk of technological obsolescence or changes in our production process, we regularly review our equipment and capitalized patent costs for possible impairments in value. The following table sets forth our loss on disposal or impairment of long-lived assets (in thousands, except percentages):

	Three Months Ended				
	September 23, 2012	September 25, 2011	Change		
Loss on disposal or impairment of long-lived assets, net	\$ 898	\$ 775	\$ 123	16%	

We recognized a net loss of \$0.9 million on the disposal of long-lived assets in the first quarter of fiscal 2013 compared to a net loss of \$0.8 million in the first quarter of fiscal 2012. These net losses resulted from the disposal of equipment due to manufacturing process changes and the impairment of certain capitalized patent costs.

Non-Operating Income

The following table sets forth our non-operating income (in thousands, except percentages):

	Three Months Ended				
	September 23, 2012	September 25, 2011	Change		
Other non-operating income, net	\$ 1,593	\$ 974	\$ 619	64 %	
Interest income, net	1,792	1,969	(177)	(9)%	
Total	\$ 3,385	\$ 2,943	\$ 442	15 %	

We have no debt or active lines of credit and we are in a net interest income position. Our investments consist of fixed interest rate securities such as high-grade corporate debt, commercial paper, government securities, municipal bonds, and other fixed interest rate investments. The primary objective of our investment policy is preservation of principal. The decrease in interest income is due to the liquidation of a significant portion of our investment portfolio to pay for the Ruud Lighting acquisition in the first quarter of fiscal 2012 and declining investment yields year over year.

Other non-operating income, net, is typically comprised of gains on sales of investments and foreign exchange gains and losses. However, the increase for the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 is due primarily to a one-time payment in connection with the SemiLEDs patent litigation settlement.

Income Tax Expense

The following table sets forth our income tax expense in dollars and our effective tax rate (in thousands, except percentages):

	Three Months Ended			Change
	September 23, 2012	September 25, 2011		
Income tax expense	\$ 4,551	\$ 3,511	\$ 1,040	30%
<i>Effective Tax Rate</i>	22.0%	21.5%		

The variation between our effective tax rate and the U.S. statutory rate of 35% is primarily due to the consolidation of our foreign operations, which are subject to income taxes at lower statutory rates and the impact of tax credits available in the current year. A change in the mix of pretax income of our various tax jurisdictions can have a material impact on our periodic effective tax rate.

We recognized income tax expense of \$4.6 million for an effective tax rate of 22.0% in the first quarter of fiscal 2013 as compared to income tax expense of \$3.5 million for an effective tax rate of 21.5% in the first quarter of fiscal 2012. The increase in our effective tax rate for the three month comparable period is primarily due to a higher percentage of our projected income for the full year being derived from U.S. operations that are taxed at a higher tax rate than international locations.

Liquidity and Capital Resources

Overview

We require cash to fund our operating expenses and working capital requirements, including outlays for research and development, capital expenditures, strategic acquisitions and investments. Our principal sources of liquidity are cash on hand, marketable investments and cash generated from operations. Our ability to generate cash from operations has been one of our fundamental strengths and has provided us with substantial flexibility in meeting our operating, financing and investing needs. We have no debt or active lines of credit and have minimal lease commitments.

Based on past performance and current expectations, we believe our cash and cash equivalents, investments, cash generated from operations and our ability to access capital markets will satisfy our working capital needs, capital expenditures, investment requirements, stock repurchases, contractual obligations, commitments and other liquidity requirements associated with our operations through at least the next 12 months.

From time to time, we evaluate strategic opportunities, including potential acquisitions, divestitures or investments in complementary businesses and we anticipate continuing to make such evaluations. We may also access capital markets through the issuance of debt or additional shares of common stock in connection with the acquisition of complementary businesses or other significant assets or for other strategic opportunities.

We have and may continue to use a portion of our available cash and cash equivalents, or funds underlying our marketable securities, to repurchase shares of our common stock. With our strong working capital position, we believe that we have the ability to continue to invest in further development of our products and, when necessary or appropriate, make selective acquisitions or other strategic investments to strengthen our product portfolio, secure key intellectual properties, or expand our production capacity.

Financial Condition

Our liquidity and capital resources depend on our cash flows from operations and our working capital. Our working capital increased to \$1.065 billion as of September 23, 2012 from \$1.015 billion as of June 24, 2012, primarily due to a net increase in cash and cash equivalents driven by cash flow from operations. The following table presents the components of our cash conversion cycle for our first quarter of fiscal 2013 and fourth quarter of fiscal 2012:

	September 23, 2012	June 24, 2012	Change	
Days of sales outstanding ^(a)	46	45	1	2 %
Days of supply in inventory ^(b)	81	85	(4)	(5)%
Days in accounts payable ^(c)	(39)	(36)	(3)	8 %
Cash conversion cycle	88	94	(6)	(6)%

- a) Days of sales outstanding (DSO) calculates the average collection period of our receivables. DSO is based on the ending net trade receivables and the revenue for the quarter then ended. DSO is calculated by dividing ending accounts receivable, net of applicable allowances and reserves, by the average net revenue per day for the respective quarter.
- b) Days of supply in inventory (DSI) measures the average number of days from procurement to sale of our product. DSI is based on ending inventory and cost of goods sold for the quarter then ended. DSI is calculated by dividing ending inventory by average cost of goods sold per day for the respective quarter.
- c) Days in accounts payable (DPO) calculates the average number of days our payables remain outstanding before payment. DPO is based on ending accounts payable and cost of goods sold for the quarter then ended. DPO is calculated by dividing ending accounts payable by the average cost of goods sold per day for the respective quarter.

The decrease in the cash conversion cycle was primarily driven by a reduction in days supply in inventory as a result of increased sales and better management of factory loading coupled with an increase in days in accounts payable.

As of September 23, 2012, all of our investments had investment grade ratings, and any such investments that were in an unrealized loss position at September 23, 2012 were in such position due to interest rate changes, sector credit rating changes or company-specific rating changes. As we intend and believe that we have the ability to hold such investments for a period of time that will be sufficient for anticipated recovery in market value, we currently expect to receive the full principal or recover our cost basis in these securities. The declines in value of the securities in our portfolio are considered to be temporary in nature and, accordingly, we do not believe these securities are impaired as of September 23, 2012.

Cash Flows

In summary, our cash flows were as follows (in thousands, except percentages):

	Three Months Ended			
	September 23, 2012	September 25, 2011	Change	
Cash provided by operating activities	\$ 85,686	\$ 41,645	\$ 44,041	106 %
Cash used in investing activities	(106,309)	(295,893)	189,584	(64)%
Cash provided by financing activities	5,328	2,355	2,973	126 %
Effects of foreign exchange changes	262	468	(206)	(44)%
Net (decrease) increase in cash and cash equivalents	\$ (15,033)	\$ (251,425)	\$ 236,392	

The following is a discussion of our primary sources and uses of cash in our operating, investing and financing activities.

Cash Flows from Operating Activities

Net cash provided by operating activities was \$85.7 million in the first three months of fiscal 2013 compared to \$41.6 million for the first three months of fiscal 2012. The increase was primarily driven by the year over year increase in our net income along with overall decrease in our non-cash and equivalent working capital including decreases in inventories and increases in accounts payable and accrued liabilities.

Cash Flows from Investing Activities

Our investing activities primarily relate to transactions within our investments, strategic acquisitions, purchase of property, plant and equipment and purchase of patent and license rights. Net cash used in investing activities was \$106.3 million for the first three months of fiscal 2013 compared to \$295.9 million for the first three months of fiscal 2012. This year over year decrease in cash used in investing activities was primarily the result of the \$456.0 million cash expended in the first quarter of fiscal 2012 for the acquisition of Ruud Lighting net of proceeds from the sale of investments to fund the acquisition.

We are continuing to actively manage our capital spending. For fiscal 2013, we target similar levels of investment as fiscal 2012 to support our strategic priorities to lead the market, drive adoption of LED lighting, accelerate cost reductions and support incremental capacity as needed.

Cash Flows from Financing Activities

Net cash provided by financing activities was \$5.3 million for the first three months of fiscal 2013 compared to \$2.4 million for the first three months of fiscal 2012. This change was primarily due to an increase in the issuance of shares related to stock option exercises.

Off-Balance Sheet Arrangements

We do not use off-balance sheet arrangements with unconsolidated entities or related parties, nor do we use other forms of off-balance sheet arrangements. Accordingly, our liquidity and capital resources are not subject to off-balance sheet risks from unconsolidated entities. As of September 23, 2012, we did not have any off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of SEC Regulation S-K.

We have entered into leases primarily for certain of our facilities in the normal course of business. These arrangements are often referred to as a form of off-balance-sheet financing. Please refer to Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended June 24, 2012, in the section entitled “Contractual Obligations” for the future minimum lease payments due under our operating leases as of June 24, 2012. There have been no significant changes to the contractual obligations discussed therein.

Critical Accounting Policies and Estimates

For information about our critical accounting policies and estimates, see the “Critical Accounting Policies and Estimates” section of “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our Annual Report on Form 10-K for the fiscal year ended June 24, 2012.

Recent Accounting Pronouncements

See Note 1, “Basis of Presentation and Changes in Significant Accounting Policies,” to our unaudited financial statements in Part I, Item 1 of this Quarterly Report for a description of recent accounting pronouncements, including the estimated effects, if any, on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

For quantitative and qualitative disclosures about our market risks, see “Part II. Item 7A. Quantitative and Qualitative Disclosures About Market Risk” of our Annual Report on Form 10-K for the fiscal year ended June 24, 2012. There have been no material changes to the amounts presented therein.

Item 4. Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Interim Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Form 10-Q. Based on such evaluation, our Chief Executive Officer and Interim Chief Financial Officer concluded that, as of the end of the period covered by the Form 10-Q, our disclosure controls and procedures are effective in that they provide reasonable assurances that the information we are required to disclose

in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods required by the SEC's rules and forms and that such information is accumulated and communicated to management, including our Chief Executive Officer and Interim Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

We routinely review our internal control over financial reporting and from time to time make changes intended to enhance the effectiveness of our internal control over financial reporting. We will continue to evaluate the effectiveness of our disclosure controls and procedures and internal control over financial reporting on an ongoing basis and will take action as appropriate. There have been no changes to our internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, during the first quarter of fiscal 2013 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

The information required by this item is set forth under Note 11, "Commitments and Contingencies," to our unaudited financial statements in Part I, Item 1 of this Quarterly Report and is incorporated herein by reference.

Item 1A. Risk Factors

Described below are various risks and uncertainties that may affect our business. The descriptions below include any material changes to and supersede the description of the risk factors affecting our business previously disclosed in "Part I, Item 1A. Risk Factors" of our Annual Report on Form 10-K for the fiscal year ended June 24, 2012. If any of the risks described below actually occurs, our business, financial condition or results of operations could be materially and adversely affected.

Our operating results are substantially dependent on the development and acceptance of new products.

Our future success may depend on our ability to develop new, higher performing and lower cost solutions for existing and new markets and for customers to accept those solutions. We must introduce new products in a timely and cost-effective manner, and we must secure production orders for those products from our customers. The development of new products is a highly complex process, and we historically have experienced delays in completing the development and introduction of new products. Our research and development efforts are aimed at solving increasingly complex problems, and we do not expect that all of our projects will be successful. The successful development and introduction of these new products depends on a number of factors, including the following:

- achievement of technology breakthroughs required to make commercially viable devices;
- the accuracy of our predictions for market requirements beyond near term visibility;
- our ability to predict, influence, and/or react to evolving standards;
- acceptance of our new product designs;
- acceptance of new technology in certain markets;
- the availability of qualified research and development personnel;
- our timely completion of product designs and development;
- our ability to expand direct customer sales and influence key distribution customers to adopt our products;
- our ability to develop repeatable processes to manufacture new products in sufficient quantities, with the desired specifications and at competitive costs for commercial sales;
- our ability to effectively transfer products and technology developed in one country to our manufacturing facilities in other countries;
- our customers' ability to develop competitive products incorporating our products; and
- acceptance of our customers' products by the market.

If any of these or other factors becomes problematic, we may not be able to develop and introduce these new products in a timely or cost-effective manner.

If we are unable to effectively develop, manage and expand our sales and distribution channels for our products, our operating results may suffer.

We have expanded into business channels that are different from those in which we have historically operated as we grow our business and sell more LED and lighting products. For example, in the third quarter of fiscal 2012, we consolidated the Cree and BetaLED lighting product lines sales agents for each major market in North America which resulted in a disruption in the project pipeline and lower than targeted sales for our indoor lighting products. Lighting sales agents may also choose to drop our product lines from their portfolio to avoid losing access to our competitors' lighting products. If we are unable to effectively penetrate these channels or develop alternate channels to ensure our products are reaching the appropriate customer base, our financial results may be adversely impacted. In addition, if we successfully penetrate or develop these channels, we cannot guarantee that customers will accept our products or that we will be able to manufacture and deliver them in the timeline established by our customers.

We sell a substantial portion of our products to distributors. We rely on distributors to develop and expand their customer base as well as anticipate demand from their customers. If they are not successful, our growth and profitability may be adversely impacted. Distributors must balance the need to have enough products in stock in order to meet their customers' needs against their internal target inventory levels and the risk of potential inventory obsolescence. The risks of inventory obsolescence are especially true with technological products. The distributors' internal target inventory levels vary depending on market cycles and a number of factors within each distributor over which we have very little, if any, control.

We typically recognize revenue on product sold to distributors when the item is shipped and title passes to the distributor (sell-in method). Certain distributors have limited rights to return inventory under stock rotation programs and have limited price protection rights for which we make estimates. We evaluate inventory levels in the distribution channel, current economic trends and other related factors in order to account for these factors in our judgments and estimates. As inventory levels and product return trends change, we revise our estimates and our operating results could be impacted.

We face significant challenges managing our growth as the market adopts LEDs for general lighting.

Our potential for growth depends significantly on the adoption of LEDs within the general lighting market and our ability to affect this rate of adoption. Although LED lighting has grown rapidly in recent years, adoption of LEDs for general lighting is relatively new, still limited and faces significant challenges before widespread adoption. In order to manage our growth and business strategy effectively in light of uncertainty related to the pace of adoption, we must continue to:

- maintain, expand and purchase adequate manufacturing facilities and equipment to meet customer demand;
- maintain a sufficient supply of raw materials to support our growth;
- expand research and development, sales and marketing, technical support, distribution capabilities and administrative functions;
- manage organizational complexity and communication;
- expand the skills and capabilities of our current management team;
- add experienced senior level managers; and
- attract and retain qualified employees.

While we intend to focus on managing our costs and expenses, over the long term we expect to invest substantially to support our growth and may have additional unexpected costs. For example, in November 2011, we broke ground on a 208,000 square foot expansion to our Wisconsin manufacturing and warehouse facilities to support our LED lighting products production in fiscal 2013 and we are targeting to continue expanding our LED products manufacturing facilities in China. However, such investments take time to become fully operational, and we may not be able to expand quickly enough to exploit targeted market opportunities. There are also inherent execution risks in starting up a new factory or expanding production capacity that could increase costs and reduce our operating results, including design and construction cost overruns, poor production process yields and reduced quality control during the start-up phase.

We are also increasingly dependent on information technology to enable us to improve the effectiveness of our operations and to maintain financial accuracy and efficiency. If we do not allocate and effectively manage the resources necessary to build, implement and sustain the proper technology infrastructure, we could be subject to transaction errors, processing inefficiencies, loss of customers, business disruptions or loss of or damage to intellectual property through security breach.

In connection with our efforts to cost-effectively manage our growth, we have increasingly relied on contractors for production capacity, logistics support and certain administrative functions including hosting of certain information technology software applications. If these service providers do not perform effectively, we may not be able to achieve the expected cost savings and may incur additional costs to correct errors or fulfill customer demand. Depending on the function involved, such errors may also lead to business disruption, processing inefficiencies or the loss of or damage to intellectual property through security breach, or impact employee morale. Our operations may also be negatively impacted if any of these service providers do not have the financial capability to meet our growing needs.

