

MoSys, Inc.
Form 10-Q
November 06, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended September 30, 2015

OR

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

For the transition period from _____ to _____

Commission file number 000-32929

MOSYS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
of Incorporation or organization)

77-0291941
(I.R.S. Employer
Identification Number)

3301 Olcott Street

Santa Clara, California, 95054

(Address of principal executive office and zip code)

(408) 418-7500

(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 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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

As of October 30, 2015, 65,495,715 shares of the Registrant's common stock, \$0.01 par value, were outstanding.

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MOSYS, INC.

FORM 10-Q

September 30, 2015

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****MOSYS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)****(In thousands, except par value)**

	September 30, 2015	December 31, 2014
ASSETS		
Current assets		
Cash and cash equivalents	\$ 1,585	\$ 3,110
Short-term investments	21,597	20,439
Accounts receivable, net	426	177
Inventories, net	1,264	881
Prepaid expenses and other	1,369	887
Total current assets	26,241	25,494
Long-term investments	2,269	2,245
Property and equipment, net	860	854
Goodwill	23,134	23,134
Other assets	756	899
Total assets	\$ 53,260	\$ 52,626
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 378	\$ 495
Accrued expenses and other	2,057	2,350
Total current liabilities	2,435	2,845
Long-term liabilities	249	241
Commitments and contingencies (Note 4)		
Stockholders' equity		
Preferred stock, \$0.01 par value; 20,000 shares authorized; none issued and outstanding		
Common stock, \$0.01 par value; 120,000 shares authorized; 65,496 shares and 49,793 shares issued and outstanding at September 30, 2015 and December 31, 2014, respectively	655	498
Additional paid-in capital	225,389	199,541
Accumulated other comprehensive loss	(3)	(10)
Accumulated deficit	(175,465)	(150,489)
Total stockholders' equity	50,576	49,540
Total liabilities and stockholders' equity	\$ 53,260	\$ 52,626

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

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MOSYS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

(Unaudited)

(In thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net revenue				
Product	\$ 565	\$ 437	\$ 1,288	\$ 1,993
Royalty and other	457	716	1,504	2,241
Total net revenue	1,022	1,153	2,792	4,234
Cost of net revenue	793	447	1,593	2,046
Gross profit	229	706	1,199	2,188
Operating expenses				
Research and development	8,793	7,507	21,475	20,993
Selling, general and administrative	1,547	1,689	4,711	4,976
Total operating expenses	10,340	9,196	26,186	25,969
Loss from operations	(10,111)	(8,490)	(24,987)	(23,781)
Other income, net	19	30	71	115
Loss before income taxes	(10,092)	(8,460)	(24,916)	(23,666)
Income tax provision	13	23	60	65
Net loss	\$ (10,105)	\$ (8,483)	\$ (24,976)	\$ (23,731)
Other comprehensive income (loss), net of tax:				
Net unrealized gains (losses) on available-for-sale securities	6	(17)	7	(20)
Comprehensive loss	\$ (10,099)	\$ (8,500)	\$ (24,969)	\$ (23,751)
Net loss per share				
Basic and diluted	\$ (0.15)	\$ (0.17)	\$ (0.41)	\$ (0.48)
Shares used in computing net loss per share				
Basic and diluted	65,317	49,634	61,486	49,441

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

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MOSYS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

	Nine Months Ended September 30,	
	2015	2014
Cash flows from operating activities:		
Net loss	\$ (24,976)	\$ (23,731)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	466	313
Stock-based compensation	2,864	3,596
Amortization of intangible assets	293	750
Changes in assets and liabilities:		
Accounts receivable	(249)	(27)
Inventories	(383)	(190)
Prepaid expenses and other assets	(624)	357
Accounts payable	(238)	(118)
Accrued expenses and other liabilities	(275)	339
Net cash used in operating activities	(23,122)	(18,711)
Cash flows from investing activities:		
Purchases of property and equipment	(369)	(289)
Proceeds from sales and maturities of marketable securities	34,172	32,985
Purchases of marketable securities	(35,347)	(15,859)
Net cash (used in) provided by investing activities	(1,544)	16,837
Cash flows from financing activities:		
Proceeds from the sale of common stock, net of issuance costs	21,368	
Proceeds from issuance of common stock	1,773	2,195
Net cash provided by financing activities	23,141	2,195
Net increase (decrease) in cash and cash equivalents	(1,525)	321
Cash and cash equivalents at beginning of period	3,110	4,364
Cash and cash equivalents at end of period	\$ 1,585	\$ 4,685

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

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MOSYS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. The Company and Summary of Significant Accounting Policies

The Company

MoSys, Inc. (the Company) was incorporated in California in September 1991, and reincorporated in September 2000 in Delaware. The Company's strategy and primary business objective is to be an IP-rich fabless semiconductor company focused on the development and sale of integrated circuit (IC) products. Prior to 2011, the Company's primary business activities were designing, developing, marketing and licensing high-performance semiconductor memory and high-speed parallel and serial interface, or SerDes, intellectual property (IP) used by the semiconductor industry and communications, networking and storage equipment manufacturers. Since 2011, the Company has developed two IC product lines under the Bandwidth Engine and LineSpeed product names. Bandwidth Engine ICs combine the Company's proprietary high-density embedded memory with its high-speed 10 gigabits per second and higher interface technology. The LineSpeed IC product line is comprised of non-memory based, high-speed SerDes devices with gearbox or retimer functionality that convert lanes of data received on line cards or by optical modules into different configurations and/or ensure signal integrity. Both product lines are being marketed to networking and communications systems companies. The Company's future success and ability to achieve and maintain profitability depends on its success in developing a market for its ICs.

