

QUICKLOGIC CORPORATION

Form 10-Q

August 05, 2015

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

FORM 10-Q  
(Mark One)

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

For the Quarterly Period Ended June 28, 2015  
OR

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

For the Transition Period From \_\_\_\_\_ To \_\_\_\_\_  
COMMISSION FILE NUMBER: 000-22671

QUICKLOGIC CORPORATION  
(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)  
1277 ORLEANS DRIVE SUNNYVALE, CA 94089  
(Address of principal executive offices, including Zip Code)  
(408) 990-4000  
(Registrant's telephone number, including area code)

77-0188504  
(I.R.S. Employer  
Identification No.)

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 requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer	<input type="checkbox"/>	Accelerated Filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller Reporting Company	<input type="checkbox"/>

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

As of July 31, 2015, the registrant had outstanding 56,587,195 shares of common stock, par value \$0.001.

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## PART I. Financial Information

## Item 1. Financial Statements

QUICKLOGIC CORPORATION  
 CONDENSED UNAUDITED CONSOLIDATED BALANCE SHEETS  
 (in thousands, except par value amount)

	June 28, 2015	December 28, 2014
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$26,415	\$30,050
Accounts receivable, net of allowances for doubtful accounts of \$0 in both periods	1,597	1,552
Inventories	3,001	4,952
Other current assets	873	1,146
Total current assets	31,886	37,700
Property and equipment, net	2,689	3,217
Other assets	229	222
<b>TOTAL ASSETS</b>	<b>\$34,804</b>	<b>\$41,139</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Revolving line of credit	\$1,000	\$—
Trade payables	2,152	2,506
Accrued liabilities	2,069	1,574
Deferred revenue	114	—
Current portion of capital lease obligations	202	225
Total current liabilities	5,537	4,305
Long-term liabilities:		
Revolving line of credit	—	1,000
Capital lease obligations, less current portion	56	191
Other long-term liabilities	155	76
Total liabilities	5,748	5,572
Commitments and contingencies (see Note 13)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 10,000 shares authorized; no shares issued and outstanding	—	—
Common stock, \$0.001 par value; 100,000 shares authorized; 56,580 and 56,182 shares issued and outstanding, respectively	56	56
Additional paid-in capital	239,824	238,419
Accumulated deficit	(210,824)	(202,908)
Total stockholders' equity	29,056	35,567
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$34,804</b>	<b>\$41,139</b>

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

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QUICKLOGIC CORPORATION  
 CONDENSED UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (in thousands, except per share amounts)

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Revenue	\$4,973	\$6,836	\$11,132	\$18,000
Cost of revenue	2,830	3,820	6,110	10,926
Gross profit	2,143	3,016	5,022	7,074
Operating expenses:				
Research and development	3,493	3,056	6,970	5,697
Selling, general and administrative	2,690	2,848	5,650	6,313
Restructuring costs	169	—	169	—
Total operating expenses	6,352	5,904	12,789	12,010
Loss from operations	(4,209 )	(2,888 )	(7,767 )	(4,936 )
Interest expense	(15 )	(17 )	(29 )	(33 )
Interest income and other expense, net	(33 )	(36 )	(59 )	(62 )
Loss before income taxes	(4,257 )	(2,941 )	(7,855 )	(5,031 )
Provision for (benefit from) income taxes	21	(44 )	61	(24 )
Net loss	\$(4,278 )	\$(2,897 )	\$(7,916 )	\$(5,007 )
Net loss per share:				
Basic	\$(0.08 )	\$(0.05 )	\$(0.14 )	\$(0.09 )
Diluted	\$(0.08 )	\$(0.05 )	\$(0.14 )	\$(0.09 )
Weighted average shares:				
Basic	56,359	55,379	56,275	54,906
Diluted	56,359	55,379	56,275	54,906

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

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QUICKLOGIC CORPORATION  
 CONDENSED UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS  
 (in thousands)

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Net loss	\$ (4,278	) \$ (2,897	) \$ (7,916	) \$ (5,007
Total other comprehensive income, net of tax	—	—	—	—
Total comprehensive loss	\$ (4,278	) \$ (2,897	) \$ (7,916	) \$ (5,007

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

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QUICKLOGIC CORPORATION  
 CONDENSED UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (in thousands)

	Six Months Ended	
	June 28, 2015	June 29, 2014
Cash flows from operating activities:		
Net loss	\$(7,916 )	\$(5,007 )
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	727	727
Stock-based compensation	988	1,298
Write-down of inventories	13	99
Gains on disposal of equipment	—	(2 )
Changes in operating assets and liabilities:		
Accounts receivable	(45 )	1,285
Inventories	1,938	(3,614 )
Other assets	409	234
Trade payables	(533 )	(1,028 )
Accrued liabilities and deferred revenue	617	(583 )
Other long-term liabilities	79	(59 )
Net cash used in operating activities	(3,723 )	(6,650 )
Cash flows from investing activities:		
Capital expenditures for property and equipment	(163 )	(522 )
Proceeds from sale of fixed assets	—	2
Net cash used in investing activities	(163 )	(520 )
Cash flows from financing activities:		
Payment of debt and capital lease obligations	(158 )	(114 )
Stock issued under share-based compensation, net	409	4,208
Net cash provided by financing activities	251	4,094
Net (decrease) in cash and cash equivalents	(3,635 )	(3,076 )
Cash and cash equivalents at beginning of period	30,050	37,406
Cash and cash equivalents at end of period	\$26,415	\$34,330
Supplemental schedule of non-cash investing and financing activities :		
Capital lease obligation to finance capital expenditures	\$258	\$435
Purchase of equipment included in accounts payable	\$36	\$306

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

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QUICKLOGIC CORPORATION  
NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — The Company and Basis of Presentation

QuickLogic Corporation ("QuickLogic" or "the Company"), was founded in 1988 and reincorporated in Delaware in 1999. The Company develops and markets low-power programmable solutions that enable customers to add differentiated features and capabilities to their mobile, consumer and industrial products. The Company is a fabless semiconductor company that designs, markets and supports ultra-low power, customizable Sensor Hub, Display, and Connectivity semiconductor solutions for smartphone, tablet, wearable, and mobile enterprise, Original Equipment Manufacturers, or OEMs. Called Customer Specific Standard Products, or CSSPs, these programmable 'silicon plus software' solutions enable our customers to bring hardware-differentiated products to market quickly and cost effectively. The Company also develops and markets low-power Field Programmable Gate Arrays, or FPGAs, application solutions, associated design software and programming hardware.

The accompanying interim condensed consolidated financial statements are unaudited. In the opinion of management, these statements have been prepared in accordance with United States generally accepted accounting principles, or U.S. GAAP, and include all adjustments, consisting only of normal recurring adjustments, necessary to provide a fair statement of results for the interim periods presented. The Company recommends that these interim condensed consolidated financial statements be read in conjunction with the Company's Form 10-K for the year ended December 28, 2014. Operating results for the six months ended June 28, 2015 are not necessarily indicative of the results that may be expected for the full year.

QuickLogic's fiscal year ends on the Sunday closest to December 31 and the fiscal quarters each end on the Sunday closest to the end of each calendar quarter. QuickLogic's second fiscal quarters for 2015 and for 2014 ended on Sunday, June 28, 2015 and June 29, 2014, respectively.

Liquidity

The Company has financed its operations and capital investments through sales of common stock, capital and operating leases, and bank lines of credit. As of June 28, 2015, the Company's principal sources of liquidity consisted of cash and cash equivalents of \$26.4 million and \$5.0 million in available credit under its revolving line of credit with Silicon Valley Bank, which expires on June 27, 2016. This line of credit provides for committed loan advances of up to \$6.0 million, subject to increase at the Company's election up to \$10.0 million.

The Company currently uses its cash to fund its capital expenditures and operating losses. Based on past performance and current expectations, the Company believes that its existing cash and cash equivalents, together with available financial resources from the revolving line of credit with Silicon Valley Bank will be sufficient to fund its operations and capital expenditures and provide adequate working capital for the next twelve months.