The markets in which we operate are highly competitive and have evolving technical requirements.

The markets for our products are highly competitive. In the LED market, we compete with companies that manufacture or sell LED chips and LED components. In the lighting market we compete with companies that manufacture and sell traditional and LED lighting products, many of which have larger and more established sales channels. Competitors continue to offer new products with aggressive pricing and improved performance. Competitive pricing pressures may change and could accelerate the rate of decline of our average sales prices.

With the growth potential for LEDs, we may face increased competition in the future. If the investment in new capacity exceeds the growth in demand, the LED market is likely to become more competitive with additional pricing pressures. Additionally, new technologies could emerge or improvements could be made in existing technologies that may also reduce the demand for LEDs in certain markets. There are also new technologies, such as organic LEDs (OLEDs), which could potentially have the same impact on LED demand for backlighting, which could impact the overall LED market.

As competition increases, in order to continue to grow our business, we need to continue to develop new products that meet or exceed the needs of our customers. Therefore, our ability to continually produce more efficient, higher brightness and lower cost LEDs and lighting products that meet the evolving needs of our customers will be critical to our success. Competitors may also try to align with some of our strategic customers. This could mean lower prices for our products, reduced demand for our products and a corresponding reduction in our ability to recover development, engineering and manufacturing costs. Any of these developments could have an adverse effect on our business, results of operations or financial condition.

Global economic conditions could materially adversely impact demand for our products and services.

Our operations and performance depend significantly on worldwide economic conditions. Uncertainty about global economic conditions could result in customers postponing purchases of our products and services in response to tighter credit, unemployment, negative financial news and/or declines in income or asset values and other macroeconomic factors, which could have a material negative effect on demand for our products and services and accordingly, on our business, results of operations and financial condition.

We rely on a number of key sole source and limited source suppliers, and are subject to high price volatility on certain commodity inputs, variations in parts quality, and raw material consistency and availability.

We depend on a number of sole source and limited source suppliers for certain raw materials, including rare earth elements, components, services and equipment used in manufacturing our products, including key materials and equipment used in critical stages of our manufacturing processes. Although alternative sources generally exist for these items, qualification of many of these alternative sources could take up to six months or longer. Where possible, we attempt to identify and qualify alternative sources for our sole and limited source suppliers.

We generally purchase these sole or limited source items with purchase orders, and we have limited guaranteed supply arrangements with such suppliers. Some of our sources can have variations in attributes and availability which can affect our ability to produce products in sufficient volume or quality. We do not control the time and resources that these suppliers devote to our business, and we cannot be sure that these suppliers will perform their obligations to us. Additionally, general shortages in the marketplace of certain raw materials or key components may adversely impact our business. In the past, we have experienced decreases in our production yields when suppliers have varied from previously agreed upon specifications that have impacted our cost of sales.

Additionally, the inability of our suppliers to access capital efficiently could cause disruptions in their businesses, thereby negatively impacting ours. This risk may increase if an economic downturn negatively affects key suppliers or a significant number of our other suppliers. Any delay in product delivery or other interruption or variation in supply from these suppliers could prevent us from meeting commercial demand for our products. If we were to lose key suppliers, our key suppliers were unable to support our demand for any reason, or we were unable to identify and qualify alternative suppliers, our manufacturing operations could be interrupted or hampered significantly.

We rely on arrangements with independent shipping companies for the delivery of our products from vendors and to customers in both the United States and abroad. The failure or inability of these shipping companies to deliver products, or the unavailability of their shipping services, even temporarily, could have a material adverse effect on our business. We may also be adversely affected by an increase in freight surcharges due to rising fuel costs and added security.

In our fabrication process we consume a number of precious metals and other commodities, which are subject to high price volatility. Our operating margins could be significantly affected if we are not able to pass along price increases to our customers. In addition, production could be disrupted by the unavailability of the resources used in production such as water, silicon, electricity and gases. Future environmental regulations could restrict supply or increase the cost of certain of those materials.

We operate in an industry that is subject to significant fluctuation in supply and demand that affects our revenue and profitability.

The LED lighting industry is in the early stages of adoption and is characterized by constant and rapid technological change, rapid product obsolescence and price erosion, evolving standards, short product life-cycles and fluctuations in product supply and demand. The industry has experienced significant fluctuations, often in connection with, or in anticipation of, product cycles and changes in general economic conditions. These fluctuations have been characterized by lower product demand, production overcapacity, higher inventory levels and increased pricing pressure. We have experienced these conditions in our business in the past and may experience such conditions in the future, which could have a material negative impact on our business and results of operations.

In addition, as we diversify our product offerings and as pricing differences in the average selling prices among our product lines widen, a change in the mix of sales among our product lines may increase volatility in our revenue and gross margin from period to period.

We depend on a limited number of customers, including distributors, for a substantial portion of our revenues, and the loss of, or a significant reduction in purchases by, one or more of these customers could adversely affect our operating results.

We receive a significant amount of our revenues from a limited number of customers, including distributors who represented our two largest customers in fiscal 2012. Most of our customer orders are made on a purchase order basis, which does not generally require any long-term customer commitments. Therefore, these customers may alter their past purchasing behavior with little or no notice to us for various reasons, including: developing, or, in the case of our distributors, their customers developing, their own product solutions; choosing to purchase product from our competitors; incorrectly forecasting end market demand for their products; or experiencing a reduction in their market share in the markets for which they purchase our products. If our customers alter their past (or expected) purchasing behavior, or if we encounter any problems collecting amounts due from them, our financial condition and results of operations could be negatively impacted.

As a result of our continued expansion into new markets existing customers may reduce orders.

Through acquisitions and organic growth, including our acquisition of Ruud Lighting, we continue to expand into new markets. Many of our existing customers who purchase our LED products develop and manufacture products using those chips and components that are offered into the same lighting markets. As a result, some of our current customers perceive us as a competitor in these new markets. In response, our customers may reduce or discontinue their orders for our LED products. This reduction in or discontinuation of orders could occur faster than our sales growth in these new markets, which could adversely affect our business, results of operations or financial condition.

Our results of operations, financial condition and business could be harmed if we are unable to balance customer demand and capacity.

As customer demand for our products changes, we must be able to ramp up or adjust our production capacity to meet demand. We are continually taking steps to address our manufacturing capacity needs for our products. For example, in November of 2011, we broke ground on a 208,000 square foot expansion to our Wisconsin manufacturing and warehouse facilities to support our LED lighting products and we are targeting to continue expanding our LED product manufacturing facilities in China. If we are not able to increase our production capacity at our targeted rate, or if there are unforeseen costs associated with adjusting our capacity levels, we may not be able to achieve our financial targets.

Conversely, due to the proportionately high fixed cost nature of our business (such as facility expansion costs), if demand does not increase at the rate forecasted, we may not be able to manage manufacturing expenses or overhead costs at the same rate as demand. This could result in lower margins and adversely impact our business and results of operations. Additionally, if product demand decreases or we fail to forecast demand accurately, we may be required to recognize impairments on our long-lived assets or recognize excess inventory write off charges. We have in the past and may in the future be required to recognize excess capacity charges, which would have a negative impact on our results of operations.

In addition, our efforts to improve quoted delivery lead-time performance may result in corresponding reductions in order backlog. A decline in backlog levels could result in more variability and less predictability in our quarter-to-quarter net sales and operating results.

If we fail to evaluate and execute strategic opportunities successfully, our business may suffer.

From time to time, we evaluate strategic opportunities available to us for product, technology or business transactions, such as business acquisitions or divestitures. For example, we acquired Ruud Lighting in August 2011. If we choose to enter into such transactions, we face certain risks, such as the failure of an acquired business to meet our performance expectations, diversion of management attention, identification of additional liabilities relating to the acquired business, retention of existing customers of our current and acquired businesses due to concerns that new product lines may be in competition with the customers of existing product lines or otherwise, and difficulty integrating an acquired business's operations, personnel and financial and operating systems into our current business.

We may not be able to adequately address these risks or any other problems that arise from our recent or future acquisitions or divestitures. Any failure to successfully evaluate strategic opportunities and address risks or other problems that arise related to any such business transaction could adversely affect our business, results of operations or financial condition.

Our LED and Power and RF revenues are highly dependent on our customers' ability to produce, market and sell more integrated products.

Our LED and Power and RF revenues depend on getting our products designed into a larger number of our customers' products and in turn, our customers' ability to produce, market and sell their products. For example, we have current and prospective customers that create, or plan to create, lighting systems using our LED components. However, the traditional lighting industry is still developing technical expertise with LED-related designs, which may limit the success of our customers' products. Even if our customers are able to develop and produce LED lighting products and products that incorporate our Power and RF products, there can be no assurance that our customers will be successful in marketing and selling these products in the marketplace.

We also have current and prospective customers that create white LED components using our blue LEDs, in combination with phosphors. Sales of blue LED chips are highly dependent upon our customers' ability to procure efficient phosphors, develop high quality and highly efficient white LED components and gain access to the necessary intellectual property rights. Even if our customers are able to develop competitive white LED components using our blue LED chips, there can be no assurance that our customers will be successful in the marketplace.

The adoption of or changes in government and/or industry policies, standards or regulations relating to the efficiency, performance or other aspects of LED lighting or changes in government and/or industry policies, standards or regulations that discourage the use of certain traditional lighting technologies, could impact the demand for our LED products.

The adoption of or changes in government and/or industry policies, standards or regulations relating to the efficiency, performance or other aspects of LED lighting may impact the demand for our LED products. For example, in 2010 the Chinese government delayed purchases of LED street and tunnel lighting while developing new standards for the required performance for such lighting products in China. The process resulted in reduced demand for those lighting applications and has continued to limit our ability to forecast demand for those applications.

Demand for our LED products may also be impacted by changes in government and/or industry policies, standards or regulations that discourage the use of certain traditional lighting technologies. These constraints may be eliminated or delayed by legislative action, which could have a negative impact on demand for our products.

If governments, their agencies or regulated utilities reduce their demand for our products or discontinue or curtail their funding, our business may suffer.

Changes in governmental budget priorities could adversely affect our business and results of operations. U.S. and foreign government agencies have purchased products directly from us and products from our customers, and U.S. government agencies have historically funded a portion of our research and development activities. When the government changes budget priorities, such as in times of war or financial crisis, our research and development funding and our product sales to government entities are at risk. For example, demand and payment for our products and our customers' products may be affected by public sector budgetary cycles, funding authorizations, or utility rebates. Funding reductions or delays could negatively impact demand for our products. If government funding is discontinued or significantly reduced, our business and results of operations could be adversely affected.

Variations in our production yields could impact our ability to reduce costs and could cause our margins to decline and our operating results to suffer.

All of our products are manufactured using technologies that are highly complex. The number of usable items, or yield, from our production processes may fluctuate as a result of many factors, including but not limited to the following:

- variability in our process repeatability and control;
- contamination of the manufacturing environment;
- equipment failure, power outages, system failures or variations in the manufacturing process;
- lack of consistency and adequate quality and quantity of piece parts and other raw materials, and other bill of materials items;
- inventory shrinkage or human errors;
- defects in production processes (including system assembly) either within our facilities or at our contractors; and
- any transitions or changes in our production process, planned or unplanned.

In the past, we have experienced difficulties in achieving acceptable yields on certain products, which has adversely affected our operating results. We may experience similar problems in the future, and we cannot predict when they may occur or their severity.

In addition, our ability to convert volume manufacturing to larger diameter substrates can be an important factor in allowing for a more cost effective manufacturing process. If we are unable to make this transition in a timely or cost effective manner, our results could be negatively impacted.

In some instances, we may offer products for future delivery at prices based on planned yield improvements or increased cost efficiencies from other production advances. Failure to achieve these planned improvements or advances could significantly affect our margins and operating results.

Catastrophic events may disrupt our business.

A disruption or failure of our systems or operations in the event of a natural disaster, health pandemic, such as an influenza outbreak within our workforce, or man-made catastrophic event could cause delays in completing sales, continuing production or performing other critical functions of our business, particularly if a catastrophic event occurred at our primary manufacturing locations in the U.S. and China. This could severely affect our ability to conduct normal business operations and, as a result, our operating results could be adversely affected. There may also be secondary impacts that are unforeseeable as well, such as impacts to our customers, which could cause delays in new orders, delays in completing sales or even order cancellations.

If our products fail to perform or fail to meet customer requirements or expectations, we could incur significant additional costs, including costs associated with the recall of those items.

The manufacture of our products involves highly complex processes. Our customers specify quality, performance and reliability standards that we must meet. If our products do not meet these standards, we may be required to replace or rework the products. In some cases, our products may contain undetected defects or flaws that only become evident after shipment. Even if our products meet standard specifications, our customers may attempt to use our products in applications they were not designed for or in products that were not designed or manufactured properly, resulting in product failures and creating customer satisfaction issues.

We have experienced product quality, performance or reliability problems from time to time and defects or failures may occur in the future. If failures or defects occur, we may need to recall our products. These recalls could result in significant losses due to:

- costs associated with the removal, collection and destruction of the product recalled;
- payments made to replace recalled product;
- the write down or destruction of existing inventory subject to the recall;
- lost sales due to the unavailability of product for a period of time;
- delays, cancellations or rescheduling of orders for our products; or
- increased product returns.

We also may be the target of product liability lawsuits, and could suffer losses from a significant product liability judgment against us if the use of our products at issue is determined to have caused injury.

We provide warranty periods ranging from ninety days to ten years on our products. The standard warranty on nearly all of our new commercial LED lighting products, which represent an increasing portion of our sales, is ten years. We may experience an increase in warranty claims as a result of the extension of the warranty period. Increased warranty claims could result in significant losses due to a rise in warranty expense and costs associated with customer support.

A significant product recall or product liability case, or a significant increase in warranty claims, could also result in adverse publicity, damage to our reputation, and a loss of customer confidence in our products.

Our operations in foreign countries expose us to certain risks inherent in doing business internationally, which may adversely affect our business, results of operations or financial condition.

As a result of acquisitions and organic growth, we have operations, manufacturing facilities and contract manufacturing arrangements in foreign countries that expose us to certain risks. For example, fluctuations in exchange rates may affect our revenues, expenses and results of operations as well as the value of our assets and liabilities as reflected in our financial statements. We are also subject to other types of risks, including the following:

- protection of intellectual property and trade secrets;
- tariffs, customs and other barriers to importing/exporting materials and products in a cost effective and timely manner;
- timing and availability of export licenses;
- rising labor costs;
- disruptions in or inadequate infrastructure of the countries where we operate;
- difficulties in accounts receivable collections;
- difficulties in staffing and managing international operations;
- the burden of complying with foreign and international laws and treaties; and
- the burden of complying with and changes in international taxation policies.

In some instances, we have been provided and may continue to receive competing incentives from foreign governments to encourage our investment in certain countries, regions, or areas outside of the United States. In particular, we have received and may continue to receive such incentives in connection with our operations in Asia, as Asian national and local governments seek to encourage the development of the technology industry. Government incentives may include tax rebates, reduced tax rates, favorable lending policies and other measures, some or all of which may be available to us due to our foreign operations. Any of these incentives could be reduced or eliminated by governmental authorities at any time. Any reduction or elimination of incentives currently provided to our operations could adversely affect our business and results of operations. These same governments also may provide increased incentives to or require production processes that favor local companies, which could further negatively impact our business and results of operations.

Abrupt political change, terrorist activity and armed conflict pose a risk of general economic disruption in affected countries, which could also result in an adverse effect on our business and results of operations.

Litigation could adversely affect our operating results and financial condition.

We are often involved in litigation, primarily patent litigation, as described in more detail in Note 12, "Commitments and Contingencies" to our consolidated financial statements included in "Item 8, Financial Statements and Supplementary Data" of our Annual Report on Form 10-K for fiscal 2012. Defending against existing and potential litigation will likely require significant attention and resources and, regardless of the outcome, result in significant legal expenses, which could adversely affect our results unless covered by insurance or recovered from third parties. If our defenses are ultimately unsuccessful, or if we are unable to achieve a favorable resolution, we could be liable for damage awards that could materially affect our results of operations and financial condition.

