SIGMA DESIGNS INC
Form 10-Q
December 06, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended October 27, 2012
or

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

For the transition period from to

Commission file number 001-32207

Sigma Designs, Inc.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| California<br>(State or other jurisdiction of incorporation or organization) | 94-2848099<br>(I.R.S. Employer Identification No.) |

1778 McCarthy Boulevard,
Milpitas, California 95035
(Address of principal executive offices including Zip Code)
(408) 262-9003
(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 R No o

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 R No o

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

| Large accelerated filer o | Accelerated filer R | Non-accelerated filer o (Do not check if a smaller reporting company) | Smaller reporting company o |
|---|---|---|---|

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

As of November 30, 2012, the Company had 33,459,341 shares of Common Stock outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

SIGMA DESIGNS, INC.
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)

| | October 27, 2012 | January 28, 2012 |
|---|---|---|
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | $49,331 | $44,283 |
| Short-term marketable securities | 17,366 | 42,134 |
| Restricted cash | 1,769 | 1,769 |
| Accounts receivable, net | 37,872 | 21,180 |
| Inventories | 30,529 | 22,037 |
| Deferred tax assets | 2,170 | 4,832 |
| Prepaid expenses and other current assets | 23,514 | 7,234 |
| Total current assets | 162,551 | 143,469 |
| Long-term marketable securities | 30,403 | 62,022 |
| Software, equipment and leasehold improvements, net | 21,699 | 19,609 |
| Intangible assets, net | 44,349 | 45,656 |
| Deferred tax assets, net of current portion | 874 | 16,595 |
| Notes receivable, net of current portion | 2,500 | 3,000 |
| Long-term investments | 6,445 | 6,443 |
| Other non-current assets | 3,612 | 430 |
| Total assets | $272,433 | $297,224 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities | | |
| Accounts payable | $22,482 | $8,438 |
| Accrued liabilities | 42,116 | 24,081 |
| Total current liabilities | 64,598 | 32,519 |
| Other long-term liabilities | 14,059 | 15,168 |
| Long-term deferred tax liabilities | 1,038 | 1,062 |
| Total liabilities | 79,695 | 48,749 |
| Commitments and contingencies (Note 11) | | |
| Shareholders' equity | | |
| Preferred stock | - | - |

| | | |
|---|---|---|
| Common stock and additional paid-in capital | 470,515 | 460,246 |
| Treasury stock | (85,941 ) | (85,941 ) |
| Accumulated other comprehensive income | 1,168 | 603 |
| Accumulated deficit | (193,004 ) | (126,433 ) |
| | | |
| Total shareholders' equity | 192,738 | 248,475 |
| | | |
| Total liabilities and shareholders' equity | $272,433 | $297,224 |

See the accompanying Notes to Unaudited Condensed Consolidated Financial Statements

SIGMA DESIGNS, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| Net revenue | $63,905 | $39,725 | $172,414 | $147,051 |
| Cost of revenue | 38,423 | 21,723 | 95,257 | 86,263 |
| Gross profit | 25,482 | 18,002 | 77,157 | 60,788 |
| | | | | |
| Operating expenses | | | | |
| Research and development | 26,741 | 21,633 | 76,505 | 65,034 |
| Sales and marketing | 12,774 | 8,545 | 27,457 | 25,475 |
| General and administrative | 6,007 | 4,828 | 21,874 | 15,460 |
| Restructuring | 821 | - | 821 | - |
| Goodwill impairment | - | 45,108 | - | 45,108 |
| Intangible assets impairment | - | 66,170 | - | 66,170 |
| Gain on acquisition | - | - | (1,417) | - |
| Total operating expenses | 46,343 | 146,284 | 125,240 | 217,247 |
| Loss from operations | (20,861) | (128,282) | (48,083) | (156,459) |
| | | | | |
| Interest and other income, net | 299 | 542 | 1,032 | 2,095 |
| | | | | |
| Loss before provision for (benefit from) income taxes | (20,562) | (127,740) | (47,051) | (154,364) |
| | | | | |
| Provision for (benefit from) income taxes | 18,889 | (6,165) | 19,520 | (5,157) |
| | | | | |
| Net loss | $(39,451) | $(121,575) | $(66,571) | $(149,207) |
| | | | | |
| Net loss per common share: | | | | |
| Basic | $(1.18) | $(3.78) | $(2.02) | $(4.67) |
| Diluted | $(1.18) | $(3.78) | $(2.02) | $(4.67) |
| | | | | |
| Shares used in computing net loss per share: | | | | |
| Basic | 33,383 | 32,139 | 33,032 | 31,928 |
| Diluted | 33,383 | 32,139 | 33,032 | 31,928 |

SIGMA DESIGNS, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(In thousands)

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |

| | | | | |
|---|---|---|---|---|
| Net loss | $(39,451) | $(121,575) | $(66,571) | $(149,207) |
| | | | | |
| Other comprehensive income (loss): | | | | |
| Foreign currency translation gain (loss) | 373 | (551) | (122) | (522) |
| Unrealized gain (loss) on marketable securities, net of tax | 360 | (177) | 687 | 228 |
| Other comprehensive income (loss) | 733 | (728) | 565 | (294) |
| | | | | |
| Comprehensive loss | $(38,718) | $(122,303) | $(66,006) | $(149,501) |

See the accompanying Notes to Unaudited Condensed Consolidated Financial Statements

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SIGMA DESIGNS, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

| | Nine months ended October 27, 2012 | Nine months ended October 29, 2011 |
|---|---|---|
| Cash flows from operating activities | | |
| Net loss | $(66,571) | $(149,207) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization | 17,082 | 23,709 |
| Stock-based compensation | 8,078 | 9,132 |
| Provision for excess and obsolete inventory | 3,613 | 8,083 |
| Provision for sales discounts and (recovery) of doubtful accounts | 174 | (44) |
| Deferred income taxes | 18,098 | (715) |
| Loss on disposal of equipment | 142 | 77 |
| Accretion of contributed leasehold improvements | (189) | (191) |
| Impairment of goodwill and acquired intangible assets | - | 111,278 |
| Gain on acquisition | (1,417) | - |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (3,456) | 5,360 |
| Inventory | 2,312 | 7,413 |
| Prepaid expenses and other current assets | (7,402) | (607) |
| Other non-current assets | (2,684) | 123 |
| Accounts payable | 11,296 | (5,218) |
| Accrued liabilities | 18,245 | (7,886) |
| Other long-term liabilities | (2,319) | (5,643) |
| Net cash used in operating activities | $(4,998) | $(4,336) |
| Cash flows from investing activities | | |
| Restricted cash | - | (154) |
| Purchase of marketable securities | (15,264) | (60,471) |
| Sales and maturities of marketable securities | 72,339 | 57,575 |
| Purchases of software, equipment and leasehold improvements | (9,521) | (9,298) |
| Net cash paid in connection with acquisitions | (39,740) | (5,000) |
| Purchase of long-term investments | - | (2,142) |
| Net cash provided by (used in) investing activities | $7,814 | $(19,490) |
| Cash flows from financing activities | | |
| Net proceeds from exercise of employee stock options and stock purchase rights | 2,536 | 3,254 |
| Excess tax benefit from share-based compensation | (345) | 399 |
| Net cash provided by financing activities | $2,191 | $3,653 |
| Effect of foreign exchange rate changes on cash and cash equivalents | 41 | 91 |

| | | |
|---|---|---|
| Net increase (decrease) in cash and cash equivalents | 5,048 | (20,082) |
| | | |
| Cash and cash equivalents, beginning of period | $44,283 | $72,732 |
| | | |
| Cash and cash equivalents, end of period | $49,331 | $52,650 |
| | | |
| Supplemental disclosure of cash flow information | | |
| Cash paid for income taxes | $2,177 | $1,037 |

See the accompanying Notes to Unaudited Condensed Consolidated Financial Statements

SIGMA DESIGNS, INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and summary of significant accounting policies

Organization and nature of operations: Sigma Designs, Inc. (referred to collectively in these consolidated financial statements as "Sigma," "we," "our", "the Company" and "us") is a leader in connected media platforms. We specialize in digi television, or DTV, media processors and chipset solutions that serve as the foundation for some of the world's leading internet protocol television, or IPTV, set-top-boxes, connected media players, residential gateways and home control systems. We sell our products to manufacturers, designers and, to a lesser extent, to distributors who, in turn, sell to manufacturers.

Basis of presentation: The consolidated financial statements include Sigma Designs, Inc. and its wholly-owned subsidiaries. All intercompany balances and transactions are eliminated upon consolidation.

The unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, or US GAAP, for interim financial information and the rules and regulations of the Securities and Exchange Commission, or SEC. They do not include all disclosures required by US GAAP for complete financial statements. However, we believe that the disclosures are adequate and fairly present the information. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with our audited consolidated financial statements and notes thereto for the year ended January 28, 2012 included in our Annual Report on Form 10-K.

The condensed consolidated financial statements included herein are unaudited; however, they contain all normal recurring accruals and adjustments that, in our opinion, are necessary to present fairly our consolidated financial position at October 27, 2012 and January 28, 2012, the consolidated results of our operations for the three and nine months ended October 27, 2012 and October 29, 2011, and the consolidated cash flows for the nine months ended October 27, 2012 and October 29, 2011. The results of operations for the three and nine months ended October 27, 2012 are not necessarily indicative of the results to be expected for future quarters or the year.

Accounting period: Each of our fiscal quarters presented herein includes 13 weeks and ends on the last Saturday of the period. The third quarter of fiscal 2013 ended on October 27, 2012. The third quarter of fiscal 2012 ended on October 29, 2011.

Reclassifications: Certain prior fiscal year balances have been reclassified to conform to the current fiscal year presentation. In the first quarter of fiscal 2013, we concluded that it was appropriate to reclassify our purchased intellectual property, or IP, that is incorporated into our products, from software, equipment and leasehold improvements to intangible assets. The reclassification has no effect on previously reported Condensed Consolidated Statements of Operations for any period and does not affect previously reported cash flows from operations or from financing activities in the Condensed Consolidated Statements of Cash Flows. For comparability purposes, the corresponding gross assets and accumulated amortization of $22.2 million and $5.9 million, respectively, have been reclassified as of January 28, 2012. Such reclassifications had no effect on previously reported results of operations or retained earnings.

Restructuring charges: On October 31, 2012, we announced a restructuring plan, which we are in the early stages of implementing. Our restructuring plan includes targeted reductions in labor costs through headcount reduction and other related actions and targeted reductions in other operating expenses such as consulting, travel and subletting excess office space. We also plan to migrate to lower cost manufacturing components and processes. We expect to execute the restructuring plan in several phases and already completed the initial phase, which consisted of headcount reduction in our North American operations and the implementation of expense management measures across worldwide operations. For the three months ended October 27, 2012, we recognized a charge of $0.8 million in connection with our restructuring activities. We anticipate we will incur additional restructuring charges in future periods as we continue to implement our plan.

Software, equipment and leasehold improvements: Software, equipment and leasehold improvements are stated at cost. Depreciation and amortization for software, equipment and leasehold improvements is computed using the straight-line method based on the useful lives of the assets (one to five years) or the remaining lease term if shorter. Any allowance for leasehold improvements received from the landlord for improvements to our facilities is amortized using the straight-line method over the lesser of the remaining lease term or the useful life of the leasehold improvements. Repairs and maintenance costs are expensed as incurred.

Long-lived assets: The amounts and useful lives assigned to finite lived intangible assets acquired, other than goodwill, impact the amount and timing of future amortization. Long-lived assets include intellectual property that we purchase for incorporation into our product designs. We begin amortizing such intellectual property at the time that we begin shipment of the associated products into which it is incorporated. We amortize the intellectual property over the estimated useful life of the associated products, which is generally two to three years. We assess the carrying value of long-lived assets, including purchased intangible assets, whenever events or changes in circumstances, such as a change in technology, indicate that the carrying value of these assets may not be recoverable. An impairment loss would be recognized when the sum of the undiscounted future net cash flows expected to result from the use of the asset and its eventual disposal is less than its carrying amount.

Use of estimates: The preparation of the consolidated financial statements in conformity with US GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ from those estimates, and such differences may be material to the consolidated financial statements.

Revenue recognition: We derive our revenue primarily from product sales. Our products, which we refer to as chipsets, consist of highly integrated semiconductors and embedded software that enables real-time processing of digital video and audio content, which we refer to as real-time software. We do not deliver software as a separate product in connection with product sales. We recognize revenue for product sales when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectability is reasonably assured. In addition, the Company derives licensing revenue from its home control and energy management market which is recognized ratably over the license term.

Inventories: Inventories are stated at the lower of standard cost, which approximates actual cost on a first-in, first-out basis, or market value. We evaluate our ending inventories for excess quantities and obsolescence on a quarterly basis. This evaluation includes analysis of historical and estimated future unit sales by product as well as product purchase commitments that are not cancelable. We develop our demand forecasts based, in part, on discussions with our customers about their forecasted supply needs. However, our customers usually only provide us with firm purchase commitments for the current period and not our entire forecasted period. Additionally, our sales and marketing personnel provide estimates of future sales to prospective customers based on actual and expected design wins. A provision is recorded for inventories in excess of estimated future demand. In addition, we write off inventories that are obsolete. Obsolescence is determined from several factors, including competitiveness of product offerings, market conditions and product life cycles. Provisions for excess and obsolete inventory are charged to cost of revenue. At the time of the loss recognition, a new, lower-cost basis for that inventory is established and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis. If this lower-cost inventory is subsequently sold, we will realize higher gross margins for those products.

Inventory write-downs inherently involve assumptions and judgments as to amount of future sales and selling prices. Although we believe that the assumptions we use in estimating inventory write-downs are reasonable, significant future changes in these assumptions could produce a significantly different result. There can be no assurances that future events and changing market conditions will not result in significant inventory write-downs.

Income taxes: Income taxes are accounted for under an asset and liability approach. Deferred income taxes reflect the net tax effects of any temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts reported for income tax purposes, and any operating losses and tax credit carry forwards. Deferred tax liabilities are recognized for future taxable amounts and deferred tax assets are recognized for future deductions, net of any valuation allowance, to reduce deferred tax assets to amounts that are considered more likely than not to be realized.

The impact of an uncertain income tax position on an income tax return must be recognized as the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained.

In the current quarter, the Company concluded it is necessary to establish a valuation allowance for certain deferred tax assets (DTA) related to Federal taxes in the United States. Due to the history of losses in the United States, it was determined that it is more likely than not that the DTAs will expire before they are fully utilized. Accordingly, the Company has established a valuation allowance in the amount of $17.9 million. Because Sigma has just begun its corporate restructuring plan and as such has not yet seen the improved financial performance, the Company will continue to assess the need for a valuation allowance periodically based on available evidence and management’s judgment.

Recent accounting pronouncements: In July 2012, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update No. 2012-02, Intangibles-Goodwill and Other (Topic 350) – Testing Indefinite-Lived Intangibles Assets for Impairment (“ASU 2012-02”), to simplify how entities both public and nonpublic, test indefinite-lived intangible assets for impairment. ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The Company early adopted this standard in the third quarter of fiscal 2013, and it had no material impact on its Consolidated Financial Statements.

2. Cash, cash equivalents and marketable securities

Cash, cash equivalents and marketable securities consist of the following (in thousands):

| | As of October 27, 2012 | | | As of January 28, 2012 | | |
|---|---|---|---|---|---|---|
| | Book Value | Net Unrealized Gains (Losses) | Fair Value | Book Value | Net Unrealized Gains (Losses) | Fair Value |
| Corporate bonds | $43,239 | $880 | $44,119 | $91,829 | $192 | $92,021 |
| Money market funds | 11,531 | - | 11,531 | 20,876 | - | 20,876 |
| Corporate commercial paper | - | - | - | 1,946 | - | 1,946 |
| US agency discount notes | 2,000 | - | 2,000 | 8,506 | (4) | 8,502 |
| Municipal bonds and notes | 1,628 | 22 | 1,650 | 1,668 | 19 | 1,687 |
| Total cash equivalents and marketable securities | $58,398 | $902 | $59,300 | $124,825 | $207 | $125,032 |
| | | | | | | |
| Cash on hand held in the United States | | | 2,380 | | | 1,030 |
| Cash on hand held overseas | | | 35,420 | | | 22,377 |
| Total cash on hand | | | 37,800 | | | 23,407 |
| Total cash, cash equivalents and marketable securities | | | $97,100 | | | $148,439 |
| | | | | | | |
| Reported as: | | | | | | |
| Cash and cash equivalents | | | 49,331 | | | 44,283 |
| Short-term marketable securities | | | 17,366 | | | 42,134 |
| Long-term marketable securities | | | 30,403 | | | 62,022 |
| | | | $97,100 | | | $148,439 |

The amortized cost and estimated fair value of cash equivalents and marketable securities, by contractual maturity, are as follows (in thousands):

| | As of October 27, 2012 | | As of January 28, 2012 | |
|---|---|---|---|---|
| | Book Value | Fair Value | Book Value | Fair Value |
| Due in one year or less | $ 28,842 | $ 28,897 | $ 62,970 | $ 63,010 |
| Due in greater than one year | 29,556 | 30,403 | 61,855 | 62,022 |
| Total | $ 58,398 | $ 59,300 | $ 124,825 | $ 125,032 |

3. Fair values of assets and liabilities

Fair value hierarchy

The accounting standards discuss valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost). The standards utilize a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

Level 1 - Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 - Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our estimate of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

Determination of Fair Value

Our cash equivalents and marketable securities are classified within Level 1 because they are valued using quoted market prices, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. The types of marketable securities valued based on quoted market prices in active markets include most U.S. government and agency securities, sovereign government obligations, money market securities and certain corporate obligations with high credit ratings and an ongoing trading market.

Our foreign currency derivative instruments are classified as Level 2 because they are valued using quoted prices and other observable data of similar instruments in active markets.

The table below presents the balances of our assets and liabilities measured at fair value on a recurring basis as of October 27, 2012 and January 28, 2012 (in thousands):

| | As of October 27, 2012 | | | |
|---|---|---|---|---|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Corporate bonds | $ 44,119 | $ 44,119 | $ - | $ - |
| Money market funds | 11,531 | 11,531 | - | - |
| US agency discount notes | 2,000 | 2,000 | - | - |
| Municipal bonds and notes | 1,650 | 1,650 | - | - |
| Total cash equivalents and short-term investments | $ 59,300 | $ 59,300 | $ - | $ - |
| Restricted cash | 1,769 | 1,769 | - | - |
| Derivative instruments | 38 | - | 38 | - |
| Total assets/liabilities measured at fair value | $ 61,107 | $ 61,069 | $ 38 | $ - |

| | As of January 28, 2012 | | | |
|---|---|---|---|---|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Corporate bonds | $ 92,021 | $ 92,021 | $ - | $ - |
| Money market funds | 20,876 | 20,876 | - | - |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Corporate commercial paper | | 1,946 | | | 1,946 | | - | | | - |
| US agency discount notes | | 8,502 | | | 8,502 | | - | | | - |
| Municipal bonds and notes | | 1,687 | | | 1,687 | | - | | | - |
| Total cash equivalents and short-term investments | $ | 125,032 | | $ | 125,032 | $ | - | | $ | - |
| Restricted cash | | 1,769 | | | 1,769 | | - | | | - |
| Derivative instruments | | (121 | ) | | - | | (121 | ) | | - |
| Total assets/liabilities measured at fair value | $ | 126,680 | | $ | 126,801 | $ | (121 | ) | $ | - |

Assets measured and recorded at fair value on a non-recurring basis

Our non-marketable convertible promissory note and preferred stock investments in privately-held venture capital funded technology companies are recorded at fair value only if an impairment charge is recognized.

As of October 27, 2012, we held equity investments in five, and promissory notes receivable in two, privately held venture capital funded technology companies and an equity investment in one joint venture, with an aggregate face value equal to cost of $9.7 million. Each of these equity investments in privately held companies constituted less than a 20% ownership position. Furthermore, we do not believe that we have the ability to exert significant influence over any of these companies.

4. Derivative financial instruments

Foreign exchange contracts are recognized either as assets or liabilities on the balance sheet at fair value at the end of each reporting period. Changes in fair value of the derivatives are recorded as operating expenses or other income (expense), or as accumulated other comprehensive income, or OCI.

We currently use and expect to continue to use foreign currency derivatives such as forward and option contracts as hedges against certain anticipated transactions denominated in Israeli shekels, or NIS. For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of OCI and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on derivatives representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

We currently do not assess our derivate contracts that are used in managing NIS denominated transactions for hedge effectiveness and thus such contracts do not qualify for hedge accounting. As of October 27, 2012, we had foreign exchange contracts to sell up to approximately $12.3 million for a total amount of approximately NIS 46.9 million, that mature on or before September 23, 2013. As of January 28, 2012, we had foreign exchange contracts to sell up to approximately $10.2 million for a total amount of approximately NIS 37.0 million, that mature on or before December 27, 2012. For the three and nine months ended October 27, 2012, we recognized gains of approximately $0.4 million and a loss of less than $0.1 million, respectively, as a result of foreign exchange contracts. For the three and nine months ended October 29, 2011, we recognized gains of approximately $0.2 million and $0.5 million, respectively, as a result of foreign exchange contracts.