Over the longer term, the Company believes that its existing cash and cash equivalents, together with financial resources from its revolving line of credit with Silicon Valley Bank and its ability to sell additional shares to capital markets will be sufficient to satisfy its operations and capital expenditures.

The Company's liquidity is affected by many factors including, among others: the level of revenue and gross profit as a result of the cyclical nature of the semiconductor industry; the conversion of design opportunities into revenue; market acceptance of existing and new products including CSSPs based on its ArcticLink® and PolarPro® solution platforms; fluctuations in revenue as a result of product end-of-life; fluctuations in revenue as a result of the stage in the product life cycle of its customers' products; costs of securing access to and availability of adequate manufacturing capacity;



levels of inventories; wafer and finished goods purchase commitments; customer credit terms; the amount and timing of research and development expenditures; the timing of new product introductions; production volumes; product quality; sales and marketing efforts; the value and liquidity of our investment portfolio; changes in operating assets and liabilities; the ability to obtain or renew debt financing and to remain in compliance with the terms of existing credit facilities; the ability to raise funds from the sale of equity in the Company; the issuance and exercise of stock options and participation in the Company's employee stock purchase plan; and other factors related to the uncertainties of the industry and global economics. Accordingly, there can be no assurance that events in the future will not require the Company to seek additional capital or, if so required, that such capital will be available on terms acceptable to the Company.

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QUICKLOGIC CORPORATION

NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Principles of Consolidation

The consolidated financial statements include the accounts of QuickLogic and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated.

Foreign Currency

The functional currency of the Company's non-U.S. operations is the U.S. dollar. Accordingly, all monetary assets and liabilities of these foreign operations are translated into U.S. dollars at current period-end exchange rates and non-monetary assets and related elements of expense are translated using historical exchange rates. Income and expense elements are translated to U.S. dollars using the average exchange rates in effect during the period. Gains and losses from the foreign currency transactions of these subsidiaries are recorded as interest income and other expense, net in the condensed unaudited consolidated statements of operations.

Uses of Estimates

The preparation of these consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the period. Actual results could differ materially from those estimates, particularly in relation to revenue recognition, the allowance for doubtful accounts, sales returns, valuation of investments, valuation of long-lived assets, valuation of inventories including identification of excess quantities, market value and obsolescence, measurement of stock-based compensation awards, accounting for income taxes and estimating accrued liabilities.

Concentration of Risk

The Company's accounts receivable are denominated in U.S. dollars and are derived primarily from sales to customers located in North America, Asia Pacific, and Europe. The Company performs ongoing credit evaluations of its customers and generally does not require collateral. See Note 11 for information regarding concentrations associated with accounts receivable.

For the three and six months ended June 28, 2015, the Company generated 41% and 40% of its total revenue from shipments to Samsung Electronics Co., Ltd. ("Samsung"). See Note 11 for information regarding concentrations associated with customers and distributors.

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QUICKLOGIC CORPORATION

NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Note 2 — Significant Accounting Policies

During the six months ended June 28, 2015, there were no changes in the Company's significant accounting policies from its disclosure in the Annual Report on Form 10-K for the year ended December 28, 2014. For a discussion of the significant accounting policies, please see the Annual Report on Form 10-K for the fiscal year ended December 28, 2014, filed with the Securities Exchange Commission, or SEC, on March 5, 2015.

New Accounting Pronouncements

In April 2015, the FASB issued ASU 2015-03, Simplifying Presentation of Debt Issuance Costs which amends the accounting guidance on the presentation of debt issuance costs. The guidance requires an entity to present debt issuance costs related to a recognized debt liability as a direct deduction from the carrying amount of that debt, consistent with debt discounts. The guidance is effective for annual reporting periods beginning after December 31, 2015 and interim periods beginning after December 15, 2016, and must be applied retrospectively to each prior reporting period presented. The Company is currently evaluating the impact of ASU 2015-03 on its consolidated financial statements and footnote disclosures.

In February 2015, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update No. 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis (ASU 2015-02), which is intended to improve the targeted areas of consolidation guidance for legal entities such as limited partnerships, limited liability corporations and securitization structures. In addition to reducing the number of consolidation models from four to two, the new standard simplifies the FASB accounting standards codification and improves the current U.S. GAAP by: placing more emphasis on risk of loss when determining a controlling financial interest; reducing the frequency of the application of related party guidance when determining a controlling financial interest in a variable interest entity, or VIE and changing consolidation conclusions for public and private companies in several industries that typically make use of limited partnerships or VIEs. This ASU 2015-02 is effective for annual periods ending after December 15, 2015, and interim periods beginning after December 15, 2015. Early adoption is permitted including adoption in an interim period. The Company is currently evaluating the impact of ASU 2015-02 on its consolidated financial statements and footnote disclosures.

In January 2015, the FASB issued Accounting Standards Update No. 2015-01, Income Statement - Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items (ASU 2015-01). This ASU 2015-01 eliminates from U.S. GAAP the concept of extraordinary items. Subtopic 225-20, Income Statement - Extraordinary and Unusual Items, requires that an entity separately classify, present and disclose extraordinary events and transactions. Presently, an event or transaction is presumed to be an ordinary and usual activity of a reporting entity unless evidence clearly supports its classification as an extraordinary item. If an event or transaction meets the criteria for extraordinary classification, an entity is required to segregate the extraordinary item from the results of ordinary operations and show such item separately in the income statement, net of tax, after income from continuing operations. The entity is also required to disclose applicable income taxes and either present or disclose earnings-per-share data applicable to the extraordinary item. This ASU 2015-01 is effective for annual periods ending after December 15, 2015, and interim periods beginning after December 15, 2015. Early adoption is permitted provided that the adopted guidance is applied from the beginning of the annual year in which such guidance is adopted. The Company is currently evaluating the impact of ASU 2015-01 on its consolidated financial statements and footnote disclosures.

Other new accounting pronouncements are disclosed on the Annual Report on Form 10-K for the fiscal year ended December 28, 2014 filed with the SEC on March 5, 2015.

Note 3 — Net Loss Per Share

Basic loss per share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share was computed using the weighted average number of common shares outstanding during the period plus potentially dilutive common shares outstanding during the period under the treasury stock method. In computing diluted net income (loss) per share, the weighted average stock price for the period is used in determining the number of shares assumed to be purchased from the exercise of stock options and warrants.

The following shares were not included in the calculation of diluted net loss per share for the second quarter and six months ended June 28, 2015 and June 29, 2014: (i) 7.1 million and 6.6 million of common shares associated with equity awards outstanding and the estimated number of shares to be purchased under the current offering period of the 2009 Employee Stock Purchase Plan, respectively, and (ii) warrants to purchase up to 2.3 million as of June 28, 2015 and 4.2 million as of June 29,

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

2014 shares of common stock respectively. These shares were not included as they were considered antidilutive due to the net loss the Company experienced during these periods.

## Note 4 — Balance Sheet Components

	As of June 28, 2015 (in thousands)	December 28, 2014
Inventories:		
Raw material	\$—	\$—
Work-in-process	1,798	1,191
Finished goods	1,203	3,761
	\$3,001	\$4,952
Other current assets:		
Prepaid expenses	\$765	\$1,042
Other	108	104
	\$873	\$1,146
Property and equipment:		
Equipment	\$14,100	\$14,047
Software	2,852	3,332
Furniture and fixtures	711	710
Leasehold improvements	714	595
	18,377	18,684
Accumulated depreciation and amortization	(15,688 )	(15,467 )
	\$2,689	\$3,217
Accrued liabilities:		
Employee related accruals	\$1,792	\$1,356
Restructuring accruals - See Note 12	169	—
Other	108	218
	\$2,069	\$1,574

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

## Note 5 — Obligations

	As of June 28, 2015 (in thousands)	December 28, 2014
Debt and capital lease obligations:		
Revolving line of credit	\$1,000	\$1,000
Capital leases	258	416
	1,258	1,416
Current portion of debt and capital lease obligations	(1,202 )	(225 )
Long term portion of debt and capital lease obligations	\$56	\$1,191

## Revolving Line of Credit

The Company and Silicon Valley Bank have entered into the Third Amended and Restated Loan and Security Agreement dated June 30, 2014, as amended September 26, 2014 ("the Third Loan Agreement"). The terms of the Third Loan Agreement include a \$6.0 million revolving line of credit available through June 27, 2016. Upon each advance, the Company can elect a fixed interest rate, which is the prime rate plus the prime rate margin, or a fixed rate, which is LIBOR plus the LIBOR rate margin. As of the end of the second quarter of 2015, the Company had \$1.0 million of revolving debt outstanding with an interest rate of 3.06%.