The accompanying condensed consolidated financial statements of the Company have been prepared without audit in accordance with the rules and regulations of the Securities and Exchange Commission (SEC). The condensed consolidated balance sheet at December 31, 2014 has been derived from the audited consolidated financial statements at that date. Certain information and disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) have been condensed or omitted in accordance with these rules and regulations. The information in this report should be read in conjunction with the Company's consolidated financial statements and notes thereto included in its most recent annual report on Form 10-K filed with the SEC.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary to summarize fairly the Company's financial position, results of operations and cash flows for the interim periods presented. The operating results for the three and nine months ended September 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015 or for any other future period.

Basis of Presentation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation. The Company's fiscal year is the calendar year.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses recognized during the reported period. Actual results could differ from those estimates.

Reclassification

Certain prior year amounts have been reclassified to conform to the current year presentation. Previously reported intangible asset amounts have been included in the other assets line item of the condensed consolidated balance sheets. The amounts for the prior periods have been reclassified to be consistent with the current year presentation and have no impact on previously reported total assets, total stockholders' equity or net loss.

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Cash Equivalents and Investments

The Company has invested its excess cash in money market accounts, certificates of deposit, commercial paper, corporate debt, government-sponsored enterprise bonds and municipal bonds and considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Investments with original maturities greater than three months and remaining maturities less than one year are classified as short-term investments. Investments with remaining maturities greater than one year are classified as long-term investments. Management generally determines the appropriate classification of securities at the time of purchase. All securities are classified as available-for-sale. The Company's available-for-sale short-term and long-term investments are carried at fair value, with the unrealized holding gains and losses reported in accumulated other comprehensive loss. Realized gains and losses and declines in the value judged to be other than temporary are included in the other income, net line item in the condensed consolidated statements of operations and comprehensive loss. The cost of securities sold is based on the specific identification method.

Fair Value Measurements

The Company measures the fair value of financial instruments using a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels:

Level 1 Inputs used to measure fair value are unadjusted quoted prices that are available in active markets for the identical assets or liabilities as of the reporting date.

Level 2 Pricing is provided by third party sources of market information obtained through the Company's investment advisors, rather than models. The Company does not adjust for, or apply, any additional assumptions or estimates to the pricing information it receives from advisors. The Company's Level 2 securities include cash equivalents and available-for-sale securities, which consisted primarily of certificates of deposit, corporate debt, and government agency and municipal debt securities from issuers with high-quality credit ratings. The Company's investment advisors obtain pricing data from independent sources, such as Standard & Poor's, Bloomberg and Interactive Data Corporation, and rely on comparable pricing of other securities because the Level 2 securities are not actively traded and have fewer observable transactions. The Company considers this the most reliable information available for the valuation of the securities.

Level 3 Unobservable inputs that are supported by little or no market activity and reflect the use of significant management judgment are used to measure fair value. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions. The determination of fair value for Level 3 investments and other financial instruments involves the most management judgment and subjectivity.

Allowance for Doubtful Accounts

The Company establishes an allowance for doubtful accounts to ensure that its trade receivables balances are not overstated due to uncollectability. The Company performs ongoing customer credit evaluations within the context of the industry in which it operates and

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generally does not require collateral from its customers. A specific allowance of up to 100% of the invoice value is provided for any problematic customer balances. Delinquent account balances are written off after management has determined that the likelihood of collection is remote. The Company grants credit only to customers deemed creditworthy in the judgment of management. There was no allowance for doubtful accounts receivable at either September 30, 2015 or December 31, 2014.

Inventory

Inventories are valued at the lower of cost or market. Charges for obsolete and slow moving inventories are recorded based upon an analysis of specific identification of obsolete inventory items and quantification of slow moving inventory items. For slow moving inventory, this analysis compares the quantity of inventory on hand to the projected sales of such inventory items. As a result of this analysis, we record an estimated charge for slow moving inventory in the form of an inventory reserve that increases cost of goods sold and decreases gross profit. When the obsolete or slow moving inventory subsequently experiences increased sales and inventory that was previously impaired is sold, cost of goods sold is decreased and gross profit is increased. Charges for the three and nine months ended September 30, 2015 were \$0.2 million.

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Revenue Recognition

General

The Company generates revenue from the sales of IC products and licensing of its IP. The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery or performance has occurred, the sales price is fixed or determinable, and collectability is reasonably assured. Evidence of an arrangement generally consists of signed agreements or customer purchase orders.