Where necessary, we may initiate litigation to enforce our patent or other intellectual property rights. Any such litigation may require us to spend a substantial amount of time and money and could distract management from our day-to-day operations. Moreover, there is no assurance that we will be successful in any such litigation.

Our business may be impaired by claims that we, or our customers, infringe the intellectual property rights of others.

Vigorous protection and pursuit of intellectual property rights characterize our industry. These traits have resulted in significant and often protracted and expensive litigation. Litigation to determine the validity of patents or claims by third parties of infringement of patents or other intellectual property rights could result in significant legal expense and divert the efforts of our technical personnel and management, even if the litigation results in a determination favorable to us. In the event of an adverse result in such litigation, we could be required to:

- pay substantial damages;
- indemnify our customers;
- stop the manufacture, use and sale of products found to be infringing;

- incur asset impairment charges;
- discontinue the use of processes found to be infringing;
- expend significant resources to develop non-infringing products or processes; or
- obtain a license to use third party technology.

There can be no assurance that third parties will not attempt to assert infringement claims against us, or our customers, with respect to our products. In addition, our customers may face infringement claims directed to the customer's products that incorporate our products, and an adverse result could impair the customer's demand for our products. We have also promised certain of our customers that we will indemnify them in the event they are sued by our competitors for infringement claims directed to the products we supply. Under these indemnification obligations, we may be responsible for future payments to resolve infringement claims against them.

From time to time, we receive correspondence asserting that our products or processes are or may be infringing patents or other intellectual property rights of others. If we believe the assertions may have merit or in other appropriate circumstances, we take steps to seek to obtain a license or to avoid the infringement. However, we cannot predict whether a license will be available; that we would find the terms of any license offered acceptable; or that we would be able to develop an alternative solution. Failure to obtain a necessary license or develop an alternative solution could cause us to incur substantial liabilities and costs and to suspend the manufacture of affected products.

There are limitations on our ability to protect our intellectual property.

Our intellectual property position is based in part on patents owned by us and patents licensed to us. We intend to continue to file patent applications in the future, where appropriate, and to pursue such applications with U.S. and foreign patent authorities.

However, our existing patents are subject to expiration and re-examination and we cannot be sure that additional patents will be issued on any new applications around the covered technology or that our existing or future patents will not be successfully contested by third parties. Also, since issuance of a valid patent does not prevent other companies from using alternative, non-infringing technology, we cannot be sure that any of our patents, or patents issued to others and licensed to us, will provide significant commercial protection, especially as new competitors enter the market.

We periodically discover products that are counterfeit reproductions of our products or that otherwise infringe on our intellectual property rights. The actions we take to establish and protect trademarks, patents, and other intellectual property rights may not be adequate to prevent imitation of our products by others, and therefore, may adversely affect our sales and our brand and result in the shift of customer preference away from our products. Further, the actions we take to establish and protect trademarks, patents and other intellectual property rights could result in significant legal expense and divert the efforts of our technical personnel and management, even if the litigation or other action results in a determination favorable to us.

We also rely on trade secrets and other non-patented proprietary information relating to our product development and manufacturing activities. We try to protect this information through appropriate efforts to maintain its secrecy, including requiring employees and third parties to sign confidentiality agreements. We cannot be sure that these efforts will be successful or that the confidentiality agreements will not be breached. We also cannot be sure that we would have adequate remedies for any breach of such agreements or other misappropriation of our trade secrets, or that our trade secrets and proprietary know-how will not otherwise become known or be independently discovered by others.

We may be required to record a significant charge to earnings if our goodwill or other intangible assets become impaired.

Goodwill and purchased intangible assets with indefinite lives are not amortized, but are reviewed for impairment annually and more frequently when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. We assess the recoverability of the unamortized balance of our definite-lived intangible assets when indicators of potential impairment are present. Factors that may indicate that the carrying value of our goodwill or other intangible assets may not be recoverable include a decline in stock price and market capitalization and slower growth rates in our industry. We may be required to recognize a significant charge to earnings in our consolidated financial statements during the period in which any impairment of our goodwill or other intangible assets is determined to exist, which could adversely impact our results of operations.

We may be subject to intellectual property theft or misuse, which could harm our business and results of operations.

We face attempts by others to gain unauthorized access to our information technology systems on which we maintain proprietary and other confidential information. Our security measures may be breached as the result of industrial or other espionage actions of outside parties, employee error, malfeasance, or otherwise, and, as a result, an unauthorized party may obtain access to our systems. Additionally, outside parties may attempt to fraudulently induce employees to disclose sensitive information in order to gain access to our systems. We actively seek to prevent, detect and investigate any unauthorized access, which sometimes occurs. We might be unaware of any such access or unable to determine its magnitude and effects. The theft and/or unauthorized use or publication of our trade secrets and other confidential business information as a result of such an incident could adversely affect our competitive position and the value of our investment in research and development could be reduced. Our business could be subject to significant disruption, and we could suffer monetary or other losses.

We are subject to risks related to international sales and purchases.

We expect that revenue from international sales will continue to represent the majority of our total revenue. As such, a significant slowdown or instability in these foreign economies, including the recent economic instability in Europe, or lower investments in new infrastructure could have a negative impact on our sales. We also purchase a portion of the materials included in our products from overseas sources.

Our international sales and purchases are subject to numerous U.S. and foreign laws and regulations, including, without limitation, tariffs, trade barriers, regulations relating to import-export control, technology transfer restrictions, the International Traffic in Arms Regulation promulgated under the Arms Export Control Act, the Foreign Corrupt Practices Act and the anti-boycott provisions of the U.S. Export Administration Act. If we fail to comply with these laws and regulations, we could be liable for administrative, civil or criminal liabilities, and in the extreme case, we could be suspended or debarred from government contracts or have our export privileges suspended, which could have a material adverse effect on our business.

International sales and purchases are also subject to a variety of other risks, including risks arising from currency fluctuations, collection issues and taxes. Our international sales are subject to variability as our selling prices become less competitive in countries with currencies that are declining in value against the U.S. Dollar and more competitive in countries with currencies that are increasing in value against the U.S. Dollar. In addition, our international purchases can become more expensive if the U.S. Dollar weakens against the foreign currencies in which we are billed.

We have not entered into any foreign currency derivative financial instruments; however, we may choose to do so in the future in an effort to manage or hedge our foreign exchange rate risk.

Our business may be adversely affected by uncertainties in the global financial markets and our or our customers' or suppliers' ability to access the capital markets.

Global financial markets continue to reflect uncertainty about a sustained global economic recovery. Given these uncertainties, there could be future disruptions in the global economy, financial markets and consumer confidence. If economic conditions deteriorate unexpectedly, our business and results of operations could be materially and adversely affected. For example, our customers, including our distributors and their customers, may experience difficulty obtaining the financing necessary to support historical or projected purchasing patterns, which could negatively affect our results of operations.

Although we believe we have adequate liquidity and capital resources to fund our operations internally, our inability to access the capital markets on favorable terms in the future, or at all, may adversely affect our financial performance. The inability to obtain adequate financing from debt or capital sources in the future could force us to self-fund strategic initiatives or even forego certain opportunities, which in turn could potentially harm our performance.

New regulations related to conflict-free minerals may force us to incur additional expenses.

The Dodd-Frank Wall Street Reform and Consumer Protection Act contains provisions to improve transparency and accountability concerning the supply of minerals originating from the conflict zones of the Democratic Republic of Congo (DRC) and adjoining countries. As a result, in August 2012 the SEC established new annual disclosure and reporting requirements for those companies who use “conflict” minerals mined from the DRC and adjoining countries in their products. These new requirements will require due diligence efforts for the 2013 calendar year, with initial disclosure requirements beginning in May 2014. These new requirements could affect the sourcing and availability of minerals used in the manufacture of our products. As a result, we may not be able to obtain minerals at competitive prices and there will likely be additional costs associated with complying with the new due diligence procedures as required by the SEC. In addition, as our supply chain is complex, we may face reputational challenges with our customers and other stakeholders if we are unable to sufficiently verify the origins of all minerals used in our products through the due diligence procedures that we implement, and we may incur additional costs as a result of changes to product, processes or sources of supply as a consequence of these new requirements.

Changes in our effective tax rate may affect our results.

Our future effective tax rates may be affected by a number of factors including:

- the jurisdiction in which profits are determined to be earned and taxed;
- changes in government administrations, such as the Presidency and Congress of the U.S. as well as in the states and countries in which we operate;
- changes in tax laws or interpretation of such tax laws and changes in generally accepted accounting principles;
- the resolution of issues arising from tax audits with various authorities;
- changes in the valuation of our deferred tax assets and liabilities;
- adjustments to estimated taxes upon finalization of various tax returns;
- increases in expenses not deductible for tax purposes, including write-offs of acquired in-process research and development and impairment of goodwill in connection with acquisitions;
- changes in available tax credits;
- the recognition and measurement of uncertain tax positions;
- the lack of sufficient excess tax benefits (credits) in our additional paid in capital pool in situations where our realized tax deductions for certain stock-based compensation awards (such as non-qualified stock options and restricted stock) are less than those originally anticipated; and
- the repatriation of non-U.S. earnings for which we have not previously provided for U.S. taxes, or any changes in legislation that may result in these earnings being taxed within the U.S., regardless of our decision regarding repatriation of funds.

For example, proposals have been made by various U.S. governmental bodies to change the U.S. tax laws that include, among other things, limiting U.S. tax deductions for expenses related to un-repatriated foreign-source income and modifying the U.S. foreign tax credit rules. Although the scope of the proposed changes is unclear, it is possible that these or other changes in U.S. tax laws could increase our U.S. income tax liability and adversely affect our profitability. At this time, we cannot determine the timing that the proposed changes, if enacted, would become effective.

Any significant increase or decrease in our future effective tax rates could impact net income for future periods. In addition, the determination of our income tax provision requires complex estimations, significant judgments and significant knowledge and experience concerning the applicable tax laws. To the extent our income tax liability materially differs from our income tax provisions due to factors, including the above, which were not anticipated at the time we estimated our tax provision, our net income or cash flows could be affected.

In order to compete, we must attract, motivate and retain key employees, and our failure to do so could harm our results of operations.

Hiring and retaining qualified executives, scientists, engineers, technical staff and sales personnel is critical to our business, and competition for experienced employees in our industry can be intense. As a global company, this issue is not limited to the United States, but includes our other locations such as Europe and China. For example, there is substantial competition in China for qualified and capable personnel, particularly experienced engineers and technical personnel, which may make it difficult for us to recruit and retain qualified employees. Also, within Huizhou, China, there are other large companies building manufacturing plants that will likely attract qualified employees. If we are unable to staff sufficient and adequate personnel at our China facilities, we may experience lower revenues or increased manufacturing costs, which would adversely affect our results of operations.

To help attract, motivate and retain key employees, we use benefits such as stock-based compensation awards, which include non-qualified stock options and restricted stock. If the value of such stock awards does not appreciate, as measured by the performance of the price of our common stock, or if our share-based compensation otherwise ceases to be viewed as a valuable benefit, our ability to attract, retain and motivate employees could be weakened, which could harm our business and results of operations.

Failure to comply with applicable environmental laws and regulations worldwide could harm our business and results of operations.

The manufacturing, assembling and testing of our products require the use of hazardous materials that are subject to a broad array of environmental, health and safety laws and regulations. Our failure to comply with any of these applicable laws or regulations could result in:

- regulatory penalties, fines, legal liabilities, and the forfeiture of certain tax benefits;
- suspension of production;
- alteration of our fabrication, assembly and test processes; and
- curtailment of our operations or sales.

In addition, our failure to manage the use, transportation, emission, discharge, storage, recycling or disposal of hazardous materials could subject us to increased costs or future liabilities. Existing and future environmental laws and regulations could also require us to acquire pollution abatement or remediation equipment, modify our product designs or incur other expenses, such as permit costs, associated with such laws and regulations. Many new materials that we are evaluating for use in our operations may be subject to regulation under existing or future environmental laws and regulations that may restrict our use of one or more of such materials in our manufacturing, assembly and test processes or products. Any of these restrictions could harm our business and results of operations by increasing our expenses or requiring us to alter our manufacturing processes.

Our results could vary as a result of the methods, estimates and judgments that we use in applying our accounting policies, including changes in the accounting regulations to be applied.

The methods, estimates and judgments that we use in applying our accounting policies have a significant impact on our results (see “Critical Accounting Policies and Estimates” in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our Annual Report on Form 10-K for fiscal 2012). Such methods, estimates and judgments are, by their nature, subject to substantial risks, uncertainties and assumptions, and factors may arise over time that lead us to change our methods, estimates and judgments. Changes in those methods, estimates and judgments could significantly affect our results.

Likewise, our results may be impacted due to changes in the accounting standards to be applied, such as the increased use of fair value measurement standards, proposed changes in revenue recognition requirements, and the potential requirement that U.S. registrants prepare financial statements in accordance with International Financial Reporting Standards.

We are exposed to fluctuations in the market value of our investment portfolio and in interest rates, and therefore, impairment of our investments or lower investment income could harm our earnings.

We are exposed to market value and inherent interest rate risk related to our investment portfolio. We have historically invested portions of our available cash in fixed interest rate securities such as high-grade corporate debt, commercial paper, government securities and other fixed interest rate investments. The primary objective of our investment policy is preservation of principal. However, our investments are generally not FDIC insured and may lose value and/or become illiquid regardless of their credit rating.

Our stock price may be volatile.

Historically, our common stock has experienced substantial price volatility, particularly as a result of significant fluctuations in our revenue, earnings and margins over the past few years, and variations between our actual financial results and the published expectations of analysts. For example, the closing price per share of our common stock on the NASDAQ Global Select Market ranged from a low of \$20.32 to a high of \$37.11 in fiscal 2012. If our future operating results or margins are below the expectations of stock market analysts or our investors, our stock price will likely decline.

Speculation in the press or investment community about our strategic position, financial condition, results of operations, or significant transactions can also cause changes in our stock price. In particular, speculation around our market opportunities for energy efficient lighting may have a dramatic effect on our stock price, especially as various government agencies announce their planned investments in energy efficient technology, including lighting.

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

There were no sales of unregistered securities during the first quarter of fiscal 2013. The following table summarizes our stock repurchase activity for the first quarter of fiscal 2013 (in thousands, except per share data):

Period	Total number of shares purchased ⁽¹⁾	Average price paid per share	Total number of shares purchased as a part of publicly announced program	Maximum dollar value of shares that may yet be purchased under the program ⁽²⁾
June 25 - July 22, 2012	—	\$ —	—	200,000
July 23 - August 19, 2012	—	—	—	200,000
August 20 - September 23, 2012	46	28.2	—	200,000
Total	46		—	

(1) Represents shares repurchased to satisfy tax withholding obligations that arose on the vesting of shares of restricted stock.

(2) On January 18, 2001, we announced the authorization by our Board of Directors of a program to repurchase shares of our outstanding common stock. Several times since then, the Board of Directors has renewed the program and increased the number of shares that can be repurchased under the program. As of September 23, 2012, we are authorized by the Board of Directors to repurchase shares of our common stock having an aggregate purchase price not exceeding \$200 million for all purchases from June 14, 2012 through the June 30, 2013 expiration of the program. During the three months ended September 23, 2012, we repurchased zero shares of common stock under the repurchase program.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

The following exhibits are being filed herewith and are numbered in accordance with Item 601 of Regulation S-K:

Exhibit No.	Description
10.1	Management Incentive Compensation Plan, as amended and restated (incorporated herein by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, dated August 13, 2012, as filed with the Securities and Exchange Commission on August 17, 2012)
10.2	Notice of Grant to Charles M. Swoboda, dated August 13, 2012 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, dated August 13, 2012, as filed with the Securities and Exchange Commission on August 17, 2012)
10.3	Form of Nonqualified Stock Option Award Agreement for Non-Employee Directors
10.4	Form of Nonqualified Stock Option Award Agreement
10.5	Form of Restricted Stock Award Agreement
31.1	Certification by Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification by Interim Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification by Interim Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following materials from Cree Inc.'s Quarterly Report on Form 10-Q for the fiscal quarter ended September 23, 2012 formatted in XBRL (eXtensible Business Reporting Language) and furnished electronically herewith: (i) Consolidated Balance Sheets; (ii) Consolidated Statements of Income; (iii) Consolidated Statements of Comprehensive Income; (iv) Consolidated Statements of Cash Flows; and (v) Notes to Consolidated Financial Statements ^(a)

(a) Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files in Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

SIGNATURE

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.