Silicon Valley Bank has a first priority security interest in substantially all of the Company's tangible and intangible assets to secure any outstanding amounts under the Third Loan Agreement. Under the terms of the Third Loan Agreement, the Company must maintain a minimum tangible net worth of at least \$15 million, an adjusted quick ratio of 2-to-1 and a minimum unrestricted cash or cash equivalents balance of at least \$8 million. The Third Loan Agreement also has certain restrictions including, among others, restrictions on the incurrence of other indebtedness, the maintenance of depository accounts, the disposition of assets, mergers, acquisitions, investments, the granting of liens, cash balances with subsidiaries and the payment of dividends. The Company was in compliance with the financial covenants of the Third Loan Agreement as of the end of the current reporting period.

## Capital Leases

In July 2014, the Company leased design software under a 41-month capital lease at an imputed interest rate of 3.15% per annum. Terms of the agreement require the Company to make payments of principal and interest of \$42,000 in August 2014, \$16,000 in December 2014, \$58,000 in January 2016 and \$58,000 in January 2017. The total payments for the lease will be \$174,000. As of June 28, 2015, \$111,000 was outstanding under this capital lease, of which \$55,000 was classified as a current liability.

In May 2014, the Company leased design software under a three-year capital lease at an imputed interest rate of 4.80% per annum. Terms of the agreement require the Company to make annual payments of approximately \$84,000 through April 2016, for a total of \$252,000. As of June 28, 2015, \$80,000 was outstanding under the capital lease, all of which was classified as a current liability.

In December 2013, the Company leased design software under a two-year capital lease at an imputed interest rate of 4.34% per annum. Terms of the agreement require the Company to make quarterly payments of approximately \$34,000 through September 2015, for a total of \$273,000. As of June 28, 2015, \$67,000 was outstanding under the capital lease, all of which was classified as a current liability.



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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

## Note 6 — Fair Value Measurements

Pursuant to the accounting guidance for fair value measurements and its subsequent updates, fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Company considers the principal or most advantageous market and it considers assumptions that market participants would use when pricing the asset or liability.

The accounting guidance for fair value measurement also specifies a hierarchy of valuation techniques based upon whether the inputs to those valuation techniques reflect assumptions other market participants would use based upon market data obtained from independent sources (observable inputs), or reflect the Company's own assumptions of market participant valuation (unobservable inputs). The fair value hierarchy consists of the following three levels:

Level 1 – Inputs are quoted prices in active markets for identical assets or liabilities.

Level 2 – Inputs are quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable and market-corroborated inputs which are derived principally from or corroborated by observable market data.

Level 3 – Inputs are derived from valuation techniques in which one or more significant inputs or value drivers are unobservable.

The following table presents the Company's financial assets that are measured at fair value on a recurring basis as of June 28, 2015 and December 28, 2014, consistent with the fair value hierarchy provisions of the authoritative guidance (in thousands):

	As of June 28, 2015				As of December 28, 2014			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Assets:								
Money market funds <sup>(1)</sup>	\$26,318	\$1,013	\$25,305	\$—	\$29,425	\$874	\$28,551	\$—
Total assets	\$26,318	\$1,013	\$25,305	\$—	\$29,425	\$874	\$28,551	\$—

(1) Money market funds are presented as a part of cash and cash equivalents on the accompanying consolidated balance sheets as of June 28, 2015 and December 28, 2014.

## Note 7 - Stockholders' Equity

## Common Stock and Preferred Stock

The Company is authorized to issue 100 million shares of common stock and has 10 million shares of authorized but unissued shares of preferred stock. Without any further vote or action by the Company's stockholders, the Board of Directors has the authority to determine the powers, preferences, rights, qualifications, limitations or restrictions granted to or imposed upon any wholly unissued shares of undesignated preferred stock.

## Issuance of Common Stock and Warrants



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On July 31, 2013, the Company filed a shelf registration statement on Form S-3 under which the Company may, from time to time, sell securities in one or more offerings up to a total dollar amount of \$40.0 million. The Company's shelf registration statement was declared effective on August 30, 2013 and expires in August 2016.

In November 2013, the Company issued an aggregate of 8,740,000 shares of common stock, \$0.001 par value, in an underwritten public offering at a price of \$2.90 per share. The Company received net proceeds from the offering of approximately \$23.1 million, net of underwriter's commission and other offering expenses of \$2.2 million.

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As of June 28, 2015, 2.3 million warrants were outstanding. Approximately 1.9 million warrants with a strike price of \$2.15 were issued in conjunction with a November 2009 financing. These warrants expired in May 2015. Remaining outstanding warrants approximately 2.3 million warrants with a strike price of \$2.98 were issued in conjunction with June 2012 financing. These warrants expire in June 2017 and can be exercised on a cash or cashless basis until August 2016. After this date, the registration statement will no longer be effective and the warrants can only be exercised on a cashless basis.

### Note 8 — Employee Stock Plans

#### 1999 Stock Plan

The 1999 Stock Plan, or 1999 Plan, provided for the issuance of incentive and non-qualified options, restricted stock units ("RSUs") and restricted stock. Equity awards granted under the 1999 Plan have a term of up to ten years. Options typically vest at a rate of 25% one year after the vesting commencement date, and one forty-eighth for each month of service thereafter. In March 2009, the Board adopted the 2009 Stock Plan, which was approved by the Company's stockholders on April 22, 2009. Effective April 22, 2009, no further stock options may be granted under the 1999 Plan.

#### 2009 Stock Plan

The 2009 Stock Plan, or 2009 Plan, was amended and restated by the Board of Directors in January 2015 and approved by the Company's stockholders on April 23, 2015 to, among other things, reserve an additional 2.5 million shares of common stock for issuance under the 2009 Plan. As of June 28, 2015, approximately 9.6 million shares were reserved for issuance under the 2009 Plan. Equity awards that are cancelled, forfeited or repurchased under the 1999 Plan become available for grant under the 2009 Plan, up to a maximum of an additional 10 million shares. Equity awards granted under the 2009 Plan have a term of up to ten years. Options typically vest at a rate of 25% one year after the vesting commencement date, and one forty-eighth for each month of service thereafter. RSUs typically vest at a rate of 25% one year after the vesting commencement date, and one eighth every six months thereafter. The Company may implement different vesting schedules in the future with respect to any new equity awards.

#### Employee Stock Purchase Plan

The 2009 Employee Stock Purchase Plan, or 2009 ESPP, was adopted in March 2009. In January 2015, the 2009 ESPP was amended by the Board of Directors and approved by the Company's stockholders on April 23, 2015 to reserve an additional 1.0 million shares of common stock for issuance under the 2009 ESPP. As of June 28, 2015 approximately 3.3 million shares were reserved for issuance under the 2009 ESPP Plan. The 2009 ESPP provides for six month offering periods. Participants purchase shares through payroll deductions of up to 20% of an employee's total compensation (maximum of 20,000 shares per offering period). The 2009 ESPP permits the Board of Directors to determine, prior to each offering period, whether participants purchase shares at: (i) 85% of the fair market value of the common stock at the end of the offering period; or (ii) 85% of the lower of the fair market value of the common stock at the beginning or the end of an offering period. The Board of Directors has determined that, until further notice, future offering periods will be made at 85% of the lower of the fair market value of the common stock at the beginning or the end of an offering period.