IC products

The Company sells products both directly to customers, as well as through distributors. Revenue from sales directly to customers is generally recognized at the time of shipment. The Company may record an estimated allowance, at the time of shipment, for future returns and other charges against revenue consistent with the terms of sale. IC product revenue and costs relating to sales made through distributors with rights of return or stock rotation are generally deferred until the distributors sell the product to end customers due to the Company's inability to estimate future returns and credits to be issued. Distributors are generally able to return up to 10% of their purchases for slow, non-moving or obsolete inventory for credit every six months. At the time of shipment to distributors, an account receivable for the selling price is recorded, as there is a legally enforceable right to receive payment, and inventory is relieved, as legal title to the inventory is transferred upon shipment. Revenues are recognized upon receiving notification from the distributors that products have been sold to end customers. Distributors provide information regarding products and quantity, end customer shipments and remaining inventory on hand. The deferred margin recorded on sales to distributors where the product has not sold through to end customers is included in the accrued expenses and other line item in the condensed consolidated balance sheets.

Royalty

The Company's licensing contracts typically also provide for royalties based on the licensees' use of the Company's memory technology in their currently shipping commercial products. The Company recognizes royalties in the quarter in which it receives the licensee's report.

Licensing

Licensing revenue consists of fees earned from license agreements, development services and support and maintenance. For stand-alone license agreements or license deliverables in multi-deliverable arrangements that do not require significant development, modification or customization, revenues are recognized when all revenue recognition criteria have been met. Delivery of the licensed technology is typically the final revenue recognition criterion met, at which time revenue is recognized. If any of the criteria are not met, revenue recognition is deferred until such time as all criteria have been met. Support and maintenance revenue is recognized ratably over the period during which the obligation exists, typically 12 months. There was no licensing revenue for the three or nine months ended September 30, 2015. Licensing revenue was less than \$0.1 million for each of the three and nine months ended September 30, 2014.

Cost of Net Revenue

Cost of net revenue consists primarily of direct and indirect costs of IC product sales and engineering personnel costs directly related to maintenance and support services specified in licensing agreements. Maintenance and support typically includes engineering support to assist in the commencement of production of a licensee's products.

Goodwill

The Company reviews goodwill for impairment on an annual basis or whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable. The Company first assesses qualitative factors to determine whether it is more-likely-than-not that the fair value of the reporting unit is less than the carrying amount as a basis for determining whether it is necessary to perform the two-step impairment test. If the qualitative assessment warrants further analysis, the Company compares the fair value of the reporting unit to its carrying value. The fair value of the reporting unit is determined using the market approach. If the fair value of the reporting unit exceeds the carrying value of net assets of the reporting unit, goodwill is not impaired, and the Company is not required to perform further testing. If the carrying value of the reporting unit's goodwill exceeds its implied fair value, then the Company must record an impairment charge equal to the difference. The Company has determined that it has a single reporting unit for purposes of performing its goodwill impairment test. As the Company uses the market approach to assess impairment in the second step of the analysis, the price of its common stock is an important component of the fair value calculation. If the Company's stock price continues to experience significant price and volume fluctuations, this will impact the fair value of the reporting unit, which can lead to potential impairment in future periods. The Company performed step one of the annual impairment test in September 2015, and concluded no factors indicated impairment of goodwill. As of September 30, 2015, the Company had not identified any factors to indicate there was an impairment of its goodwill and determined that no additional impairment analysis was required.

Table of Contents*Per Share Amounts*

Basic net loss per share is computed by dividing net loss for the period by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per share gives effect to all potentially dilutive common shares outstanding during the period. Potentially dilutive common shares consist of incremental shares of common stock issuable upon the exercise of stock options, vesting of stock awards and purchases under the employee stock purchase plan. As of September 30, 2015 and 2014, stock awards to purchase approximately 9,322,000 and 10,190,000 shares, respectively, were excluded from the computation of diluted net loss per share as their inclusion would be anti-dilutive.

Comprehensive Loss

Comprehensive loss includes unrealized gains and losses on available-for-sale securities. Realized gains and losses on available-for-sale securities are reclassified from accumulated other comprehensive loss and included in other income, net in the condensed consolidated statements of operations and comprehensive loss. All amounts recorded in the three and nine months ended September 30, 2015 and 2014 were not considered significant.

Note 2: Fair Value of Financial Instruments

The estimated fair values of financial instruments outstanding were (in thousands):

	Cost	September 30, 2015		Fair Value
		Unrealized Gains	Unrealized Losses	
Cash and cash equivalents	\$ 1,585	\$	\$	\$ 1,585
Short-term investments:				
U.S. government-sponsored enterprise bonds	\$ 8,439	\$ 2	\$ (1)	\$ 8,440
Corporate notes	11,924		(3)	11,921
Municipal bonds	996			996
Certificates of deposit	240			240
Commercial paper				
Total short-term investments	\$ 21,599	\$ 2	\$ (4)	\$ 21,597
Long-term investments:				
Corporate notes	2,270		(1)	2,269
Total long-term investments	\$ 2,270	\$	\$ (1)	\$ 2,269

	Cost	December 31, 2014		Fair Value
		Unrealized Gains	Unrealized Losses	
Cash and cash equivalents	\$ 3,110	\$	\$	\$ 3,110
Short-term investments:				
U.S. government-sponsored enterprise bonds	\$ 1,250	\$	\$	\$ 1,250
Municipal bonds	841			841