The following table presents the fair value of our outstanding derivative instruments as of October 27, 2012 and January 28, 2012 (in thousands):

| Derivative Assets | Balance Sheet Location | | October 27, 2012 | | January 28, 2012 | |
|---|---|---|---|---|---|---|
| Foreign exchange contracts not designated as cash flow hedges | Current assets (liabilities) | $ | 38 | $ | (121 | ) |
| Total fair value of derivative instruments | | $ | 38 | $ | (121 | ) |

The effects of derivative instruments on income and accumulated other comprehensive income for the three months and nine months ended October 27, 2012 and October 29, 2012 are summarized below (in thousands):

| | Gains (Losses) Recognized in Accumulated Other Comprehensive Income on | Gains Reclassified from Accumulated Other Comprehensive Income into Earnings | Gains (Losses) Recognized in Earnings on Derivatives (Including Ineffective Portion) |
|---|---|---|---|

| Derivatives instruments | Derivatives (Effective Portion) Amount | Amount | Location | Amount | Location |
|---|---|---|---|---|---|
| Three months ended October 27, 2012 foreign exchange contracts | $ - | $ - | - | $ 386 | Interest and other income, net |
| Nine months ended October 27, 2012 foreign exchange contracts | $ - | $ - | - | $ (44 ) | Interest and other income, net |
| | | | | | |
| Three months ended October 29, 2011 foreign exchange contracts | $ - | $ (9 ) | Operating expenses and cost of revenue | $ (178 ) | Interest and other income, net |
| Nine months ended October 29, 2011 foreign exchange contracts | $ - | $ 94 | Operating expenses and cost of revenue | $ 422 | Interest and other income, net |

5. Restricted cash

As of October 27, 2012 and January 28, 2012, we had $1.8 million of restricted cash related to deposits pledged to a financial institution in connection with our foreign exchange forward hedging transactions and an office operating lease.

6. Investments in and notes receivable from privately held companies

The following table sets forth the value of investments in and notes receivable from privately held companies as of October 27, 2012 and January 28, 2012 (in thousands):

| Equity investments | October 27, 2012 | January 28, 2012 |
|---|---|---|
| Issuer A | $ 2,000 | $ 2,000 |
| Issuer B | 1,000 | 1,000 |
| Issuer C | 1,000 | 1,000 |
| Issuer D | 300 | 300 |
| Issuer E | 2,000 | 2,000 |
| Issuer F | 145 | 143 |
| Total equity investments | $ 6,445 | $ 6,443 |
| | | |
| Notes receivable | | |
| Issuer A | 750 | 1,000 |
| Issuer G | 2,500 | 2,500 |
| Total notes receivable | $ 3,250 | $ 3,500 |
| | | |
| Total investments and notes | $ 9,695 | $ 9,943 |

Issuer A, B, C, D, E and F

During fiscal 2009, we purchased shares of preferred stock in a privately held venture capital funded technology company ("Issuer A") at a total investment cost of $1.0 million. In the fourth quarter of fiscal 2010, we purchased additional shares of preferred stock in Issuer A at a cost of $1.0 million.

In the third quarter of fiscal 2011, we purchased shares of preferred stock in another privately held technology company ("Issuer B") at a total investment cost of $1.0 million.

In the fourth quarter of fiscal 2011, we purchased shares of preferred stock in another privately held technology company ("Issuer C") at a total investment cost of $1.0 million.

In the fourth quarter of fiscal 2011, we also purchased a convertible note from another privately held technology company ("Issuer D") with a face value equal to the cost of $0.3 million.

In the second quarter of fiscal 2012, we purchased shares of preferred stock in another privately held technology company ("Issuer E") at a total investment cost of $2.0 million.

In the third quarter of fiscal 2012, we made an equity investment of $0.2 million in a privately held joint venture ("Issuer F").

As of October 27, 2012 and January 28, 2012, our equity investments in privately held companies were valued at $6.4 million, representing their cost.

Notes receivable from privately held companies

In November 2010, we loaned $1.0 million to Issuer A and received a secured promissory note. This promissory note is secured by the assets of Issuer A, bearing interest at a rate of 5% per annum, and is scheduled to be fully repaid by June 2013. The balance outstanding as of October 27, 2012 was $0.8 million.

In January 2012, we loaned $2.5 million to a privately held venture capital funded technology company ("Issuer G"), pursuant to a strategic agreement dated January 27, 2012. We made this loan in exchange for a secured promissory note, bearing interest at a rate of 3% per annum. The note plus the accrued interest is due 36 months from the anniversary of the agreement date. The note is secured by the assets of Issuer G. Additionally, pursuant to this agreement we have the right, subject to certain performance conditions by Issuer G for one year from the agreement date, to acquire all the outstanding securities of Issuer G for $11.2 million cash, plus the forgiveness of the $2.5 million loan. In June 2012, we amended this agreement to clarify the Company's obligation regarding the performance criteria. As of October 27, 2012, these performance conditions had not been met by Issuer G. This right will expire in January 2013. We have a variable interest in Issuer G and it is a variable interest entity, however, we have concluded that we are not the primary beneficiary of Issuer G because we do not have the power to direct the activities that most significantly impact Issuer G's financial performance.

As of October 27, 2012 and January 28, 2012, our notes receivable from privately held companies were valued at $3.3 million and $3.5 million, respectively, representing their cost. We made each of the above-described investments because we viewed the issuer as either having strategic technology or a business that would complement our technological capabilities or help create an opportunity for us to sell our chipset solutions. The Chief Executive Officer of the Company is on the board of five of the seven companies we have invested in. Two of our directors held equity interests in Issuer A in which we had invested an aggregate of $5.0 million and one of these directors was also a director of Issuer A. In the aggregate, these equity and debt interests did not rise to the level of a material or a controlling interest in Issuer A. Our board of directors appointed our director who had no interest in Issuer A to evaluate each investment in Issuer A and to recommend appropriate action to the board of directors. All investment transactions with Issuer A were approved and recommended by this independent director and made as the result of an arms-length negotiation process between Issuer A and us, with our negotiations led by our non-interested director. We viewed this investment as a strategic investment in a technology platform into which we could potentially sell our chipset solutions. In connection with this investment, we entered into a commercial agreement with Issuer A as well. The Company analyzes each investment quarterly for evidence of impairment.

7. Inventories

Inventories consist of the following (in thousands):

| | October 27, 2012 | | January 28, 2012 | |
|---|---|---|---|---|
| Inventory | | | | |
| Wafers and other purchased materials | $ | 16,469 | $ | 11,006 |
| Work-in-process | | 2,548 | | 191 |
| Finished goods | | 11,512 | | 10,840 |
| Total | $ | 30,529 | $ | 22,037 |

8. Business Combinations

On May 4, 2012, we completed our acquisition of certain assets from Trident Microsystems, Inc. and certain of its subsidiaries (collectively referred to as “Trident”) used in or related to Trident’s digital television and PC television businesses (the “DTV Business”) for a purchase price of $21.0 million plus additional cash consideration of $18.7 million as a result of adjustments based on the closing asset balance of the DTV Business, plus the assumption of certain employee related liabilities pursuant to an Asset Purchase Agreement dated March 23, 2012 (the “Purchase Agreement”). The addition of Trident's industry-leading DTV media processor System-on-a-Chip, or SoC, products for next-generation Internet-enabled digital televisions is expected to significantly expand our served available market. DTV products complement our existing IPTV set-top-box and connected media player SoC solutions and will augment our ability to develop innovative solutions for the anticipated convergence of IP-video delivery across any device within the home.

Pursuant to the Purchase Agreement, we acquired all of Trident’s DTV business products, certain licensed intellectual property rights, specified tangible assets and other assets specified in the Purchase Agreement. We also acquired the right to use certain facilities of Trident under short-term facilities use agreements for facilities located in Shanghai and Beijing, China, Germany, The Netherlands, Taiwan and California. We hired approximately 320 employees whose services are used in the DTV Business. We also entered into a transition services agreement with Trident under which Trident agreed to provide certain services to us following the closing. The purchaser of Trident's set-top box business also agreed to provide transition support services to us.

In connection with this acquisition, we obtained a valuation of the assets acquired in order to allocate the purchase price. The total purchase price was allocated to the net tangible and identified intangible assets based upon fair values as of May 4, 2012. The fair value of the tangible assets and identifiable intangible assets acquired, net of liabilities assumed, exceeded the purchase price by $1.4 million, which was recognized in the condensed statements of operations as a gain on acquisition. The purchase price in the transaction was allocated as follows (in thousands, except years):

| | | Amount | Estimated Useful Lives (in years) |
|---|---|---|---|
| Purchase consideration: | | | |
| Cash | $ | 39,740 | |
| | | | |
| Tangible assets acquired and liabilities assumed | $ | 40,019 | |
| Identifiable intangible assets: | | | |
| Developed technology | | 1,138 | 3 |
| Gain on acquisition | | (1,417 ) | |
| Total consideration | $ | 39,740 | |

Beginning in the second quarter of fiscal 2013, the results of operations of the DTV business are included in the condensed consolidated results of operations. For the three and nine months ended October 27, 2012, net sales of approximately $27.8 million and $54.4 million, respectively and an operating profit of approximately $1.2 million and operating loss of $0.9 million, respectively, attributable to the DTV business, were included in the condensed consolidated results of operations.

The following unaudited pro forma consolidated results of operations give effect to the acquisition of the DTV business as if it had occurred at January 30, 2011. The unaudited pro forma consolidated results of operations are provided for informational purposes only and do not purport to represent actual consolidated results of operations had the acquisition occurred on the date assumed, nor are these financial statements necessarily indicative of future consolidated results of operations. We expect to incur costs and realize benefits associated with integrating the operations of the DTV business. The unaudited pro forma consolidated results of operations do not reflect the cost of any integration activities or any benefits that may result from operating efficiencies or revenue synergies. The pro forma consolidated results of operations for the nine months ended October 27, 2012 include non-recurring adjustments of $4.0 million of direct acquisition costs (in thousands, except per share data).

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| Net revenue | $63,905 | $87,085 | $195,358 | $289,863 |
| Net loss | (39,451 ) | (136,118 ) | (85,116 ) | (181,826 ) |
| Basic and diluted net loss per share | $(1.18 ) | $(4.24 ) | $(2.58 ) | $(5.69 ) |

On March 21, 2011, we executed a definitive agreement to acquire certain assets, including intangible assets and products, from a business division of a large computer manufacturer for $5.0 million in cash, which we paid on May 3, 2011.

The assets we acquired include a low-power High Definition, or HD, video encoder processor aimed at capturing HD video for visual telephony between personal computers, set-top boxes, connected media players, Voice over Internet Protocol, or VoIP, devices, video phones, video conferencing TV's and video surveillance devices.

In connection with this acquisition, we obtained a valuation of the assets acquired in order to allocate the purchase price. The total purchase price was allocated to the net tangible and identified intangible assets based upon fair values as of March 21, 2011. The excess purchase price over the value of the net tangible and identifiable intangible assets was recorded as goodwill. The purchase price in the transaction was allocated as follows (in thousands, except years):

| | | Amount | |
|---|---|---|---|
| Purchase consideration: | | | |
| Cash | $ | 5,000 | |
| | | | |
| Tangible assets acquired and liabilities assumed | $ | 752 | |
| | | | Estimated Useful Lives (in years) |
| Identifiable intangible assets: | | | |
| Developed technology | | | |
| Technology | | 1,250 | 5 |
| Technology leveraged | | 1,680 | 8 |
| Customer relationships | | 750 | 5 |
| In-process research and development | | 370 | — |
| Goodwill | | 198 | — |
| Total consideration | $ | 5,000 | |

9. Intangible assets

In the first quarter of fiscal 2013, we concluded that it was appropriate to reclassify our purchased intellectual property, or IP, that is incorporated into our products, from software, equipment and leasehold improvements to intangible assets. For comparability purposes, corresponding gross assets and accumulated amortization of $22.2 million and $5.9 million, respectively, have been reclassified as of January 28, 2012. The reclassification has no effect on previously reported Condensed Consolidated Statements of Operations for any period and does not materially affect previously reported cash flows from operations or from financing activities in the Condensed Consolidated Statements of Cash Flows.

We amortize purchased IP over the estimated useful life of the associated products, which is generally two to three years, and begin amortization at the time that we begin shipment of the associated products into which it is incorporated.

The table below presents the balances of our intangible assets as of October 27, 2012 and January 28, 2012 (in thousands):

| | October 27, 2012 | January 28, 2012 |
|---|---|---|
| Acquired intangible assets | $ 76,289 | $ 75,978 |
| Purchased IP | 26,587 | 22,204 |
| Total | $ 102,876 | $ 98,182 |
| Accumulated amortization | (58,527) | (52,526) |
| Intangible assets, net | $ 44,349 | $ 45,656 |

We assess the carrying value of long-lived assets whenever events or changes in circumstances indicate that the carrying value of these assets may not be recoverable. On October 29, 2011, we performed a review of the carrying value of our acquired intangible assets due to continued reductions in our profitability and sales forecasts, and negative cash flows from operations. In performing this review, we developed a forecast of the total undiscounted cash flow expected to be generated by each acquired intangible asset group and compared the result to the carrying value. The results of this review indicated that two of these intangible asset groups, consisting primarily of certain developed technology and customer relationship intangibles related to our CopperGate acquisition, were not fully recoverable. Therefore, we performed the second step of the analysis by developing a discounted cash flow analysis for each of the individual identifiable assets in these two groups to determine the amount of impairment. Our analysis resulted in an intangible asset impairment charge of $55.1 million during the third quarter of fiscal 2012. In addition, as a result of our review of indefinite-lived intangible assets during the third quarter of fiscal 2012, we recorded an impairment charge for our in-process research and development intangible assets of $11.1 million and a goodwill impairment charge of $45.1 million, which reduced the carrying value of goodwill to zero. There were no such impairment charges recorded during the three and nine months ended October 27, 2012.

Acquired intangible assets, subject to amortization, were as follows as of October 27, 2012 and January 28, 2012 (in thousands, except for years):

| | As of October 27, 2012 | | | | |
|---|---|---|---|---|---|
| | Gross Value | Impairment | Accumulated Amortization and Effect of Currency Translation | Net Value | Weighted Average Remaining Amortization Period |

| | | | | | |
|---|---|---|---|---|---|
| | | | | | (Years) |
| Developed technology | $76,607 | $(24,614) | $ (32,872) | $19,121 | 4.0 |
| Customer relationships | 50,705 | (30,486) | (15,446) | 4,773 | 4.1 |
| Purchased IP - amortizing | 15,876 | - | (6,872) | 9,004 | 2.3 |
| Trademarks | 2,677 | - | (1,937) | 740 | 6.1 |
| Non-compete agreements | 1,400 | - | (1,400) | - | - |
| | $147,265 | $(55,100) | $ (58,527) | $33,638 | 3.6 |
| Purchased IP - not yet deployed | 10,711 | - | - | 10,711 | |
| In-process research and development | 11,070 | (11,070) | - | - | |
| | $169,046 | $(66,170) | $ (58,527) | $44,349 | |

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| | As of January 29, 2012 | | | | |
|---|---|---|---|---|---|
| | Gross Value | Impairment | Accumulated Amortization and Effect of Currency Translation | Net Value | Weighted Average Remaining Amortization Period (Years) |
| Developed technology | $75,827 | $(24,614) | $ (28,455) | $22,758 | 4.7 |
| Customer relationships | 51,174 | (30,486) | (14,966) | 5,722 | 4.8 |
| Purchased IP - amortizing | 8,395 | - | (5,900) | 2,495 | 1.9 |
| Trademarks | 2,677 | - | (1,805) | 872 | 6.6 |
| Non-compete agreements | 1,400 | - | (1,400) | - | - |
| | $139,473 | $(55,100) | $ (52,526) | $31,847 | 4.8 |
| Purchased IP - not yet deployed | 13,809 | - | - | 13,809 | |
| In-process research and development | 11,070 | (11,070) | - | - | |
| | $164,352 | $(66,170) | $ (52,526) | $45,656 | |

Amortization expense related to acquired intangible assets and purchased IP was $3.0 million and $7.9 million for the three and nine months ended October 27, 2012, respectively, and $4.8 million and $14.3 million for the three and nine months ended October 29, 2011, respectively. As of October 27, 2012, we had $10.7 million of purchased IP which we have not yet begun to amortize. As of October 27, 2012, we expect the amortization expense in future periods to be as follows (in thousands):

| Fiscal years | Purchased IP-Amortizing | Developed Technology | Customer Relationships | Trademarks | Total |
|---|---|---|---|---|---|
| Remaining three months of fiscal 2013 | $ 1,088 | $ 1,624 | $ 316 | $44 | $3,072 |
| 2014 | 4,153 | 5,757 | 1,265 | 119 | 11,294 |
| 2015 | 2,793 | 4,272 | 1,265 | 118 | 8,448 |
| 2016 | 970 | 3,955 | 1,109 | 118 | 6,152 |
| 2017 | - | 3,019 | 818 | 118 | 3,955 |
| Thereafter | - | 494 | - | 223 | 717 |
| Total | $ 9,004 | $ 19,121 | $ 4,773 | $740 | $33,638 |

10. Product warranty

In general, we sell products with a one-year limited warranty that our products will be free from defects in materials and workmanship. Warranty cost is estimated at the time revenue is recognized based on historical activity, and additionally, for any specific known product warranty issues. Accrued warranty cost includes hardware repair and/or replacement and software support costs and is included in accrued liabilities on the consolidated balance sheets.

Details of the change in accrued warranty as of October 27, 2012 and October 29, 2011 are as follows (in thousands):

| Three Months Ended | Balance Beginning of Period | Additions | Deductions | Balance End of Period |
|---|---|---|---|---|
| October 27, 2012 | $ 1,157 | 373 | (203) | $ 1,327 |
| October 29, 2011 | $ 1,327 | 326 | (312) | $ 1,341 |

| Nine Months Ended | | Additions | Deductions | |
|---|---|---|---|---|

| | Balance Beginning of Period | | | Balance End of Period |
|---|---|---|---|---|
| October 27, 2012 | $ 1,326 | 729 | (728 ) | $ 1,327 |
| October 29, 2011 | $ 1,300 | 856 | (815 ) | $ 1,341 |

11. Commitments and contingencies

Commitments

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Leases

Our primary facility in Milpitas, California is leased under a non-cancelable operating lease which was amended in September 2012 to extend the term through September 2015, and slightly decrease the monthly base rent. We also lease facilities in Canada, China, Denmark, France, Germany, Hong Kong, Israel, Japan, Singapore, Taiwan and Vietnam, and vehicles in Israel under non-cancelable operating leases. Future minimum annual payments under operating leases are as follows (in thousands):

| Fiscal Years | Operating Leases |
|---|---|
| Remaining three months of fiscal 2013 | $ 1,372 |
| 2014 | 4,732 |
| 2015 | 4,218 |
| 2016 | 3,304 |
| 2017 | 2,120 |
| 2018 | 684 |
| Thereafter | 182 |
| Total minimum lease payments | $ 16,612 |

Purchase commitments

We place non-cancelable orders to purchase semiconductor products from our suppliers on an eight to twelve week lead-time basis. As of October 27, 2012, the total amount of outstanding non-cancelable purchase orders was approximately $27.0 million.

Indemnifications

In certain limited circumstances, we have agreed and may agree in the future to indemnify certain customers against patent infringement claims from third parties related to our intellectual property. In these limited circumstances, the terms and conditions of sale generally limit the scope of the available remedies to a variety of industry-standard methods including, but not limited to, a right to control the defense or settlement of any claim, procure the right for continued usage, and a right to replace or modify the infringing products to make them non-infringing. To date, we have not incurred or accrued any significant costs related to any claims under such indemnification provisions.

Our corporate articles of incorporation and bylaws require that we indemnify our officers and directors against expenses, judgments, fines, settlements and other amounts actually and reasonably incurred in connection with any proceedings arising out of their services to us. In addition, we have entered into separate indemnification agreements with each of our directors and executive officers which provide for indemnification of these individuals under similar circumstances and under additional circumstances. The indemnification obligations are more fully described in our charter documents and the form of indemnification agreement filed with our SEC reports. We purchase insurance to cover claims or a portion of the claims made against our directors and officers. Since a maximum obligation is not explicitly stated in our charter documents or in our indemnification agreements and will depend on the facts and circumstances that arise out of any future claims, the overall maximum amount of the obligations cannot be reasonably estimated. The fair value of these obligations was zero on our consolidated balance sheet as of October 27, 2012.

Royalties

We pay royalties for the right to sell certain products under various license agreements. During the three and nine months ended October 27, 2012, we recorded royalty expense of $0.4 million and $1.2 million, respectively, and $0.5 million and $1.6 million for the three and nine months ended October 29, 2011, respectively, which was recorded to cost of revenue.