### Note 9 — Stock-Based Compensation

The Company's equity incentive program is a broad-based, long-term retention program intended to attract, motivate, and retain talented employees as well as align stockholder and employee interests. The Company provides stock-based incentive compensation, or awards, to eligible employees and non-employee directors. Awards that may be granted

under the program include non-qualified and incentive stock options, restricted stock units, or RSUs, performance-based restricted stock units, or PRSUs, and cash settlement of stock appreciation rights, or SARs. To date, awards granted under the program consist of stock options, RSUs and PRSUs. The majority of stock-based awards granted under the program vest over four years. Stock options granted under the program have a maximum contractual term of ten years.

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

The stock-based compensation expense included in the Company's consolidated financial statements for the three and six months ended June 28, 2015 and June 29, 2014 was as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Cost of revenue	\$27	\$36	\$66	\$78
Research and development	212	221	403	574
Selling, general and administrative	252	309	519	646
Total costs and expenses	\$491	\$566	\$988	\$1,298

No stock-based compensation was capitalized during any period presented above.

## Valuation Assumptions

The Company uses the Black-Scholes option pricing model to estimate the fair value of employee stock options and rights to purchase shares under the Company's 2009 ESPP. Using the Black-Scholes pricing model requires the Company to develop highly subjective assumptions including the expected term of awards, expected volatility of its stock, expected risk-free interest rate and expected dividend rate over the term of the award. The Company's expected term of awards assumption is based primarily on its historical experience with similar grants. The Company's expected stock price volatility assumption for both stock options and ESPP shares is based on the historical volatility of the Company's stock, using the daily average of the opening and closing prices and measured using historical data appropriate for the expected term. The risk-free interest rate assumption approximates the risk-free interest rate of a Treasury Constant Maturity bond with a maturity approximately equal to the expected term of the stock option or ESPP shares. This fair value is expensed over the requisite service period of the award. The fair value of RSUs and PRSUs is based on the closing price of the Company's common stock on the date of grant. Equity compensation awards which vest with service are expensed using the straight-line attribution method over the requisite service period.

In addition to the assumptions used in the Black-Scholes pricing model, the amended authoritative guidance requires that the Company recognize expense for awards ultimately expected to vest; therefore the Company is required to develop an estimate of the number of awards expected to be forfeited prior to vesting, or forfeiture rate. The forfeiture rate is estimated based on historical pre-vest cancellation experience and is applied to all share-based awards.

The following weighted average assumptions are included in the estimated fair value calculations for stock option grants:

	Three Months Ended		Six Months Ended		
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014	
Expected term (years)	—	6.00	4.78	6.19	
Risk-free interest rate	—	% 1.90	% 1.40	% 1.98	%
Expected volatility	—	% 55.70	% 52.11	% 55.10	%
Expected dividend yield	—	—	—	—	

No stock options were granted in the second quarter of 2015. The weighted average estimated fair value for options granted during the second quarter of 2014 was \$1.86 per option. The weighted average estimated fair value for options

granted during the six months of 2015 and 2014 was \$0.90 and \$2.10, per option, respectively. As of June 28, 2015 and June 29, 2014, the fair value of unvested stock options, net of expected forfeitures, was approximately \$2.7 million and \$2.1 million, respectively. This unrecognized stock-based compensation expense is expected to be recorded over a weighted average period of 2.26 years.

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

## Stock-Based Compensation Award Activity

The following table summarizes the activity in the shares available for grant under the 2009 Plan during the six months ended June 28, 2015:

	Shares Available for Grant (in thousands)
Balance at December 28, 2014	1,139
Authorized	2,500
Options granted	(80 )
Options forfeited or expired	174
RSUs granted	(298 )
PRSUs granted	(20 )
RSUs forfeited or expired	35
Balance at June 28, 2015	3,450

## Stock Options

The following table summarizes stock options outstanding and stock option activity under the 1999 Plan and the 2009 Plan, and the related weighted average exercise price, for the first six months of 2015:

	Number of Shares  (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Term  (in years)	Aggregate Intrinsic Value  (in thousands)
Balance outstanding at December 28, 2014	5,682	\$2.67		
Granted	80	2.00		
Forfeited or expired	(174 )	3.41		
Exercised	(117 )	0.98		
Balance outstanding at June 28, 2015	5,471	\$2.67	4.84	\$292
Exercisable at June 28, 2015	4,631	\$2.61	4.20	\$292
Vested and expected to vest at June 28, 2015	5,317	\$2.66	4.72	\$292

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on the Company's closing stock price of \$1.61 as of the end of the Company's current reporting period, which would have been received by the option holders had all option holders exercised their options as of that date.

The total intrinsic value of options exercised during the first six months of 2015 and 2014 was \$81,000 and \$3.6 million, respectively. Total cash received from employees as a result of employee stock option exercises during the first six months of 2015 and 2014 was approximately \$114,000 and \$4.2 million respectively. The Company settles employee stock option exercises with newly issued common shares. In connection with these exercises, there was no tax benefit realized by the Company due to the Company's current loss position. Total stock-based compensation related to stock options was \$211,000 and \$459,000 for the three months and six months ended June 28, 2015.

## Restricted Stock Units and Performance-based Restricted Stock Units

The Company began issuing RSUs and PRSUs in the third quarter of 2007. RSUs entitle the holder to receive, at no cost, one common share for each RSU as it vests. In general, the Company's policy is to withhold shares in settlement of employee tax withholding obligations upon the vesting of RSUs. The stock-based compensation related to RSUs and PRSUs was \$188,000 and \$20,000, for the three months and \$343,000 and \$35,000 for the six months ended June 28, 2015, respectively. As of June 28, 2015, there was \$1.7 million in unrecognized compensation expense related to RSUs and PRSUs.

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

A summary of activity for the Company's RSUs and PRSUs for the six months ended June 28, 2015 and information regarding RSUs and PRSUs outstanding and expected to vest as of June 28, 2015 is as follows:

	RSUs & PRSUs Outstanding	
	Number of Shares	Weighted Average Grant Date Fair Value
	(in thousands)	
Nonvested at December 28, 2014	650	\$ 3.47
Granted	318	1.85
Vested	(54)	) 2.04
Forfeited	(35)	) —
Nonvested at June 28, 2015	879	\$ 3.10

## Employee Stock Purchase Plan

The weighted average estimated fair value, as defined by the amended authoritative guidance, of rights issued pursuant to the Company's 2009 ESPP during the second quarters of 2015 and 2014 was \$0.48 and \$1.01 per right, respectively.

As of June 28, 2015, 1,634,000 shares remained available for issuance under the 2009 ESPP including 1.0 million additional shares authorized in the second quarter. For the second quarter and first six months ended June 28, 2015, the Company recorded stock-based compensation expense related to the 2009 ESPP of \$72,000 and \$151,000, respectively.

The fair value of rights issued pursuant to the Company's 2009 ESPP was estimated on the commencement date of each offering period using the following weighted average assumptions:

	Three Months Ended		Six Months Ended		
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014	
Expected term (months)	6.08	6.09	6.08	6.09	
Risk-free interest rate	0.08	% 0.05	% 0.08	% 0.05	%
Volatility	51.54	% 49.17	% 51.54	% 49.17	%
Dividend yield	—	—	—	—	

As of June 28, 2015, the unrecognized stock-based compensation expense relating to the Company's 2009 ESPP was \$121,000 and is expected to be recognized over a weighted average period of approximately 4.5 months.

## Note 10 — Income Taxes

In the second quarters of 2015 and 2014, the Company recorded net income tax expense of \$21,000 and a net income tax benefit of \$44,000, respectively. For the six months ended June 28, 2015 and June 29, 2014, the Company recorded net income tax expense of \$61,000 and a net income tax benefit of \$24,000, respectively. The income tax expense for the second quarter of 2015 relates to income taxes from the Company's foreign operations, which are cost-plus entities. The income tax benefit for the second quarter of 2014 includes the net effect of the following: (i)



income taxes from its foreign operations which are cost-plus entities; and (ii) the release of an unrecognized tax benefit in the period.

Based on the available objective evidence, management believes it is more likely than not that the Company's net deferred tax assets will not be fully realizable. Accordingly, with the exception of its foreign subsidiaries, the Company has provided a full valuation allowance against the associated deferred tax assets. The Company will continue to assess the realizability of the deferred tax assets in future periods.