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Corporate notes	15,921	2	(6)	15,917
Certificates of deposit	2,430	1		2,431
Total short-term investments	\$ 20,442	\$ 3	\$ (6)	\$ 20,439
Long-term investments:				
U.S. government-sponsored enterprise bonds	\$ 1,000	\$	\$ (2)	\$ 998
Corporate notes	1,252		(5)	1,247
Total long-term investments	\$ 2,252	\$	\$ (7)	\$ 2,245

The estimated fair values of available-for-sale securities with unrealized losses were (in thousands):

	September 30, 2015		
	Cost	Unrealized Losses	Fair Value
Short-term investments:			
U.S. government-sponsored enterprise bonds	\$ 3,363	\$ (1)	\$ 3,362
Corporate notes	7,461	(3)	7,458
Total short-term investments	\$ 10,824	\$ (4)	\$ 10,820
Long-term investments:			
Corporate notes	2,270	(1)	2,269
Total long-term investments	\$ 2,270	\$ (1)	\$ 2,269

	December 31, 2014		
	Cost	Unrealized Losses	Fair Value
Short-term investments:			
Corporate notes	\$ 13,006	\$ (6)	\$ 13,000
Total short-term investments	\$ 13,006	\$ (6)	\$ 13,000
Long-term investments:			
U.S. government-sponsored enterprise bonds	\$ 1,000	\$ (2)	\$ 998
Corporate notes	1,252	(5)	1,247
Total long-term investments	\$ 2,252	\$ (7)	\$ 2,245

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As of September 30, 2015 and December 31, 2014, all of the available-for-sale securities with unrealized losses had been in a loss position for less than 12 months.

Cost and fair value of investments based on two maturity groups were (in thousands):

	September 30, 2015					Fair Value
	Cost	Unrealized Gains		Unrealized Losses		
Due within 1 year	\$ 21,599	\$ 2		\$ (4)		\$ 21,597
Due in 1-2 years	2,270			(1)		2,269
Total	\$ 23,869	\$ 2		\$ (5)		\$ 23,866

	December 31, 2014					Fair Value
	Cost	Unrealized Gains		Unrealized Losses		
Due within 1 year	\$ 20,442	\$ 3		\$ (6)		\$ 20,439
Due in 1-2 years	2,252			(7)		2,245
Total	\$ 22,694	\$ 3		\$ (13)		\$ 22,684

The following table represents the Company's fair value hierarchy for its financial assets (cash equivalents and investments) as of September 30, 2015 and December 31, 2014 (in thousands):

	September 30, 2015				
	Fair Value	Level 1	Level 2	Level 3	
Money market funds	\$ 203	\$ 203			\$
U.S. government-sponsored enterprise bonds	8,440		8,440		
Corporate notes	14,190		14,190		
Municipal bonds	996		996		
Certificates of deposit	405		405		
Commercial paper	650		650		
Total assets	\$ 24,884	\$ 203	\$ 24,681		\$

	December 31, 2014				
	Fair Value	Level 1	Level 2	Level 3	
Money market funds	\$ 1,837	\$ 1,837			\$
U.S. government-sponsored enterprise bonds	2,248		2,248		
Municipal bonds	1,243		1,243		
Corporate notes	17,164		17,164		
Certificates of deposit	2,676		2,676		
Total assets	\$ 25,168	\$ 1,837	\$ 23,331		\$

There were no transfers in or out of Level 1 and Level 2 securities during the three or nine months ended September 30, 2015 and 2014.

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	September 30, 2015	December 31, 2014
	(in thousands)	
Inventories:		
Work-in-process	\$ 1,214	\$ 651
Finished goods	50	230
	\$ 1,264	\$ 881

Identifiable intangible assets relating to business combinations and a patent license were (dollar amounts in thousands):

		September 30, 2015		
	Life (years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Developed technology	3-5	\$ 9,240	\$ 9,240	\$
Patent license	7	780	418	362
Total		\$ 10,020	\$ 9,658	\$ 362

		December 31, 2014		
	Life (years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Developed technology	3-5	\$ 9,240	\$ 9,031	\$ 209
Patent license	7	780	334	446
Total		\$ 10,020	\$ 9,365	\$ 655

Intangible assets acquired in business combinations, referred to as purchased intangible assets, are accounted for based on the fair value of assets purchased and are amortized over the period in which economic benefit is estimated to be received. The net carrying value of identifiable assets has been included in the other assets line item in the condensed consolidated balance sheets. Amortization expense has been included in research and development expense in the condensed consolidated statements of operations and comprehensive loss. The estimated aggregate amortization expense to be recognized in future years is less than \$0.1 million for the remainder of 2015 and \$0.1 million annually for 2016 through 2018.

Note 4. Commitments and Contingencies**Indemnification**

In the ordinary course of business, the Company enters into contractual arrangements under which it may agree to indemnify the counterparties from any losses incurred relating to breach of representations and warranties, failure to perform certain covenants, or claims and losses arising from certain events as outlined within the particular contract, which may include, for example, losses arising from litigation or claims relating to past performance. Such indemnification clauses may not be subject to maximum loss clauses. The Company has also entered into

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indemnification agreements with its officers and directors. No material amounts were reflected in the Company's condensed consolidated financial statements for the three or nine months ended September 30, 2015 or 2014 related to these indemnifications.