Our wholly-owned subsidiary, Sigma Designs Israel SDI Ltd. (formerly, CopperGate Communication Ltd.), participated in programs sponsored by the Office of the Chief Scientist of Israel's Ministry of Industry, Trade and Labor, or the OCS, for the support of research and development activities that we conducted in Israel. Through October 27, 2012, we had obtained grants from the OCS aggregating to $4.8 million for certain of our research and development projects in Israel. We completed the most recent of these projects in 2007. We are obligated to pay royalties to the OCS, amounting to 4.5% of the sales of certain products up to an amount equal to the amount of the grants received, plus LIBOR-based interest. As of October 27, 2012, our remaining obligation under these programs was $0.7 million.

Contingencies

Litigation

On August 6, 2011, Powerline Innovations, LLC, or Powerline, filed suit against us, certain of our subsidiaries and many other named defendants, including Qualcomm Incorporated, Qualcomm Atheros, Inc., Broadcom Corporation and ST Microelectronics N.V. in the United States District Court for the Eastern District of Texas asserting infringement of U.S. Patent No. 5,471,190. The Powerline complaint seeks unspecified monetary damages and injunctive relief. At this time, we are unable to predict the outcome of this matter and, accordingly, cannot estimate the potential financial impact this action could have on our business, operating results, cash flows or financial position.

From time to time, we are involved in claims and legal proceedings that arise in the ordinary course of business. We expect that the number and significance of these matters will increase as our business expands. In particular, we could face an increasing number of patent and other intellectual property claims as the number of products and competitors in our industry grows. Any claims or proceedings against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time, result in the diversion of significant operational resources or cause us to enter into royalty or licensing agreements which, if required, may not be available on terms favorable to us or at all. If an unfavorable outcome were to occur against us, there exists the possibility of a material adverse impact on our financial position and results of operations for the period in which the unfavorable outcome occurs and, potentially, in future periods.

Third-party licensed technology

We license technologies from various third parties and incorporate that technology into our products. From time to time, we are audited by licensors of these technologies for compliance with the terms of these licenses. In the first quarter of fiscal 2013, we settled one such audit for $1.4 million. In the third quarter of fiscal 2013, we settled and accrued another audit for $6.3 million and the Company paid an amount of $6.0 million in the fourth quarter of fiscal 2013. The remaining $0.3 million will be paid in fiscal 2014 as per the settlement. Also in the third quarter of fiscal 2013, we settled another audit for $0.3 million payable in four quarterly equal installments commencing in September 2012. Concurrently, we negotiated a license agreement for this technology for a period of three years for an amount of $3.5 million, also payable in four quarterly equal installments from September 2012. The full amount of the license fees were recorded as Purchased IP during the third quarter of fiscal 2013 and will be amortized over the term. On December 4, 2012, we received a letter from another technology licensor notifying us of their intent to audit our compliance with the terms of a license agreement that we use in our DTV business. As of October 27, 2012, the end of our third fiscal quarter to which this report relates, we believed we were in compliance with our license agreements. However, we could be required to make additional payments as a result of pending or future compliance audits.

12. Net loss per share

Basic and diluted net loss per share for the periods presented is computed by dividing net loss by the weighted average number of common shares outstanding.

The following table sets forth the excluded anti-dilutive and excluded potentially dilutive securities for the three and nine months ended October 27, 2012 and October 29, 2011 (in thousands):

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| Stock options excluded because the effect of including would be anti-dilutive | 149 | 296 | 157 | 412 |
| Stock options excluded because exercise price is in excess of average stock price | 5,380 | 5,338 | 5,460 | 4,732 |
| Restricted stock awards and units excluded because the effect of including would be anti-dilutive | 147 | - | 87 | - |
| Restricted stock awards and units excluded because potential buyback shares exceed weighted average restricted stock units and awards outstanding | 68 | - | 290 | - |

13. Equity incentive plans and employee benefits

Stock incentive plans

We have adopted equity incentive plans that provide for the grant of stock option awards to employees, directors and consultants which are designed to encourage and reward their long-term contributions to us and provide an incentive for them to remain with us. These plans also align our employees' interest with the creation of long-term shareholder value. As of October 27, 2012, we have four stock option plans: the 2003 Director Stock Option Plan (the "2003 Director Plan"), the 2001 Stock Plan (the "2001 Plan"), the Amended and Restated 2009 Stock Incentive Plan (the "2009 Incentive Plan") and the CopperGate Share Option Plan (the "CopperGate Plan"). The 2009 Incentive Plan was approved by our shareholders in July 2009 along with the approval of a one-time stock option exchange program. The CopperGate Plan was assumed by us in connection with the acquisition of CopperGate in November 2009.

Our 2009 Incentive Plan provides for the grant of stock options, restricted stock, restricted stock units, and other stock-related and performance awards that may be settled in cash, stock or other property. In July 2009, 2,900,000 shares of common stock were reserved for issuance and in July 2011 an additional 2,000,000 shares were reserved for issuance under the 2009 Incentive Plan. In addition, up to 1,000,000 shares of common stock subject to stock awards outstanding under the 2001 Plan but terminated prior to exercise and would otherwise be returned to the share reserves under our 2001 Plan may become available for issuance under the 2009 Incentive Plan.

As of October 27, 2012, 2,008,500 shares were available for future grants under our stock incentive plans. Additionally, up to 648,106 shares of common stock subject to stock awards outstanding under the 2001 Plan may become available for issuance under the 2009 Incentive Plan. As of September 23, 2009, the 2001 Plan and the 2003 Director Plan were closed for future grants, however, these plans will continue to govern all outstanding options that we originally granted from each plan.

Stock Options

The total stock option activities and balances of our stock option plans are summarized as follows:

| | Number of Shares Outstanding | Weighted Average Exercise Price per Share | Weighted Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value |
|---|---|---|---|---|
| As of January 28, 2012 | 5,846,027 | $ 12.47 | 6.2 | $ 885,840 |
| Granted | - | - | | |
| Cancelled | (152,654) | 11.33 | | |
| Exercised | (25,801) | 2.18 | | |
| As of April 28, 2012 | 5,667,572 | $ 12.54 | 6.0 | 710,739 |
| Granted | 100,000 | 5.56 | | |
| Cancelled | (84,414) | 12.34 | | |
| Exercised | (5,201) | 3.23 | | |
| As of July 28, 2012 | 5,677,957 | $ 12.43 | 5.7 | 1,163,897 |
| Granted | 25,000 | 6.67 | | |
| Cancelled | (178,570) | 12.89 | | |
| Exercised | (113,142) | 2.67 | | |
| As of October 27, 2012 | 5,411,245 | $ 12.59 | 5.5 | 377,349 |

| | | | | |
|---|---|---|---|---|
| Ending vested and expected to vest | 5,348,767 | 12.64 | 5.5 | 357,049 |
| Ending exercisable | 3,929,066 | 13.35 | 4.8 | 236,950 |

The aggregate intrinsic value as of October 27, 2012 in the table above represents the total pretax intrinsic value, based on our closing stock price of $5.86 on that date, which would have been received by the option holders had all options holders exercised their options as of that date. The aggregate exercise date intrinsic value of options that were exercised under our stock option plans, determined as of the dates of option exercises, was $0.4 million and $0.5 million for the three and nine months ended October 27, 2012, respectively, and $0.3 million and $1.2 million for the three and nine months ended October 29, 2011, respectively. The total fair value of options which vested, determined as of the dates such options vested, was $1.7 million and $5.2 million during the three and nine months ended October 27, 2012, respectively, and $2.3 million and $8.4 million during the three and nine months ended October 29, 2011, respectively.

As of October 27, 2012, the unrecorded stock-based compensation balance related to stock options outstanding excluding estimated forfeitures was $11.9 million and will be recognized over an estimated weighted average amortization period of 2.5 years. The amortization period is based on the expected remaining vesting term of the options.

Restricted Stock Awards

We value restricted stock awards, or RSAs, using the quoted market price of the underlying stock on the date of grant. RSAs are granted under our 2009 Incentive Plan and reduce shares available to grant under the plan by 1.3 shares for every one share of restricted stock granted and consist of time-based restricted shares, which shares are subject to forfeiture until vested if length of service requirements are not met. The majority of RSAs vest over five years according to the terms specified in the individual grants. As of October 27, 2012, the unrecorded stock-based compensation balance related to RSAs outstanding excluding estimated forfeitures was $1.5 million and will be recognized over an estimated weighted average amortization period of 3.0 years. The following table sets forth the shares of restricted stock awards outstanding as of October 27, 2012:

| | Restricted Stock Awards | Weighted Average Grant Date Fair Value per Award | Aggregate Value |
|---|---|---|---|
| As of January 28, 2012 | 231,179 | $ 8.82 | |
| Granted | - | - | |
| Released | - | - | |
| As of April 28, 2012 | 231,179 | $ 8.82 | |
| Granted | - | - | |
| Released | (28,070 ) | 8.63 | |
| As of July 28, 2012 | 203,109 | $ 8.84 | |
| Granted | 10,980 | 6.83 | |
| Released | - | - | |
| As of October 27, 2012 | 214,089 | $ 8.74 | $ 1,871,138 |

Restricted Stock Units

We value restricted stock units, or RSUs, using the quoted market price of the underlying stock on the date of grant. RSUs are granted under our 2009 Incentive Plan and reduce shares available to grant under the plan by 1.3 shares for every one restricted stock unit granted and consist of time-based restricted stock units. The RSUs granted under this plan primarily vest over a period of four years according to the terms specified in the individual grants. As of October 27, 2012, the unrecorded stock-based compensation balance related to RSUs outstanding excluding estimated forfeitures was $3.5 million and will be recognized over an estimated weighted average amortization period of 3.1 years. The following table sets forth the shares of RSUs outstanding as of October 27, 2012:

| | Restricted Stock Units | Weighted Average Grant Date Fair Value per Unit | Aggregate Value |
|---|---|---|---|
| As of January 28, 2012 | 547,500 | $ 5.92 | |
| Granted | 23,075 | 6.03 | |
| Cancelled | (7,600 ) | 6.44 | |

| | | | | | | |
|---|---|---|---|---|---|---|
| As of April 28, 2012 | 562,975 | | $ | 5.62 | | |
| Granted | 84,625 | | | 5.56 | | |
| Released | (234 | ) | | 5.95 | | |
| Cancelled | (21,975 | ) | | 6.36 | | |
| As of July 28, 2012 | 625,391 | | $ | 6.74 | | |
| Granted | 91,778 | | | 6.79 | | |
| Released | (47 | ) | | 6.06 | | |
| Cancelled | (32,900 | ) | | 6.55 | | |
| As of October 27, 2012 | 684,222 | | $ | 5.86 | $ | 4,009,541 |

Employee stock purchase plan

As of October 27, 2012, we had reserved a total of 2,500,000 shares of common stock for issuance under the 2010 Purchase Plan, of which 1,106,269 shares had been issued

Valuation of stock-based compensation

The fair value of RSA and RSU awards is based on the quoted market price of the underlying stock at the date of grant. The fair value of stock option and employee stock purchase plan right awards is estimated at the grant date using the Black-Scholes option valuation model. The determination of fair value of stock option and employee stock purchase plan right awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards and actual employee stock option exercise behavior.

The fair value of each option and employee stock purchase plan right was estimated on the date of grant using the Black-Scholes option valuation model with the following weighted-average assumptions:

| | Three months ended | | | |
|---|---|---|---|---|
| | October 27, 2012 | | October 29, 2011 | |
| | Stock Option Plan | Employee Stock Purchase Plan | Stock Option Plan | Employee Stock Purchase Plan |
| Expected volatility | 50.58 % | 41.54 % | - | 49.49 % |
| Risk-free interest rate | 1.02 % | 0.16 % | - | 0.10 % |
| Expected term (in years) | 5.87 | 0.50 | - | 0.50 |
| Dividend yield | 0 % | 0 % | - | 0 % |
| Weighted average fair value at grant date | $3.18 | $1.70 | - | $2.27 |

| | Nine months ended | | | |
|---|---|---|---|---|
| | October 27, 2012 | | October 29, 2011 | |
| | Stock Option Plan | Employee Stock Purchase Plan | Stock Option Plan | Employee Stock Purchase Plan |
| Expected volatility | 51.77 % | 41.54 % | 51.78 % | 49.49 % |
| Risk-free interest rate | 0.86 % | 0.16 % | 1.90 % | 0.10 % |
| Expected term (in years) | 5.88 | 0.50 | 5.93 | 0.50 |
| Dividend yield | 0 % | 0 % | 0 % | 0 % |
| Weighted average fair value at grant date | $2.79 | $1.70 | $6.25 | $2.27 |

The computation of the expected volatility assumptions used in the Black-Scholes calculations for new stock option and employee stock purchase plan right awards is based on the historical volatility of our stock price, measured over a period equal to the expected term of the grants or purchase rights. The risk-free interest rate is based on the yield available on U.S. Treasury Strips with an equivalent remaining term. The expected term of stock options represents the weighted-average period that the stock options are expected to remain outstanding and was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based payment awards and vesting schedules. The expected term of employee stock purchase rights is the period of time remaining in the current offering period. The dividend yield assumption is based on our history of not paying dividends and assumption that we will not pay dividends in the future.

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The following table sets forth the total stock-based compensation expense that is included in each functional line item in the Condensed Consolidated Statements of Operations (in thousands):

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| Cost of revenue | $131 | $123 | $380 | $352 |
| Research and development | 1,375 | 1,544 | 4,346 | 4,760 |
| Sales and marketing | 458 | 475 | 1,412 | 1,634 |
| General and administrative | 539 | 664 | 1,940 | 2,386 |
| Total stock-based compensation | $2,503 | $2,806 | $8,078 | $9,132 |

401(k) tax deferred savings plan

We maintain a 401(k) tax deferred savings plan for the benefit of qualified employees who are U.S. based. Under the 401(k) tax deferred savings plan, U.S. based employees may elect to reduce their current annual taxable compensation up to the statutorily prescribed limit. We have a matching contribution program whereby we match employee contributions made by each employee at a rate of $0.25 per $1.00 contributed. The matching contributions to the 401(k) tax deferred savings plan totaled $0.2 million and $0.7 million for the three and nine months ended October 27, 2012, respectively, and $0.2 million and $0.7 million for the three and nine months ended October 29, 2011, respectively.

Group registered retirement savings plan

We maintain a Group Registered Retirement Savings Plan, or GRRSP, for the benefit of qualified employees who are based in Canada. Under the GRRSP, Canadian based employees may elect to reduce their annual taxable compensation up to the statutorily prescribed limit, which is $22,970 Canadian in calendar year 2012. We have a matching contribution program under the GRRSP whereby we match employee contributions made by each employee up to 2.5% of their annual salary. The matching contributions to the GRRSP for the three and nine months ended October 27, 2012 and October 29, 2011 were not significant.

Endowment insurance pension plan

Related to our acquisition of our DTV business in the second quarter of fiscal 2013, we added operations in Shanghai, China. It is required by the “Procedures of Shanghai Municipality on Endowment Insurance for Town Employees” to provide pension insurance for Shanghai employees. The plan is managed by the local authority and it is a mandatory plan. Under the current plan, the employee will contribute 8.0% of the annual base to the plan and the employer will match 22% of the annual base. For calendar year 2012, the annual base is capped at RMB 12,993. The matching contributions to the Pension Insurance totaled $0.5 million and $0.6 million for the three and nine months ended October 27, 2012, respectively.

Retirement pension plan

We maintain a Retirement Pension Plan for the benefit of qualified employees who are based in Denmark. Under the Retirement Pension Plan, Denmark-based employees may elect to reduce their annual taxable compensation up to their annual salary. We have a discretionary matching contribution program whereby we will contribute 3.0% of our employee’s annual salary and may elect to suspend or terminate future contributions at our option at any time. The matching contributions to the Retirement Pension Plan for the three and nine months ended October 27, 2012 and October 29, 2011 were not significant.

Severance plan

We maintain a severance plan for several Israeli employees pursuant to Israel's Severance Pay Law based on the most recent salary of the employees multiplied by the number of years of employment. Upon termination of employment, employees are entitled to one month salary for each year of employment or a portion thereof. As of October 27, 2012, we have an accrued severance liability of $1.3 million partially offset by $1.2 million of severance employee funds.

14. Segment and geographical information

Operating segments are defined as components of an enterprise for which separate financial information is available and evaluated regularly by the chief operating decision-maker in deciding how to allocate resources and in assessing performance. We are organized as, and operate in, one reportable segment. Our operating segment consists of our geographically based entities in the United States, Hong Kong, Israel and Singapore. Our chief operating decision-maker reviews consolidated financial information, accompanied by information about revenue by product group, target market and geographic region. We do not assess the performance of our geographic regions on other measures of income or expense or net income.

The following table sets forth net revenue for each geographic region based on the ship-to location of customers (in thousands):

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| Asia | $ 38,514 | $ 34,919 | $ 119,432 | $ 135,108 |
| North America | 4,799 | 2,176 | 11,990 | 7,076 |
| Europe | 17,589 | 2,563 | 34,101 | 4,492 |
| Other Regions | 3,003 | 67 | 6,891 | 375 |
| Net revenue | $ 63,905 | $ 39,725 | $ 172,414 | $ 147,051 |

The following table sets forth net revenue to each significant country based on the ship-to location of customers (in thousands):

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| China including Hong Kong | $26,108 | $29,163 | $88,651 | $116,260 |
| Hungary | 14,601 | - | 26,759 | - |
| Rest of World | 23,196 | 10,562 | 57,004 | 30,791 |
| Net revenue | $63,905 | $39,725 | $172,414 | $147,051 |

The following table sets forth the major customers that accounted for 10% or more of our net revenue:

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| TP Vision | 23 % | * | 16 % | * |
| Flextronics | 10 % | * | 11 % | * |
| Motorola | * | 13 % | * | 17 % |
| Alpha Networks | * | 14 % | * | * |
| Gemtek | * | 14 % | * | 25 % |

* This customer provided less than 10% of our net revenue in this period.

Two international customers accounted for 30% and 12% of total accounts receivable as of October 27, 2012. Four international customers accounted for 17%, 17%, 15% and 13% of total accounts receivable as of January 28, 2012.

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

You should read the following discussion in conjunction with our unaudited condensed consolidated financial statements and related notes in this Form 10-Q and our Form 10-K previously filed with the Securities and Exchange Commission. Except for historical information, the following discussion contains forward-looking statements within the meaning of Section 27A of the Securities Exchange Act of 1933 and Section 21E of the Securities Exchange Act of 1934. In some cases, you can identify forward-looking statements by terms such as "may," "might," "will," "objective," "intend," "should," "could," "can," "would," "expect," "believe," "estimate," "predict," "potential," "plan," or the negative of these terms, and similar expressions intended to identify forward-looking statements. These forward-looking statements, include, but are not limited to, statements about our capital resources and needs, including the adequacy of our current cash reserves, revenue, anticipated seasonality associated with our DTV business and our expectations that our gross margin will vary from period to period. These forward-looking statements involve risks and uncertainties. Our actual results may differ significantly from those projected in the forward-looking statements. Factors that might cause future results to differ materially from those discussed in the forward-looking statements include, but are not limited to, those discussed under Part II, Item 1A "Risk Factors" in this Form 10-Q as well as other information found in the documents we file from time to time with the Securities and Exchange Commission. Also, these forward-looking statements represent our estimates and assumptions only as of the date of this Form 10-Q. Unless required by U.S. federal securities laws, we do not intend to update any of these forward-looking statements to reflect circumstances or events that occur after the statement is made.

Overview

Our goal is to be a leader in intelligent media platforms for use in home entertainment and control. We focus on integrated chipset solutions that serve as the foundation for some of the world's leading consumer and business products, including televisions, set-top boxes and video networking products. We now have two primary business units that are responsible for driving business within our target markets through a common sales force. Our home Multimedia primarily system-on-chip (SoC) offerings for video entertainment applications. Our Home Connectivity business develops and markets primarily network controllers' offerings for video entertainment and home control applications.

Our chipset products and target markets

Products

Media Processor SoCs

Our media processor SoC product line consists of a range of functionally similar platforms that are based on highly integrated chips, embedded software, and hardware reference designs. These highly integrated chips typically include all the functions required to create a complete system solution with only the addition of memory. The integrated functions include applications processing (CPU), graphics processing (GPU), media processing (audio and video decoding/encoding), display processing, security management, memory control, and peripheral interfaces. Our embedded software suite provides an operating environment and coordinates the real-time processing of digital video and audio content, is readily customizable by our customers and is interoperable with multiple standard operating systems. Our reference system designs provide a hardware implementation of the circuit board, access to our embedded software suite, and sometimes provide a prototypical end-use product example for customer evaluation and use. We believe our SoC products deliver industry-leading performance in video decoding, picture quality, and software breadth, and this value proposition is why manufacturers select Sigma products.

Our SoCs are generally configured for a specific market segments, either digital television (DTV) or set-top box (STB), the latter of which includes related products such as connected media players. The primary difference between these devices is the interfaces they support. SoCs created for the DTV market offer HDMI plus analog encoded video as inputs and result in output to flat panel interfaces. SoCs created for the STB market offer Ethernet and other broadcast interfaces inputs and result in output to HDMI plus analog encoded video. Core components are therefore shared across these products while their configured hardware/software platforms and support are offered separately.