CREE, INC.

October 17, 2012

/s/ MICHAEL E. MCDEVITT

Michael E. McDevitt

Vice President and Interim Chief Financial Officer

(Authorized Officer and Principal Financial and Chief Accounting Officer)

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**NONQUALIFIED STOCK OPTION
AWARD AGREEMENT
(for Non-Employee Directors)**



Participant: _____
Award Number: _____
Plan: 2004 Long-Term Incentive Compensation Plan
Award Type: Nonqualified Stock Option
Grant Date: _____
Number Shares: _____
Exercise Price: _____
Expiration Date: 11:59 p.m. local time in Durham, NC on the 7th anniversary of the Grant

Cree, Inc. (the "Company") has awarded you a nonqualified stock option (the "Option") to purchase _____ shares (the "Shares") of the common stock of the Company at a purchase price of ___ per share, effective _____, the Grant Date of the award. The Option is subject to and governed by the Cree, Inc. 2004 Long-Term Incentive Compensation Plan (the "Plan") and the terms of this Nonqualified Stock Option Award Agreement (the "Agreement").

You may exercise the Option to purchase up to the number of Shares for which it has vested unless and until the Option expires or is earlier terminated. In accordance with this Agreement and the Plan, upon any Termination of Service (as defined in this Agreement), the Option will be forfeited as to all Shares not then vested and will terminate thereafter as to vested Shares. If not previously terminated or expired, the Option will vest on _____, provided that on the indicated vesting date you are an employee of the Company or another Employer under the Plan or serving as a member of the Board of Directors of the Company, and further provided that all options not then vested shall vest on the date of the _____ Annual Meeting of Shareholders of the Company.

Capitalized terms defined in the Plan and used in this Agreement without definition have the meaning specified in the Plan. THE TERMS AND CONDITIONS ON THE PAGES FOLLOWING THIS SIGNATURE PAGE, INCLUDING THE APPENDIX, ARE AN INTEGRAL PART OF THIS AGREEMENT AND ARE INCORPORATED HEREIN BY THIS REFERENCE. BY SIGNING BELOW YOU ACKNOWLEDGE THAT YOU HAVE READ, UNDERSTAND AND AGREE TO BE BOUND BY SUCH TERMS AND CONDITIONS. FAILURE TO SIGN WILL RESULT IN FORFEITURE OF THE AWARD.

Dated: _____

FOR CREE, INC.: ACCEPTED AND AGREED:

/s/ CHARLES M. SWOBODA

Charles M. Swoboda, Chairman, President
and Chief Executive Officer

TERMS AND CONDITIONS

1. **Grant of Option.** Subject to the terms of the Plan and this Agreement, the Company hereby grants you an Option as set forth on the first page of this Agreement.

2. **Term of Options.** Unless sooner terminated in accordance with the Plan or this Agreement the Option will expire and cease to be exercisable upon the first to occur of the following:

(a) the later of the expiration of (i) one (1) year following your Termination of Service as a member of the Board, whether or not you become an employee of the Company or any other Employer prior to or upon terminating service as a member of the Board, or (ii) the ninety (90) calendar days following your Termination of Service, provided that at the time of such termination you were a regular full-time employee of the Company or any other Employer or a regular part-time employee of the Company or any other Employer scheduled to work a minimum of 30 hours per week, except where the termination in either scenario results from your death or Disability or where your death occurs following the termination but while the Option is otherwise still exercisable;

(b) the expiration of one (1) year following your Termination of Service if the termination results from your death;

(c) the expiration of one (1) year following your Termination of Service if the termination results from your Disability, except where your death occurs after the termination but while the Option is otherwise still exercisable;

(d) the expiration of one (1) year following your death if your death occurs after your Termination of Service but while the Option is otherwise still exercisable; or

(e) the seventh (7th) anniversary of the Grant Date of the Option, at 11:59 P.M., local time, Durham, North Carolina.

Upon expiration or termination of the Option, it will have no further effect and cannot thereafter be exercised to purchase any Shares.

3. **Vesting.** The Option will vest and become exercisable in accordance with the schedule set out on the first page of this Agreement and will become fully vested and exercisable to purchase all Shares subject to the Option, to the extent not already vested and exercisable, upon your Termination of Service on account of your death or Disability, unless otherwise provided in this Agreement or the Plan.

4. **Forfeiture upon Termination of Service.** Except as otherwise provided in this Agreement or the Plan, upon your Termination of Service, you will forfeit the Option with respect to any Shares as to which the Option has not vested as of the date of your Termination of Service.

5. **Exercise of Option.** To exercise the Option, you must complete, execute and deliver to the Company a notice of exercise in a form approved by the Company and pay to the Company the purchase price for the number of Shares specified in the notice together with all Tax-Related Items (as defined in Section 6 below) the Company is required to withhold, collect, or account for pursuant to this Agreement. Exercise of the Option will be effective only when the notice and required payments are actually received by the Company or upon your execution of a "broker-assisted exercise" or "cashless exercise" transaction with a broker approved by the Company. Furthermore, if the exercise is facilitated through a "broker-assisted exercise" or "cashless exercise" transaction by a brokerage firm you have designated, you agree that the brokerage firm is acting as your agent in the transaction and that the Company may rely upon notices, instructions and information given by such firm in connection with the exercise, as if the same were given by you. The Company will make the Shares available for electronic delivery in the U.S., and where allowed by applicable law outside the U.S., to an account you designate in writing, within three (3) business days after the Company receives the notice of exercise and required payments. In situations where electronic delivery is not available, the Company will deliver a certificate or certificates for the purchased Shares to you, or to such other person as you designate in writing.

6. **Responsibility for Taxes.**

(a) For purposes of this Agreement, "Tax-Related Items" means any or all income tax, social insurance tax, payroll tax, payment on account or other tax-related items that may be applicable this Award by law or regulation of any governmental authority, whether federal, state or local, domestic or foreign. Regardless of any action the Company takes with respect to withholding Tax-Related Items, you acknowledge that you are ultimately responsible for all Tax-Related Items and that such Tax-Related Items may exceed the amount actually withheld by the Company or the Employer. You further

acknowledge that the Company and/or the Employer (1) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the Option, including, without limitation, the grant, vesting or exercise of the Option, the subsequent sale of Shares acquired pursuant to such exercise and the receipt of any dividends or dividend equivalents pursuant to Shares; and (2) do not commit to and are under no obligation to structure the terms of the grant or any aspect of the Option to reduce or eliminate your liability for Tax-Related Items or to achieve any particular tax result. Furthermore, if you have become subject to tax in more than one jurisdiction between the Grant Date and the date of any relevant taxable event, you acknowledge that the Company and/or the Employer (or former Employer, as applicable) may be required to withhold or account for Tax-Related Items in more than one jurisdiction.

(b) Prior to any relevant taxable or tax withholding event, as applicable, you will pay or make adequate arrangements satisfactory to the Company and/or the Employer to satisfy all Tax-Related Items. In this regard, you authorize the Company and/or the Employer, or their respective agents, at their discretion, to satisfy the obligations with regard to all Tax-Related Items by one or a combination of the following: (1) withholding from your wages or other cash compensation paid to you by the Company and/or the Employer; or (2) withholding from proceeds of the sale of Shares acquired upon exercise of the Option; or (3) withholding in Shares to be issued upon exercise of the Option.

(c) Depending upon the withholding method, the Company or the Employer may withhold or account for Tax-Related Items by considering applicable minimum or maximum statutory withholding amounts or other applicable withholding rates. In the event Tax-Related Items are over-withheld, you will receive a refund in cash for any over-withheld amounts and will have no entitlement to the Shares equivalent. If the obligation for Tax-Related Items is satisfied by withholding of Shares, you shall be deemed, for tax purposes, to have been issued the full number of Shares subject to the exercised Option, notwithstanding that a number of Shares is held back solely for the purpose of paying the Tax-Related Items due as a result of any aspect of your participation in the Plan.

(d) You shall pay to the Company or the Employer any amount of Tax-Related Items that the Company or the Employer may be required to withhold or account for as a result of your participation in the Plan that cannot be satisfied by the means previously described. The Company may refuse to honor the exercise of the Option and refuse to deliver the Shares if you fail to comply with your obligations in connection with the Tax-Related Items.

7. *Transfer of Option.* Neither the Option nor any rights under the Option may be assigned, pledged as collateral or otherwise transferred, except as permitted by the Plan, nor may the Option or such rights be subject to attachment, execution or other judicial process. In the event of any attempt to assign, pledge or otherwise dispose of the Option or any rights under the Option, except as permitted by the Plan, or in the event of the levy of any attachment, execution or similar judicial process upon the rights or interests conferred by the Option, the Committee may in its discretion terminate the Option upon notice to you.

8. *Rights Prior to Exercise.* You will have no rights as a shareholder with respect to any Shares until such Shares have been duly issued by the Company or its transfer agent pursuant to exercise of the Option.

9. *Termination of Service.*

(a) Unless otherwise provided in this Agreement or the Plan, for purposes of this Agreement “Termination of Service” means the discontinuance of your relationship with the Company as an employee of the Company or the Employer or any subsidiary or affiliate of the Company under the Plan or as a member of the Board of Directors of Cree, Inc. Except as determined otherwise by the Committee, you will not be deemed to have incurred a Termination of Service if the capacity in which you provide services to the Company changes (for example, you change from being a non-employee director to being an employee) or if you transfer employment among the various subsidiaries or affiliates of the Company constituting the Employer, so long as there is no interruption in your provision of services to the Company or other Employer as an employee or as a non-employee member of the Board of Directors of Cree, Inc. The Committee, in its discretion, will determine whether you have incurred a Termination of Service. You will not be deemed to have incurred a Termination of Service during a period for which you are on military leave, sick leave, or other leave of absence approved by the Employer.

(b) If you are deemed to have incurred a Termination of Service other than a Termination of Service on account of your death or Disability, your right to vest in the Option under this Agreement of the Plan, if any, will terminate and any post-termination exercise period will commence effective as of the date that you are no longer actively providing services to the Company or one of its subsidiaries or affiliates (regardless of the reason for the termination and whether or not later found to be invalid or in breach of employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any), and will not be extended by any notice period mandated under local law (e.g., active employment would not include a period of “garden leave” or similar period mandated under the employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any); the Committee, in its discretion, will determine when you are

no longer actively providing services for purposes of the Option grant (including whether you may still be considered to be providing services while on a leave of absence).

10. Provisions of the Plan. The provisions of the Plan are incorporated by reference in this Agreement as if set out in full in this Agreement. To the extent that any conflict may exist between any other provision of this Agreement and a provision of the Plan, the Plan provision will control. All decisions of the Committee with respect to the interpretation, construction and application of the Plan or this Agreement shall be final, conclusive and binding upon you and the Company.

11. Detrimental Activity. The Committee in its sole discretion may cancel, terminate, suspend or otherwise limit or restrict exercise of the unexercised portion of the Option if you engage in any "Detrimental Activity" (as defined below). In addition, if you engage in any Detrimental Activity prior to or within one (1) year after your Termination of Service, the Committee in its sole discretion may require you to pay to the Company the amount of all gain you realized from any exercise of the Option beginning six (6) months prior to your Termination of Service, provided that the Committee gives you notice of such requirement within one (1) year after your Termination of Service. In that event, the Company will be entitled to setoff such amount against any amount the Company owes to you, in addition to any other rights the Company may have. For purposes of this section:

(a) "Company" includes Cree, Inc. and all other Employers under the Plan.

(b) "Detrimental Activity" means any of the following conduct, as determined by the Committee in good faith:

(1) the performance of services for any Competing Business (as defined below), whether as an employee, officer, director, consultant, agent, contractor or in any other capacity, except to the extent expressly permitted by any written agreement between you and the Company;

(2) the unauthorized disclosure or use of any trade secrets or other confidential information of the Company;

(3) any attempt to induce an employee to leave employment with the Company to perform services elsewhere, or any attempt to cause a customer or supplier of the Company to curtail or cancel its business with the Company;

(4) breach of any confidentiality, noncompetition, nonsolicitation or nondisparagement obligations, or any obligations relating to the disclosure, assignment or protection of inventions, undertaken by you in any written agreement between you and the Company; or

(5) any act of fraud, misappropriation, embezzlement, or tortious or criminal behavior that adversely impacts the Company.

(c) "Competing Business" means any corporation, partnership, university, government agency or other entity or person (other than the Company) that is conducting research directed to, developing, manufacturing, marketing, distributing, or selling any product, service, or technology that is competitive with any part of the Company's Business (as defined below). "Company's Business" means the development, manufacture, marketing, distribution, or sale of, or the conduct of research directed to, any product, service, or technology that the Company is developing, manufacturing, marketing, distributing, selling, or conducting research directed to, at any time during your employment or other relationship with the Company, except that following your Termination of Service the Company's Business will be determined as of the time of such termination. As of the effective date of this Agreement, the Company's Business includes but is not limited to the conduct of research directed to, development, manufacture, marketing, distribution, and/or sale of the following products, services, and technologies: (1) silicon carbide (SiC) materials for electronic applications; (2) SiC materials for gemstone applications; (3) AlN nitride materials for electronic applications; (4) light-emitting diode (LED) devices and components; (5) power semiconductor devices made using SiC and/or AlN nitride materials and components incorporating such devices; (6) radio frequency (RF) and microwave devices made using SiC and/or AlN nitride materials and components and modules incorporating such devices; (7) LED backlights for liquid crystal displays (LCDs); (8) lighting products, modules, fixtures or devices incorporating any of the above materials or technology; and (9) other semiconductor devices made using SiC and/or AlN nitride materials and components incorporating such devices. You acknowledge that during your employment or other relationship with the Company the Company's Business may expand or change and you agree that any such expansions and changes shall expand or contract the definition of the Company's Business accordingly.

12. Data Privacy. You hereby explicitly and unambiguously consent to the collection, use and transfer, in electronic or other form, of your personal data as described in this Agreement and any other option grant materials ("Data") by and

among, as applicable, your Employer, the Company and its subsidiaries and affiliates, for the exclusive purpose of implementing, administering and managing your participation in the Plan.

You understand that the Employer holds or may hold certain personal information about you, including, but not limited to, your name, home address and telephone number, date of birth, social insurance number or other identification number, salary, nationality, position title, any shares of stock or directorships held in the Company, details of all options or any other entitlement to Shares awarded, canceled, exercised, vested, unvested or outstanding in your favor, for the purpose of implementing, administering and managing the Plan.