The Company has not estimated the maximum potential amount of indemnification liability under these agreements due to the limited history of prior claims and the unique facts and circumstances applicable to each particular agreement. To date, the Company has not made any material payments related to these indemnification agreements.

Legal Matters

The Company is not a party to any material legal proceeding that the Company believes is likely to have a material adverse effect on its consolidated financial position or results of operations. From time to time the Company may be subject to legal proceedings and claims in the ordinary course of business. These claims, even if not meritorious, could result in the expenditure of significant financial resources and diversion of management efforts.

Table of Contents**Note 5. Business Segments, Concentration of Credit Risk and Significant Customers**

The Company operates in one business segment and uses one measurement of profitability for its business. Net revenue attributed to the United States and to all foreign countries is based on the geographical location of the customer.

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, cash equivalents, short-term and long-term investments and accounts receivable. Cash, cash equivalents and short-term and long term investments are deposited with high credit-quality institutions.

The Company recognized revenue from licensing of its technologies and shipment of ICs to customers by geographical location as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
United States	\$ 507	\$ 311	\$ 1,233	\$ 1,094
Taiwan	329	485	1,065	1,358
Japan	177	356	431	1,755
Rest of world	9	1	63	27
Total net revenue	\$ 1,022	\$ 1,153	\$ 2,792	\$ 4,234

Customers who accounted for at least 10% of total net revenue were:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Customer A	36%	*	27%	*
Customer B	32%	40%	37%	31%
Customer C	14%	27%	12%	37%
Customer D	*	10%	10%	11%

*Represents less than 10%

One customer accounted for 76% of net accounts receivable at September 30, 2015. Three customers accounted for 97% of net accounts receivable at December 31, 2014.

Note 6. Income Tax Provision

The Company determines deferred tax assets and liabilities based upon the differences between the financial statement and tax bases of the Company's assets and liabilities using tax rates in effect for the year in which the Company expects the differences to affect taxable income. A valuation allowance is established for any deferred tax assets for which it is more likely than not that all or a portion of the deferred tax assets will not be realized.

The Company files U.S. federal and state and foreign income tax returns in jurisdictions with varying statutes of limitations. 2004 through 2014 tax years generally remain subject to examination by federal, state and foreign tax authorities. As of September 30, 2015, the Company has not recorded any liability for unrecognized tax benefits related to uncertain tax positions.

Note 7. Stock-Based Compensation

The expense relating to stock options is recognized on a straight-line basis over the requisite service period, usually the vesting period, based on the grant-date fair value. The unamortized compensation cost, net of expected forfeitures, as of September 30, 2015 was \$2.9 million related to stock options and is expected to be recognized as expense over a weighted average period of approximately 2.2 years. The expense related to restricted stock units (RSUs) is recognized over a three-to-five year vesting period and is based on the fair value of the underlying stock on the dates of grant. The unamortized compensation cost, net of expected forfeitures, as of September 30, 2015 was \$0.7 million related to RSUs and is expected to be recognized as expense over a weighted average period of approximately 1.6 years.

The Company presents the tax benefits resulting from tax deductions in excess of the compensation cost recognized from the exercise of stock options as financing cash flows in the condensed consolidated statements of cash flows. For the three and nine months ended September 30, 2015 and 2014, there were no such tax benefits associated with the exercise of stock options due to the Company's loss positions.

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The fair value of the Company's share-based payment options for the three and nine months ended September 30, 2015 and 2014 was estimated on the grant dates using the Black-Scholes valuation option-pricing model with the following assumptions:

Employee stock options:	Three Months Ended September 30,		Nine Months Ended September 30,			
	2015	2014	2015		2014	
Risk-free interest rate	1.4%	1.3% - 1.7%	0.6%	1.7%	1.3%	1.7%
Volatility	59.3%	53.7% - 55.6%	55.7%	59.3%	53.7%	57.5%
Expected life (years)	4.0	4.0-5.0	4.0-5.0		4.0-5.0	
Dividend yield	0%	0%	0%		0%	

The risk-free interest rate was derived from the Daily Treasury Yield Curve Rates as published by the U.S. Department of the Treasury as of the grant date for terms equal to the expected terms of the options. The expected volatility was based on the historical volatility of the Company's stock price over the expected term of the options. The expected term of options granted was derived from historical data based on employee exercises and post-vesting employment termination behavior. A dividend yield of zero is applied because the Company has never paid dividends and has no intention to pay dividends in the near future.

The stock-based compensation expense recorded is adjusted based on estimated forfeiture rates. An annualized forfeiture rate has been used as a best estimate of future forfeitures based on the Company's historical forfeiture experience. The stock-based compensation expense will be adjusted in later periods if the actual forfeiture rate is different from the estimate.