Home Networking Controllers

Our home networking product line consists of wired home networking controller chipsets that are designed to provide connectivity solutions between various home entertainment products and incoming video streams. We believe these connectivity solutions provide consumers additional connection choices with greater flexibility and allow system integrators and service providers an opportunity to reduce their time and cost of home networking installations. Our home networking solutions are based on the HomePNA (HPNA), HomePlug AV (HPAV), and G.hn standards. HPNA and HPAV are two of the current leading technology standards used for transferring internet protocol, or IP, content across coaxial cables, phone lines and power lines. G.hn is the next generation ITU standard ratified in 2010 to create a unified global standard across coaxial cables, phone lines and power lines. Products based on these technologies enable service providers such as telecommunication carriers, cable operators and satellite providers to deliver high definition television services (HDTV) and other media-rich applications throughout the home. To date, we have not generated significant revenue from our products based on HPAV or G.hn technologies.

Home Control and Energy Management Automation

Our home control and energy management automation product line consists of our wireless Z-Wave chipsets. These chipsets enable consumers to enjoy advanced home control and energy management automation functionality, such as home security, environmental and energy control and monitoring, within both new and existing homes. These devices consist of wireless transceiver devices along with a mesh networking protocol. Our Z-Wave chipsets utilize a low-bitrate, low-power; low-cost RF communication technology that provides an interoperable connected home security, monitoring and automation solution. These Z-Wave chipsets and the protocol they use to communicate commands have been built-into an ecosystem of over 700 certified products, mostly intelligent appliances for use within the home.

Other Products

We also offer certain legacy products that are sold into prosumer and other industrial applications. These products include our VXP brand video image processor chipsets and our video encoder chipsets. Our VXP chipsets are standalone high performance semiconductors that provide studio-quality video output or input for professional, prosumer and consumer applications and address applications including audio/video receivers, broadcast studios, digital cinema, digital signage, front-projection home theatre televisions, HDTV, medical imaging and video conferencing systems. Our video encoder chipsets are designed to capture video for visual telephony between set-top boxes, connected media players, VoIP devices, video conferencing TVs and video surveillance devices. These products account for a minor portion of Sigma's revenue.

Markets

Digital Television Market

We target the digital television market with our media processor SoC products. Specifically, we are focused on providing leading edge solutions for next generation Internet-enabled digital televisions or "SmartTV". These solutions include our enhanced picture quality, our frame-rate conversion chips, and our Internet-access software suite. We believe the SmartTV market will continue its strong growth and over time, incorporate much of the set-top box functionality. Additionally, we also sell selected legacy products into older television applications, such as analog TV and PC/TV products.

Set-top Box Market

We target the set-top box market with our media processor SoC products, our network controller products, and our home control products. Currently, our STB sales are primarily to set-top box OEMs (such as Motorola, Pace, Samsung, Tatung, and Netgem) that in turn sell to Telco network operators that deploy IPTV set-top boxes for delivering video services over a DSL network. We are a leading provider of high definition digital media processors for set-top boxes in the IPTV media processor market in terms of units shipped. Driven by market trends, we have also begun to market hybrid solutions (IP + broadcast) for use by Cable and Satellite network operators as well.

IPTV set-top boxes incorporating our media processors are deployed by telecommunications carriers globally including carriers in Asia, Europe and North America, such as AT&T, Deutsche Telekom, and SFR. We work with these carriers and set-top box providers as well as with systems software providers, such as Microsoft and various Linux providers, to design solutions that address carriers' specific requirements regarding features and performance.

Connected Media Player Market

We target the connected media player (CMP) market with our media processor SoC products. The connected media player market consists primarily of digital media adapters, or DMAs, portable media devices and wireless display devices that perform playback of digital media. Our media processors SoCs are used by consumer electronics providers, such as Iomega, Netgear and Western Digital in applications such as DMAs and other connected media player devices.

Video Networking Markets

We target gateways, routers, and other network equipment with our network controller products. This market consists of communication devices that use a standard protocol to connect equipment inside the home and stream IP-based video and audio, VoIP or data through wired connectivity. Our home networking products are currently used in residential gateways, optical network terminals, multiple-dwelling unit, or MDU, masters and network adapters by leading OEMs, such as Actiontec, Cisco Systems, Pace and Motorola.

Home Control Market

We target the home control market with our unique Z-Wave wireless product line. This market consists of a wide range of intelligent consumer appliances and home controllers that use wireless connectivity and control protocols to enable remote control of energy, security, and convenience features. Our Z-Wave devices are used in consumer products such as thermostats, light switches and door locks. These consumer products are designed by leading industry participants such as Danfoss, Ingersoll-Rand (Schlage and Trane), Leviton and Cooper Wiring.

Other Markets

We also sell products into other markets, such as Prosumer, digital signage, projection TV and PC-based add-in markets, which we refer to as our other markets. The prosumer market consists of studio quality audio/video receivers and monitors, video conferencing, digital projectors and medical video monitors. We derive minor revenue from sales of our products into these other markets.

Characteristics of Our Business

We do not enter into long-term commitment contracts with our customers and generate substantially all of our net revenue based on customer purchase orders. We forecast demand for our products based not only on our assessment of the requirements of our direct customers, but also on the anticipated requirements of the telecommunications carriers that our direct customers serve. We work with both our direct customers and these carriers to address the market demands and the necessary specifications for our technologies. However, our failure to accurately forecast demand can lead to product shortages that can impede production by our customers and harm our relationship with these customers or lead to excess inventory, which could negatively impact our gross margins in a particular period. During the year ended January 28, 2012, we recorded provisions for excess inventory of $9.0 million primarily due to a large end customer's transition to a next generation product sold by one of our competitors.

Our business is substantially dependent upon being designed into set-top boxes of large telecommunications carriers. If we are not designed into a particular generation of set-top boxes for our large target end customers, our operating results can be materially and adversely affected. We must spend a considerable amount of resources to compete for these design wins and the failure to obtain a design win for a particular generation of set-top boxes, and in particular for our large target end customers, means we likely would not recover a substantial portion of our expenses in competing for these design wins. However, if we do obtain these design wins, it is often the case that our end customer and direct customer will continue to incorporate our chipset solutions for that generation of set-top boxes. The set-top box industry is cyclical due to product transitions from generation to generation. Each generation typically incorporates emerging technologies, and so we must expend a considerable amount of research and development resources in order to compete in each of these cycles. Our failure to obtain a design win in a particular generation does not mean we necessarily will be unable to obtain a design win in the next generation. For example, our sales in the IPTV media processor market decreased in the past four fiscal quarters as a result of our inability to obtain certain design wins for our last generation of chipset solutions. However, we are in the process of competing for the next generation of set-top boxes, and we believe our chipset solutions contain features and prices that compete favorably with competitive offerings.

Many of our target markets are characterized by intense price competition. The semiconductor industry is highly competitive and, as a result, we expect our average selling prices to decline over time. On occasion, we have reduced our prices for individual customer volume orders as part of our strategy to obtain a competitive position in our target markets. The willingness of customers to design our chipsets into their products depends to a significant extent upon our ability to sell our products at competitive prices. If we are unable to reduce our costs sufficiently to offset any declines in product selling prices or are unable to introduce more advanced products with higher gross margins in a timely manner, we could see declines in our market share or gross margins. We expect our gross margins will vary from period to period due to changes in our average selling prices and average costs, volume order discounts, mix of product sales, amount of development revenue and provisions for inventory excess and obsolescence.

Our business is subject to seasonality as a result of selling a number of our semiconductor products to customers who manufacture products for the consumer electronics market. We expect to experience lower sales in our first and/or fourth fiscal quarters and higher sales in our second and/or third fiscal quarters as a result of the seasonality of demand associated with the consumer electronics markets. For example, we expect that our DTV business may experience seasonality typical of the consumer electronics markets, resulting in slower DTV sales in the first and fourth quarter of each calendar year and strongest DTV sales in the third calendar quarter. As a result of the seasonality in our business, our operating results may vary significantly from quarter to quarter.

Restructuring Plan

On October 31, 2012, we announced a restructuring plan, which we are in the early stages of implementing. Our restructuring plan includes targeted reductions in labor costs through headcount reduction and other related actions and targeted reductions in other operating expenses such as consulting, travel and subletting excess office space. We also plan to migrate to lower cost manufacturing components and processes. We expect to execute the restructuring plan in several phases and already completed the initial phase, which consisted of headcount reduction in our North American operations and the implementation of expense management measures across worldwide operations. For the three months ended October 27, 2012, we recognized a charge of $0.8 million in connection with our restructuring activities. We anticipate we will incur additional restructuring charges in future periods as we continue to implement our plan.

Critical Accounting Policies and Estimates

Management’s discussion and analysis of financial condition and results of operations are based on our unaudited condensed consolidated financial statements which have been prepared in accordance with United States generally accepted accounting principles. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts and disclosures of the assets and liabilities at the date of the unaudited condensed consolidated financial statements and also revenue and expenses during the period reported. By their nature, these estimates and judgments are subject to an inherent degree of uncertainty. Management bases its estimates and judgments on historical experience, market trends and other factors that are believed to be reasonable under the circumstances. These estimates form the basis for judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from what we anticipate and different assumptions or estimates about the future could change our reported results. Management believes the critical accounting policies as disclosed in our Annual Report on Form 10-K for the year ended January 28, 2012 reflect the more significant judgments and estimates used in preparation of our annual and interim financial statements except for the updated policies below.

Reclassifications: Certain prior fiscal year balances have been reclassified to conform to the current fiscal year presentation. In the first quarter of fiscal 2013, we concluded that it was appropriate to reclassify our purchased intellectual property, or IP, that is incorporated into our products, from software, equipment and leasehold improvements to intangible assets. The reclassification has no effect on previously reported Condensed Consolidated Statements of Operations for any period and does not affect previously reported cash flows from operations or from financing activities in the Condensed Consolidated Statements of Cash Flows. For comparability purposes, the corresponding gross assets and accumulated amortization of $22.0 million and $5.9 million, respectively, have been reclassified as of January 28, 2012. Such reclassifications had no effect on previously reported results of operations or retained earnings.

Restructuring charges: As discussed above, we announced a restructuring plan in October 2012 and began to execute the first phase under this plan. In the third quarter of fiscal 2013 we communicated a plan of termination to some employees. As a result, for the three months ended October 27, 2012, we recognized a charge of $0.8 million, of which $0.6 million related to research and development activities and $0.2 million related sales and marketing activities.

Software, equipment and leasehold improvements: Software, equipment and leasehold improvements are stated at cost. Depreciation and amortization for software, equipment and leasehold improvements are computed using the straight-line method based on the useful lives of the assets (one to five years) or the remaining lease term if shorter. Any allowance for leasehold improvements received from the landlord for improvements to our facilities is amortized using the straight-line method over the lesser of the remaining lease term or the useful life of the leasehold improvements. Repairs and maintenance costs are expensed as incurred.

Long-lived assets: The amounts and useful lives assigned to finite-lived intangible assets acquired, other than goodwill, impact the amount and timing of future amortization. Long-lived assets include intellectual property that we purchase for incorporation into our product designs. We begin amortizing such intellectual property at the time that we begin shipment of the associated products into which it is incorporated. We amortize the intellectual property over the estimated useful life of the associated products, which is generally two to three years. We assess the carrying value of long-lived assets, including purchased intangible assets, whenever events or changes in circumstances, such as a change in technology, indicate that the carrying value of these assets may not be recoverable. An impairment loss would be recognized when the sum of the undiscounted future net cash flows expected to result from the use of the asset and its eventual disposal is less than its carrying amount.

Results of Operations

The following table is derived from our unaudited condensed consolidated financial statements and sets forth our historical operating results as a percentage of net revenue for each of the periods indicated (in thousands, except percentages):

| | Three months ended | | | | Nine months ended | | | |
|---|---|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue |
| Net revenue | $ 63,905 | 100 % | $ 39,725 | 100 % | $ 172,414 | 100 % | $ 147,051 | 100 % |
| Cost of revenue | 38,423 | 60 % | 21,723 | 55 % | 95,257 | 55 % | 86,263 | 59 % |
| Gross profit | 25,482 | 40 % | 18,002 | 45 % | 77,157 | 45 % | 60,788 | 41 % |
| Operating expenses | | | | | | | | |
| Research and development | 26,741 | 42 % | 21,633 | 54 % | 76,505 | 44 % | 65,034 | 44 % |
| Sales and marketing | 12,774 | 20 % | 8,545 | 22 % | 27,457 | 16 % | 25,475 | 17 % |
| General and administrative | 6,007 | 10 % | 4,828 | 12 % | 21,874 | 13 % | 15,460 | 11 % |
| Restructuring | 821 | 1 % | - | * | 821 | 1 % | - | * |
| Goodwill impairment | - | * | 45,108 | 114 % | - | * | 45,108 | 31 % |
| Intangible assets impairment | - | * | 66,170 | 166 % | - | * | 66,170 | 45 % |
| Gain on acquisition | - | * | - | * | (1,417 ) | -1 % | - | * |
| Total operating expenses | 46,343 | 73 % | 146,284 | 368 % | 125,240 | 73 % | 217,247 | 148 % |
| Loss from operations | (20,861 ) | -33 % | (128,282 ) | -323 % | (48,083 ) | -28 % | (156,459 ) | -106 % |
| Interest and other income, net | 299 | 1 % | 542 | 1 % | 1,032 | 1 % | 2,095 | 1 % |
| Loss before provision for (benefit from) income taxes | (20,562 ) | -32 % | (127,740 ) | -322 % | (47,051 ) | -27 % | (154,364 ) | -105 % |
| Provision for (benefit from) income taxes | 18,889 | 30 % | (6,165 ) | -16 % | 19,520 | 12 % | (5,157 ) | -4 % |
| Net loss | $ (39,451 ) | -62 % | $ (121,575 ) | -306 % | $ (66,571 ) | -39 % | $ (149,207 ) | -101 % |

* The percentage of net revenue is less than one percent.

Net revenue

Our net revenue for the three months ended October 27, 2012 increased $24.2 million, or 61%, compared to the corresponding period in the prior fiscal year. Net revenue benefited $27.8 million from the addition of the DTV product line, resulting from our acquisition of certain assets from Trident Microsystems in the second quarter of fiscal 2013. Excluding DTV, our net revenue for the three months ended October 27, 2012 decreased $3.7 million, or 9%, compared to the corresponding period in the prior fiscal year. The net revenue decrease was primarily attributable to decreases in sales in the IPTV media processor and connected media player markets of $4.4 million and $6.4 million, respectively, partially offset by increases in the home networking market and license revenue from our home control and energy management technology of $5.3 million and $2.4 million, respectively.

Our net revenue for the nine months ended October 27, 2012 increased $25.4 million, or 17%, compared to the corresponding period in the prior fiscal year. Net revenue benefited $54.4 million from the addition of the DTV product line, resulting from our acquisition of certain assets from Trident Microsystems in the second quarter of fiscal 2013. Excluding DTV, our net revenue for the nine months ended October 27, 2012 decreased $29.0 million, or 20%, compared to the corresponding period in the prior fiscal year. The net revenue decrease was primarily attributable to decreases in sales in the IPTV media processor, connected media player and prosumer and digital audio/video markets of $24.6 million, $14.9 million, and $1.4 million respectively, partially offset by an increase in sales to the home networking market and license revenue from our home control and energy management technology of $8.0 million and $3.8 million, respectively.

Net revenue by target market

We sell our products into six primary target markets, which are the DTV market, home networking market, IPTV media processor market, home control and energy management market, prosumer and industrial audio/video market and connected media player market. We also sell a small amount of our chipsets into other markets, such as the digital signage, projection TV and PC-based add-in markets, which we refer to as our other market.

The following table sets forth our net revenue by target market and the percentage of net revenue represented by our product sales to each target market (in thousands, except percentages):

| | Three months ended | | | | Nine months ended | | | |
|---|---|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue |
| DTV | $27,831 | 44 % | $- | * | $54,407 | 32 % | $- | * |
| Home networking | 19,733 | 31 % | 14,418 | 36 % | 62,989 | 37 % | 54,971 | 38 % |
| IPTV media processor | 6,328 | 10 % | 10,774 | 27 % | 26,868 | 16 % | 51,431 | 35 % |
| Home control and energy management | 4,783 | 7 % | 2,339 | 6 % | 12,476 | 7 % | 8,632 | 6 % |
| Prosumer and industrial audio/video | 2,321 | 4 % | 2,839 | 7 % | 7,583 | 4 % | 8,992 | 6 % |
| Connected media player | 2,764 | 4 % | 9,136 | 23 % | 7,742 | 4 % | 22,614 | 15 % |
| Other | 145 | * | 219 | 1 % | 349 | * | 411 | * |
| Net revenue | $63,905 | 100 % | $39,725 | 100 % | $172,414 | 100 % | $147,051 | 100 % |

* This market provided less than 1% of our net revenue in this period.

DTV market: Our acquisition of the DTV assets of Trident Microsystems in the second quarter of fiscal 2013 allowed us to expand our participation in the DTV market, which previously had not been significant and had been included in the other markets category. We believe DTV products complement our existing IPTV media processor and connected media player products, which will provide substantial research and development leverage and improved operating scale to augment our ability to develop innovative solutions for the anticipated convergence of IP-video delivery across any device within the connected home. Net revenue from sales of our products into the DTV market was $27.8 million and $54.4 million for the three and nine months ended October 27, 2012, respectively, or 44% and 32%, respectively, of total net revenue. We expect that our DTV business may experience some seasonality common to consumer electronics markets as Trident Microsystems typically experienced slower DTV sales in the first quarter of the calendar year and strongest DTV sales in the third calendar quarter. We expect our revenue from the DTV market to continue to be a significant percentage of net revenues but will fluctuate in future periods as we develop and introduce new products for this market.

Home networking market: For the three and nine months ended October 27, 2012, net revenue from sales of our products into the home networking market increased $5.3 million or 37%, and $7.9 million, or 14%, respectively, compared to the corresponding periods in the prior fiscal year. The increase was primarily the result of a higher volume of units shipped partially due to our expansion into South America. Excluding DTV net revenues, our revenue from the home networking market as a percentage of total net revenue for the three and nine months ended October 27, 2012 was 55% and 53%, respectively, increases of 19 and 16 percentage points, respectively, compared to the corresponding periods in the prior fiscal year. The increase in home networking market revenues as a percentage of net revenues, excluding DTV, was primarily the result of the increase in demand in the home networking market as well as the decline in demand for our products in the connected media player and IPTV media processor markets. We expect our revenue from the home networking market to fluctuate in future periods based on changes in inventory levels at contract manufacturers who manufacture equipment incorporating our products for deployment by telecommunication providers.

IPTV media processor market: For the three and nine months ended October 27, 2012, net revenue from sales of our products into the IPTV media processor market decreased $4.4 million, or 41%, and $24.6 million, or 48%, respectively, compared to the corresponding periods in the prior fiscal year. This decline was attributable to a decline in units shipped, and lower average selling prices (“ASP”), as a result of reduced demand for our chipsets in the IPTV media processor market as a result of competitive factors in connection with product transitions at telecommunications service providers to the next generation IPTV media processor solutions. Excluding DTV net revenues, our revenue from the IPTV media processor market as a percentage of our total net revenue for the three and nine months ended October 27, 2012 was 18% and 23%, respectively, decreases of 10 and 12 percentage points, respectively, compared to the corresponding periods in the prior fiscal year. We expect our revenue from the IPTV media processor market to fluctuate in future periods as this revenue is dependent on IPTV service deployments by telecommunication service providers, adoption of our newer and future generations of our technology, changes in inventory levels at the contract manufacturers that supply them and competitive market pressures.

Home control and energy management market: For the three and nine months ended October 27, 2012, net revenue from sales of our products into the home control and energy management market increased $2.4 million, or 104%, and $4.0 million, or 47%, respectively, compared to the corresponding periods in the prior fiscal year. The increase was primarily the result of $2.1 million and $3.5 million of technology license revenue for the three and nine months ended October 27, 2012, respectively, and a slight increase in demand in the home control and energy management market evidenced by slightly increased unit shipments and improved ASPs. Excluding DTV net revenues, our revenue from the home control and energy management market as a percentage of our total net revenue for the three and nine months ended October 27, 2012 was 13% and 11%, respectively, increases of 7 and 5 percentage points compared to the corresponding periods in the prior fiscal year. The percentage point increase is primarily the result of the slight increase in demand and technology license revenue in the home control and energy management market as well as the decline in demand in the connected media player and IPTV media processor markets. We expect our revenue from the home control and energy management market to continue to increase in the foreseeable future.