You understand that Data may be transferred to any third parties as may be selected by the Company currently or in the future, which are assisting the Company in the implementation, administration and management of the Plan. You understand that these recipients may be located in the United States or elsewhere, and that the recipient's country (e.g., the United States) may have different data privacy laws and protections than your country. You understand that you may request a list with the names and addresses of any potential recipients of the Data by contacting the Company's Stock Plan Administrator. You authorize the Company and any other possible recipients that may assist the Company (presently or in the future) with implementing, administering and managing the Plan to receive, possess, use, retain and transfer the Data, in electronic or other form, for the purposes of implementing, administering and managing your participation in the Plan, including any requisite transfer of such Data as may be required to a broker or other third party whom you subsequently may elect to deposit any Shares acquired under the Plan. You understand that Data will be held pursuant to this Agreement only as long as the Company considers it necessary to implement, administer and manage your participation in the Plan. You understand that you may, at any time, view Data, request additional information about the storage and processing of Data, require any necessary amendments to Data or refuse or withdraw the consents above, in any case without cost, by contacting in writing the Company's Stock Plan Administrator. Further, you understand that you are providing the consents herein on a purely voluntary basis. If you do not consent, your employment status or service and career with the Employer will not be adversely affected; the only adverse consequence of refusing or withdrawing consent is that the Company would not be able to grant you Options or receive any other equity awards or administer or maintain such awards. Therefore, you acknowledge, however, that refusing or withdrawing your consent may affect your ability to participate in the Plan. For more information on the consequences of your refusal to consent or withdrawal of consent, you may contact the Stock Plan Administrator of the Company.

13. Language. If you have received this Agreement or any other document related to the Plan translated into a language other than English and if the translated version differs in meaning from the English version, the English version will control.

14. Electronic Delivery. The Company may, in its sole discretion, deliver any documents related to current or future participation in the Plan by electronic means. You hereby consent to receive such documents by electronic delivery and agree to participate in the Plan through an on-line or electronic system established and maintained by the Company or another third party designated by the Company. Signed documents delivered to either party via facsimile or in portable document format will have the same effect as an original, unless otherwise required by applicable law.

15. General.

(a) Nothing in this Agreement will be construed as: (1) constituting a commitment, agreement or understanding of any kind that the Company or any other Employer will continue your employment or other relationship with the Company; or (2) limiting or restricting either party's right to terminate your employment or other relationship.

(b) This Agreement shall be binding upon and inure to the benefit of the parties and their respective successors and permitted assigns. You may not assign any rights under this Agreement without the written consent of the Company, which it may withhold in its sole discretion; any such attempted assignment without the Company's written consent shall be void. The Company may assign its rights under this Agreement at any time upon notice to you.

(c) Notices under this Agreement must be in writing and delivered either by hand or by a reputable domestic or international carrier (postage prepaid and return receipt or proof of delivery requested), and, in the case of notices to the Company, addressed to its principal executive offices to the attention of the Stock Plan Administrator, and, in your case, addressed to your address as shown on the Employer's records.

(d) This Agreement shall be governed by and construed in accordance with the laws of the State of North Carolina, without regard to the conflict of law provisions thereof, as if made and to be performed wholly within such State. For purposes of litigating any dispute that arises directly or indirectly from the relationship of the parties evidenced by the Option or this Agreement, the parties hereby submit to and consent to the exclusive jurisdiction of the State of North Carolina, agree

that such litigation shall be conducted in the courts of Durham County, North Carolina, or the federal courts for the United States for the Middle District of North Carolina, and no other courts, where the Option grant is made and/or to be performed.

(e) If any provision of this Agreement is held to be invalid or unenforceable, such determination shall not affect the other provisions of the Agreement and the Agreement shall be construed as if the invalid or unenforceable provision were omitted and a valid and enforceable provision, as nearly comparable as possible, substituted in its place.

(f) Notwithstanding any prior option award agreement between you and the Company under which options may have been awarded, this Agreement and the Plan set forth all of the promises, agreements and understandings between you and Company relating to the Option granted pursuant to this Agreement, constitutes the complete agreement between the parties regarding the Option, and replaces any prior oral or written communications regarding the same.

(g) Shares issued upon exercise of the Option may be subject to such stop transfer orders and other restrictions as the Committee may deem advisable under applicable law or the rules and regulations of the U.S. Securities and Exchange Commission or any stock exchange or trading system upon which the common stock of the Company is listed, and the Committee may cause a legend or legends to be placed on any such certificates or the stock records of the Company to make appropriate reference to such restrictions.

(h) You agree that the Option, even if later forfeited, serves as additional, valuable consideration for your obligations, if any, undertaken in any existing agreement between you and the Company and/or other Employer regarding confidential information, noncompetition, nonsolicitation or similar covenants.

(i) You acknowledge, represent and warrant to the Company, and agree with the Company, that (i) except for information provided in the Company's filings with the U.S. Securities and Exchange Commission and in the Company's current prospectus relating to the Plan, you have not relied and will not rely upon the Committee, the Company, an Employer or any employee or agent of the Company or an Employer in determining whether to accept or exercise the Option, or in connection with any disposition of Shares purchased upon exercise of the Option, or with respect to any tax consequences related to the grant or exercise of the Option or the disposition of Shares purchased pursuant to exercise of the Option, and (ii) you will seek from your own professional advisors such investment, tax and other advice as you believe necessary.

(j) You acknowledge that you may incur a substantial tax liability as a result of exercise of the Option. You assume full responsibility for all such consequences and the filing of all tax returns and related elections you may be required or find desirable to file. If you are required to make any valuation of the Option or Shares purchased pursuant to exercise of the Option under any federal, state or other applicable tax law, and if the valuation affects any tax return or election of the Company or the Employer or affects the Company's financial statement reporting, you agree that the Company may determine the value and that you will observe any determination so made by the Company in all tax returns and elections filed by you.

(k) You acknowledge that copies of the Plan and Plan prospectus are available upon written or telephonic request to the Company's Stock Plan Administrator.

16. Severability. The provisions of this Agreement are severable and if any one or more provisions is determined to be illegal or otherwise unenforceable, in whole or in part, the remaining provisions shall nevertheless be binding and enforceable.

17. Nature of Grant. In accepting this grant, you acknowledge, understand and agree that:

(a) the Plan is established voluntarily by the Company, is discretionary in nature and may be modified, amended, suspended or terminated by the Company at any time, unless expressly provided otherwise in the Plan or the Agreement;

(b) the grant of the Option is voluntary and does not create any contractual or other right to receive future grants of options, or benefits in lieu of options, even if options have been granted repeatedly in the past;

(c) all decisions with respect to future option grants, if any, will be at the sole discretion of the Company;

(d) your participation in the Plan is voluntary;

(e) your participation in the Plan will not create a right to employment with the Company or the Employer and will not interfere with the ability of the Company, the Employer or any subsidiary or affiliate to terminate your employment or service relationship at any time;

(f) if you are employed by a non-U.S. entity and provide services outside the U.S., the Option and the Shares subject to the Option are extraordinary items that do not constitute compensation of any kind for services of any kind rendered to your Employer, and they are outside the scope of your employment or service contract, if any, with your Employer;

(g) the Option and the Shares subject to the Option are not intended to replace any pension rights or compensation;

(h) the Option and the Shares subject to the Option are not part of normal or expected compensation or salary for any purposes, including, but not limited to, calculating any severance, resignation, termination, redundancy, dismissal, end-of-service payments, bonuses, long-service awards, pension or retirement or welfare benefits or similar payments;

(i) the Option grant and your participation in the Plan will not be interpreted to form an employment or service contract or relationship with the Company, the Employer or any subsidiary or affiliate of the Company;

(j) the future value of the Shares is unknown and cannot be predicted with certainty;

(k) if the Shares do not increase in value, the Option will have no value;

(l) if you exercise the Option and obtain Shares, the value of those Shares acquired upon exercise may increase or decrease in value, even below the Share purchase price;

(m) no claim or entitlement to compensation or damages shall arise from forfeiture of the Option resulting from termination of your employment or service relationship by the Company or the Employer (for any reason whatsoever and whether or not later found to be invalid or in breach of employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any), and, in consideration of the grant of the Option, to which you otherwise are not entitled, you irrevocably agree (i) never to institute any such claim against the Company, the Employer, or any subsidiary or affiliate of the Company, (ii) to waive your ability, if any, to bring any such claim, and (iii) to release the Company and the Employer and any subsidiary or affiliate from any such claim; if, notwithstanding the foregoing, any such claim is allowed by a court of competent jurisdiction, then, by participating in the Plan, you shall be deemed irrevocably to have agreed not to pursue such claim and agree to execute any and all documents necessary to request dismissal or withdrawal of such claims;

(n) the Option and the benefits under the Plan, if any, will not automatically transfer to another company in the case of a merger, takeover, or transfer of liability;

(o) neither the Company, the Employer nor any subsidiary or affiliate of the Company shall be liable for any foreign exchange rate fluctuation between your local currency and the United States Dollar that may affect the value of the Option or if any payments due to you pursuant to settlement of the Option or the subsequent sale of any Shares acquired upon settlement; and

(p) this award and any other award(s) granted under the Plan on the Grant Date are intended to fulfill any and all agreements, obligations or promises, whether legally binding or not, previously made by the Company or another Employer under the Plan to grant you options or other rights to common stock of the Company. By signing this Agreement, you accept such awards, along with all prior awards received by you, in full satisfaction of any such agreement, obligation or promise.

18. No Advice Regarding Grant. The Company is not providing any tax, legal, or financial advice, nor is the Company making any recommendations regarding your participation in the Plan, or your acquisition or sale of the underlying Shares. You are hereby advised to consult with your own personal tax, legal and financial advisors regarding your participation in the Plan before taking any action related to the Plan.

19. Compliance with Law. Notwithstanding any other provision of the Plan or this Agreement, unless there is an available exemption from any registration, qualification or other legal requirement applicable to the shares of Common Stock, the Company shall not be required to deliver any shares issuable upon purchase of shares under the Plan prior to the completion of any registration or qualification of the shares under any local, state, federal or foreign securities or exchange control law or under rulings or regulations of the U.S. Securities and Exchange Commission ("SEC") or of any other governmental regulatory body, or prior to obtaining any approval or other clearance from any local, state, federal or foreign governmental agency, which registration, qualification or approval the Company shall, in its absolute discretion, deem necessary or advisable. You understand that the Company is under no obligation to register or qualify the shares with the SEC or any state or foreign securities commission or to seek approval or clearance from any governmental authority for the issuance or sale of the shares. Further, you agree that the Company shall have unilateral authority to amend the Plan and the Agreement without your consent to the extent necessary to comply with securities or other laws applicable to issuance of shares.

20. Waiver. You acknowledge that a waiver by the Company of breach of any provision of this Agreement shall not operate or be construed as a waiver of any other provision of this Agreement, or of any subsequent breach by you or any other participant.

21. Appendix. Notwithstanding any provisions in this Agreement, the Option grant shall be subject to any special terms and conditions set forth in any Appendix to this Agreement for your country to the extent that the Company determines that the application of such terms and conditions is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan. Moreover, if you relocate to or from one of the countries included in any such Appendix, the special terms and conditions for the country you are moving from and/or the country you are moving to will apply to you to the extent that the Company determines that the application of such terms and conditions is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan. If included, the Appendix is incorporated in and constitutes part of this Agreement.

22. Imposition of Other Requirements. The Company reserves the right to impose other requirements on your participation in the Plan, on the Option and on any Shares acquired under the Plan, to the extent that the Company determines it is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan, and to require you to sign any additional agreements or undertakings that may be necessary to accomplish the foregoing.



**NONQUALIFIED STOCK OPTION
AWARD AGREEMENT**

Participant: _____
 Award Number: _____
 Plan: 2004 Long-Term Incentive Compensation Plan
 Award Type: Nonqualified Stock Option
 Grant Date: _____
 Number Shares: _____
 Exercise Price: _____
 Expiration Date: 11:59 p.m. local time in Durham, NC on the 7th anniversary of the Grant

Cree, Inc. (the "Company") has awarded you a nonqualified stock option (the "Option") to purchase _____ shares (the "Shares") of the common stock of the Company at a purchase price of _____ per share, effective _____, the Grant Date of the award. The Option is subject to and governed by the Cree, Inc. 2004 Long-Term Incentive Compensation Plan (the "Plan") and the terms of this Nonqualified Stock Option Award Agreement (the "Agreement").

You may exercise the Option to purchase up to the number of Shares for which it has vested unless and until the Option expires or is earlier terminated. In accordance with this Agreement and the Plan, upon any Termination of Service (as defined in this Agreement), the Option will be forfeited as to all Shares not then vested and will terminate thereafter as to vested Shares. If not previously terminated or expired, the Option will vest at 12:00 a.m. local time in Durham, NC in installments as follows, provided that you have not experienced a Termination of Service prior to the indicated vesting date:

____ Shares on _____;
 ____ additional Shares on _____; and
 ____ additional Shares on _____.

Capitalized terms defined in the Plan and used in this Agreement without definition have the meaning specified in the Plan.

THE TERMS AND CONDITIONS ON THE PAGES FOLLOWING THIS SIGNATURE PAGE, INCLUDING THE APPENDIX, ARE AN INTEGRAL PART OF THIS AGREEMENT AND ARE INCORPORATED HEREIN BY THIS REFERENCE. BY SIGNING BELOW YOU ACKNOWLEDGE THAT YOU HAVE READ, UNDERSTAND AND AGREE TO BE BOUND BY SUCH TERMS AND CONDITIONS. FAILURE TO SIGN WILL RESULT IN FORFEITURE OF THE AWARD.

Dated: _____

FOR CREE, INC.: ACCEPTED AND AGREED:

/s/ CHARLES M. SWOBODA

 Charles M. Swoboda, Chairman, President
 and Chief Executive Officer

TERMS AND CONDITIONS

1. Grant of Option. Subject to the terms of the Plan and this Agreement, the Company hereby grants you an Option as set forth on the first page of this Agreement.

2. Term of Option. Unless sooner terminated in accordance with the Plan or this Agreement, the Option will expire and cease to be exercisable upon the first to occur of the following:

(a) the expiration of ninety (90) calendar days following your Termination of Service, except where the termination results from your death or Disability or where your death occurs following the termination but while the Option is otherwise still exercisable;

(b) the expiration of one (1) year following your Termination of Service if the termination results from your death;

(c) the expiration of one (1) year following your Termination of Service if the termination results from your Disability, except where your death occurs after the termination but while the Option is otherwise still exercisable;

(d) the expiration of one (1) year following your death if your death occurs after your Termination of Service but while the Option is otherwise still exercisable; or

(e) the seventh (7th) anniversary of the Grant Date of the Option, at 11:59 P.M., local time, Durham, North Carolina.

Upon expiration or termination of the Option, it will have no further effect and cannot thereafter be exercised to purchase any Shares.

3. Vesting. The Option will vest and become exercisable in accordance with the schedule set out on the first page of this Agreement and will become fully vested and exercisable to purchase all Shares subject to the Option, to the extent not already vested and exercisable, upon your Termination of Service on account of your death or Disability, unless otherwise provided in this Agreement or the Plan.

4. Forfeiture upon Termination of Service. Except as otherwise provided in this Agreement or the Plan, upon your Termination of Service, you will forfeit the Option with respect to any Shares as to which the Option has not vested as of the date of your Termination of Service.

5. Exercise of Option. To exercise the Option, you must complete, execute and deliver to the Company a notice of exercise in a form approved by the Company and pay to the Company the purchase price for the number of Shares specified in the notice together with all Tax-Related Items (as defined in Section 6 below) the Company is required to withhold, collect, or account for pursuant to this Agreement. Exercise of the Option will be effective only when the notice and required payments are actually received by the Company or upon your execution of a "broker-assisted exercise" or "cashless exercise" transaction with a broker approved by the Company. Furthermore, if the exercise is facilitated through a "broker-assisted exercise" or "cashless exercise" transaction by a brokerage firm you have designated, you agree that the brokerage firm is acting as your agent in the transaction and that the Company may rely upon notices, instructions and information given by such firm in connection with the exercise, as if the same were given by you. The Company will make the Shares available for electronic delivery in the U.S., and where allowed by applicable law outside the U.S., to an account you designate in writing, within three (3) business days after the Company receives the notice of exercise and required payments. In situations where electronic delivery is not available, the Company will deliver a certificate or certificates for the purchased Shares to you, or to such other person as you designate in writing.