The Company had approximately \$52,000 and \$51,000 of unrecognized tax benefits at June 28, 2015 and December 28, 2014, respectively, which will result in a change in the Company's effective tax rate if recognized in future years. The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. For the six month period ended

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

June 28, 2015, the Company accrued \$3,000 of interest and penalties. As of June 28, 2015, the Company had approximately \$27,000 of accrued interest and penalties related to uncertain tax positions.

Included in the balance of unrecognized tax benefits at June 28, 2015 is \$17,000 related to tax positions, interest, and penalties for which it is reasonably possible that the statute of limitations will expire in various jurisdictions within the next twelve months.

The Company is subject to U.S. federal income tax as well as income taxes in many U.S. states and foreign jurisdictions in which the Company operates. As of December 28, 2014, fiscal years 2010 onward remain open to examination by the U.S. taxing authorities and fiscal years 2006 onward remain open to examination in Canada. The U.S. federal and U.S. state taxing authorities may choose to audit tax returns for tax years beyond the statute of limitation period due to significant tax attribute carryforwards from prior years, making adjustments only to carryforward attributes.

## Note 11 — Information Concerning Product Lines, Geographic Information and Revenue Concentration

The Company identifies its business segment based on business activities, management responsibility and geographic location. For all periods presented, the Company operated in a single reportable business segment.

The following is a breakdown of revenue by product line (in thousands):

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Revenue by product line <sup>(1)</sup> :				
New products	\$2,953	\$4,482	\$7,097	\$13,398
Mature products	2,020	2,354	4,035	4,602
Total revenue	\$4,973	\$6,836	\$11,132	\$18,000

(1) For all periods presented: New products include all products manufactured on 180 nanometer or smaller semiconductor processes. Mature products include all products produced on semiconductor processes larger than 180 nanometers.

The following is a breakdown of revenue by shipment destination (in thousands):

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Revenue by geography:				
Asia Pacific <sup>(1)</sup>	\$3,482	\$4,511	\$7,290	\$13,839
North America <sup>(2)</sup>	1,087	973	2,929	2,073
Europe	404	1,352	913	2,088
Total revenue	\$4,973	\$6,836	\$11,132	\$18,000

- (1) Asia Pacific includes revenue from South Korea of \$2.1 million, or 42%, of total revenue and \$2.7 million, or 39%, of total revenue for the quarters ended June 28, 2015 and June 29, 2014, respectively. For the six months ended June 28, 2015 and June 29, 2014, revenue from South Korea was \$4.5 million, or 40%, of total revenue and \$10.4 million, or 58%, respectively.
- (2) North America includes revenue from the United States of \$1.0 million, or 20%, of total revenue and \$891,000, or 13%, for the quarters ended June 28, 2015 and June 29, 2014, respectively. For the six months ended June 28, 2015 and June 29, 2014, revenue from United States was \$2.8 million, or 25%, and \$2.0 million, or 11%, respectively.

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

The following distributors and customers accounted for 10% or more of the Company's revenue for the periods presented:

	Three Months Ended		Six Months Ended		
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014	
Distributor "A"	24	% 18	% 27	% 12	%
Customer "B"	14	% 11	% 15	% *	
Customer "G"	41	% 40	% 40	% 59	%

\*Represents less than 10% of revenue for the period presented.

The following distributors and customers accounted for 10% or more of the Company's accounts receivable as of the dates presented:

	June 28, 2015	December 28, 2014	
Distributor "A"	39	% 34	%
Customer "G"	38	% 28	%

As of June 28, 2015, less than 10% of the Company's long-lived assets, including property and equipment and other assets, were located outside the United States.

## Note 12 — Restructuring Charges

In June 2015, the Company implemented a restructuring plan to re-align the organization to support the Company's sensor processing provider business model and growth strategy. This re-alignment resulted in a reduction of nine employees or 9% of the Company's global workforce. Pursuant to the restructuring plan, the Company recorded \$169,000 of restructuring liabilities, consisting primarily of employee severance related costs. The restructuring liabilities are included in the "Liabilities" line item in its consolidated balance sheet. The activities affecting the liabilities for the second quarter of 2015 are summarized as follows:

	Restructuring Liabilities (In Thousands)
Balance at December 28, 2014	\$—
Accruals	169
Payments	—
Balance at June 28, 2015	\$ 169

## Note 13 — Commitments and Contingencies

## Commitments

The Company's manufacturing suppliers require us to forecast wafer starts several months in advance. The Company is committed to take delivery of and pay for a portion of forecasted wafer volume. As of June 28, 2015 and December 28, 2014, the Company had \$913,000 and \$552,000, respectively, of outstanding commitments for the purchase of wafer and finished goods inventory.

The Company has obligations with certain suppliers for the purchase of other goods and services entered into in the ordinary course of business. As of June 28, 2015, total outstanding purchase obligations were \$1.9 million, of which \$1.6 million were due within the next twelve months.

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## QUICKLOGIC CORPORATION

## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

The Company leases its primary facility under a non-cancelable operating lease that expires at the end of 2018. In addition, the Company rents development facilities in India as well as sales offices in Europe and Asia. Total rent expense, net of sublease income, for the second quarters of 2015 and 2014 was approximately \$238,000 and \$240,000, respectively. Total rent expense, net of sublease income, for the six months of 2015 and 2014 was \$477,000 and \$471,000, respectively.

As of June 28, 2015, future minimum lease commitments under the Company's operating leases, excluding property taxes and insurance are as follows:

Fiscal Years	Operating Leases (in thousands)
2015 (Remaining 6 months)	\$395
2016	698
2017	628
2018	642
	\$2,363

## Contingencies

One of the Company's licensors contends that the Company owes back royalties on sales of the Company's ArcticLink III VX devices. Based on the terms and conditions of the Amended and Restated License Agreement between the parties, the Company does not believe it is liable for any royalty payments on these sales. Counsel for the Company has spoken with counsel for the licensor; however, the matter remains unresolved. The possible loss relating to this matter ranges between \$0 and \$250,000 as of June 28, 2015.

## Note 14 — Litigation

From time to time, the Company may become involved in legal actions arising in the ordinary course of business including, but not limited to, intellectual property infringement and collection matters. Absolute assurance cannot be given that any such third party assertions will be resolved: (i) without costly litigation; (ii) in a manner that is not adverse to the Company's financial position, results of operations or cash flows; or (iii) without requiring royalty or other payments which may adversely impact gross profit.

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

Forward-Looking Statements

The following Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as information contained in "Risk Factors" in Part II, Item 1A and elsewhere in this Quarterly Report on Form 10-Q, contain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We intend that these forward-looking statements be subject to the safe harbor created by those provisions. Forward-looking statements are generally written in the future tense and/or are preceded by words such as "will," "may," "should," "forecast," "could," "expect," "suggest," "believe," "anticipate," "intend," "plan," or other similar words. Forward-looking statements include statements regarding our strategies as well as (1) our revenue levels, including the commercial success of our Customer Specific Standard Products, or CSSPs, and new products, (2) the conversion of our design opportunities into revenue, (3) our liquidity, (4) our research and development efforts, (5) our gross profit and factors that affect gross profit, (6) our level of operating expenses, (7) our partners and suppliers and (8) industry trends. The following discussion should be read in conjunction with the attached condensed unaudited consolidated financial statements and notes thereto, and with our condensed audited consolidated financial statements and notes thereto for the fiscal year ended December 28, 2014, found in our Annual Report on Form 10-K filed with the Securities and Exchange Commission, or SEC, on March 5, 2015. Although we believe that the assumptions underlying the forward-looking statements contained in this Quarterly Report are reasonable, any of the assumptions could be inaccurate, and therefore there can be no assurance that such statements will be accurate. The risks, uncertainties and assumptions referred to above that could cause our results to differ materially from the results expressed or implied by such forward-looking statements include, but are not limited to, those discussed under the heading "Risk Factors" in Part II, Item 1A hereto and the risks, uncertainties and assumptions discussed from time to time in our other public filings and public announcements. All forward-looking statements included in this document are based on information available to us as of the date hereof. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that the results or conditions described in such statements or our objectives and plans will be achieved. Furthermore, past performance in operations and share price is not necessarily indicative of future performance. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