Common Stock Options and Restricted Stock

A summary of the option and RSU activity under the Company's Amended and Restated 2000 Stock Option and Equity Incentive Plan (Amended 2000 Plan) and Amended and Restated 2010 Equity Incentive Plan (Amended 2010 Plan), referred to collectively as the Plans, is presented below (in thousands, except exercise price):

	Available for Grant	Number of Shares	Options Outstanding	
				Weighted Average Exercise Prices
Balance at December 31, 2014	1,760	5,994	\$	3.87
Additional shares authorized under the Amended 2010 Plan	500			
Restricted stock units cancelled	6			
Options granted	(1,323)	1,323	\$	2.05
Options cancelled	153	(153)	\$	5.00
Options exercised		(22)	\$	1.60
Options expired	(78)		\$	5.79

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Balance at March 31, 2015	1,018	7,142	\$	3.52
Additional shares authorized under the Amended 2010 Plan				
Restricted stock units cancelled	10			
Options granted	(95)	95	\$	2.04
Options cancelled	128	(128)	\$	4.00
Options exercised		(40)	\$	1.65
Options expired	(15)		\$	4.35
Balance at June 30, 2015	1,046	7,069	\$	3.50
Additional shares authorized under the Amended 2010 Plan				
Restricted stock units cancelled	4			
Options granted	(120)	120	\$	1.70
Options cancelled	203	(203)	\$	2.90
Options exercised		(20)	\$	1.65
Options expired	(121)		\$	2.26
Balance at September 30, 2015	1,012	6,966	\$	3.49

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The Company also has awarded options to new employees outside of the Plans and may continue to do so, as material inducements to the acceptance of employment with the Company, as permitted under the Listing Rules of the Nasdaq Stock Market. These grants must be approved by the compensation committee of the board of directors, a majority of the independent directors or, below a specified share level, by an authorized executive officer.

A summary of the inducement grant option activity is presented below (in thousands, except exercise price):

	Number of Shares	Options Outstanding Weighted Average Exercise Prices
Balance at December 31, 2014 and March 31, 2015	2,233	\$ 3.68
Granted		
Cancelled	(2)	\$ 3.86
Exercised	(512)	\$ 1.55
Expired	(16)	\$ 1.55
Balance at June 30, 2015	1,703	\$ 4.34
Granted		
Cancelled	(28)	\$ 3.57
Exercised	(6)	\$ 1.50
Expired		\$
Balance at September 30, 2015	1,669	\$ 4.36

A summary of RSU activity under the Plans is presented below (in thousands, except for fair value):

	Number of Shares	Weighted Average Grant-Date Fair Value
Non-vested shares at December 31, 2014	394	\$ 4.61
Vested	(120)	\$ 4.60
Cancelled	(6)	\$ 4.60
Non-vested shares at March 31, 2015	268	\$ 4.61
Vested	(3)	\$ 4.46
Cancelled	(10)	\$ 4.62
Non-vested shares at June 30, 2015	255	\$ 4.60
Vested	(8)	\$ 4.46
Cancelled	(4)	\$ 4.62
Non-vested shares at September 30, 2015	243	\$ 4.76

The total intrinsic value of the restricted stock units outstanding as of September 30, 2015 was \$0.4 million.

The following table summarizes significant ranges of outstanding and exercisable options as of September 30, 2015 (in thousands, except contractual life and exercise price):

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Range of Exercise Price	Options Outstanding				Options Exercisable		
	Number Outstanding	Weighted Average Remaining Contractual Life (in Years)	Weighted Average Exercise Price	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price	Aggregate Intrinsic Value
\$1.68 - \$2.24	1,612	9.19	\$ 2.01	261	\$ 2.05		
\$2.25 - \$3.15	1,429	2.94	\$ 2.97	1,196	\$ 2.96		
\$3.16 - \$3.80	1,483	2.90	\$ 3.42	1,239	\$ 3.43		
\$3.81 - \$4.34	1,435	3.33	\$ 3.96	1,222	\$ 3.96		
\$4.35 - \$4.69	1,386	5.58	\$ 4.47	974	\$ 4.46		
\$4.70 - \$6.11	1,290	2.01	\$ 5.56	1,217	\$ 5.57		
\$1.68 - \$6.11	8,635	4.45	\$ 3.66	6,109	\$ 3.98	\$	
Vested and expected to vest	8,415	4.35	\$ 3.69			\$	
Exercisable	6,109	3.13	\$ 3.98			\$	

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The aggregate intrinsic value of employee stock options exercised during the nine months ended September 30, 2015 and 2014 was approximately \$0.3 million and \$0.7 million, respectively.

Employee Stock Purchase Plan

In June 2010, the Company's stockholders approved the 2010 Employee Stock Purchase Plan (ESPP). A total of 2,000,000 shares of common stock were initially reserved for issuance under the ESPP in 2010. On September 1, 2010, the Company commenced the first offering period under the ESPP. On April 16, 2015, the board of directors approved an amendment to the ESPP to increase the number of shares reserved for issuance by 2,000,000 shares, subject to stockholder approval. At the Annual Meeting of Stockholders held on May 26, 2015, the Company's stockholders approved the increase. The ESPP, which is intended to qualify under Section 423 of the Internal Revenue Code, is administered by the board of directors or the compensation committee of the board of directors. The ESPP provides that eligible employees may purchase up to \$25,000 worth of the Company's common stock annually over the course of two six-month offering periods. The purchase price to be paid by participants is 85% of the price per share of the Company's common stock either at the beginning or the end of each six-month offering period, whichever is less.

On February 28, 2015, approximately 339,000 shares of common stock were issued at an aggregate purchase price of \$518,000 under the ESPP. On August 31, 2015, approximately 268,000 shares of common stock were issued at an aggregate purchase price of \$339,000 under the ESPP. As of September 30, 2015, there were approximately 2.2 million shares authorized and unissued under the ESPP.