Prosumer and industrial audio/video market: For the three and nine months ended October 27, 2012, net revenue from sales of our products into the prosumer and industrial audio/video market decreased $0.5 million, or 18%, and $1.4 million, or 16%, respectively, compared to the corresponding periods in the prior fiscal year. The three month decrease was primarily attributable to a decrease in demand for our products resulting in lower volume of units shipped partially offset by increased ASP. The nine month decrease was primarily attributable to a lower ASP. Excluding DTV net revenues, our revenue from sales into the prosumer and industrial audio/video market as a percentage of total net revenue for the three and nine months ended October 27, 2012 was 6%, a decrease of one percentage point and no change, respectively, compared to the corresponding periods in the prior fiscal year. We expect our revenue from the prosumer and industrial audio/video market to fluctuate based on our ability to obtain design wins in our customers' newer generation products, broad economic trends affecting business spending on video conferencing and high-end audio/video products and also discretionary consumer spending.

Connected media player market: For the three and nine months ended October 27, 2012, net revenue from sales of our products into the connected media player market decreased $6.4 million, or 70%, and $14.9 million, or 66%, respectively, compared to the corresponding periods in the prior fiscal year. The decrease in revenue was the result of a decrease of approximately 70% in units shipped, which was primarily due to competitive factors. Excluding DTV net revenues, our revenue from the connected media player market as a percentage of our total net revenue for the three and nine months ended October 27, 2012 was 8% and 7%, respectively, decreases of 15 and 9 percentage points, respectively, compared to the corresponding periods in the prior fiscal year. We expect our revenue from the connected media player market to fluctuate in future periods primarily due to the timing and nature of new product introductions by consumer electronics companies that incorporate our products and their transition to our newer-generation products. Additionally, due to decreases in the ASPs of our newer generation products relative to our older generation products, we must increase unit shipments of our products substantially in order to increase our revenue.

Other markets: Our other markets consist of PC add-in boards, development contracts, services and other ancillary markets. The revenue derived from our other markets was not a significant portion of our total net revenue.

Net revenue by product group

Our primary product group consists of our chipsets. Our chipsets are targeted toward manufacturers and large volume designer and manufacturer customers building products for the DTV, home networking, IPTV, home control and energy management, prosumer and industrial audio/video consumer electronic and connected media player markets. For the nine months ended October 27, 2012, sales of our chipsets accounted for approximately 98% of our net revenue compared to approximately 99% in the corresponding period in the prior fiscal year.

We derive a minor portion of our revenue from other products and services, including technology licenses, software development kits, engineering support services for hardware and software, engineering development for customization of chipsets and other accessories. The revenue derived from other products and services was not a significant portion of our total net revenue.

Net revenue by geographic region

The following table sets forth net revenue for each geographic region based on the ship-to location of customers (in thousands, except percentages):

| | Three months ended | | | | Nine months ended | | | |
|---|---|---|---|---|---|---|---|---|
| | October 27, | % of Net | October 29, | % of Net | October 27, | % of Net | October 29, | % of Net |

| | 2012 | Revenue | | 2011 | Revenue | | 2012 | Revenue | | 2011 | Revenue | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Asia | $38,514 | 60 | % | $34,919 | 88 | % | $119,432 | 69 | % | $135,108 | 92 | % |
| North America | 4,799 | 7 | % | 2,176 | 6 | % | 11,990 | 6 | % | 7,076 | 5 | % |
| Europe | 17,589 | 28 | % | 2,563 | 6 | % | 34,101 | 20 | % | 4,492 | 3 | % |
| Other Regions | 3,003 | 5 | % | 67 | * | | 6,891 | 5 | % | 375 | * | |
| Net revenue | $63,905 | 100 | % | $39,725 | 100 | % | $172,414 | 100 | % | $147,051 | 100 | % |

* The percentage of net revenue is less than one percent.

Asia: Our net revenue in absolute dollars from Asia increased $3.6 million, or 10%, and decreased $15.7 million, or 12%, for the three and nine months ended October 27, 2012, respectively, compared to the corresponding periods in the prior fiscal year. Excluding DTV revenue of $9.6 million and $19.2 million for the three and nine months ended October 27, 2012, respectively, absolute dollars from Asia decreased $6.0 million, or 17%, and $34.9 million, or 26%, respectively, compared to the corresponding periods in the prior fiscal year. For the comparative three and nine month periods, the decrease was primarily attributable to lower demand in the IPTV media processor and connected media player markets, partially offset by an increase in demand in the home networking market. Excluding DTV, our net revenue from Asia as a percentage of our total net revenue for the three and nine months ended October 27, 2012 was 80% and 85%, respectively, representing decreases of 8 and 7 percentage points, respectively, compared to the corresponding periods in the prior fiscal year.

As a percentage of total net revenue, China, including Hong Kong, represented 41% and 51% for the three and nine months ended October 27, 2012, respectively, decreases of 33 and 28 percentage points, respectively, compared to the corresponding periods in the prior fiscal year. The reduction in China as a percentage of total net revenue reflects the addition of DTV customers with operations located in Europe.

Europe: Our net revenue in absolute dollars from Europe increased $15.0 million, or 586%, and $29.6 million, or 659%, for the three and nine months ended October 27, 2012, respectively, compared to the corresponding periods in the prior fiscal year. Excluding DTV revenue of $17.0 million and $32.2 million for the three and nine months ended October 27, 2012, respectively, absolute dollars from Europe decreased $1.9 million, or 75%, and $2.6 million, or 57%, respectively, compared to the corresponding periods in the prior fiscal year. For the comparative three and nine month periods, the decrease in net revenue was primarily in the home networking market, and to a lesser extent, the prosumer and industrial audio/video and home control and energy management markets. Excluding DTV, our net revenue from Europe as a percentage of our total net revenue for the three and nine months ended October 27, 2012 was 2%, a decrease of 4 and 1 percentage points compared to the corresponding periods in the prior fiscal year.

As a result of the addition of DTV customers in the second quarter of fiscal 2013, sales into Hungary as a percentage of total net revenue was 23% and 16% for the three and nine months ended October 27, 2012, respectively, compared to none in the prior fiscal year.

North America: Our net revenue in absolute dollars from North America increased $2.6 million, or 121%, and $4.9 million, or 69%, for the three and nine months ended October 27, 2012, respectively, compared to the corresponding periods in the prior fiscal year. Excluding DTV revenue of $1.3 million and $3.1 million for the three and nine months ended October 27, 2012, respectively, absolute dollars from North America increased $1.4 million, or 63%, and $1.8 million, or 26%, respectively, compared to the corresponding periods in the prior fiscal year. For the comparative three-month periods, the increase in net revenue was primarily in the home control and energy management market, partially offset by declines in the prosumer and industrial audio/video and the connected media player markets. For the comparative nine-month periods, the increase in net revenue was primarily an increase in the home control and energy management market, partially offset by decreases in the prosumer and industrial audio/video, connected media player and IPTV media processor markets. Excluding DTV, our net revenue from North America as a percentage of our total net revenue for the three and nine months ended October 27, 2012 was 10% and 8%, respectively, an increase of 4 and 3 percentage points compared to the corresponding periods in the prior fiscal year.

Other regions: Our net revenue in absolute dollars from other regions increased $2.9 million, or 4,382%, and $6.5 million, or 1,738%, respectively, for the three and nine months ended October 27, 2012 compared to the corresponding periods in the prior fiscal year, primarily due to an increase in demand in the home networking market in Brazil. DTV revenues to customers in other regions were less than $0.1 million and $0.6 million for the three and nine months ended October 27, 2012, respectively.

Major Customers

The following table sets forth the major customers that accounted for 10% or more of our net revenue:

| | Three months ended | | | | Nine months ended | | | |
|---|---|---|---|---|---|---|---|---|
| | October 27, 2012 | | October 29, 2011 | | October 27, 2012 | | October 29, 2011 | |
| TP Vision | 23 | % | * | | 16 | % | * | |
| Flextronics | 10 | % | * | | 11 | % | * | |
| Motorola | * | | 13 | % | * | | 17 | % |

| | | | | |
|---|---|---|---|---|
| Alpha Networks | * | 14 % | * | * |
| Gemtek | * | 14 % | * | 25 % |

* This customer provided less than 10% of our net revenue in this period.

Gross Profit and Gross Margin

The following table sets forth our gross profit and gross margin (in thousands, except percentages):

| | Three months ended | | | Nine months ended | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % Change | October 29, 2011 | October 27, 2012 | % Change | October 29, 2011 |
| Gross profit | $ 25,482 | 42 % | $ 18,002 | $ 77,157 | 27 % | $ 60,788 |
| Gross margin | 39.9 % | | 45.3 % | 44.8 % | | 41.3 % |

Gross profit of $25.5 million for the three months ended October 27, 2012 increased $7.5 million compared to the corresponding period in the prior fiscal year. Gross profit during this period benefited from our expansion into the DTV market in the second quarter of fiscal 2013 and most of our other markets also contributed to the increase in gross profit. Our home networking market benefited from net revenue growth with higher margins. Our home control and energy management market benefited from an increase in net revenues primarily as a result of technology license revenue. Revenues in our connected media player decreased and our ASP reduced slightly with a reduction in costs to minimize the impact of the lower volumes.

The 5.4 percentage point decrease in gross margin percentage for the three months ended October 27, 2012 compared to the corresponding period in the prior fiscal year is primarily due to the addition of lower margin DTV revenue, which reduced our gross margin by approximately 11 percentage points. Excluding DTV, our gross margin improved compared to the prior year period due to growth in sales of higher-margin home networking products and a reduction in lower-margin revenues of our IPTV media processor and connected media player markets.

Gross profit of $77.2 million for the nine months ended October 27, 2012 increased $16.4 million compared to the corresponding period in the prior fiscal year primarily due to our expansion into the DTV market in the second quarter of fiscal 2013. However, gross profits in our other markets remained at approximately the same level as the corresponding period a year ago, while the provision for excess inventory was $5.7 million lower for the nine months ended October 27, 2012 than for the same period in the prior year. Additionally, for the nine months ended October 27, 2012, gross profit benefited from net revenue growth in the home networking market which have higher margins.

The 3.5 percentage point increase in gross margin percentage for the nine months ended October 27, 2012 compared to the corresponding period in the prior fiscal year is primarily due to revenue growth in our higher-margin home networking market and technology license revenue in our home control and energy management market, partially offset by sales of products acquired in our acquisition of the DTV business from Trident Microsystems. Additionally, our provision for excess inventory was lower during the nine months ended October 27, 2012, 1.3% as a percentage of total net revenue, than during the three months ended October 27, 2011, which was 5.4% as a percentage of total net revenue. For the three and nine months ended October 27, 2012, we benefited from the sale of previously written down products of $0.4 million and $3.0 million, respectively, which contributed to our gross margin by 0.6 percentage points and 4.8 percentage points, respectively.

Research and development expense

Research and development expense consists primarily of compensation and benefits for our employees engaged in research, design and development activities, stock-based compensation expense, engineering design tools, mask and prototyping costs, testing and subcontracting costs, and costs for facilities and equipment.

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The following table sets forth details of research and development expense for the three and nine months ended October 27, 2012 and October 29, 2011 (in thousands, except percentages):

| | Three months ended | | | | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | Increase/ (Decrease) | % Change |
| Compensation and benefits | $ 16,991 | 27 % | $ 12,514 | 31 % | $ 4,477 | 36 % |
| Development and design costs | 3,090 | 5 % | 3,247 | 8 % | (157 ) | -5 % |
| Depreciation and amortization | 2,346 | 4 % | 2,705 | 7 % | (359 ) | -13 % |
| Stock-based compensation | 1,375 | 2 % | 1,544 | 4 % | (169 ) | -11 % |
| Other | 2,939 | 4 % | 1,623 | 4 % | 1,316 | 81 % |
| Total research and development expense | $ 26,741 | 42 % | $ 21,633 | 54 % | $ 5,108 | 24 % |

| | Nine months ended | | | | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | Increase/ (Decrease) | % Change |
| Compensation and benefits | $ 49,876 | 29 % | $ 37,113 | 25 % | $ 12,763 | 34 % |
| Development and design costs | 9,535 | 6 % | 10,549 | 7 % | (1,014 ) | -10 % |
| Depreciation and amortization | 6,543 | 4 % | 7,409 | 5 % | (866 ) | -12 % |
| Stock-based compensation | 4,346 | 2 % | 4,760 | 3 % | (414 ) | -9 % |
| Other | 6,205 | 3 % | 5,203 | 4 % | 1,002 | 19 % |
| Total research and development expense | $ 76,505 | 44 % | $ 65,034 | 44 % | $ 11,471 | 18 % |

The three and nine months ended October 27, 2012 include $5.2 million and $11.9 million, respectively, for DTV research and development activities subsequent to our acquisition of certain assets used in the digital TV business from Trident Microsystems in the second quarter of fiscal 2013. Additionally, for the three and nine months ended October 27, 2012, compensation and benefits increased primarily due to an increase in headcount to support new product development as well as salary increases. For the nine months ended October 27, 2012, Development and design costs decreased mainly due to a reduction in engineering supplies, prototype masks and wafer purchases, partially offset by an increase in outside services. For the nine months ended October 27, 2012, Depreciation and amortization decreased due to lower amortization of acquired intangible assets as a result of related acquired intangible assets impairment charges. Other expense increased mainly due to an increase in IT infrastructure expenses, rent and travel incurred by the higher headcount. As part of our restructuring plan discussed above, we anticipate reductions in research and development expense.

Sales and marketing expense

Sales and marketing expense consists primarily of compensation and benefits costs, including commissions to our direct sales force, stock-based compensation expense, trade show, travel and entertainment expense and external commissions.

The following table sets forth details of sales and marketing expense for the three and nine months ended October 27, 2012 and October 29, 2011 (in thousands, except percentages):

| | Three months ended | | | | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | Increase/ (Decrease) | % Change |
| Compensation and benefits | $ 4,369 | 7 % | $ 4,130 | 11 % | $ 239 | 6 % |
| Depreciation and amortization | 486 | 1 % | 2,116 | 5 % | (1,630 ) | -77 % |
| Trade shows, travel and entertainment | 819 | 1 % | 824 | 2 % | (5 ) | -1 % |
| Stock-based compensation | 458 | 1 % | 475 | 1 % | (17 ) | -4 % |
| External commissions | 160 | * | 228 | 1 % | (68 ) | -30 % |
| Other | 6,482 | 10 % | 772 | 2 % | 5,710 | 740 % |
| Total sales and marketing expense | $ 12,774 | 20 % | $ 8,545 | 22 % | $ 4,229 | 49 % |

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| | Nine months ended | | | | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | Increase/ (Decrease) | % Change |
| Compensation and benefits | $ 13,821 | 8 % | $ 11,722 | 8 % | $ 2,099 | 18 % |
| Depreciation and amortization | 1,347 | 1 % | 6,319 | 4 % | (4,972 ) | -79 % |
| Trade shows, travel and entertainment | 2,232 | 1 % | 2,532 | 2 % | (300 ) | -12 % |
| Stock-based compensation | 1,412 | 1 % | 1,634 | 1 % | (222 ) | -14 % |
| External commissions | 519 | * | 1,012 | 1 % | (493 ) | -49 % |
| Other | 8,125 | 5 % | 2,256 | 1 % | 5,869 | 260 % |
| Total sales and marketing expense | $ 27,457 | 16 % | $ 25,475 | 17 % | $ 1,982 | 8 % |

* The percentage of net revenue is less than one percent.

The three and nine months ended October 27, 2012 include $0.5 million and $1.4 million, respectively, for DTV sales and marketing activities subsequent to our acquisition of certain assets used in the digital TV business from Trident Microsystems in the second quarter of fiscal 2013. Additionally, for the three and nine months ended October 27, 2012, compensation and benefits increased primarily due to salary increases, the increase in headcount and increased commissions due to the higher revenue. Depreciation and amortization decreased due to lower amortization of acquired intangible assets as a result of related acquired intangible asset impairment charges recorded in our third quarter of fiscal 2012. Other expense increased due to a $5.7 million settlement recorded in the current period in connection with a failure to comply with a third party technology licensor's custodial and reporting requirements (see note 11 of the Notes to the Unaudited Condensed Consolidated Financial Statements ). As part of our restructuring plan discussed above, we anticipate reductions in sales and marketing expense.

General and administrative expense

General and administrative expense consists primarily of compensation and benefits costs, stock-based compensation expense, legal, accounting and other professional fees and facilities expenses.

The following table sets forth details of general and administrative expense for the three and nine months ended October 27, 2012 and October 29, 2011 (in thousands, except percentages):

| | Three months ended | | | | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % of Net Revenue | October 29, 2011 | % of Net Revenue | Increase/ (Decrease) | % Change |
| Compensation and benefits | $ 2,088 | 3 % | $ 2,049 | 5 % | $ 39 | 2 % |
| Legal and accounting fees | 1,027 | 2 % | 768 | 2 % | 259 | 34 % |
| Stock-based compensation | 539 | 1 % | 664 | 2 % | (125 ) | -19 % |

| | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Outside service fees | | 259 | * | | | 145 | * | | | 114 | | 79 | % |
| Facilities and IT infrastructure costs | | 1,208 | 2 | % | | 600 | 2 | % | | 608 | | 101 | % |
| Other | | 886 | * | | | 602 | 1 | % | | 284 | | 47 | % |
| Total general and administration expense | $ | 6,007 | 9 | % | $ | 4,828 | 12 | % | $ | 1,179 | | 24 | % |

| | | Nine months ended | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | October 27, 2012 | % of Net Revenue | | | October 29, 2011 | % of Net Revenue | | | Increase/ (Decrease) | | % Change | |
| Compensation and benefits | $ | 6,916 | 4 | % | $ | 6,255 | 5 | % | $ | 661 | | 11 | % |
| Legal and accounting fees | | 4,417 | 3 | % | | 2,636 | 2 | % | | 1,781 | | 68 | % |
| Stock-based compensation | | 1,940 | 1 | % | | 2,386 | 2 | % | | (446 | ) | -19 | % |
| Outside service fees | | 1,372 | 1 | % | | 524 | * | | | 848 | | 162 | % |
| Facilities and IT infrastructure costs | | 3,748 | 2 | % | | 1,706 | 1 | % | | 2,042 | | 120 | % |
| Other | | 3,481 | 2 | % | | 1,953 | 1 | % | | 1,528 | | 78 | % |
| Total general and administration expense | $ | 21,874 | 13 | % | $ | 15,460 | 11 | % | $ | 6,414 | | 41 | % |

* The percentage of net revenue is less than one percent.

The three and nine months ended October 27, 2012 include $0.5 million and $2.3 million, respectively, for DTV general and administrative activities subsequent to our acquisition of certain assets used in the digital TV business from Trident Microsystems in the second quarter of fiscal 2013. Additionally, for the three and nine months ended October 27, 2012, compensation and benefits increased primarily due to salary increases and an increase in headcount. The increase in legal and accounting fees is primarily due to legal fees incurred in connection with our acquisition of certain assets used in the digital TV business from Trident Microsystems and our annual meeting of shareholders. The decrease in stock-based compensation expense is primarily due to the timing of options and awards grants and option cancellations. The increase in facilities and IT infrastructure is primarily due to higher IT infrastructure expenses related to the integration of DTV. As part of our restructuring plan discussed above, we anticipate reductions in general and administration expense.

Goodwill and indefinite-lived intangible assets impairment

As of October 29, 2011, we concluded that an interim review of the carrying value of our goodwill and indefinite-lived intangible assets should be performed due to continued reductions in our profitability, sales forecasts and market capitalization. As a result, we recognized a goodwill impairment charge of $45.1 million and an impairment charge for our indefinite-lived in-process research and development intangible assets of $11.1 million during the third quarter of fiscal 2012. There have been no such charges recorded during the three and nine months ended October 27, 2012.

Impairment and amortization of intangible assets

We begin amortizing intellectual property at the time that we begin shipment of the associated products into which it is incorporated. We amortize the intellectual property over the estimated useful life of the associated products, which is generally two to three years. During the third quarter of fiscal 2012, we performed a review of the carrying value of our acquired intangible assets due to continued reductions in our profitability and sales forecasts, and negative cash flows from operations. As a result, we recognized an intangible asset impairment charge of $55.1 million.