6. Responsibility for Taxes.

(a) For purposes of this Agreement, "Tax-Related Items" means any or all income tax, social insurance tax, payroll tax, payment on account or other tax-related items that may be applicable this Award by law or regulation of any governmental authority, whether federal, state or local, domestic or foreign. Regardless of any action the Company takes with respect to withholding Tax-Related Items, you acknowledge that you are ultimately responsible for all Tax-Related Items and that such Tax-Related Items may exceed the amount actually withheld by the Company or the Employer. You further acknowledge that the Company and/or the Employer (1) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the Option, including, without limitation, the grant, vesting or exercise of the Option, the subsequent sale of Shares acquired pursuant to such exercise and the receipt of any dividends or dividend equivalents pursuant to Shares; and (2) do not commit to and are under no obligation to structure the terms of the grant or any

aspect of the Option to reduce or eliminate your liability for Tax-Related Items or to achieve any particular tax result. Furthermore, if you have become subject to tax in more than one jurisdiction between the Grant Date and the date of any relevant taxable event, you acknowledge that the Company and/or the Employer (or former Employer, as applicable) may be required to withhold or account for Tax-Related Items in more than one jurisdiction.

(b) Prior to any relevant taxable or tax withholding event, as applicable, you will pay or make adequate arrangements satisfactory to the Company and/or the Employer to satisfy all Tax-Related Items. In this regard, you authorize the Company and/or the Employer, or their respective agents, at their discretion, to satisfy the obligations with regard to all Tax-Related Items by one or a combination of the following: (1) withholding from your wages or other cash compensation paid to you by the Company and/or the Employer; or (2) withholding from proceeds of the sale of Shares acquired upon exercise of the Option; or (3) withholding in Shares to be issued upon exercise of the Option.

(c) Depending upon the withholding method, the Company or the Employer may withhold or account for Tax-Related Items by considering applicable minimum or maximum statutory withholding amounts or other applicable withholding rates. In the event Tax-Related Items are over-withheld, you will receive a refund in cash for any over-withheld amounts and will have no entitlement to the Shares equivalent. If the obligation for Tax-Related Items is satisfied by withholding of Shares, you shall be deemed, for tax purposes, to have been issued the full number of Shares subject to the exercised Option, notwithstanding that a number of Shares is held back solely for the purpose of paying the Tax-Related Items due as a result of any aspect of your participation in the Plan.

(d) You shall pay to the Company or the Employer any amount of Tax-Related Items that the Company or the Employer may be required to withhold or account for as a result of your participation in the Plan that cannot be satisfied by the means previously described. The Company may refuse to honor the exercise of the Option and refuse to deliver the Shares if you fail to comply with your obligations in connection with the Tax-Related Items.

7. Transfer of Option. Neither the Option nor any rights under the Option may be assigned, pledged as collateral or otherwise transferred, except as permitted by the Plan, nor may the Option or such rights be subject to attachment, execution or other judicial process. In the event of any attempt to assign, pledge or otherwise dispose of the Option or any rights under the Option, except as permitted by the Plan, or in the event of the levy of any attachment, execution or similar judicial process upon the rights or interests conferred by the Option, the Committee may in its discretion terminate the Option upon notice to you.

8. Rights Prior to Exercise. You will have no rights as a shareholder with respect to any Shares until such Shares have been duly issued by the Company or its transfer agent pursuant to exercise of the Option.

9. Termination of Service.

(a) Unless otherwise provided in this Agreement or the Plan, for purposes of this Agreement “Termination of Service” means the discontinuance of your relationship with the Company as an employee of the Company or the Employer or any subsidiary or affiliate of the Company under the Plan or as a member of the Board of Directors of Cree, Inc. Except as determined otherwise by the Committee, you will not be deemed to have incurred a Termination of Service if the capacity in which you provide services to the Company changes (for example, you change from being a non-employee director to being an employee) or if you transfer employment among the various subsidiaries or affiliates of the Company constituting the Employer, so long as there is no interruption in your provision of services to the Company or other Employer as an employee or as a non-employee member of the Board of Directors of Cree, Inc. The Committee, in its discretion, will determine whether you have incurred a Termination of Service. You will not be deemed to have incurred a Termination of Service during a period for which you are on military leave, sick leave, or other leave of absence approved by the Employer.

(b) If you are deemed to have incurred a Termination of Service other than a Termination of Service on account of your death or Disability, your right to vest in the Option under this Agreement of the Plan, if any, will terminate and any post-termination exercise period will commence effective as of the date that you are no longer actively providing services to the Company or one of its subsidiaries or affiliates (regardless of the reason for the termination and whether or not later found to be invalid or in breach of employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any), and will not be extended by any notice period mandated under local law (e.g., active employment would not include a period of “garden leave” or similar period mandated under the employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any); the Committee, in its discretion, will determine when you are no longer actively providing services for purposes of the Option grant (including whether you may still be considered to be providing services while on a leave of absence).

10. Provisions of the Plan. The provisions of the Plan are incorporated by reference in this Agreement as if set out in full in this Agreement. To the extent that any conflict may exist between any other provision of this Agreement and a provision of the Plan, the Plan provision will control. All decisions of the Committee with respect to the interpretation, construction and application of the Plan or this Agreement shall be final, conclusive and binding upon you and the Company.

11. Detrimental Activity. The Committee in its sole discretion may cancel, terminate, suspend or otherwise limit or restrict exercise of the unexercised portion of the Option if you engage in any "Detrimental Activity" (as defined below). In addition, if you engage in any Detrimental Activity prior to or within one (1) year after your Termination of Service, the Committee in its sole discretion may require you to pay to the Company the amount of all gain you realized from any exercise of the Option beginning six (6) months prior to your Termination of Service, provided that the Committee gives you notice of such requirement within one (1) year after your Termination of Service. In that event, the Company will be entitled to setoff such amount against any amount the Company owes to you, in addition to any other rights the Company may have. For purposes of this section:

(a) "Company" includes Cree, Inc. and all other Employers under the Plan.

(b) "Detrimental Activity" means any of the following conduct, as determined by the Committee in good faith:

(1) the performance of services for any Competing Business (as defined below), whether as an employee, officer, director, consultant, agent, contractor or in any other capacity, except to the extent expressly permitted by any written agreement between you and the Company;

(2) the unauthorized disclosure or use of any trade secrets or other confidential information of the Company;

(3) any attempt to induce an employee to leave employment with the Company to perform services elsewhere, or any attempt to cause a customer or supplier of the Company to curtail or cancel its business with the Company;

(4) breach of any confidentiality, noncompetition, nonsolicitation or nondisparagement obligations, or any obligations relating to the disclosure, assignment or protection of inventions, undertaken by you in any written agreement between you and the Company; or

(5) any act of fraud, misappropriation, embezzlement, or tortious or criminal behavior that adversely impacts the Company.

(c) "Competing Business" means any corporation, partnership, university, government agency or other entity or person (other than the Company) that is conducting research directed to, developing, manufacturing, marketing, distributing, or selling any product, service, or technology that is competitive with any part of the Company's Business (as defined below). "Company's Business" means the development, manufacture, marketing, distribution, or sale of, or the conduct of research directed to, any product, service, or technology that the Company is developing, manufacturing, marketing, distributing, selling, or conducting research directed to, at any time during your employment or other relationship with the Company, except that following your Termination of Service the Company's Business will be determined as of the time of such termination. As of the effective date of this Agreement, the Company's Business includes but is not limited to the conduct of research directed to, development, manufacture, marketing, distribution, and/or sale of the following products, services, and technologies: (1) silicon carbide (SiC) materials for electronic applications; (2) SiC materials for gemstone applications; (3) AlN nitride materials for electronic applications; (4) light-emitting diode (LED) devices and components; (5) power semiconductor devices made using SiC and/or AlN nitride materials and components incorporating such devices; (6) radio frequency (RF) and microwave devices made using SiC and/or AlN nitride materials and components and modules incorporating such devices; (7) LED backlights for liquid crystal displays (LCDs); (8) lighting products, modules, fixtures or devices incorporating any of the above materials or technology; and (9) other semiconductor devices made using SiC and/or AlN nitride materials and components incorporating such devices. You acknowledge that during your employment or other relationship with the Company the Company's Business may expand or change and you agree that any such expansions and changes shall expand or contract the definition of the Company's Business accordingly.

12. Data Privacy. You hereby explicitly and unambiguously consent to the collection, use and transfer, in electronic or other form, of your personal data as described in this Agreement and any other option grant materials ("Data") by and among, as applicable, your Employer, the Company and its subsidiaries and affiliates, for the exclusive purpose of implementing, administering and managing your participation in the Plan.

You understand that the Employer holds or may hold certain personal information about you, including, but not limited to, your name, home address and telephone number, date of birth, social insurance number or other identification number, salary, nationality, position title, any shares of stock or directorships held in the Company, details of all options or any other entitlement to Shares awarded, canceled, exercised, vested, unvested or outstanding in your favor, for the purpose of implementing, administering and managing the Plan.

You understand that Data may be transferred to any third parties as may be selected by the Company currently or in the future, which are assisting the Company in the implementation, administration and management of the Plan. You understand that these recipients may be located in the United States or elsewhere, and that the recipient's country (e.g., the United States) may have different data privacy laws and protections than your country. You understand that you may request a list with the names and addresses of any potential recipients of the Data by contacting the Company's Stock Plan Administrator. You authorize the Company and any other possible recipients that may assist the Company (presently or in the future) with implementing, administering and managing the Plan to receive, possess, use, retain and transfer the Data, in electronic or other form, for the purposes of implementing, administering and managing your participation in the Plan, including any requisite transfer of such Data as may be required to a broker or other third party whom you subsequently may elect to deposit any Shares acquired under the Plan. You understand that Data will be held pursuant to this Agreement only as long as the Company considers it necessary to implement, administer and manage your participation in the Plan. You understand that you may, at any time, view Data, request additional information about the storage and processing of Data, require any necessary amendments to Data or refuse or withdraw the consents above, in any case without cost, by contacting in writing the Company's Stock Plan Administrator. Further, you understand that you are providing the consents herein on a purely voluntary basis. If you do not consent, your employment status or service and career with the Employer will not be adversely affected; the only adverse consequence of refusing or withdrawing consent is that the Company would not be able to grant you Options or receive any other equity awards or administer or maintain such awards. Therefore, you acknowledge, however, that refusing or withdrawing your consent may affect your ability to participate in the Plan. For more information on the consequences of your refusal to consent or withdrawal of consent, you may contact the Stock Plan Administrator of the Company.

13. Language. If you have received this Agreement or any other document related to the Plan translated into a language other than English and if the translated version differs in meaning from the English version, the English version will control.

14. Electronic Delivery. The Company may, in its sole discretion, deliver any documents related to current or future participation in the Plan by electronic means. You hereby consent to receive such documents by electronic delivery and agree to participate in the Plan through an on-line or electronic system established and maintained by the Company or another third party designated by the Company. Signed documents delivered to either party via facsimile or in portable document format will have the same effect as an original, unless otherwise required by applicable law.

15. General.

(a) Nothing in this Agreement will be construed as: (1) constituting a commitment, agreement or understanding of any kind that the Company or any other Employer will continue your employment or other relationship with the Company; or (2) limiting or restricting either party's right to terminate your employment or other relationship.

(b) This Agreement shall be binding upon and inure to the benefit of the parties and their respective successors and permitted assigns. You may not assign any rights under this Agreement without the written consent of the Company, which it may withhold in its sole discretion; any such attempted assignment without the Company's written consent shall be void. The Company may assign its rights under this Agreement at any time upon notice to you.

(c) Notices under this Agreement must be in writing and delivered either by hand or by a reputable domestic or international carrier (postage prepaid and return receipt or proof of delivery requested), and, in the case of notices to the Company, addressed to its principal executive offices to the attention of the Stock Plan Administrator, and, in your case, addressed to your address as shown on the Employer's records.

(d) This Agreement shall be governed by and construed in accordance with the laws of the State of North Carolina, without regard to the conflict of law provisions thereof, as if made and to be performed wholly within such State. For purposes of litigating any dispute that arises directly or indirectly from the relationship of the parties evidenced by the Option or this Agreement, the parties hereby submit to and consent to the exclusive jurisdiction of the State of North Carolina, agree that such litigation shall be conducted in the courts of Durham County, North Carolina, or the federal courts for the United States for the Middle District of North Carolina, and no other courts, where the Option grant is made and/or to be performed.

(e) If any provision of this Agreement is held to be invalid or unenforceable, such determination shall not affect the other provisions of the Agreement and the Agreement shall be construed as if the invalid or unenforceable provision were omitted and a valid and enforceable provision, as nearly comparable as possible, substituted in its place.

(f) Notwithstanding any prior option award agreement between you and the Company under which options may have been awarded, this Agreement and the Plan set forth all of the promises, agreements and understandings between you and Company relating to the Option granted pursuant to this Agreement, constitutes the complete agreement between the parties regarding the Option, and replaces any prior oral or written communications regarding the same.

(g) Shares issued upon exercise of the Option may be subject to such stop transfer orders and other restrictions as the Committee may deem advisable under applicable law or the rules and regulations of the U.S. Securities and Exchange Commission or any stock exchange or trading system upon which the common stock of the Company is listed, and the Committee may cause a legend or legends to be placed on any such certificates or the stock records of the Company to make appropriate reference to such restrictions.

(h) You agree that the Option, even if later forfeited, serves as additional, valuable consideration for your obligations, if any, undertaken in any existing agreement between you and the Company and/or other Employer regarding confidential information, noncompetition, nonsolicitation or similar covenants.

(i) You acknowledge, represent and warrant to the Company, and agree with the Company, that (i) except for information provided in the Company's filings with the U.S. Securities and Exchange Commission and in the Company's current prospectus relating to the Plan, you have not relied and will not rely upon the Committee, the Company, an Employer or any employee or agent of the Company or an Employer in determining whether to accept or exercise the Option, or in connection with any disposition of Shares purchased upon exercise of the Option, or with respect to any tax consequences related to the grant or exercise of the Option or the disposition of Shares purchased pursuant to exercise of the Option, and (ii) you will seek from your own professional advisors such investment, tax and other advice as you believe necessary.

(j) You acknowledge that you may incur a substantial tax liability as a result of exercise of the Option. You assume full responsibility for all such consequences and the filing of all tax returns and related elections you may be required or find desirable to file. If you are required to make any valuation of the Option or Shares purchased pursuant to exercise of the Option under any federal, state or other applicable tax law, and if the valuation affects any tax return or election of the Company or the Employer or affects the Company's financial statement reporting, you agree that the Company may determine the value and that you will observe any determination so made by the Company in all tax returns and elections filed by you.

(k) You acknowledge that copies of the Plan and Plan prospectus are available upon written or telephonic request to the Company's Stock Plan Administrator.

16. Severability. The provisions of this Agreement are severable and if any one or more provisions is determined to be illegal or otherwise unenforceable, in whole or in part, the remaining provisions shall nevertheless be binding and enforceable.