We develop and market low-power customizable semiconductor solutions that: enable customers to add new differentiated features; enable always-on and contextually aware sensor applications; extend battery life; and improve the customer's visual experience with their mobile, consumer and enterprise products. Our targeted mobile market segment includes Smartphones, Tablets, Wearables, and Mobile Enterprise. Our solutions typically fall into one of three product categories: Display and Visual Enhancement; Smart Connectivity; and Ultra-Low Power Sensor Hubs. We are a fabless semiconductor company that designs Customer Specific Standard Products, or CSSPs, which are complete, customer-specific solutions that include one or more of the following: a combination of silicon solution platforms; Proven System Blocks, or PSBs; customer-specific logic; SenseMe™ algorithm library; software drivers; and firmware. Our main platform families, EOS™, ArcticLink® and PolarPro®, are standard silicon platforms. Recent examples of PSBs that have been developed and that are available to customers include driving one or more Light Emitting Diodes, or LEDs, Barcode transmission via InfraRed (IR) LED, and TV remote control via LED. The variety of PSBs offered by us allows system designers to combine multiple discrete chips onto a single CSSP, simplifying design and board layout, lowering bill of material cost, and accelerating time-to-market. The programmable logic of the platforms is used for adding differentiated features and provides flexibility to address hardware-based product requirements quickly.

Utilizing a focused customer engagement model, we market CSSPs to Original Equipment Manufacturers, or OEMs, and Original Design Manufacturers, or ODMs, that offer differentiated mobile products, and to processor vendors that wish to expand their served available market through the deployment of reference designs to their customers. Our solutions enable OEMs and ODMs to add new features, deploy sensor-enabled applications, extend battery life, and improve the visual experience of their handheld mobile devices. In addition to working directly with our customers, we partner with other companies with expertise in certain technologies to develop additional intellectual property, reference platforms, and system software to provide application solutions.

We work with mobile processor manufacturers and sensor suppliers in the development of reference designs. Through the use of reference designs that incorporate our CSSPs, we believe mobile processor manufacturers can expand the served



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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

available market for their processors. In the event that a CSSP development with a processor manufacturer or a set of sensor vendors is applicable to a set of common OEMs or ODMs, we can amortize our research and development investment over that set of OEMs/ODMs. We call this type of solution a Catalog CSSP. We are placing a greater emphasis on developing and marketing Catalog CSSPs in the future.

In order to grow our revenue from its current level, we depend upon increased revenue from our new products, including existing new product platforms and platforms currently in development. We expect our business growth to be driven by CSSPs and our CSSP revenue growth needs to be strong enough to enable us to sustain profitability while we continue to invest in the development, sales and marketing of our new solution platforms, PSBs, algorithms, firmware, and new CSSPs. The gross margin associated with our CSSPs is generally lower than the gross margin of our FPGA products, due primarily to the price sensitive nature of the higher volume mobile consumer opportunities that we are pursuing with CSSPs.

During the second quarter of 2015, we generated total revenue of \$5.0 million. This represents a decrease of 19% from the prior quarter and a decrease of 27% over the second quarter of 2014. Our new product revenue was \$3.0 million, down 29% sequentially and down 34% year over year. The sequential and year over year decrease was primarily due to reduced shipment of our ArcticLink III display solution platform to Samsung for certain Android tablets and Eclipse product. We anticipate new product revenue generated from our Display and Visual Enhancement product category will continue to fluctuate depending on the demand in the Android tablet market.

For the second quarter of 2015, revenue generated from Samsung accounted for 69% of our new product revenue and 41% of our total revenue compared to 58% and 39%, respectively, for the first quarter of 2015. During the second quarter of 2015, new products were shipped into the Tablet, Smartphone and Mobile Enterprise markets. Our mature product revenue was \$2.0 million, sequentially flat and down 14% year over year. We devote substantially all of our development, sales and marketing efforts to our new solution platforms, PSBs and CSSPs. Overall, we reported a net loss of \$4.3 million for the second quarter of 2015 compared to a net loss of \$2.9 million for the second quarter of 2014 primarily due to decreased revenue.

Critical Accounting Estimates

The methods, estimates and judgments we use in applying our most critical accounting policies have a significant impact on the results we report in our consolidated financial statements. The SEC has defined critical accounting policies as those that are most important to the portrayal of our financial condition and results of operations and require us to make difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, our critical policies include revenue recognition, valuation of inventories including identification of excess quantities and product obsolescence, valuation of investments, valuation of long-lived assets, measurement of stock-based compensation and estimation of accrued liabilities. We believe that we apply judgments and estimates in a consistent manner and that this consistent application results in consolidated financial statements and accompanying notes that fairly represent all periods presented. However, any factual errors or errors in these judgments and estimates may have a material impact on our financial statements. For a discussion of critical accounting policies and estimates, please see Item 7 in our Annual Report on Form 10-K for the fiscal year ended December 28, 2014, filed with the SEC on March 5, 2015.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

## Results of Operations

The following table sets forth the percentage of revenue for certain items in our condensed consolidated statements of operations for the periods indicated:

	Three Months Ended		Six Months Ended		
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014	
Revenue	100	% 100	% 100	% 100	%
Cost of revenue	57	% 56	% 55	% 61	%
Gross profit	43	% 44	% 45	% 39	%
Operating expenses:					
Research and development	70	% 45	% 63	% 32	%
Selling, general and administrative	54	% 42	% 51	% 35	%
Restructuring Costs	3	% —	% 2	%	
Loss from operations	(85)	)% (42)	)% (70)	)% (27)	)%
Interest expense	—	% —	% —	% —	%
Interest income and other expense, net	(1)	)% (1)	)% (1)	)% (1)	)%
Loss before income taxes	(86)	)% (43)	)% (71)	)% (28)	)%
Provision for income taxes	—	% (1)	)% —	% —	%
Net loss	(86)	)% (42)	)% (71)	)% (28)	)%

Insignificant percentages are rounded to zero percentage (-%) for disclosure.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

Three Months Ended June 28, 2015 and June 29, 2014

## Revenue

The table below sets forth the changes in revenue for the three months ended June 28, 2015, as compared to the three months ended June 29, 2014 (in thousands, except percentage data):

	Three Months Ended June 28, 2015		June 29, 2014		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue by product line <sup>(1)</sup> :						
New products	\$2,953	59 %	\$4,482	66 %	\$(1,529)	(34)%
Mature products	2,020	41 %	2,354	34 %	(334)	(14)%
Total revenue	\$4,973	100 %	\$6,836	100 %	\$(1,863)	(27)%

(1) For all periods presented: New products include all products manufactured on 180 nanometer or smaller semiconductor processes. Mature products include all products produced on semiconductor processes larger than 180 nanometers.

The \$1.5 million decrease in new product revenue was primarily due to decreased shipments of our ArcticLink III display bridge solution platform to Samsung for certain Android tablets and lower sales of Eclipse II products. Revenue from Samsung in the second quarter of 2015 was \$2.0 million compared to \$2.7 million for our second quarter of 2014. Eclipse II revenue in the second quarter of 2015 was \$326,000 compared with \$1.1 million in the same period of 2014. Shrinkage of sales in the tablet market continues to impact the Company's revenue from Samsung, which accounted for 69% of new product revenue and 41% of total revenue in the second quarter of 2015. The decrease in mature product revenue is primarily due to decreased orders from our customers in the aerospace, test and instrumentation sectors and royalty income.

We continue to seek to expand our revenue through the pursuit of high volume sales opportunities in our target market segments and the sale of CSSPs incorporating our PSBs. Our industry is characterized by intense price competition and by lower margins as order volumes increase. Due to the concentration of our new product revenue in Samsung, combined with the cyclical nature of the mobile market, we have experienced significant fluctuations in new product revenue. While winning large-volume sales opportunities will increase our revenue, due to the pricing negotiation leverage of large companies, these opportunities may decrease our gross profit as a percentage of revenue. In the current quarter, the impact of price reductions on revenue was insignificant. In addition, these large companies provide longer-term purchase forecasts which are not binding and may not result in revenue.