Note 8. Stockholders' Equity

On March 4, 2015, the Company sold 14,375,000 shares of common stock in an equity offering and raised approximately \$21.4 million, net of transaction expenses. Two of the Company's executive officers between them purchased a total of 406,250 shares at the public offering price.

Note 9. Related Party Transactions

In February 2012, the Company entered into a strategic development and marketing agreement with Credo Semiconductor (Hong Kong) Ltd. (Credo), a privately-funded, fabless semiconductor company, to develop, market and sell integrated circuits. Two of the Company's executive officers between them loaned a total of \$250,000 to Credo for a portion of the seed funding needed by Credo to commence its integrated circuit design efforts. These loans may be converted into minority equity interests in Credo. The strategic development and marketing agreement, as amended, calls for the Company to make payments to Credo upon Credo achieving certain development and verification milestones towards the development of IC products and provides the Company with exclusive sales and marketing rights for such IC products. As of September 30, 2015, the Company has paid Credo \$4.7 million for achievement of development milestones, as well as for mask costs and wafer purchases from third-party vendors. All amounts incurred have been recorded as research and development expenses. Currently, under the strategic development and marketing agreement, the Company is entitled to a remaining reimbursement amount of \$3.6 million of development costs based on payments made to Credo to date. This amount is subject to increase as additional payments are made to Credo. The reimbursement will be funded by the gross profits earned by the Company from the sale of the products, with the initial gross profits being primarily applied to reimbursing the Company for these development payments and a portion paid to Credo. Once the full amount has been reimbursed, the gross

profits will be shared equally by the Company and Credo.

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the accompanying condensed consolidated financial statements and notes included in this report. This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which include, without limitation, statements about the market for our technology, our strategy, competition, expected financial performance and capital raising efforts, all information disclosed under Item 3 of this Part I, and other aspects of our business identified in our most recent annual report on Form 10-K filed with the Securities and Exchange Commission on March 13, 2015 and in other reports that we file from time to time with the Securities and Exchange Commission. Any statements about our business, financial results, financial condition and operations contained in this Form 10-Q that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes, anticipates, expects, intends, plans, projects, or similar expressions are intended to identify forward-looking statements. Our actual results could differ materially from those expressed or implied by these forward-looking statements as a result of various factors, including the risk factors described below in Company Overview, Liquidity and Capital Resources; Changes in Financial Condition, Risk Factors and elsewhere in this report and under Item 1A of our annual report on Form 10-K for the year ended December 31, 2014. We undertake no obligation to update publicly any forward-looking statements for any reason, except as required by law, even as new information becomes available or events occur in the future.

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Company Overview

Our strategy and primary business objective is to become a fabless semiconductor company focused on the development and sale of integrated circuits, or ICs, for the high-speed networking, communications, storage and computing markets. Our solutions deliver time-to-market, performance, power, area and economic benefits for system original equipment manufacturers, or OEMs. We have developed two families of ICs under the Bandwidth Engine® and LineSpeed product names. Bandwidth Engine ICs combine our proprietary 1T-SRAM® high-density embedded memory, integrated macro functions and high-speed serial interface, or SerDes, I/O, with our intelligent access technology and a highly efficient interface protocol. The LineSpeed IC product line is comprised of non-memory, high-speed SerDes I/O devices with gearbox and retimer functionality, which convert lanes of data received on line cards or by optical modules into different configurations and/or ensure signal integrity. Certain SerDes products have been developed under a strategic development and marketing agreement with Credo Semiconductor Ltd., or Credo, to whom we have paid a total of \$4.7 million for the development of these new products. The initial gross profits earned by us from the sale of Credo developed products will be primarily applied to reimbursing us for these development payments and a portion will be paid to Credo. Once a remaining \$3.6 million of this amount has been reimbursed, all gross profits from the sale of the Credo-developed products worldwide will be shared equally by Credo and us.

Historically, our primary business was the design, development, marketing, sale and support of differentiated intellectual property, or IP, including embedded memory and high-speed parallel and SerDes I/O used in advanced systems-on-chips, or SoCs. Currently, we are focused on developing differentiated IP-rich IC products and are dedicating all our research and development, marketing and sales budget to these IC products.

Our future success and ability to achieve and maintain profitability will be dependent on the marketing and sales of our IC products into networking, communications and other markets requiring high-bandwidth memory access. We are currently supporting approximately 25 existing customers, with whom we have achieved over 70 design-wins, which reflects broadening acceptance of our products. We define a design win as the point at which a customer has made a commitment to build a board against the fixed schematic for his system, and this board will utilize our IC Products. We continue to actively pursue additional design wins for the use of our ICs in networking and communication equipment. Our design wins represent the potential for significant future revenues. With limited history to date, however, we cannot estimate how much revenue each design win is likely to generate, or how much revenue all of these (and future design wins) are likely to generate. For example, our first design wins from 2012 and 2013 are starting to ramp into production, and, while we cannot predict how steep these ramps might be, we expect our revenues from them to grow in successive periods over the next few years. Another factor limiting our ability to predict future revenue levels is that, although we have established initial pricing of our IC products ordered to date, longer-term volume prices will be subject to negotiations with our customers and may vary substantially from these initial prices.