Acquired intangible assets subject to amortization were as follows as of October 27, 2012 (in thousands, except for years):

| | As of October 27, 2012 | | | | |
|---|---|---|---|---|---|
| | Gross Value | Impairment | Accumulated Amortization and Effect of Currency Translation | Net Value | Weighted Average Remaining Amortization Period (Years) |
| Developed technology | 76,607 | (24,614) | (32,872) | 19,121 | 4.0 |
| Customer relationships | 50,705 | (30,486) | (15,446) | 4,773 | 4.1 |
| Purchased IP - amortizing | 15,876 | - | (6,872) | 9,004 | 2.3 |
| Trademarks | 2,677 | - | (1,937) | 740 | 6.1 |
| Non-compete agreements | 1,400 | - | (1,400) | - | - |
| | 147,265 | (55,100) | (58,527) | 33,638 | 3.6 |
| | 10,711 | - | - | 10,711 | |

| | | | | |
|---|---|---|---|---|
| Purchased IP - not yet deployed | | | | |
| In-process research and development | 11,070 | (11,070 ) | - | - |
| | 169,046 | (66,170 ) | (58,527 ) | 44,349 |

We classify amortization of acquired developed technology as a cost of revenue, which was $1.6 million and $4.8 million for the three and nine months ended October 27, 2012, respectively, and $2.7 million and $8.1 million for the three and nine months ended October 29, 2011, respectively. We also classify amortization of purchased IP as a cost of revenue, which was $1.1 million and $2.0 million for the three and nine months ended October 27, 2012, respectively, and $0.9 million and $1.9 million for the three and nine months ended October 29, 2011, respectively. We classify as sales and marketing expense our expense from the amortization of acquired customer relationships and trademarks, which was $0.4 million and $1.1 million for the three months and nine months ended October 27, 2012, respectively, and $2.0 million and $6.1 million for the three and nine months ended October 29, 2011, respectively. As of October 27, 2012, the unamortized balance from our intangible assets was $44.3 million, which we intend to amortize to future periods based on the remaining estimated useful life of each acquired intangible asset. If we purchase additional intangible assets in the future, our cost of revenue or other operating expenses may increase from the amortization of those assets.

Stock-based compensation expense

The following table sets forth the total stock-based compensation expense that is included in each functional line item in the Condensed Consolidated Statements of Operations (in thousands):

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | October 27, 2012 | October 29, 2011 | October 27, 2012 | October 29, 2011 |
| Cost of revenue | $ 131 | $ 123 | $ 380 | $ 352 |
| Research and development | 1,375 | 1,544 | 4,346 | 4,760 |
| Sales and marketing | 458 | 475 | 1,412 | 1,634 |
| General and administrative | 539 | 664 | 1,940 | 2,386 |
| Total share-based compensation | $ 2,503 | $ 2,806 | $ 8,078 | $ 9,132 |

The expensing of employee stock options, restricted stock awards and restricted stock units grants will continue to have an adverse impact on our results of operations.

Interest and other income, net

The following table sets forth net interest and other income and the related percentage change (in thousands, except percentages):

| | Three months ended | | | Nine months ended | | |
|---|---|---|---|---|---|---|
| | October 27, 2012 | % Change | October 29, 2011 | October 27, 2012 | % Change | October 29, 2011 |
| Interest and other income, net | $ 299 | -45 % | $ 542 | $ 1,032 | -51 % | $ 2,095 |

Our other income and expense, net, primarily consists of interest income from marketable securities, income from refundable research and development credits, gains or losses on foreign exchange transactions, gains or losses on sales of marketable securities and gains or losses on currency hedging activities. The decrease of $0.2 million and $1.1 million for the three and nine months ended October 27, 2012, respectively, compared to the corresponding periods in the prior fiscal year was due primarily to foreign exchange losses as a result of the U.S. dollar weakening compared to the Israeli shekel, Euro, Danish krone and Canadian dollar and losses from hedging activities. Additionally, investment income decreased in connection with market value fluctuations and a lower level of marketable security investments from liquidating marketable securities to fund our acquisition of certain assets used in the digital TV business from Trident Microsystems in the second quarter of fiscal 2013.

Provisions for income taxes

We recorded provisions for income taxes of $18.9 million and $19.5 million for the three and nine months ended October 27, 2012, respectively, and a benefit of $6.2 million and $5.2 million for the three and nine months ended October 29, 2011, respectively. Included in our provisions for income taxes are foreign exchange gains or losses on unsettled income tax liabilities.

In assessing the carrying value of its deferred tax assets, the Company considers whether it is more likely than not that some portion, or all, of the deferred tax assets will be realized. The ultimate realization of the deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences and tax attributes are deductible.

During the three months ended October 27, 2012, the Company recorded a non-cash charge to establish a valuation allowance of $17.9 million against its gross U.S. federal deferred tax assets. The valuation allowance is determined in accordance with the provisions of ASC 740, Tax Provisions, which requires an assessment of both positive and negative evidence when measuring the need for a valuation allowance. Evidence, such as operating results during recent years, is given more weight than anticipated future income when, due to a current lack of visibility, there is a greater degree of uncertainty that the level of future profitability needed to recognize the deferred assets will be achieved. The Company's cumulative U.S. loss in the most recent three-year period, inclusive of the U.S. loss for the quarter ended October 27, 2012, represented sufficient negative evidence to require a valuation allowance under the provisions of ASC 740. The Company intends to maintain a valuation allowance until sufficient positive evidence exists to support its reversal. The amount of the deferred tax assets actually realized, however, could vary if there are differences in the timing or amount of future reversals of existing deferred tax liabilities.

Liquidity and Capital Resources

The following table sets forth the balances of cash and cash equivalents and short-term marketable securities (in thousands):

| | October 27, 2012 | January 28, 2012 |
|---|---|---|
| Cash and cash equivalents | $ 49,331 | 44,283 |
| Short-term marketable securities | $ 17,366 | 42,134 |
| | $ 66,697 | $ 86,417 |

As of October 27, 2012, our principal sources of liquidity consisted of cash and cash equivalents and short-term marketable securities of $66.7 million, which represents a decrease of $19.7 million from $86.4 million at January 28, 2012. We liquidated a significant portion of our short-term marketable securities to generate $39.7 million cash used for our asset acquisition of certain assets from Trident Microsystems, which was completed in the second quarter of fiscal 2013. Cash used in operations was $5.0 million and purchases of software, equipment and leasehold improvements were $9.5 million. These outflows of cash, cash equivalents and short-term marketable securities were partially offset by $2.5 million of net proceeds from employee stock plans and transfers from long-term marketable securities.

As of October 27, 2012, we held $30.4 million of long-term marketable securities. Although these marketable securities have maturities of greater than one year, we classify them as available-for-sale and may access these funds prior to their contractual maturities.

The following table sets forth the primary net cash inflows and outflows (in thousands):

| | Nine months ended | |
|---|---|---|
| | October 27, 2012 | October 29, 2011 |
| Net cash provided by (used in): | | |
| Operating activities | $ (4,998) | $ (4,336) |
| Investing activities | 7,814 | (19,490) |
| Financing activities | 2,191 | 3,653 |
| Effect of foreign exchange rate changes on cash and cash equivalents | 41 | 91 |
| Net increase (decrease) in cash and cash equivalents | $ 5,048 | $ (20,082) |

Cash flows from operating activities

Net cash used in operating activities of $5.0 million for the nine months ended October 27, 2012 was primarily due to a net loss of $66.6 million, partially offset by $45.6 million of non-cash charges included in the net loss and $16.0 million of cash flow increases reflected in the net change of operating assets and liabilities. Non-cash charges consisted primarily of an $18.1 million change in deferred tax assets, $17.1 million of depreciation and amortization, $8.1 million of stock-based compensation and a $3.6 million provision for excess and obsolete inventories, partially offset by a $1.4 million gain recognized from our acquisition of the DTV business from Trident Microsystems, reflecting that the sum of the fair value of net assets we acquired exceeded the acquisition cost. Cash flow increases reflected in the net change of operating assets and liabilities consisted primarily of an $18.2 million increase in accrued liabilities, an $11.3 million increase in accounts payable, and a $2.3 million decrease in inventories, partially offset by a $7.4 million increase in prepaid expenses and other current assets, $3.5 million increase in accounts receivable, a $2.7 million increase in other non-current assets and a $2.3 million reduction in other long-term liabilities. The changes in operating assets and liabilities generally reflect the increase in revenues and related expenses resulting from the expansion of our DTV business subsequent to the Trident Microsystems asset acquisition.

Net cash used in operating activities of $4.3 million for the nine months ended October 29, 2011 was primarily due to a net loss of $149.2 million, a decrease of $7.9 million in accrued liabilities, a decrease of $5.6 million in other long-term liabilities, a decrease of $5.2 million in accounts payable and a $0.6 million increase in prepaid expenses and other current assets. These amounts were partially offset by a $7.4 million decrease in inventories, a $5.4 million decrease in accounts receivable, and non-cash expenses of $151.3 million, consisting primarily of $111.3 million in impairment of goodwill and intangible assets, $23.7 million in depreciation and amortization, $9.1 million in stock-based compensation expense and $8.1 million in provision for excess and obsolete inventory. The decrease in accounts receivable was primarily the result of the decrease in revenues. The decrease in inventories was primarily due to an $8.1 million write-off of excess inventory in the level of our die bank and other purchased materials during the current nine-month period in response to lower demand. Additionally, lower demand has resulted in a decrease in our annualized rate of inventory turns to 4.2 times per year for the fiscal quarter ended October 27, 2012 compared to 3.8 times per year for the same quarter last year. The decreases in accounts payable and accrued liabilities were primarily due to lower inventory purchases and the timing of payments for inventories and engineering software tools. The decrease in other long-term liabilities was due to a reduction in long-term deferred tax liabilities as a result of the impairment of intangible assets.

Cash flows from our operating activities will continue to fluctuate based upon our ability to grow net revenues while managing the timing of payments to us from customers and from us to vendors, the timing of inventory purchases and subsequent manufacture and sale of our products.

Cash flows from investing activities

Net cash provided by investing activities was $7.8 million for the nine months ended October 27, 2012, which was primarily due to net sales of marketable securities of $57.1 million, partially offset by payments of $39.7 million in connection with the Trident Microsystems asset acquisition and $9.5 million for capital assets, primarily to support research and development activities.

Net cash used in investing activities was $19.5 million for the nine months ended October 29, 2011, which was primarily due to purchases of capital assets such as engineering software tools, equipment and leasehold improvements of $9.3 million, cash paid in connection with the May 21, 2011 acquisition of $5.0 million, receipt of an additional note receivable from a privately held company of $2.1 million, and net purchases of marketable securities of $2.9 million.

Cash flows from financing activities

Net cash provided by financing activities was $2.2 million in the nine months ended October 27, 2012, which was primarily due to proceeds from exercises of employee stock options of $2.5 million.

Net cash provided by financing activities was $3.7 million in the nine months ended October 29, 2011, which primarily consisted of proceeds from participation in the employee stock purchase plan and exercises of employee stock options.

While we generated cash from operations for fiscal 2011, 2010 and 2009, we consumed cash in operations in fiscal 2012 and in the first nine months of fiscal 2013 and it is possible that our operations will consume additional cash in future periods. Based on our current anticipated cash needs, we believe that our current balances of cash, cash equivalents and short-term marketable securities will be sufficient to meet our anticipated working capital requirements, obligations, capital expenditures, strategic investments and other cash needs for at least the next twelve months. However, it is possible that we may need to raise additional funds to finance our activities during or beyond the next 12 months and our future capital requirements may vary significantly from those currently planned. Our cash, cash equivalent and marketable securities balances will continue to fluctuate based upon our ability to grow revenue, reduce our expenses, the timing of payments to us from customers and to vendors from us and the timing of inventory purchases and subsequent manufacture and sale of our products. From time to time, we may also increase our long-term investments which will cause our marketable securities balances to decrease.

Our marketable securities include primarily corporate bonds, money market funds, US agency discount notes and municipal notes and bonds. We monitor all our marketable securities for impairment and if these securities are reported to have had a decline in fair value, we may need to use significant judgment to identify events or circumstances that would likely have a significant adverse effect on the future value of each investment including: (i) the nature of the investment; (ii) the cause and duration of any impairment; (iii) the financial condition and near term prospects of the issuer; (iv) for securities with a reported decline in fair value, our ability to hold the security for a period of time sufficient to allow for any anticipated recovery of fair value; (v) the extent to which fair value may differ from cost; and (vi) a comparison of the income generated by the securities compared to alternative investments. We would recognize an impairment charge if a decline in the fair value of our marketable securities is judged to be other-than-temporary.

Contractual obligations and commitments

We generally do not have guaranteed price or quantity commitments from any of our suppliers. Additionally, we generally acquire products for sale to our customers based on purchase orders received as well as forecasts from such customers. Purchase orders with delivery dates greater than twelve weeks are typically cancelable without penalty to our customers. We currently place non-cancelable orders to purchase semiconductor wafers, other materials and finished goods from our suppliers on an eight to twelve week lead-time basis.

The following table sets forth the amounts of payments due under specified contractual obligations as of October 27, 2012 (in thousands):

| | Payments Due by Period | | | | |
|---|---|---|---|---|---|
| | Remainder Fiscal 2013 | Fiscal 2014 - 2015 | Fiscal 2016 - 2017 | Fiscal 2018 and Thereafter | Total |
| Operating leases | $ 1,372 | $ 8,950 | $ 5,424 | $ 866 | $ 16,612 |
| Purchase obligations | 27,043 | - | - | - | $ 27,043 |
| Total contractual obligations | $ 28,415 | $ 8,950 | $ 5,424 | $ 866 | $ 43,655 |

Recent accounting pronouncements

See Note 1, “Recent Accounting Pronouncements,” of the Notes to Unaudited Condensed Consolidated Financial Statements of this Form 10-Q.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following discussion about our market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We face exposure to market risk from adverse movements in interest rates and foreign currency exchange rates, which could impact our operations and financial condition. To mitigate some of the foreign currency exchange rate risk, we utilize derivative financial instruments to hedge certain foreign currency exposures. We do not use derivative financial instruments for speculative or trading purposes.

Interest rate sensitivity: As of October 27, 2012 and January 28, 2012, we held approximately $97.1 million and $148.4 million, respectively, of cash, cash equivalents and short-term and long-term marketable securities. If short-term interest rates were to decrease 10%, the decreased interest income associated with these cash, cash equivalents and marketable securities would not have a significant impact on our net income and cash flows.

Foreign currency exchange rate sensitivity: We transact our revenues in U.S. dollars. The U.S. dollar is our functional and reporting currency except for our subsidiaries in Canada, China, Denmark, France, Germany, Japan, The Netherlands, Taiwan and Vietnam where the Canadian dollar, Chinese renambi, Danish krone, Euro, Euro, Japanese Yen, Euro, Taiwanese dollar and Vietnamese dong are the primary financial currencies, respectively. Additionally, significant portions of our Israel subsidiary’s expenses are payroll related and are denominated in Israeli shekels. This foreign currency exposure gives rise to market risk associated with exchange rate movements of the U.S. dollar against the Israeli shekel. To the extent the U.S. dollar weakens against the Israeli shekel, our Israeli subsidiary will experience a negative impact on its results of operations.

As of October 27, 2012, with the exception of our Israel operation, we had not entered into foreign exchange forward contracts to hedge certain balance sheet exposures or inter-company balances against future movements in foreign exchange rates. For our Israel operation, we do hedge portions of our forecasted expenses that are denominated in the Israeli shekel with foreign exchange forward contracts. As of October 27, 2012, we had foreign exchange contracts with notional values of approximately $12.3 million that mature on or before September 23, 2013. These hedges of cash flow exposures will only mitigate a portion of our foreign exchange exposure. If foreign exchange rates were to weaken against the U.S. dollar immediately and uniformly by 10% from the exchange rates at October 27, 2012, the notional value of our derivative instruments would decline and we would record a foreign exchange loss of approximately $0.8 million, a portion of which should be offset by our foreign exchange hedging activities.

We maintain certain cash balances denominated in the Canadian dollar, Chinese renambi, Danish krone, Euro, Hong Kong dollar, Israeli shekel, Singapore dollar, Taiwanese dollar and Vietnamese Dong. If foreign exchange rates were to weaken against the U.S. dollar immediately and uniformly by 10% from the exchange rates at October 27, 2012, the fair value of these foreign currency amounts would decline by $0.7 million.

ITEM 4. CONTROLS AND PROCEDURES

We are committed to maintaining disclosure controls and procedures designed to ensure that information required to be disclosed in our periodic reports filed under the Securities and Exchange Act of 1934, as amended (the "Exchange Act") is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and we necessarily are required to apply our judgment in evaluating the cost-benefit relationship of possible controls and procedures and implementing controls and procedures.

As of October 27, 2012, the end of the period covered by this Quarterly Report on Form 10-Q, we have, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of the design and effectiveness of our disclosure controls and procedures, as such terms are defined in Rule 13a-15(e) and Rule 15d-15(e) under the Exchange Act. Based on this evaluation, we have concluded that our disclosure controls and procedures were effective as of October 27, 2012.

During the second and third quarters of fiscal 2013, we experienced a significant amount of turnover in our finance and accounting department. We have hired necessary and key personnel in response to certain departures in this department. We are still assessing the impact that this employee turnover may have on our internal control over financial reporting.

On May 4, 2012, we completed our acquisition of certain assets used in the digital TV, or DTV, business from Trident Microsystems. See Note 8. "Business Combinations" in Notes to Unaudited Condensed Consolidated Financial Statements for discussion of the acquisition and related financial data. We consider this transaction to be material to our results of operations, cash flows and financial position from May 4, 2012 through October 27, 2012 and believe the internal controls and procedures of the DTV operations will have a material effect on our internal control over financial reporting. During the second quarter of fiscal 2013, we began to evaluate and implement the alignment and integration of the DTV business into our systems, processes and procedures. Other than for DTV, there have been no other changes in our internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act, during the quarter ended October 27, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

We are currently in the process of integrating DTV operations. We anticipate a successful integration of operations and internal controls over financial reporting. Our management will continue to evaluate its internal control over financial reporting as it executes integration activities.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

On August 6, 2011, Powerline Innovations, LLC, or Powerline, filed suit against us, certain of our subsidiaries and many other named defendants, including Qualcomm Incorporated, Qualcomm Atheros, Inc., Broadcom Corporation and ST Microelectronics N.V. in the United States District Court for the Eastern District of Texas asserting infringement of U.S. Patent No. 5,471,190. The Powerline complaint seeks unspecified monetary damages and injunctive relief. At this time, we are unable to determine the outcome of this matter and, accordingly, cannot estimate the potential financial impact this action could have on our business, operating results, cash flows or financial position.

From time to time, we are involved in claims and legal proceedings that arise in the ordinary course of business. We expect that the number and significance of these matters will increase as our business expands. In particular, we could face an increasing number of patent and other intellectual property claims as the number of products and competitors in our industry grows. Any claims or proceedings against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of our time, result in the diversion of significant operational resources, or require us to enter into royalty or licensing agreements which, if required, may not be available on terms favorable to us or at all. Were an unfavorable outcome to occur against us, there exists the possibility of a material adverse impact on our financial position and results of operations for the period in which the unfavorable outcome occurs, and potentially in future periods.

### ITEM 1A. RISK FACTORS

If any of the following risks actually occurs, our business, financial condition and results of operations could be harmed. In that case, the trading price of our common stock could decline and you might lose all or part of your investment in our common stock. The risks and uncertainties described below are not the only ones we face. You should also refer to other information set forth in this Form 10-Q, including our unaudited condensed consolidated financial statements and the related notes. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business operations.

#### Risks Related to Our Business and Our Industry

If we do not successfully anticipate market needs and develop products and product enhancements in a timely manner that meet those needs, or if those products do not gain market acceptance, we may not be able to compete effectively and our ability to generate revenue will suffer.

We may not be able to accurately anticipate future market needs or be able to develop new products or product enhancements to meet such needs or to meet them in a timely manner. Our ability to develop and deliver new products successfully will depend on various factors, including our ability to:

- accurately predict market requirements and evolving industry standards;
- accurately design new chipset products;
- timely complete and introduce new product designs;
- timely qualify and obtain industry interoperability certification of our products and the equipment into which our products will be incorporated;

- ensure that our subcontractors have sufficient foundry, assembly and test capacity and packaging materials and achieve acceptable manufacturing yields;
- shift our products to smaller geometry process technologies to achieve lower cost and higher levels of design integration; and
- gain market acceptance of our products and our customers' products.

If we fail to anticipate market requirements or to develop new products or product enhancements to meet those needs in a cost-effective and timely manner, it could substantially decrease market acceptance and sales of our present and future products and we may be unable to attract new customers or retain our existing customers, which would significantly harm our business and financial results.

Even if we are able to anticipate, develop and commercially introduce new products and enhancements, our new products or enhancements may not achieve widespread market acceptance. Any failure of our products to achieve market acceptance could adversely affect our business and financial results.

If demand for our chipsets declines or does not grow, we will be unable to increase or sustain our net revenue.

We expect our chipsets to account for a substantial majority of our net revenue for the foreseeable future. For fiscal 2012, sales of our chipsets represented nearly all of our net revenue. Even if the consumer electronic markets that we target continue to expand, manufacturers of consumer products in these markets may not choose to utilize our chipsets in their products. The markets for our products are characterized by frequent introduction of new technologies, short product life cycles and significant price competition. If we or our customers are unable to manage product transitions in a timely and cost effective manner, our net revenue would suffer. In addition, frequent technological changes and introduction of next generation products may result in inventory obsolescence which would increase our cost of revenue and adversely affect our operating performance. If demand for our chipsets declines or fails to grow or we are unable to develop new products to meet our customers' demand, our net revenue could be harmed.

Our industry is highly competitive and we may not be able to compete effectively, which would harm our market share and cause our revenue to decline.