## Gross Profit

The table below sets forth the changes in gross profit for the three months ended June 28, 2015 as compared to the three months ended June 29, 2014 (in thousands, except percentage data):

	Three Months Ended June 28, 2015		June 29, 2014		Change	
	Amount	% of Total	Amount	% of Total	Amount	Percentage

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		Revenues			Revenues					
Revenue	\$4,973	100	%	\$6,836	100	%	\$(1,863	)	(27	)%
Cost of revenue	2,830	57	%	3,820	56	%	(990	)	(26	)%
Gross Profit	\$2,143	43	%	\$3,016	44	%	\$(873	)	(29	)%

The \$873,000 decrease in gross profit in the second quarter of 2015 as compared to the second quarter of 2014 was primarily due to the overall decrease in revenue from our new and matured products, particularly ArcticLink III and Eclipse II products. The sale of previously reserved inventory was \$57,000 and \$233,000 in the second quarters of 2015 and 2014, respectively. Reduction of gross profit by 1% in the second quarter of 2014 compared to 2014 was primarily due to decreased revenue.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

Our semiconductor products have historically had long product life cycles and obsolescence has not been a significant factor in the valuation of inventories. However, as we continue to pursue opportunities in the mobile market and develop new CSSPs and products, our product life cycle will be shorter and the risk of obsolescence will increase.

We regularly review the cost of inventories and purchase commitments against estimated market value and record a lower of cost or market reserve for inventories that have a cost in excess of estimated market value. This could have a material impact on our gross margin and inventory balances based on additional write-downs to net realizable value or a benefit from inventories previously written down. In general, our standard manufacturing lead times are longer than the binding forecasts we receive from customers. The revenue fluctuations we have experienced with Samsung have increased the risk of inventory obsolescence of our ArcticLink III display solution platform family.

## Operating Expenses

The table below sets forth the changes in operating expenses for the three months ended June 28, 2015, as compared to the three months ended June 29, 2014 (in thousands, except percentage data):

	Three Months Ended			June 29, 2014		Change			
	June 28, 2015			June 29, 2014		Amount	Percentage		
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount		Amount	Percentage	
R&D expense	\$3,493	70 %	\$3,056	45 %	\$437		14	%	
SG&A expense	2,690	54 %	2,848	42 %	(158 )		(6 )	%	
Restructuring charges	169	3 %	—	— %	169		100	%	
Total operating expenses	\$6,352	127 %	\$5,904	87 %	\$448		8	%	

## Research and Development

Our research and development, or R&D, expenses consist primarily of personnel, overhead and other costs associated with engineering process improvements, sensor hub and algorithm development, programmable logic design, CSSP design and software development. The \$437,000 increase in R&D expenses in the second quarter of 2015, as compared to the second quarter of 2014, was primarily attributable to a \$527,000 increase in compensation expenses due to increased headcount and a \$297,000 increase in third-party chip design costs, partially offset by decreases in IP purchases of \$279,000 and other expenses of \$93,000. We expect our R&D expenses to continue to increase due to new product development.

## Selling, General and Administrative Expense

Our selling, general and administrative, or SG&A, expenses consist primarily of personnel and related overhead costs for sales, marketing, finance, administration, human resources and general management. The \$158,000 decrease in SG&A expenses in the second quarter of 2015, as compared to the second quarter of 2014, was primarily due to lower outside services costs of \$354,000 partially offset by higher stock-based compensation of \$160,000 and higher depreciation costs of \$39,000.

## Restructuring Charges

In June 2015, the Company implemented a restructuring plan to re-align the organization to support the Company's sensor processing provider business model and growth strategy. This re-alignment resulted in a reduction of nine

employees or 9% of the Company's global workforce. Pursuant to the restructuring plan, the Company recorded \$169,000 of restructuring liabilities, consisting primarily of employee severance related costs. The restructuring liabilities are included in the "Accrual Liabilities" line item in its consolidated balance sheet. Please see Note 12 of the Condensed Unaudited Consolidated Financial Statements for further details.

Interest Expense and Interest Income and Other Expense, Net

The table below sets forth the changes in interest expense and interest income and other expense, net, for the three months ended June 28, 2015 as compared to the three months ended June 29, 2014 (in thousands, except percentage data):

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

	Three Months Ended		Change	
	June 28, 2015	June 29, 2014	Amount	Percentage
Interest expense	\$ (15 )	\$ (17 )	\$ 2	(12 )%
Interest income and other expense, net	(33 )	(36 )	3	(8 )%
	\$ (48 )	\$ (53 )	\$ 5	(9 )%

The decrease in interest expense was primarily due to slightly lower interest on our revolving line of credit.

We conduct a portion of our research and development activities in Canada and India and we have sales and marketing activities in various countries outside of the United States. Most of these international expenses are incurred in local currency. Foreign currency transaction gains and losses are included in interest and other income (expense), net, as they occur. We do not use derivative financial instruments to hedge our exposure to fluctuations in foreign currency and, therefore, our results of operations are, and will continue to be, susceptible to fluctuations in foreign exchange gains or losses. Historically, impact of foreign exchange fluctuations on the profit or loss has been immaterial.

## Provision for (Benefit from) Income Taxes

The table below sets forth the changes in the income tax provision (benefit) for the three months ended June 28, 2015 as compared to the three months ended June 29, 2014 (in thousands, except percentage data):

	Three Months Ended		Change	
	June 28, 2015	June 29, 2014	Amount	Percentage
Provision for income taxes	\$ 21	\$ (44 )	\$ 65	(148 )%

The income tax provision for the second quarter of 2015 was primarily from our foreign operations, which are cost-plus entities. The income tax benefit for the second quarter of 2014 was primarily from a release of tax contingency reserves where the statute of limitations has expired offset by tax on foreign operations, which are cost plus entities.

As of June 28, 2015, our ability to utilize our income tax loss carryforwards in future periods is uncertain and, accordingly, we recorded a full valuation allowance against the related U.S. tax provision. We will continue to assess the realizability of deferred tax assets in future periods.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

Six Months Ended June 28, 2015 and June 29, 2014

## Revenue

The table below sets forth the changes in revenue for the six months ended June 28, 2015, as compared to the six months ended June 29, 2014 (in thousands, except percentage data):

	Six Months Ended June 28, 2015		June 29, 2014		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue by product line <sup>(1)</sup> :						
New products	\$7,097	64 %	\$13,398	74 %	\$(6,301)	(47)%
Mature products	4,035	36 %	4,602	26 %	(567)	(12)%
Total revenue	\$11,132	100 %	\$18,000	100 %	\$(6,868)	(38)%

(1) For all periods presented: New products include all products manufactured on 180 nanometer or smaller semiconductor processes. Mature products include all products produced on semiconductor processes larger than 180 nanometers.

The decrease in new product revenue was primarily driven by lower shipments of our ArcticLink III VX device to Samsung. In the first six months of 2015 revenue from ArcticLink III was \$4.5 million compared to \$10.9 million in 2014. Revenue generated from Samsung for the first six months accounted for 63% of new product revenue and 40% of total revenue. The decrease in mature product revenue was due primarily to orders from our customers in the aerospace, test and instrumentation sectors.

We continue to seek to expand our revenue through the pursuit of high volume sales opportunities in the consumer market segment and the sale of CSSPs incorporating our PSBs. Our industry is characterized by intense price competition and lower margins as order volumes increase. While winning large volume sales opportunities will increase our revenue, we believe these opportunities may decrease our gross profit as a percentage of revenue.