17. Nature of Grant. In accepting this grant, you acknowledge, understand and agree that:

(a) the Plan is established voluntarily by the Company, is discretionary in nature and may be modified, amended, suspended or terminated by the Company at any time, unless expressly provided otherwise in the Plan or the Agreement;

(b) the grant of the Option is voluntary and does not create any contractual or other right to receive future grants of options, or benefits in lieu of options, even if options have been granted repeatedly in the past;

(c) all decisions with respect to future option grants, if any, will be at the sole discretion of the Company;

(d) your participation in the Plan is voluntary;

(e) your participation in the Plan will not create a right to employment with the Company or the Employer and will not interfere with the ability of the Company, the Employer or any subsidiary or affiliate to terminate your employment or service relationship at any time;

(f) if you are employed by a non-U.S. entity and provide services outside the U.S., the Option and the Shares subject to the Option are extraordinary items that do not constitute compensation of any kind for services of any kind rendered to your Employer, and they are outside the scope of your employment or service contract, if any, with your Employer;

(g) the Option and the Shares subject to the Option are not intended to replace any pension rights or compensation;

(h) the Option and the Shares subject to the Option are not part of normal or expected compensation or salary for any purposes, including, but not limited to, calculating any severance, resignation, termination, redundancy, dismissal, end-of-service payments, bonuses, long-service awards, pension or retirement or welfare benefits or similar payments;

(i) the Option grant and your participation in the Plan will not be interpreted to form an employment or service contract or relationship with the Company, the Employer or any subsidiary or affiliate of the Company;

(j) the future value of the Shares is unknown and cannot be predicted with certainty;

(k) if the Shares do not increase in value, the Option will have no value;

(l) if you exercise the Option and obtain Shares, the value of those Shares acquired upon exercise may increase or decrease in value, even below the Share purchase price;

(m) no claim or entitlement to compensation or damages shall arise from forfeiture of the Option resulting from termination of your employment or service relationship by the Company or the Employer (for any reason whatsoever and whether or not later found to be invalid or in breach of employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any), and, in consideration of the grant of the Option, to which you otherwise are not entitled, you irrevocably agree (i) never to institute any such claim against the Company, the Employer, or any subsidiary or affiliate of the Company, (ii) to waive your ability, if any, to bring any such claim, and (iii) to release the Company and the Employer and any subsidiary or affiliate from any such claim; if, notwithstanding the foregoing, any such claim is allowed by a court of competent jurisdiction, then, by participating in the Plan, you shall be deemed irrevocably to have agreed not to pursue such claim and agree to execute any and all documents necessary to request dismissal or withdrawal of such claims;

(n) the Option and the benefits under the Plan, if any, will not automatically transfer to another company in the case of a merger, takeover, or transfer of liability;

(o) neither the Company, the Employer nor any subsidiary or affiliate of the Company shall be liable for any foreign exchange rate fluctuation between your local currency and the United States Dollar that may affect the value of the Option or if any payments due to you pursuant to settlement of the Option or the subsequent sale of any Shares acquired upon settlement; and

(p) this award and any other award(s) granted under the Plan on the Grant Date are intended to fulfill any and all agreements, obligations or promises, whether legally binding or not, previously made by the Company or another Employer under the Plan to grant you options or other rights to common stock of the Company. By signing this Agreement, you accept such awards, along with all prior awards received by you, in full satisfaction of any such agreement, obligation or promise.

18. No Advice Regarding Grant. The Company is not providing any tax, legal, or financial advice, nor is the Company making any recommendations regarding your participation in the Plan, or your acquisition or sale of the underlying Shares. You are hereby advised to consult with your own personal tax, legal and financial advisors regarding your participation in the Plan before taking any action related to the Plan.

19. Compliance with Law. Notwithstanding any other provision of the Plan or this Agreement, unless there is an available exemption from any registration, qualification or other legal requirement applicable to the shares of Common Stock, the Company shall not be required to deliver any shares issuable upon purchase of shares under the Plan prior to the completion of any registration or qualification of the shares under any local, state, federal or foreign securities or exchange control law or under rulings or regulations of the U.S. Securities and Exchange Commission ("SEC") or of any other governmental regulatory body, or prior to obtaining any approval or other clearance from any local, state, federal or foreign governmental agency, which registration, qualification or approval the Company shall, in its absolute discretion, deem necessary or advisable. You understand that the Company is under no obligation to register or qualify the shares with the SEC or any state or foreign securities commission or to seek approval or clearance from any governmental authority for the issuance or sale of the shares. Further, you agree that the Company shall have unilateral authority to amend the Plan and the Agreement without your consent to the extent necessary to comply with securities or other laws applicable to issuance of shares.

20. Waiver. You acknowledge that a waiver by the Company of breach of any provision of this Agreement shall not operate or be construed as a waiver of any other provision of this Agreement, or of any subsequent breach by you or any other participant.

21. Appendix. Notwithstanding any provisions in this Agreement, the Option grant shall be subject to any special terms and conditions set forth in any Appendix to this Agreement for your country to the extent that the Company determines that the application of such terms and conditions is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan. Moreover, if you relocate to or from one of the countries included in the Appendix, the special terms and conditions for the country you are moving from and/or the country you are moving to will apply to you to the extent that the Company determines that the application of such terms and conditions is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan. If included, the Appendix is incorporated in and constitutes part of this Agreement.

22. Imposition of Other Requirements. The Company reserves the right to impose other requirements on your participation in the Plan, on the Option and on any Shares acquired under the Plan, to the extent that the Company determines it is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan, and to require you to sign any additional agreements or undertakings that may be necessary to accomplish the foregoing.



**RESTRICTED STOCK
AWARD AGREEMENT**

Participant: _____
 Award Number: _____
 Plan: 2004 Long-Term Incentive Compensation Plan
 Award Type: Restricted Stock
 Grant Date: _____
 Number Shares: _____
 Purchase Price: \$0.00
 Restriction Period: Grant Date through _____

Cree, Inc. (the "Company") has awarded you _____ shares (the "Shares") of the common stock of the Company (the "Restricted Stock") effective _____, the Grant Date of the Award, pursuant to the Cree, Inc. 2004 Long-Term Incentive Compensation Plan (the "Plan") and the terms of this Restricted Stock Award Agreement (the "Agreement").

The Restricted Stock will be held in escrow by the Company until vested or forfeited. In accordance with this Agreement and the Plan, upon any Termination of Service (as defined in this Agreement) before the end of the Restriction Period, all Restricted Stock that is not then vested will be forfeited. If not previously vested or forfeited, the Restricted Stock will vest at 12:00 a.m. local time in Durham, NC in installments as follows, provided that you have not experienced a Termination of Service prior to the indicated vesting date:

____ Shares on _____;
 ____ additional Shares on _____;
 ____ additional Shares on _____; and
 ____ additional Shares on _____.

Capitalized terms defined in the Plan and used in this Agreement without definition have the meaning specified in the Plan.

THE TERMS AND CONDITIONS ON THE PAGES FOLLOWING THIS SIGNATURE PAGE, INCLUDING ANY APPENDIX, ARE AN INTEGRAL PART OF THIS AGREEMENT AND ARE INCORPORATED HEREIN BY THIS REFERENCE. BY SIGNING BELOW YOU ACKNOWLEDGE THAT YOU HAVE READ, UNDERSTAND AND AGREE TO BE BOUND BY SUCH TERMS AND CONDITIONS. FAILURE TO SIGN WILL RESULT IN FORFEITURE OF THE AWARD.

Dated: _____

FOR CREE, INC.: ACCEPTED AND AGREED:

/s/ CHARLES M. SWOBODA

 Charles M. Swoboda, Chairman, President
 and Chief Executive Officer

TERMS AND CONDITIONS

- 1. Grant of Restricted Stock.** Subject to the terms of the Plan and this Agreement, the Company hereby grants you the Restricted Stock as set forth on the first page of this Agreement. Shares issued pursuant to this Award will be registered in your name and evidenced by one or more certificates delivered to and deposited with the Secretary of the Company as escrow agent or, at the discretion of the Company, held in a restricted book entry account in lieu of issuing a certificate or certificates. Such certificates or such book entry shares are to be held by the escrow agent until the Restricted Stock vests, at which time the escrow agent will release the vested Shares, or is forfeited; provided, however, that a portion of the Shares may be surrendered in payment of required withholding taxes in accordance with Section 8(b) below, unless alternative procedures for the payment of required withholding taxes are established by the Company.
- 2. Vesting.** The Restricted Stock will vest in accordance with the schedule set out on the first page of this Agreement and will become fully vested, to the extent not already vested, upon your Termination of Service on account of your death or Disability, unless otherwise provided in this Agreement or the Plan.
- 3. Forfeiture of Restricted Stock upon Termination of Service.** Except as otherwise provided in this Agreement or the Plan, upon your Termination of Service, you will forfeit all of the Restricted Stock that is not vested as of the date of your Termination of Service.
- 4. Forfeiture of Restricted Stock upon Section 83(b) Election.** As permitted under Section 15.6 of the Plan, this Award is conditioned upon and subject to your not making an election under Section 83(b) of the Code with respect to the Restricted Stock. If you make an election under Section 83(b) of the Code with respect to any of the Restricted Stock, you will forfeit such Restricted Stock.
- 5. Forfeiture of Restricted Stock for Awards Not Timely Accepted.** This Award is conditioned upon and subject to your accepting the Award by signing and delivering to the Company this Agreement no later than the first date Shares are scheduled to vest pursuant to the Award. In the event of your death or incapacitation prior to accepting the Award, the Company will deem the Award as being accepted. If the Company issues the Restricted Stock pursuant to an Award prior to your acceptance of the Award, and if you fail to accept the Award within the time described above, you will forfeit such Restricted Stock.
- 6. Settlement of Restricted Stock.** As soon as administratively practicable following the vesting of any portion of this Award, the Company shall deliver to you (or, in the event of your death, to your estate or, if the Committee establishes a beneficiary designation procedure pursuant to Section 11 of the Plan, to any beneficiary that you have designated pursuant to such procedure) one or more certificates for the vested Shares or in the Company's discretion may cause the vested Shares to be deposited in an account maintained by a broker designated by the Company.
- 7. Responsibility for Taxes.**

(a) For purposes of this Agreement, "Tax-Related Items" means any or all income tax, social insurance tax, payroll tax, payment on account or other tax-related items that may be applicable to this Award by law or regulation of any governmental authority, whether federal, state or local, domestic or foreign. Regardless of any action the Company takes with respect to withholding Tax-Related Items, you acknowledge that you are ultimately responsible for all Tax-Related Items and that such Tax-Related Items may exceed the amount actually withheld by the Company or the Employer. You further acknowledge that the Company and/or the Employer (1) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the Restricted Stock, including, without limitation, the grant, vesting or release of the Restricted Stock, the subsequent sale of Shares and the receipt of any dividends or dividend equivalents pursuant to Shares; and (2) do not commit to and are under no obligation to structure the terms of the grant or any aspect of the Restricted Stock to reduce or eliminate your liability for Tax-Related Items or to achieve any particular tax result. Furthermore, if you have become subject to tax in more than one jurisdiction between the Grant Date and the date of any relevant taxable event, you acknowledge that the Company and/or the Employer (or former Employer, as applicable) may be required to withhold or account for Tax-Related Items in more than one jurisdiction.

(b) Prior to any relevant taxable or tax withholding event, as applicable, you will pay or make adequate arrangements satisfactory to the Company and/or the Employer to satisfy all Tax-Related Items. In this regard, you authorize the Company and/or the Employer, or their respective agents, at their discretion, to satisfy the obligations with regard to all Tax-Related Items by one or a combination of the following: (1) withholding from your wages or other cash compensation paid to you by the Company and/or the Employer; or (2) selling or arranging for the sale of Shares that you acquire under the Plan; or (3) withholding of Shares consistent with the "Share Withholding" provisions under Section 13.2 of the Plan.

(c) Depending upon the withholding method, the Company or the Employer may withhold or account for Tax-Related Items by considering applicable minimum or maximum statutory withholding amounts or other applicable withholding rates. In the event Tax-Related Items are over-withheld, you will receive a refund in cash for any over-withheld amounts and will have no entitlement to the Shares equivalent. If the obligation for Tax-Related Items is satisfied by withholding of Shares, you shall be deemed, for tax purposes, to have been issued the full number of Shares, notwithstanding that a number of Shares is held back solely for the purpose of paying the Tax-Related Items due as a result of any aspect of your participation in the Plan.

(d) You shall pay to the Company or the Employer any amount of Tax-Related Items that the Company or the Employer may be required to withhold or account for as a result of your participation in the Plan that cannot be satisfied by the means previously described. The Company may refuse to honor the vesting of the Restricted Stock and refuse to release from escrow the Shares if you fail to comply with your obligations in connection with the Tax-Related Items.

8. Transfer of Restricted Stock. The Restricted Stock and any rights under this Agreement may not be assigned, pledged as collateral or otherwise transferred, except as permitted by the Plan, nor may the Restricted Stock or such rights be subject to attachment, execution or other judicial process until the Restricted Stock becomes vested pursuant to Section 2 above. In the event of any attempt to assign, pledge or otherwise dispose of the Restricted Stock which is not then vested, or any rights under this Agreement, except as permitted by the Plan, or in the event of the levy of any attachment, execution or similar judicial process upon the rights or interests with respect to the Restricted Stock which is not then vested, the Committee may in its discretion, upon notice to you, cause you to forfeit such Restricted Stock.

9. Rights Prior to Vesting of Shares of Restricted Stock.

(a) You will have at all times all rights as a shareholder with respect to the Restricted Stock, including, but not limited to, voting rights and rights to receive dividends, except for the right to transfer the Restricted Stock as set forth in Section 9 above; provided, however, that any dividends on the Restricted Stock will be automatically deferred and reinvested in additional Restricted Stock subject to the same restrictions as the underlying Restricted Stock.

(b) In the event of a change in capitalization within the meaning of Section 4.3 of the Plan, the number and class of Shares or other securities that you are entitled to pursuant to this Agreement shall be appropriately adjusted or changed as determined by the Committee to reflect the change in capitalization, provided that any such additional Shares or additional or different shares of securities shall remain subject to the restrictions in this Agreement.

10. Termination of Service.

(a) Unless otherwise provided in this Agreement or the Plan, for purposes of this Agreement "Termination of Service" means the discontinuance of your relationship with the Company as an employee of the Company or the Employer or any subsidiary or affiliate of the Company under the Plan or as a member of the Board of Directors of Cree, Inc. Except as determined otherwise by the Committee, you will not be deemed to have incurred a Termination of Service if the capacity in which you provide services to the Company changes (for example, you change from being a non-employee director to being an employee) or if you transfer employment among the various subsidiaries or affiliates of the Company constituting the Employer, so long as there is no interruption in your provision of services to the Company or other Employer as an employee or as a non-employee member of the Board of Directors of Cree, Inc. The Committee, in its discretion, will determine whether you have incurred a Termination of Service. You will not be deemed to have incurred a Termination of Service during a period for which you are on military leave, sick leave, or other leave of absence approved by the Employer.

(b) If you are deemed to have incurred a Termination of Service other than a Termination of Service on account of your death or Disability, your right to vest in the Restricted Stock under this Agreement or the Plan, if any, will terminate effective as of the date that you are no longer actively providing services to the Company or one of its subsidiaries or affiliates (regardless of the reason for the termination and whether or not later found to be invalid or in breach of employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any), and will not be extended by any notice period mandated under local law (e.g., active employment would not include a period of "garden leave" or similar period mandated under the employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any); the Committee, in its discretion, will determine when you are no longer actively providing services for purposes of this Award (including whether you may still be considered to be providing services while on a leave of absence).

11. Provisions of the Plan. The provisions of the Plan are incorporated by reference in this Agreement as if set out in full in this Agreement. To the extent that any conflict may exist between any other provision of this Agreement and a provision of the Plan, the Plan provision will control. All decisions of the Committee with respect to the interpretation, construction and application of the Plan or this Agreement shall be final, conclusive and binding upon you and the Company.

12. Detrimental Activity. The Committee in its sole discretion may cancel and cause to be forfeited any Shares of the Restricted Stock not previously vested or released from escrow under this Agreement if you engage in any "Detrimental Activity" (as defined below). In addition, if you engage in any Detrimental Activity prior to or within one (1) year after your Termination of Service, the Committee in its sole discretion may require you to pay to the Company the amount of all gain you realized from any vesting of Shares of the Restricted Stock beginning six (6) months prior to your Termination of Service, provided that the Committee gives you notice of such requirement within one (1) year after your Termination of Service. In that event, the Company will be entitled to setoff such amount against any amount the Company owes to you, in addition to any other rights the Company may have. For purposes of this section:

(a) "Company" includes Cree, Inc. and all other Employers under the Plan.