The markets in which we operate are extremely competitive and are characterized by rapid technological change, continuously evolving customer requirements and declining average selling prices. We may not be able to compete successfully against current or potential competitors. Most of our products compete with large semiconductor providers that have substantial experience and expertise in video, audio and multimedia technology and in selling to consumer equipment providers. Many of these companies have substantially greater engineering, marketing and financial resources than we have. As a result, our competitors may be able to respond better to new or emerging technologies or standards and to changes in customer requirements. Further, some of our competitors are in a better financial and marketing position from which to influence industry acceptance of a particular industry standard or competing technology than we are. Our competitors may also be able to devote greater resources to the development, promotion and sale of products, and may be able to deliver competitive products at a lower price. We also may face competition from newly established competitors, suppliers of products based on new or emerging technologies and customers who choose to develop their own chipsets. Additionally, some of our competitors operate their own fabrication facilities or may have stronger manufacturing partner relationships than we have. We expect our current customers, particularly in the IPTV media processor and connected media player markets, to seek additional suppliers of chipsets for inclusion in their products, which will increase competition and could reduce our market share. If we do not compete successfully, our market share and net revenue could decline.

Our restructuring efforts may not be effective, might have unintended consequences, and could negatively impact our business.

On October 31, 2012, we announced a restructuring plan to significantly reduce our operating expenses which we are in the early stages of implementing. Despite our efforts to structure our business to operate in a cost-effective manner, some cost reduction measures could have unexpected negative consequences. While our restructuring efforts are intended to reduce our costs, we cannot be certain that all restructuring efforts will be successful, or that we will not be required to implement additional restructuring activities in the future. If we are unable to recognize the anticipated benefit from our restructuring plan, our result of operations would be harmed.

If we fail to achieve initial design wins for our products, we may be unable to recoup our investments in our products and revenue could decline.

We expend considerable resources in order to achieve design wins for our products, especially our new products and product enhancements, without any assurance that a customer will select our product. Once a customer designs a semiconductor into a product, it is likely to continue to use the same semiconductor or enhanced versions of that semiconductor from the same supplier across a number of similar and successor products for a lengthy period of time due to the significant costs and risks associated with qualifying a new supplier and potentially redesigning the product to incorporate a different semiconductor. As a result, if we fail to achieve an initial design win in a customer's qualification process, we may lose the opportunity for significant sales to that customer for a number of its products and for a lengthy period of time, or we would only be able to sell our products to these customers as a second source, which usually means we would only be able to sell a limited amount of product to them. Also, even if we achieve new design wins with customers, these manufacturers may not purchase our products in sufficient volumes to recoup our development costs, and they can choose at any time to stop using our products, for example, if their own products are not commercially successful. This may cause us to be unable to recoup our investments in the development of our products and cause our revenue to decline.

We depend on a limited number of customers and any reduction, delay or cancellation of an order from these customers or the loss of any of these customers could cause our revenue to decline.

Our dependence on a limited number of customers means that the loss of a major customer or any reduction in orders by a major customer could materially reduce our net revenue and adversely affect our results of operations. We expect that sales to relatively few customers will continue to account for a significant percentage of our net revenue for the foreseeable future. We have no firm, long-term volume commitments from any of our major customers and we generally accept purchase commitments from our customers based upon their purchase orders. Customer purchase orders may be cancelled and order volume levels can be changed, cancelled or delayed with limited or no penalties. We have experienced fluctuations in order levels from period to period and expect that we will continue to experience such fluctuations and may experience cancellations in the future. We may not be able to replace the cancelled, delayed or reduced purchase orders with new orders. Any difficulty in the collection of receivables from key customers could also harm our business.

For the three months ended October 27, 2012, TP Vision and Flextronics accounted for 23% and 10% of our net revenue. For the three months ended October 29, 2011, Gemtek, Alpha Networks and Motorola accounted for 14%, 14% and 13%, respectively, of our net revenue.

Our business also depends on demand for our chipsets from companies, such as large telecommunication carriers, who are not our direct customers but deploy IPTV set-boxes that incorporate our chipsets. Large carriers often use multiple set-top box providers, who in turn sometimes use multiple contract manufacturers to purchase our chipsets and manufacture set-top boxes. Even though we do not sell our products directly to these companies that ultimately deploy set-top boxes to consumers, these companies have a significant impact on the demand for our chipsets. For example, a significant number of our chipsets are incorporated into set-top boxes deployed by AT&T. This significant concentration on AT&T set-top boxes was increased by our acquisition of CopperGate. A significant percentage of the chipsets sold by CopperGate are also used in set-top boxes as well as gateways deployed by AT&T. In the past, companies that deploy set-top boxes incorporating our chipsets have had significant fluctuations in demand, which has resulted in a decline in our business from our direct customers, such as original equipment manufacturers and contract manufacturers. We may experience increased competition as companies that deploy set-top boxes incorporating our chipsets seek additional or alternate sources of supply of chipsets for inclusion in their products. Any decrease in the demand from the companies that deploy IPTV set-top boxes incorporating our chipsets, and in particular AT&T, could have a material and adverse effect on our net revenue and results of operation.

We base orders for inventory on our forecasts of our customers' demand and if our forecasts are inaccurate, our financial condition and liquidity will suffer.

We place orders with our suppliers based on our forecasts of our customers' demand. Our forecasts are based on multiple assumptions, each of which may introduce errors into our estimates. When the demand for our customers' products increases significantly, we may not be able to meet demand on a timely basis and we may need to expend a significant amount of time working with our customers to allocate a limited supply and maintain positive customer relations. If we underestimate customer demand, we may forego revenue opportunities, lose market share and damage our customer relationships. Conversely, if we overestimate customer demand, we may allocate resources to manufacturing products that we may not be able to sell when we expect to or at all. For example, during fiscal 2012, we recorded a provision for excess inventory of $9.0 million which was primarily the result of our end customer’s transition to a next generation product sold by one of our competitors. When we have excess or obsolete inventory, the value of our inventory declines, which increases our cost of revenue and reduces our liquidity.

We have engaged, and may in the future engage in acquisitions of other businesses and technologies which could divert our attention and prove difficult to integrate with our existing business and technology.

We continue to consider investments in and acquisitions of other businesses, technologies or products as part of our efforts to improve our market position, broaden our technological capabilities and expand our product offerings. For example, in May 2012, we completed the acquisition of certain assets used in the digital TV business of Trident Microsystems, where we hired approximately 320 new employees. In March 2011, we completed the acquisition of certain assets from a large computer manufacturer and in November 2009, we completed the acquisition of CopperGate Communications Ltd., an Israeli company, which added substantial operations, including 141 employees. We also completed the acquisition of Zensys Holdings Corporation in December 2008, the acquisition of certain assets of the VXP Group from Gennum Corporation in February 2008 and the acquisition of Blue7 Communications in February 2006. In the future, we may not be able to acquire or successfully identify companies, products or technologies that would enhance our business. We are currently evaluating the completion of an acquisition of one of our private company investments for $11.2 million, subject to the investment company achieving certain mile stones. Once we identify a strategic opportunity, the process to consummate a transaction could divert our attention from the operation of our business causing our financial results to decline.

Acquisitions may require large one-time charges and can result in increased debt or contingent liabilities, adverse tax consequences, additional stock-based compensation expense, and the recording and subsequent amortization of amounts related to certain purchased intangible assets, any of which items could negatively impact our results of operations. We may also record goodwill in connection with an acquisition and incur goodwill impairment charges in the future. For example, in fiscal 2012, we recorded a goodwill impairment charge of $45.1 million, which represented a full write-off of all goodwill associated with our acquisitions to date, which had a materially adverse impact to our results of operations. In addition, in order to complete acquisitions, we may issue equity securities and incur debt, which would result in dilution to our existing shareholders and could negatively impact profitability.

We may experience difficulties in integrating acquired businesses. Integrating acquired businesses involves a number of risks, including:

- potential disruption of our ongoing business and the diversion of management resources from other business concerns;

- unexpected costs or incurring unknown liabilities;
- difficulties relating to integrating the operations and personnel of the acquired businesses;
- adverse effects on the existing customer relationships of acquired companies; and
- adverse effects associated with entering into markets and acquiring technologies in areas in which we have little experience.

If we are unable to successfully integrate the businesses we acquire, our operating results could be harmed.

The timing of our customer orders and product shipments can adversely affect our operating results and stock price.

Our net revenue and operating results depend upon the volume and timing of customer orders received during a given period and the percentage of each order that we are able to ship and recognize as net revenue during each period. Customers may change their cycle of product orders from us, which would affect the timing of our product shipments. Any failure or delay in the closing of orders expected to occur within a quarterly period, particularly from significant customers, would adversely affect our operating results. Further, to the extent we receive orders late in any given quarter; we may not be able to ship products to fill those orders during the same period in which we received the corresponding order which could have an adverse impact on our operating results for that period.

We are facing and may face additional intellectual property claims that could be costly to defend and result in our loss of significant rights.

The semiconductor industry is characterized by frequent litigation regarding patent and intellectual property rights. We believe that it may be necessary, from time to time, to initiate litigation against one or more third parties to preserve our intellectual property rights. From time to time, we have received, and may receive in the future, notices that claim we have infringed upon, misappropriated or misused other parties' proprietary rights. Any of the foregoing events or claims could result in litigation. We have been named in a lawsuit alleging certain of our products infringe the patents held by another party. Any litigation, including the litigation to which we are currently a party, could result in significant expense to us and divert the efforts of our technical and management personnel. In the event of an adverse result in any such litigation, we could be required to pay substantial damages, cease the manufacture, use and sale of certain products or expend significant resources to develop non-infringing technology or to obtain licenses to the technology that is the subject of the litigation, and we may not be successful in such development or in obtaining such licenses on acceptable terms, if at all. In addition, patent disputes in the electronics industry have often been settled through cross-licensing arrangements. Although we have a portfolio of applicable issued patents, we may not be able to settle an alleged patent infringement claim through a cross-licensing arrangement.

To remain competitive, we need to continue to transition our chipsets to increasingly smaller sizes while maintaining or increasing functionality, and our failure to do so may harm our business.

We periodically evaluate the benefits, on a product-by-product basis, of migrating to more advanced technology to reduce the size of our chipsets. The smaller chipset size reduces our production and packaging costs, which enables us to be competitive in our pricing. We also continually strive to increase the functionality of our chipsets, which is essential to competing effectively in our target markets. The transition to smaller geometries while maintaining or increasing functionality requires us to work with our contractors to modify the manufacturing processes for our products and to redesign some products. This effort requires considerable development investment and a risk of reduced yields as a new process is brought to acceptable levels of operating and quality efficiency. In the past, we have experienced difficulties in shifting to smaller geometry process technologies or new manufacturing processes, which resulted in reduced manufacturing yields, delays in product deliveries and increased expenses. We may face similar difficulties, delays and expenses as we continue to transition our products to smaller geometry processes, all of which could harm our relationships with our customers, and our failure to do so would impact our ability to provide competitive prices to our customers, which would have a negative impact on our sales.

The average selling prices of semiconductor products have historically decreased rapidly and will likely do so in the future, which could harm our revenue and gross margins.

The semiconductor industry, in general, and the consumer electronics markets that we target, specifically, are characterized by intense price competition, frequent introductions of new products and short product life cycles, which can result in rapid price erosion in the average selling prices for semiconductor products. A decline in the average selling prices of our products could harm our revenue and gross margins. The willingness of customers to design our chipsets into their products depends to a significant extent upon our ability to sell our products at competitive prices. In the past, we have reduced our prices to meet customer requirements or to maintain a competitive advantage. Reductions in our average selling prices to one customer could impact our average selling prices to all customers. If we are unable to reduce our costs sufficiently to offset declines in product selling prices or are unable to introduce more advanced products with higher margins in a timely manner, we could experience declines in our net revenue and gross margins.

We recently added three new directors to our board of directors, which may lead to changes in the execution of our business strategies and objectives.

In connection with our annual meeting of shareholders in August 2012, three new directors were elected to our board of directors and constitute a majority of our five-member board of directors. Because of these additions, our board of directors has not worked together as a group for an extended period of time. This may lead to changes in the execution of our business strategies and objectives as these new directors analyze our business and contribute to the formulation of our business strategies and objectives.

We rely upon patents, trademarks, copyrights and trade secrets to protect our proprietary rights and if these rights are not sufficiently protected, it could harm our ability to compete and to generate revenue.

Our ability to compete may be affected by our ability to protect our proprietary information. As of January 28, 2012, we held 105 patents, which were due to expire from one to fifteen years, and had 94 patent applications under review. These patents and patent applications cover the technology underlying our products. We cannot assure you that any additional patents for which we have applied will be issued or that any issued patents will provide meaningful protection of our product innovations. Like other semiconductor companies, we rely primarily on trade secrets and technological know-how in the conduct of our business. We use measures such as confidentiality agreements to protect our intellectual property. However, these methods of protecting our intellectual property may not be sufficient.

The complexity of our products could result in unforeseen delays or expenses and in undetected defects, which could damage our reputation with current or prospective customers, adversely affect the market acceptance of new products and result in warranty claims.

Highly complex products, such as those that we offer, frequently contain defects, particularly when they are first introduced or as new versions are released. Our chipsets contain highly sophisticated silicon technology and complex software. In the past we have experienced, and may in the future experience, defects in our products, both with our chipsets and the related software products we offer. If any of our products contain defects or have reliability, quality or compatibility problems, our reputation may be damaged and our customers may be reluctant to buy our products, which could harm our ability to retain existing customers and attract new customers. In addition, these defects could interrupt or delay sales or shipment of our products to our customers. Manufacturing defects may not be detected by the testing process performed by our subcontractors. If defects are discovered after we have shipped our products, it could result in unanticipated costs, order cancellations or deferrals and product returns or recalls, harm to our reputation and a decline in our net revenue, income from operations and gross margins.

In addition, our agreements with some customers contain warranty provisions which provide the customer with a right to damages if a defect is traced to our products or if we cannot correct errors in our product reported during the warranty period. However, any contractual limitations to our liability may be unenforceable in a particular jurisdiction. We do not have insurance coverage for any warranty or product liability claims and a successful claim could require us to pay substantial damages. A successful warranty or product liability claim against us, or a requirement that we participate in a product recall, could have adverse effects on our business results.

If our third-party manufacturers do not achieve satisfactory yields or quality, our relationships with our customers and our reputation will be harmed, which in turn would harm our operating results and financial performance.

The fabrication of semiconductors is a complex and technically demanding process. Minor deviations in the manufacturing process can cause substantial decreases in yields and, in some cases, cause production to be stopped or suspended. Although we work closely with our third-party manufacturers to minimize the likelihood of reduced manufacturing yields, their facilities have from time to time experienced lower than anticipated manufacturing yields that have resulted in our inability to meet our customer demand. It is not uncommon for yields in semiconductor fabrication facilities to decrease in times of high demand, in addition to reduced yields that may result from normal wafer lot loss due to workmanship or operational problems at these facilities. When these events occur, especially simultaneously, as happens from time to time, we may be unable to supply our customers' demand. Many of these problems are difficult to detect at an early stage of the manufacturing process and may be time consuming and expensive to correct. Poor yields from the wafer foundries or defects, integration issues or other performance problems in our products could cause us significant customer relations and business reputation problems or force us to sell our products at lower gross margins and therefore harm our financial results.

If the growth of demand in the consumer electronics market does not continue, our ability to increase our revenue could suffer.

Our business is highly dependent on developing sectors of the consumer electronics market, including DTV, home networking, IPTV media processor, home control and energy management, prosumer and industrial audio/video and connected media player. The consumer electronics market is highly competitive and is characterized by, among other things, frequent introductions of new products and short product life cycles. The consumer electronics market may also be negatively impacted by a slowdown in overall consumer spending. The worldwide economy, generally, and consumer spending, specifically, has significantly declined, which has negatively impacted our target markets. If our target markets do not grow as rapidly or to the extent we anticipate, our business could suffer. We expect the majority of our revenue for the foreseeable future to come from the sale of our chipsets for use in emerging consumer applications. Our ability to sustain and increase revenue is in large part dependent on the continued growth of these rapidly evolving market sectors, whose future is largely uncertain. Many factors could impede or interfere with the expansion of these consumer market sectors, including consumer demand in these sectors, general economic conditions, and other competing consumer electronic products, delays in the deployment of telecommunications video services and insufficient interest in new technology innovations. In addition, if market acceptance of the consumer products that utilize our products does not occur as expected, our business could be harmed.

Due to the cyclical nature of the semiconductor industry, our operating results may fluctuate significantly, which could adversely affect the market price of our common stock.

The semiconductor industry is highly cyclical and subject to rapid change and evolving industry standards and, from time to time, has experienced significant downturns. These downturns are characterized by decreases in product demand, excess customer inventories and accelerated erosion of prices. These factors have caused, and could cause, substantial fluctuations in our net revenue and in our operating results. Any downturns in the semiconductor industry may be severe and prolonged, and any failure of this industry to fully recover from downturns could harm our business. The semiconductor industry also periodically experiences increased demand and production capacity constraints, which may affect our ability to ship products. Accordingly, our operating results have varied and may vary significantly as a result of the general conditions in the semiconductor industry, which could cause our stock price to decline.

Our ability to raise capital in the future may be limited and our failure to raise capital when needed could prevent us from executing our growth strategy.

We believe that our existing cash and cash equivalents, and short-term and long-term marketable securities will be sufficient to meet our anticipated cash needs for at least the next 12 months. The timing and amount of our working capital and capital expenditure requirements may vary significantly depending on numerous factors, including:

- market acceptance of our products;
- the need to adapt to changing technologies and technical requirements;
- the existence of opportunities for expansion; and
- access to and availability of sufficient management, technical, marketing and financial personnel.

If our capital resources are insufficient to satisfy our liquidity requirements, we may seek to sell additional equity securities or debt securities or obtain debt financing. During the second quarter of fiscal 2013, we made cash payments aggregating $39.7 million. During fiscal 2009, we used an aggregate of $85.9 million to purchase 4.2 million shares of our common stock. In November 2009, we used approximately $116.0 million in cash (which included approximately $28.0 million of acquired CopperGate cash) for the acquisition of CopperGate. The amount of cash we used for these acquisitions and common stock repurchases could limit our ability to execute our business plans and require us to raise additional capital in the future in order to fund any further repurchases or for other purposes. The sale of additional equity securities or convertible debt securities would result in additional dilution to our shareholders. Additional debt would result in increased expenses and could result in covenants that would restrict our operations. We have not made arrangements to obtain additional financing and there is no assurance that financing, if required, will be available in amounts or on terms acceptable to us, if at all.

Changes in our effective tax rate or tax liability may have an adverse effect on our results of operations.

As a global company, we are subject to taxation in Hong Kong, Israel, Singapore, the United States and various other countries and states. Significant judgment is required to determine and estimate worldwide tax liabilities. Any significant change in our future effective tax rates could adversely impact our consolidated financial position, results of operations and cash flows. Our future effective tax rates may be adversely affected by a number of factors including:

- changes in tax laws in the countries in which we operate or the interpretation of such tax laws;

- changes in the valuation of our deferred tax assets and liabilities, including the effect of foreign exchange rate fluctuations relative to the US Dollar;

- 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 stock-based compensation expense;

- changes in generally accepted accounting principles; and

- our ability to use our tax attributes such as research and development tax credits and net operating losses of acquired companies to the fullest extent.

In an effort to increase commercial activities in Singapore, an agency of the government of Singapore negotiated with us a reduction in its customary income tax rates in return for our commitment to fulfill a defined set of milestones that were comprised of business activities in Singapore including the establishment of an operations center. During fiscal 2009, we established a foreign operating subsidiary in Singapore. However, due to changes in our business conditions, product development cycles and other factors, we have only been able to fulfill a portion of these milestones. As a result, we have initiated renewed negotiations with the Singapore tax agency in an effort to modify the business milestones to be more achievable and continue to benefit from a reduced rate of taxation. Even though the agency continues to negotiate with us, there is a risk that we will not be able to achieve the modified milestones which could result in a significantly higher tax rate on the income we recognize in Singapore. The increased tax rate could be applied to current profits or retroactively to income generated over previous years in Singapore, which could have a material adverse impact on our consolidated financial results.

We anticipate that a portion of our consolidated pre-tax income will continue to be subject to foreign tax at relatively lower tax rates when compared to the United States' federal statutory tax rate and, as a consequence, our effective income tax rate has been and is expected to continue to be lower than the United States' federal statutory rate. Our future effective income tax rates could be adversely affected if tax authorities challenge our international tax structure, if the relative mix of United States and international income or losses changes for any reason, or if we lose the benefit of our reduced tax rate in Singapore. Accordingly, there can be no assurance that our income tax rate will be less than the United States' federal statutory rate.

We have a history of fluctuating operating results, including net losses in fiscal 2012 and 2013 and we may not be able to return to profitability in the future, which may cause the market price of our common stock to decline.