Sources of Revenue

Product. Product revenue is generally recognized at the time of shipment to our customers. An estimated allowance may be recorded, at the time of shipment, for future returns and other charges against revenue consistent with the terms of sale. IC product revenue and costs relating to sales made through distributors with rights of return and stock rotation are deferred until the distributors sell the product to end customers due to our inability to estimate future returns and credits to be issued. At the time of shipment to distributors, an account receivable for the selling price is

recorded, as there is a legally enforceable right to receive payment, inventory is relieved, as legal title to the inventory is transferred upon shipment, and the associated deferred margin is recorded as deferred revenues in the condensed consolidated balance sheets. Revenues are recognized upon receiving notification from the distributors that products have been sold to end customers.

Royalty. Royalty revenue represents amounts earned under provisions in our memory licensing contracts that require our licensees to report royalties and make payments at a stated rate based on actual units manufactured or sold by licensees for products that include our memory IP. Our license agreements require the licensee to report the manufacture or sale of products that include our technology after the end of the quarter in which the sale or manufacture occurs, and we recognize royalties in the quarter in which we receive the licensee's report. The timing and level of royalties are difficult to predict. They depend on the licensee's ability to market, produce and sell products incorporating our technology.

Licensing. Licensing revenue, which is included in royalty and other revenue, consists of fees earned from license agreements, development services, and support and maintenance. Our licensing revenue consists primarily of fees for providing circuit design, layout and design verification and granting licenses to customers that embed our technology into their products. The vast majority of our contracts allow for milestone billing based on work performed. We currently have no active license agreements generating licensing revenue.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires us to make certain estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis we make these estimates based on our historical experience and on assumptions that we consider reasonable under the circumstances. Actual results may differ from these estimates, and reported results could differ under different assumptions or conditions. Our significant accounting policies and estimates are disclosed in Note 1 of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2014. As of September 30, 2015, there have been no material changes to our significant accounting policies and estimates.

Table of Contents**Results of Operations***Net Revenue.*

		September 30, 2015	September 30, 2014	Change 2014 to 2015	
		(dollar amounts in thousands)			
Product three months ended	\$	565	\$ 437	\$ 128	29%
Percentage of total net revenue		55%	38%		
Product nine months ended	\$	1,288	\$ 1,993	\$ (705)	(35)%
Percentage of total net revenue		46%	47%		

Product revenue increased for the three months ended September 30, 2015 compared with the same period of 2014 primarily due to higher shipment volumes. The decrease in product revenue for the nine months ended September 30, 2015 compared with the same period in 2014 is primarily due to lower distributor sales revenue and lower shipment volumes. Additionally, product revenue for the first nine months of 2014 included a reversal of \$0.4 million of sales return reserves, which had been recorded in prior periods.

		September 30, 2015	September 30, 2014	Change 2014 to 2015	
		(dollar amounts in thousands)			
Royalty and other three months ended	\$	457	\$ 716	\$ (259)	(36)%
Percentage of total net revenue		45%	62%		
Royalty and other nine months ended	\$	1,504	\$ 2,241	\$ (737)	(33)%
Percentage of total net revenue		54%	53%		

Royalty and other revenue include revenues generated from licensing agreements. Royalty and other revenue decreased primarily due to a decrease in shipment volumes by licensees whose products incorporate our licensed IP and a decrease in revenue recognized from residual licensing agreements entered into in prior years.

Cost of Net Revenue and Gross Profit.

		September 30, 2015	September 30, 2014	Change 2014 to 2015	
		(dollar amounts in thousands)			
Cost of net revenue three months ended	\$	793	\$ 447	\$ 346	77%
Percentage of total net revenue		78%	39%		
Cost of net revenue nine months ended	\$	1,593	\$ 2,046	\$ (453)	(22)%
Percentage of total net revenue		57%	48%		

		September 30, 2015	September 30, 2014	Change 2014 to 2015	
		(dollar amounts in thousands)			

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Gross profit	three months ended	\$	229	\$	706	\$	(477)	(68)%
	Percentage of total net revenue		22%		61%			
Gross profit	nine months ended	\$	1,199	\$	2,188	\$	(989)	(45)%
	Percentage of total net revenue		43%		52%			

Cost of net revenue is primarily comprised of direct and indirect costs related to the sale of IC products.

Cost of net revenue increased for the three months ended September 30, 2015 compared with the same period of 2014 primarily due to higher IC shipment volumes and a \$0.2 million provision for slow moving inventory. The decrease in cost of net revenue for the nine months ended September 30, 2015 compared with the same period of 2014 was primarily due to lower IC shipment volumes, partially offset by the provision for slow moving inventory recorded in the third quarter of 2015.

Gross profit decreased for the three and nine months ended September 30, 2015, compared with the same periods of 2014, primarily due to the decrease in our total revenue.

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Research and Development.

	September 30, 2015	September 30, 2014	Change 2014 to 2015	
	(dollar amounts in thousands)			
Research and development three months ended	\$ 8,793	\$ 7,507	\$ 1,286	17%
Percentage of total net revenue	860%	651%		