(b) "Detrimental Activity" means any of the following conduct, as determined by the Committee in good faith:

(1) the performance of services for any Competing Business (as defined below), whether as an employee, officer, director, consultant, agent, contractor or in any other capacity, except to the extent expressly permitted by any written agreement between you and the Company;

(2) the unauthorized disclosure or use of any trade secrets or other confidential information of the Company;

(3) any attempt to induce an employee to leave employment with the Company to perform services elsewhere, or any attempt to cause a customer or supplier of the Company to curtail or cancel its business with the Company;

(4) breach of any confidentiality, noncompetition, nonsolicitation or nondisparagement obligations, or any obligations relating to the disclosure, assignment or protection of inventions, undertaken by you in any written agreement between you and the Company; or

(5) any act of fraud, misappropriation, embezzlement, or tortious or criminal behavior that adversely impacts the Company.

(c) "Competing Business" means any corporation, partnership, university, government agency or other entity or person (other than the Company) that is conducting research directed to, developing, manufacturing, marketing, distributing, or selling any product, service, or technology that is competitive with any part of the Company's Business (as defined below). "Company's Business" means the development, manufacture, marketing, distribution, or sale of, or the conduct of research directed to, any product, service, or technology that the Company is developing, manufacturing, marketing, distributing, selling, or conducting research directed to, at any time during your employment or other relationship with the Company, except that following your Termination of Service the Company's Business will be determined as of the time of such termination. As of the effective date of this Agreement, the Company's Business includes but is not limited to the conduct of research directed to, development, manufacture, marketing, distribution, and/or sale of the following products, services, and technologies: (1) silicon carbide (SiC) materials for electronic applications; (2) SiC materials for gemstone applications; (3) AIII nitride materials for electronic applications; (4) light-emitting diode (LED) devices and components; (5) power semiconductor devices made using SiC and/or AIII nitride materials and components incorporating such devices; (6) radio frequency (RF) and microwave devices made using SiC and/or AIII nitride materials and components and modules incorporating such devices; (7) LED backlights for liquid crystal displays (LCDs); (8) lighting products, modules, fixtures or devices incorporating any of the above materials or technology; and (9) other semiconductor devices made using SiC and/or AIII nitride materials and components incorporating such devices. You acknowledge that during your employment or other relationship with the Company the Company's Business may expand or change and you agree that any such expansions and changes shall expand or contract the definition of the Company's Business accordingly.

13. Data Privacy. *You hereby explicitly and unambiguously consent to the collection, use and transfer, in electronic or other form, of your personal data as described in this Agreement and any other grant materials ("Data") by and among, as applicable, your Employer, the Company and its subsidiaries and affiliates, for the exclusive purpose of implementing, administering and managing your participation in the Plan.*

You understand that the Employer holds or may hold certain personal information about you, including, but not limited to, your name, home address and telephone number, date of birth, social insurance number or other identification number, salary, nationality, position title, any shares of stock or directorships held in the Company, details of the Restricted Stock or any other entitlement to Shares awarded, canceled, exercised, vested, unvested or outstanding in your favor, for the purpose of implementing, administering and managing the Plan.

You understand that Data may be transferred to any third parties as may be selected by the Company currently or in the future, which are assisting the Company in the implementation, administration and management of the Plan. You understand that these recipients may be located in the United States or elsewhere, and that the recipient's country (e.g., the United States) may have different data privacy laws and protections than your country. You understand that you may request a list with the names and addresses of any potential recipients of the Data by contacting the Company's Stock Plan Administrator. You authorize the Company and any other possible recipients that may assist the Company (presently or in the future) with implementing, administering and managing the Plan to receive, possess, use, retain and transfer the Data, in electronic or other form, for the purposes of implementing, administering and managing your participation in the Plan, including any requisite transfer of such Data as may be required to a broker or other third party whom you subsequently may elect to deposit any Shares acquired under the Plan. You understand that Data will be held pursuant to this Agreement only as long as the Company considers it necessary to implement, administer and manage your participation in the Plan. You understand that you may, at any time, view Data, request additional information about the storage and processing of Data, require any necessary amendments to Data or refuse or withdraw the consents above, in any case without cost, by contacting in writing the Company's Stock Plan Administrator. Further, you understand that you are providing the consents herein on a purely voluntary basis. If you do not consent, your employment status or service and career with the Employer will not be adversely affected; the only adverse consequence of refusing or withdrawing consent is that the Company would not be able to grant you the Restricted Stock or any other equity awards or administer or maintain such awards. Therefore, you acknowledge, however, that refusing or withdrawing your consent may affect your ability to participate in the Plan. For more information on the consequences of your refusal to consent or withdrawal of consent, you may contact the Stock Plan Administrator of the Company.

14. Language. If you have received this Agreement or any other document related to the Plan translated into a language other than English and if the translated version differs in meaning from the English version, the English version will control.

15. Electronic Delivery. The Company may, in its sole discretion, deliver any documents related to current or future participation in the Plan by electronic means. You hereby consent to receive such documents by electronic delivery and agree to participate in the Plan through an on-line or electronic system established and maintained by the Company or another third party designated by the Company. Signed documents delivered to either party via facsimile or in portable document format will have the same effect as an original, unless otherwise required by applicable law.

16. General.

(a) Nothing in this Agreement will be construed as: (1) constituting a commitment, agreement or understanding of any kind that the Company or any other Employer will continue your employment or other relationship with the Company; or (2) limiting or restricting either party's right to terminate your employment or other relationship.

(b) This Agreement shall be binding upon and inure to the benefit of the parties and their respective successors and permitted assigns. You may not assign any rights under this Agreement without the written consent of the Company, which it may withhold in its sole discretion; any such attempted assignment without the Company's written consent shall be void. The Company may assign its rights under this Agreement at any time upon notice to you.

(c) Notices under this Agreement must be in writing and delivered either by hand or by a reputable domestic or international carrier (postage prepaid and return receipt or proof of delivery requested), and, in the case of notices to the Company, addressed to its principal executive offices to the attention of the Stock Plan Administrator, and, in your case, addressed to your address as shown on the Employer's records.

(d) This Agreement shall be governed by and construed in accordance with the laws of the State of North Carolina without regard to the conflict of law provisions thereof, as if made and to be performed wholly within such State. For purposes of litigating any dispute that arises directly or indirectly from the relationship of the parties evidenced by the Award or this Agreement, the parties hereby submit to and consent to the exclusive jurisdiction of the State of North Carolina, agree that such litigation shall be conducted in the courts of Durham County, North Carolina, or the federal courts for the United States for the Middle District of North Carolina, and no other courts, where the Award of Restricted Stock is made and/or to be performed.

(e) If any provision of this Agreement is held to be invalid or unenforceable, such determination shall not affect the other provisions of the Agreement and the Agreement shall be construed as if the invalid or unenforceable provision were omitted and a valid and enforceable provision, as nearly comparable as possible, substituted in its place.

(f) Notwithstanding any prior award agreement between you and the Company under which Restricted Stock may have been awarded, this Agreement and the Plan set forth all of the promises, agreements and understandings between you

and Company relating to the Restricted Stock granted pursuant to this Agreement, constitutes the complete agreement between the parties regarding the Restricted Stock and replaces any prior oral or written communications regarding the same.

(g) Shares issued pursuant to this Award may be subject to such stop transfer orders and other restrictions as the Committee may deem advisable under applicable law or the rules and regulations of the U.S. Securities and Exchange Commission or any stock exchange or trading system upon which the common stock of the Company is listed, and the Committee may cause a legend or legends to be placed on any such certificates or the stock records of the Company to make appropriate reference to such restrictions.

(h) You agree that the Restricted Stock, even if later forfeited, serves as additional, valuable consideration for your obligations, if any, undertaken in any existing agreement between you and the Company and/or other Employer regarding confidential information, noncompetition, nonsolicitation or similar covenants.

(i) You acknowledge, represent and warrant to the Company, and agree with the Company, that (i) except for information provided in the Company's filings with the U.S. Securities and Exchange Commission and in the Company's current prospectus relating to the Plan, you have not relied and will not rely upon the Committee, the Company, an Employer or any employee or agent of the Company or an Employer in determining whether to accept the Restricted Stock, or in connection with any disposition of Shares obtained pursuant to the Restricted Stock Award, or with respect to any tax consequences related to the grant of the Restricted Stock or the disposition of Shares obtained pursuant to the Restricted Stock Award; and (ii) you will seek from your own professional advisors such investment, tax and other advice as you believe necessary.

(j) You acknowledge that you may incur a substantial tax liability as a result of vesting of the Restricted Stock. You assume full responsibility for all such consequences and the filing of all tax returns and related elections you may be required or find desirable to file. If you are required to make any valuation of Shares obtained pursuant to the Restricted Stock Award under any federal, state or other applicable tax law, and if the valuation affects any tax return or election of the Company or the Employer or affects the Company's financial statement reporting, you agree that the Company may determine the value and that you will observe any determination so made by the Company in all tax returns and elections filed by you.

(k) You acknowledge that copies of the Plan and Plan prospectus are available upon written or telephonic request to the Company's Stock Plan Administrator.

17. Severability. The provisions of this Agreement are severable and if any one or more provisions is determined to be illegal or otherwise unenforceable, in whole or in part, the remaining provisions shall nevertheless be binding and enforceable.

18. Nature of Grant. In accepting this grant, you acknowledge, understand and agree that:

(a) the Plan is established voluntarily by the Company, is discretionary in nature and may be modified, amended, suspended or terminated by the Company at any time, unless expressly provided otherwise in the Plan or the Agreement;

(b) the grant of the Restricted Stock is voluntary and does not create any contractual or other right to receive future grants of Restricted Stock, or benefits in lieu of Restricted Stock, even if Restricted Stock has been granted repeatedly in the past;

(c) all decisions with respect to future grants of Restricted Stock, if any, will be at the sole discretion of the Company;

(d) your participation in the Plan is voluntary;

(e) your participation in the Plan will not create a right to employment with the Company or the Employer and will not interfere with the ability of the Company, the Employer or any subsidiary or affiliate to terminate your employment or service relationship at any time;

(f) if you are employed by a non-U.S. entity and provide services outside the U.S., the Restricted Stock is an extraordinary item that does not constitute compensation of any kind for services of any kind rendered to your Employer, and they are outside the scope of your employment or service contract, if any, with your Employer;

(g) the grant of the Restricted Stock is not intended to replace any pension rights or compensation;

(h) the grant of the Restricted Stock is not part of normal or expected compensation or salary for any purposes, including, but not limited to, calculating any severance, resignation, termination, redundancy, dismissal, end-of-service payments, bonuses, long-service awards, pension or retirement or welfare benefits or similar payments;

(i) the grant of the Restricted Stock and your participation in the Plan will not be interpreted to form an employment or service contract or relationship with the Company, the Employer or any subsidiary or affiliate of the Company;

(j) the future value of the Restricted Stock is unknown and cannot be predicted with certainty;

(k) no claim or entitlement to compensation or damages shall arise from forfeiture of the Restricted Stock resulting from termination of your employment or service relationship by the Company or the Employer (for any reason whatsoever and whether or not later found to be invalid or in breach of employment laws in the jurisdiction where you are employed or the terms of your employment agreement, if any), and, in consideration of the grant of the Restricted Stock, to which you otherwise are not entitled, you irrevocably agree (i) never to institute any such claim against the Company, the Employer, or any subsidiary or affiliate of the Company, (ii) to waive your ability, if any, to bring any such claim, and (iii) to release the Company and the Employer and any subsidiary or affiliate from any such claim; if, notwithstanding the foregoing, any such claim is allowed by a court of competent jurisdiction, then, by participating in the Plan, you shall be deemed irrevocably to have agreed not to pursue such claim and agree to execute any and all documents necessary to request dismissal or withdrawal of such claims;

(l) the grant of the Restricted Stock and the benefits under the Plan, if any, will not automatically transfer to another company in the case of a merger, takeover, or transfer of liability;

(m) neither the Company, the Employer nor any subsidiary or affiliate of the Company shall be liable for any foreign exchange rate fluctuation between your local currency and the United States Dollar that may affect the value of the Restricted Stock or if any payments due to you pursuant to the subsequent sale of any Shares acquired upon the vesting of the Restricted Stock; and

(n) this award and any other award(s) granted under the Plan on the Grant Date are intended to fulfill any and all agreements, obligations or promises, whether legally binding or not, previously made by the Company or another Employer under the Plan to grant you the Restricted Stock or other rights to common stock of the Company. By signing this Agreement, you accept such awards, along with all prior awards received by you, in full satisfaction of any such agreement, obligation or promise.

19. No Advice Regarding Grant. The Company is not providing any tax, legal, or financial advice, nor is the Company making any recommendations regarding your participation in the Plan or sale of Shares. You are hereby advised to consult with your own personal tax, legal and financial advisors regarding your participation in the Plan before taking any action related to the Plan.

20. Compliance with Law. Notwithstanding any other provision of the Plan or this Agreement, unless there is an available exemption from any registration, qualification or other legal requirement applicable to the Restricted Stock, the Company shall not be required to deliver any shares of the Restricted Stock prior to the completion of any registration or qualification of the shares under any local, state, federal or foreign securities or exchange control law or under rulings or regulations of the U.S. Securities and Exchange Commission ("SEC") or of any other governmental regulatory body, or prior to obtaining any approval or other clearance from any local, state, federal or foreign governmental agency, which registration, qualification or approval the Company shall, in its absolute discretion, deem necessary or advisable. You understand that the Company is under no obligation to register or qualify the Restricted Stock with the SEC or any state or foreign securities commission or to seek approval or clearance from any governmental authority for the issuance of the Restricted Stock. Further, you agree that the Company shall have unilateral authority to amend the Plan and the Agreement without your consent to the extent necessary to comply with securities or other laws applicable to issuance of shares.

21. Waiver. You acknowledge that a waiver by the Company of breach of any provision of this Agreement shall not operate or be construed as a waiver of any other provision of this Agreement, or of any subsequent breach by you or any other participant.

22. Appendix. Notwithstanding any provisions in this Agreement, this Award shall be subject to any special terms and conditions set forth in any Appendix to this Agreement for your country to the extent that the Company determines that the application of such terms and conditions is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan. Moreover, if you relocate to or from one of the countries included on any such Appendix, the special terms and conditions for the country you are moving from and/or the country you are moving to will apply to you to the extent that the Company determines that the application of such terms and conditions is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan. If included, the Appendix is incorporated in and constitutes part of this Agreement.

23. Imposition of Other Requirements. The Company reserves the right to impose other requirements on your participation in the Plan, on the Restricted Stock and on any Shares acquired under the Plan, to the extent that the Company determines it is necessary or advisable in order to comply with local law or to facilitate the administration of the Plan, and to require you to sign any additional agreements or undertakings that may be necessary to accomplish the foregoing.

**Certification by Chief Executive Officer
pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted
pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Charles M. Swoboda, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cree, 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.

October 17, 2012

/s/ CHARLES M. SWOBODA

Charles M. Swoboda

Chairman, Chief Executive Officer and President

**Certification by Chief Financial Officer
pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted
pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Michael E. McDevitt, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cree, 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.

October 17, 2012

/s/ MICHAEL E. MCDEVITT

Michael E. McDevitt

Vice President and Interim Chief Financial Officer

**Certification by Chief Executive Officer
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 Cree, Inc. (the "Company") on Form 10-Q for the quarterly period ended September 23, 2012 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Charles M. Swoboda, Chairman, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

- 1 The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- 2 The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ CHARLES M. SWOBODA

Charles M. Swoboda

Chairman, Chief Executive Officer and President

October 17, 2012

This Certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed "filed" by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and shall not be incorporated by reference into any filing of the Company 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 Report, irrespective of any general incorporation language contained in such filing.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**Certification by Chief Financial Officer
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 Cree, Inc. (the "Company") on Form 10-Q for the quarterly period ended September 23, 2012 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael E. McDevitt, Vice President and Interim Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

- 1 The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- 2 The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MICHAEL E. MCDEVITT

Michael E. McDevitt

Vice President and Interim Chief Financial Officer

October 17, 2012

This Certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed "filed" by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and shall not be incorporated by reference into any filing of the Company 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 Report, irrespective of any general incorporation language contained in such filing.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.