We have a history of fluctuating operating results. We reported net income of $70.2 million in fiscal 2008, net income of $26.4 million in fiscal 2009, net income of $2.5 million in fiscal 2010, net income of $9.1 million in fiscal 2011 and a net loss of $168.0 million in fiscal 2012. To return to profitability, we will need to successfully develop new products and product enhancements and sustain higher revenue while controlling our cost and expense levels. In recent years, we made significant investments in our product development efforts and have expended substantial funds to enhance our sales and marketing efforts and otherwise operate our business. However, we may not realize the benefits of these investments. We may incur operating losses in future quarterly periods or fiscal years, which in turn could cause the price of our common stock to decline.

Our sales cycle can be lengthy, which could result in uncertainty and delays in generating net revenue.

Because our products are based on constantly evolving technologies, we have experienced a lengthy sales cycle for some of our chipsets, particularly those designed for set-top box applications in the IPTV media processor market. After we have qualified a product with a customer, the customer will usually test and evaluate our product with its service provider prior to the customer completing the design of its own equipment that will incorporate our product. Our customers and the telecommunications carriers our customers serve may need from three months to more than a year to test, evaluate and adopt our product and an additional three to more than nine months to begin volume production of equipment that incorporates our product. Our complete sales cycle typically ranges from nine to eighteen months, but could be longer. As a result, we may experience a significant delay between the time we increase expenditures for research and development, sales and marketing efforts and inventory and the time we generate net revenue, if any, from these expenditures. In addition, because we do not have long-term commitments from our customers, we must repeat our sales process on a continual basis even for current customers looking to purchase a new product. As a result, our business could be harmed if a customer reduces or delays its orders, chooses not to release products incorporating our chipsets or elects not to purchase a new product or product enhancements from us.

The complexity of our international operations may increase our operating expenses and disrupt our business.

We transact business and have operations worldwide. For example, we derive a substantial portion of our net revenue from our customers outside of North America and we plan to continue expanding our business in international markets in the future. For fiscal 2012, we derived 95% of our revenue from customers outside of North America. We also have significant international operations, including research and development facilities in Canada and Vietnam, sales and research and development facilities in China, Denmark, France, Israel, Japan, Singapore, Taiwan, Germany and The Netherlands and a sales and distribution facility in Hong Kong.

As a result of our international business, we are affected by economic, regulatory and political conditions in foreign countries, including the imposition of government controls, changes or limitations in trade protection laws, unfavorable changes in tax treaties or laws, varying statutory equity requirements, difficulties in collecting receivables and enforcing contracts, natural disasters, labor unrest, earnings expatriation restrictions, misappropriation of intellectual property, changes in import/export regulations, tariffs and freight rates, economic instability, public health crises, acts of terrorism and continued unrest in many regions and other factors, which could have a material impact on our international revenue and operations. In particular, in some countries we may experience reduced intellectual property protection. Our results of operations could also be adversely affected by exchange rate fluctuations, which could increase the sales price in local currencies of our products in international markets. Overseas sales and purchases to date have been denominated in U.S. dollars. Although we engage in some hedging of our foreign currency exposures, we do not hedge all such exposures and our hedging arrangements may not always be effective. See “Foreign currency exchange rate sensitivity” under Part I Item 3“Quantitative and Qualitative Disclosures about Market Risk” in this Form 10-Q. Moreover, local laws and customs in many countries differ significantly from those in the United States. We also face challenges in staffing and managing our global operations. If we are unable to manage the complexity of our global operations successfully, our financial performance and operating results could suffer.

The volatile global economy could negatively affect our business, results of operations and financial condition.

Current uncertainty in global economic conditions poses a risk to the overall economy as consumers and businesses may defer purchases in response to tighter credit and negative financial news, which could negatively affect demand for our products and other related matters. Consequently, demand for our products could be different from our expectations due to factors including:

- changes in business and economic conditions, including conditions in the credit market that could negatively affect consumer confidence;
- customer acceptance of our products and those of our competitors;
- changes in customer order patterns including order cancellations; and
- reductions in the level of inventory our customers are willing to hold.

There could also be a number of secondary effects from the current uncertainty in global economic conditions, such as insolvency of suppliers resulting in product delays, an inability of our customers to obtain credit to finance purchases of our products or a desire of our customers to delay payment to us for the purchase of our products. The effects, including those mentioned above, of the current global economic environment could negatively impact our business, results of operations and financial condition.

We rely on a limited number of independent third-party manufacturers for the fabrication, assembly and testing of our chipsets and the failure of any of these third-party manufacturers to deliver products or otherwise perform as requested could damage our relationships with our customers, decrease our sales and limit our growth.

We are a fabless semiconductor company and thus we do not own or operate a fabrication or manufacturing facility. We depend on independent manufacturers, each of whom is a third-party manufacturer for numerous companies, to manufacture, assemble and test our products. We currently rely on Taiwan Semiconductor Manufacturing Corporation, or TSMC, and, to a lesser extent, United Microelectronics Corporation, or UMC, and NXP Semiconductors, or NXP, to produce substantially all of our chipsets. We only recently began working with NXP as a result of our acquisition of certain assets of the DTV business from Trident Microsystems. As we continue to establish a relationship with NXP, we may experience delays, disruptions and technical or quality control problems as we integrate them into our manufacturing processes. We rely on Advanced Semiconductor Engineering, Inc., or ASE, to assemble, package and test substantially all of our products. These third-party manufacturers may allocate capacity to the production of other companies' products while reducing product deliveries or the provision of services to us on short notice or they may increase the prices of the products and services they provide to us with little or no notice. In particular, other clients that are larger and better financed than we are or that have long-term agreements with ASE, TSMC, UMC or NXP may cause any or all of them to reallocate capacity to those clients, decreasing the capacity available to us.

If we fail to effectively manage our relationships with the third-party manufacturers, if we are unable to secure sufficient capacity at our third-party manufacturers' facilities or if any of them should experience delays, disruptions or technical or quality control problems in our manufacturing operations or if we had to change or add additional third-party manufacturers or contract manufacturing sites, our ability to ship products to our customers could be delayed, our relationships with our customers would suffer and our market share and operating results would suffer. If our third-party manufacturers' pricing for the products and services they provide increases and we are unable to pass along such increases to our customers, our operating results would be adversely affected. Also, the addition of manufacturing locations or additional third-party subcontractors would increase the complexity of our supply chain management. Moreover, all of our product manufacturing, assembly and packaging is performed in Asian countries and is therefore subject to risks associated with doing business in these countries such as quarantines or closures of manufacturing facilities due to the outbreak of viruses such as swine flu, SARS, avian flu or any similar outbreaks. Each of these factors could harm our business and financial results.

We may not be able to effectively manage our growth or develop our financial and managerial control and reporting systems, and we may need to incur significant expenditures to address the additional operational and control requirements of our growth, either of which could harm our business and operating results.

To continue to grow, we must continue to expand and improve our operational, engineering, accounting and financial systems, procedures, controls and other internal management systems. This may require substantial managerial and financial resources and our efforts in this regard may not be successful. Our current systems, procedures and controls may not be adequate to support our future operations. For example, we implemented a new enterprise resource management system in fiscal 2009. We integrated the operations of CopperGate into our enterprise resource management system in fiscal 2011. We integrated DTV business operations, having completed the acquisition of certain assets of the DTV business of Trident Microsystems in the second quarter of fiscal 2013. Any integration efforts could be costly and time consuming. If we fail to adequately manage our growth or to improve and develop our operational, financial and management information systems or fail to effectively motivate or manage our current and future employees, the quality of our products and the management of our operations could suffer, which could adversely affect our operating results.

In the event we seek or are required to use a new manufacturer to fabricate or to assemble and test all or a portion of our chipset products, we may not be able to bring new manufacturers on-line rapidly enough, which could damage our relationships with our customers, decrease our sales and limit our growth.

We use a single wafer foundry to manufacture a substantial majority of our products and a single source to assemble and test substantially all of our products, which exposes us to a substantial risk of delay, increased costs and customer dissatisfaction in the event our third-party manufacturers are unable to provide us with our chipset requirements. Particularly during times when semiconductor capacity is limited, we may seek to, and in the event that our current foundry were to stop producing wafers for us altogether, we would be required to, qualify one or more additional wafer foundries to meet our requirements, which would be time consuming and costly. In order to bring any new foundries on-line, our customers and we would need to qualify their facilities, which process could take as long as several months. Once qualified, each new foundry would then require an additional number of months to actually begin producing chipsets to meet our needs, by which time our perceived need for additional capacity may have passed, or the opportunities we previously identified may have been lost to our competitors. Similarly, qualifying a new provider of assembly, packaging and testing services would be a lengthy and costly process and, in both cases, they could prove to be less reliable than our existing manufacturers, which could result in increased costs and expenses as well as delays in deliveries of our products to our customers.

Our ability to develop, market and sell products could be harmed if we are unable to retain or hire key personnel.

Our future success depends upon our ability to recruit and retain the services of key executive, engineering, finance and accounting, sales, marketing and support personnel. The supply of highly qualified individuals, in particular engineers in very specialized technical areas, or sales people specializing in the semiconductor industry, is limited and competition for such individuals is intense. None of our officers or key employees is bound by an employment agreement for any specific term. The loss of the services of any of our key employees, the inability to attract or retain key personnel in the future or delays in hiring required personnel, particularly engineers and sales people, and the complexity and time involved in hiring and training new employees, could delay the development and introduction of new products, and negatively impact our ability to market, sell or support our products.

Litigation due to stock price volatility or other factors could cause us to incur substantial costs and divert our attention and resources.

In the past, securities class action litigation has often been brought against a company following periods of volatility in the market price of its securities. Companies such as ours in the semiconductor industry and other technology industries are particularly vulnerable to this kind of litigation due to the high volatility of their stock prices. While we are not aware of any such contemplated class action litigation against us, we may in the future be the target of securities litigation. Any future lawsuits to which we may become a party will likely be expensive and time consuming to investigate, defend and resolve. Such costs, which include investigation and defense, the diversion of our attention and resources and any losses resulting from these claims, could significantly increase our expenses and adversely affect our profitability and cash flow.

Our business is subject to seasonality, which may cause our revenue to fluctuate.

Our business is subject to seasonality as a result of our target markets, particularly the DTV business, which historically has peaked in the third quarter. We sell a number of our semiconductor products to our customers who manufacture products for the consumer electronics market. Our customers who manufacture products for the consumer electronics market typically experience seasonality in the sales of their products which in turn may affect the timing and volume of orders for our chipsets. We expect to experience lower sales in our first and/or fourth fiscal quarters and higher sales in our second and/or third fiscal quarters as a result of the seasonality of demand associated with the consumer electronics markets. For example, we expect that our DTV business may experience some seasonality typical of the consumer electronics markets, resulting in slower DTV sales in the first and fourth quarter of each calendar year and strongest DTV sales in the third calendar quarter. As a result of the potential seasonality in our business, our operating results may vary significantly from quarter to quarter.

If credit market conditions deteriorate further, it could have a material adverse impact on our investment portfolio.

U.S. sub-prime mortgage defaults have had a significant impact across various sectors of the financial markets, causing global credit and liquidity related difficulties. Beginning mid-2007, global short-term funding markets have experienced credit issues, leading to liquidity issues and failed auctions in the auction rate securities market. If the global credit market continues to be weak or deteriorates further, the liquidity of our investment portfolio may be impacted and we could determine that some of our investments are impaired. This could materially adversely impact our results of operations and financial condition.

Regional instability in Israel may adversely affect business conditions and may disrupt our operations and negatively affect our revenues and profitability.

As a result of our acquisition of CopperGate in November 2009, we have engineering facilities, administrative and sales support operations and, as of October 27, 2012, we had 143 employees located in Israel. Accordingly, political, economic and military conditions in Israel may directly affect our business. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors, as well as incidents of civil unrest. In addition, in the past, Israel and companies doing business with Israel has been the subject of economic boycott. Although Israel has entered into various agreements with Egypt, Jordan and the Palestinian Authority, Israel has been and is subject to civil unrest and terrorist activity, with varying levels of severity since September 2000. Recently, there has been an increase in civil unrest and political instability in the Middle East. Any future armed conflicts, civil unrest or political instability in the region may negatively affect business conditions and adversely affect our results of operations.

In addition, our business insurance does not cover losses that may occur as a result of events associated with the security situation in the Middle East. Although the Israeli government currently covers the reinstatement value of direct damages that are caused by terrorist attacks or acts of war, we cannot assure you that this government coverage will be maintained. Any losses or damages incurred by us could have a material adverse effect on our business and financial results.

The income tax benefits in Israel to which we are currently entitled from our approved enterprise program may be reduced or eliminated by the Israeli government in the future and also require us to satisfy specified conditions. If they are reduced or if we fail to satisfy these conditions, we may be required to pay increased taxes and would likely be denied these benefits in the future.

The Investment Center of the Ministry of Industry, Trade and Labor has granted “approved and/or beneficiary enterprise” status to certain product development programs at our facility in Tel Aviv. Sigma Designs Israel’s taxable income from the approved and beneficiary enterprise programs is exempt from tax for a period of two years commencing calendar year 2008 and 2009, respectively, and will be subject to a reduced tax rate for an additional eight years thereafter, depending on the percentage of Sigma Designs Israel’s share capital held by non-Israelis. The Israeli government may reduce, or eliminate in the future, tax benefits available to approved enterprise programs. Our approved and beneficiary programs and the resulting tax benefits may not continue in the future at their current levels or at any level. The termination or reduction of these tax benefits would likely increase our tax liability. Additionally, the benefits available to an approved and beneficiary enterprise program are dependent upon the fulfillment of conditions stipulated under applicable law and in the certificate of approval. If we fail to comply with these conditions, in whole or in part, we may be required to pay additional taxes for the period in which we benefited from the tax exemption or reduced tax rates and would likely be denied these benefits in the future. In either case, the amount by which our taxes would increase will depend on the difference between the then applicable tax rate for non-approved enterprises and the rate of tax, if any, that we would otherwise pay as an approved enterprise, and the amount of any taxable income that we may earn in the future. The current maximum enterprise tax rate in Israel is 25%.

Failure to maintain effective internal controls over financial reporting may cause us to delay filing our periodic reports with the SEC, affect our NASDAQ listing and adversely affect our stock price.

The SEC, as directed by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring public companies to include a report of management on internal control over financial reporting in their annual reports on Form 10-K. Our management is responsible for maintaining internal control over financial reporting designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with GAAP. Our management assessed the effectiveness of our internal control over financial reporting as of January 28, 2012 and concluded that our internal control over financial reporting was effective. During the second quarter of fiscal 2013, we acquired certain assets used in the DTV business of Trident Microsystems. We believe the internal controls and procedures of the DTV operations will have a material effect on our internal control over financial reporting. If we are unable to successfully integrate the DTV operations into our systems, processes and procedures, we may not be able to maintain effective internal control over financial reporting. Although we review our internal control over financial reporting in order to ensure compliance with the Section 404 requirements, our failure to maintain adequate internal controls over financial reporting could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements, which ultimately could negatively impact our stock price.

Our headquarters, certain of our other facilities, and some of our suppliers and third-party manufacturers are located in active earthquake zones. Earthquakes, tsunamis, floods or other types of natural disasters affecting our suppliers, our manufacturers or us could cause resource shortages and production delays, which would disrupt and harm our business, results of operations and financial condition.

We are headquartered in the San Francisco Bay Area, have research and development and sales offices in Japan and outsource most of our manufacturing to Taiwan. Each of these areas is an active earthquake zone, and certain of our suppliers and third-party manufacturers conduct operations in the same regions or in other locations that are susceptible to natural disasters. The occurrence of a natural disaster, such as an earthquake, tsunami or flood, or localized extended outages of critical utilities or transportation systems, or any critical resource shortages, affecting us, our suppliers or our third-party manufacturers could cause a significant interruption in our production, business, damage or destroy our facilities or those of our suppliers and cause us to incur significant costs or result in limitations on the availability of our raw materials, any of which could harm our business, financial condition and results of operations.

Risks Related to Our Common Stock

Our operating results are subject to significant fluctuations due to many factors and any of these factors could adversely affect our stock price.

Our operating results have fluctuated in the past and may continue to fluctuate in the future due to a number of factors, including:

- failure to reduce our expenses sufficiently to achieve profitability at current revenue levels;
- the loss of one or more significant customers;
- changes in our pricing models and product sales mix;
- unexpected reductions in unit sales and average selling prices, particularly if they occur precipitously;

- new product introductions by us and our competitors;
- the level of acceptance of our products by our customers and acceptance of our customers' products by their end user customers;
- an interrupted or inadequate supply of semiconductor chips or other materials included in our products;
- availability of third-party manufacturing capacity for production of certain products;
- shifts in demand for the technology embodied in our products and those of our competitors;

- the timing of, and potential unexpected delays in, our customer orders and product shipments;
- the impairment and associated write-down of strategic investments that we may make from time-to-time;
- write-downs of accounts receivable;
- inventory obsolescence;
- a significant increase in our effective tax rate in any particular period as a result of the exhaustion, disallowance or accelerated recognition of our net operating loss carry-forwards or otherwise;
- technical problems in the development, production ramp up and manufacturing of products, which could cause shipping delays;
- the impact of potential economic instability in the United States and Asia-Pacific region, including the continued effects of the recent worldwide economic slowdown;
- expenses related to implementing and maintaining a new enterprise resource management system and other information technologies; and
- expenses related to our compliance efforts with Section 404 of the Sarbanes-Oxley Act of 2002.

In addition, the market prices of securities of semiconductor and other technology companies have been volatile. This volatility has significantly affected the market prices of securities of many technology companies for reasons frequently unrelated to the operating performance of the specific companies.

Accordingly, you may not be able to resell your shares of common stock at or above the price you paid.

Our stock price has demonstrated volatility and continued volatility in the stock market or our operating performance may cause further fluctuations or decline in our stock price.

The market for our common stock has been subject to significant volatility which is expected to continue. For example, during the nine months ended October 27, 2012, the high and low closing sale price per share of our common stock on the NASDAQ Global Market ranged from a high of $7.13 on August 28, 2012 to a low of $4.68 on April 10, 2012. This volatility may or may not be related or proportionate to our operating performance. Our operating performance as well as general economic and market conditions, could cause the market price of our common stock to decline.

If securities or industry analysts do not publish research or reports about our business or if they issue an adverse opinion regarding our stock, our stock price and trading volume could decline.

The trading market for our common stock is influenced by the research and reports that industry or securities analysts publish about our business or us. If one or more of the analysts who cover us issue an adverse opinion regarding our stock, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets which in turn could cause our stock price or trading volume to decline.

Provisions in our organizational documents and California law could delay or prevent a change in control of Sigma that our shareholders may consider favorable.

Our articles of incorporation and bylaws contain provisions that could limit the price that investors might be willing to pay in the future for shares of our common stock. Our Board of Directors can authorize the issuance of preferred stock that can be created and issued by our Board of Directors without prior shareholder approval, commonly referred to as "blank check" preferred stock, with rights senior to those of our common stock. The rights of the holders of our common stock will be subject to, and may be adversely affected by, the rights of the holders of any preferred stock that we may issue in the future. The issuance of preferred stock could have the effect of delaying, deterring or preventing a change in control and could adversely affect the voting power of your shares. In addition, provisions of California law could make it more difficult for a third party to acquire a majority of our outstanding voting stock by discouraging a hostile bid or delaying or deterring a merger, acquisition or tender offer in which our shareholders could receive a premium for their shares or a proxy contest for control of Sigma or other changes in our management.

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

None.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. MINE SAFETY DISCLOSURES

None.

## ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

(a) Exhibits

The following exhibits are filed herewith:

10.1 First Amendment to Lease Agreement entered into as of October 8, 2012 by and between Prologis, L.P. and Sigma Designs, Inc. (incorporated by reference to Exhibit 10.1 filed with the Company's Current Report on Form 8-K on October 12, 2012).

31.1 Certification of the President and Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Chief Financial Officer and Secretary pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.

32.1 Certificate of President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)

32.2 Certificate of Chief Financial Officer and Secretary pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)

101.INS** XBRL Instance Document.
101.SCH**XBRL Taxonomy Extension Schema Document.
101.CAL**XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF**XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB**XBRL Taxonomy Extension Label Linkbase Document.
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** Furnished with this Form 10-Q/A. In accordance with Rule 406T of Regulation S-T, the interactive data files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for the 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 Exchange Act of 1934, as amended, and otherwise are not subject to liability under these sections.

(1) The certificates contained in Exhibits 32.1 and 32.2 are not deemed "filed" for purposes of Section 18 of the Securities and Exchange Act of 1934 and are not to be incorporated by reference into any filing of the registrant under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof irrespective of any general incorporation by reference language contained in any such filing, except to the extent that the registration specifically incorporates it by reference.

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SIGNATURES

Pursuant to the requirement 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.

| | | |
|---|---|---|
| | SIGMA DESIGNS, INC. | |
| Date: December 6, 2012 | By: | /s/ Thinh Q. Tran<br>Thinh Q. Tran<br><br>President and Chief Executive Officer<br>(Principal Executive Officer) |
| | By: | /s/ Thomas E. Gay III<br>Thomas E. Gay III<br><br>Chief Financial Officer and Secretary<br>(Principal Financial and Accounting Officer) |

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EXHIBIT INDEX

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