## Gross Profit

The table below sets forth the changes in gross profit for the six months ended June 28, 2015 as compared to the six months ended June 29, 2014 (in thousands, except percentage data):

	Six Months Ended June 28, 2015		June 29, 2014		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue	\$11,132	100 %	\$18,000	100 %	\$(6,868)	(38)%
Cost of revenue	6,110	55 %	10,926	61 %	(4,816)	(44)%
Gross Profit	\$5,022	45 %	\$7,074	39 %	\$(2,052)	(29)%



The increase of gross margin by 6% in the first six months of 2015 compared to the first six months of 2014 was primarily due to a product mix change and declining sales into the low cost Android tablet market. The \$2.1 million decrease in gross profit in the first six months of 2015 as compared to the first six months of 2014 was primarily due to the decrease in revenue and unfavorable purchase price variance, partially offset by the higher margin product mix. Inventory reserve provisions were \$13,000 and \$99,000 in the first six months of 2015 and 2014, respectively. The sale of previously reserved inventories was \$121,000 and \$352,000 in the first six months of 2015 and 2014, respectively.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

## Operating Expenses

The table below sets forth the changes in operating expenses for the six months ended June 28, 2015 as compared to the six months ended June 29, 2014 (in thousands, except percentage data):

	Six Months Ended		June 29, 2014		Change			
	June 28, 2015		June 29, 2014		Amount	Percentage		
	Amount	% of Total Revenues	Amount	% of Total Revenues				
R&D expense	\$6,970	63 %	\$5,697	32 %	\$1,273		22	%
SG&A expense	5,650	51 %	6,313	35 %	(663 )		(11	)%
Restructuring Charges	169	2 %	—	— %	169		100	%
Total operating expenses	\$12,789	116 %	\$12,010	67 %	\$779		6	%

## Research and Development

The \$1.3 million increase in R&D expenses in the first six months of 2015 as compared to the first six months of 2014 was attributable primarily to a \$1.0 million increase in compensation expenses related to an increase in headcount; increase in third-party chip design costs of \$944,000, partially offset by a decrease in IP purchase cost of \$325,000; and a decrease in stock-based compensation of \$299,000.

## Selling, General and Administrative Expense

The \$663,000 decrease in SG&A expenses in the first six months of 2015 as compared to the first six months of 2014 was primarily due to a decrease of \$544,000 in administration consulting expenses related to stock expense, legal, recruiting, and a decrease of stock-based compensation of \$567,000, partially offset by increased salaries cost of \$285,000, increased MIS and other expenses of \$139,000, and increased depreciation cost of \$72,000.

## Interest Expense and Interest Income and Other, Net

The table below sets forth the changes in interest expense and interest income and other, net, for the six months ended June 28, 2015, as compared to the six months ended June 29, 2014 (in thousands, except percentage data):

	Six Months Ended		Change			
	June 28, 2015	June 29, 2014	Amount	Percentage		
Interest expense	\$(29 )	\$(33 )	\$4	(12 )%		
Interest income and other, net	(59 )	(62 )	3	(5 )%		
	\$(88 )	\$(95 )	\$7	(7 )%		

The decrease in interest expense was due primarily to the changes in interest rates on our line of credit in the first six months of 2015 compared to the first six months of 2014. The increase in interest income and other, net was due primarily to the foreign exchange losses in the first six months of 2015 as compared to the first six months of 2014.

## Provision for (Benefit from) Income Taxes

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The table below sets forth the changes for income taxes provision (benefit) for the six months ended June 28, 2015 as compared to the six months ended June 29, 2014 (in thousands, except percentage data):

	Six Months Ended		Change Amount	Percentage
	June 28, 2015	June 29, 2014		
Provision for (Benefit from) Income Taxes	\$61	(24 )	\$85	(354 )%

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

The income tax provision for the six months ended June 28, 2015 was primarily from our foreign operations which are cost-plus entities. The income tax benefit for the six months ended June 29, 2014 was primarily from a release of tax contingency reserves where the statute of limitations has expired offset by tax on foreign operations which are cost plus entities.

As of June 28, 2015, our ability to utilize our income tax loss carryforwards in future periods is uncertain and, accordingly, we recorded a full valuation allowance against the related U.S. tax provision. We will continue to assess the realizability of deferred tax assets in future periods.

## Liquidity and Capital Resources

We have financed our operating losses and capital investments through sales of common stock, private equity investments, capital and operating leases, a revolving line of credit and cash flows from operations. As of June 28, 2015, our principal sources of liquidity consisted of our cash and cash equivalents of \$26.4 million and available credit under our \$5.0 million revolving line of credit with Silicon Valley Bank, which expires on June 27, 2016. Borrowing under the Company's line of credit is subject to the Company maintaining a tangible net worth of at least \$15.0 million, an unrestricted cash or cash equivalent balance of at least \$8.0 million and a quick ratio of 2-to-1. Upon each advance, the Company can elect one of two interest rates: (i) the prime rate plus the prime rate margin, or (ii) the LIBOR plus the LIBOR rate margin. We were in compliance with all loan covenants as of the end of the second quarter of 2015. As of June 28, 2015, the Company had \$1.0 million of revolving debt outstanding with an interest rate of 3.06%.

Most of our cash and cash equivalents were invested in money market funds with investment bankers rated AAAm/Aaa. Our interest-bearing debt consisted of \$258,000 outstanding under capital leases and \$1.0 million outstanding under our revolving debt (see Note 5 of the Condensed Unaudited Consolidated Financial Statements).

Cash balances held at our foreign subsidiaries were approximately \$1.1 million and \$868,000 at June 28, 2015 and December 28, 2014, respectively. Earnings from our foreign subsidiaries are currently deemed to be indefinitely reinvested. We do not expect such reinvestment to affect our liquidity and capital resources, and we continually evaluate our liquidity needs and ability to meet global cash requirements as a part of our overall capital deployment strategy. Factors which affect our global capital deployment strategy include anticipated cash flows, the ability to repatriate cash in a tax efficient manner, funding requirements for operations and investment activities, acquisitions and divestitures and capital market conditions.

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

	Six Months Ended	
	June 28, 2015	June 29, 2014
Net cash (used in) operating activities	\$(3,723)	\$(6,650)
Net cash (used in) investing activities	(163)	(520)
Net cash (used in) provided by financing activities	251	4,094
Net cash from operating activities		

Net cash used for operating activities was \$3.7 million in the first six months of 2015. The cash used for operating activities was a result of the net loss of \$7.9 million, partially offset by cash provided by changes in operating assets

and liabilities of \$2.5 million, and \$1.7 million of net non-cash charges. Non-cash charges consisted primarily of stock-based compensation of \$988,000, depreciation and amortization of \$727,000, and a write-down of inventory of \$13,000. The cash from changes in operating assets and liabilities was mostly due to a decrease in inventories of \$1.9 million as a result of sales of existing new product inventory and an increase in accrued liabilities and deferred revenue of \$617,000, partially offset by a reduction in accounts payable of \$533,000 due to the timing of payments.

Net cash used for operating activities was \$6.7 million in the first six months of 2014. The cash used for operating activities resulted primarily from the net loss of \$5.0 million and cash used for operating assets and liabilities of \$3.8 million partially offset by \$2.1 million of non-cash charges. These non-cash charges consisted primarily of stock-based compensation of \$1.3 million, depreciation and amortization of \$727,000, and a write-down of inventory of \$99,000. The cash used for operating assets and liabilities was mostly due to an increase in inventories of \$3.6 million in anticipation of future revenues, a

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

reduction in accounts payable of \$1.0 million due to timing of payments and a reduction of accrued liabilities \$583,000, partially offset by an increase of trade receivables \$1.3 million.

Net cash from investing activities

Net cash used for investing activities in the first six months of 2015 was \$163,000, which was primarily from cash used to acquire equipment and software used for the production and development of new products. Capital expenditures, which are largely driven by the development of new products and manufacturing levels are projected to be approximately \$300,000 during the remainder of fiscal year 2015.

Net cash used for investing activities in the first six months of 2014 was \$520,000, which was primarily from cash used to acquire equipment and software used for the production and development of new products.

Net cash from financing activities

Net cash provided by financing activities was \$251,000 in the first six months of 2015, primarily related to the issuance of common shares to employees under our equity plans of \$409,000, partially offset by scheduled repayments of lease obligations of \$158,000.

Net cash provided by financing activities was \$4.1 million for the first six months of 2014, primarily derived from proceeds related to the issuance of common shares to employees under our equity plans of \$4.2 million, partially offset by scheduled repayments of lease obligations of \$114,000.

We require substantial cash to fund our business and currently use cash to fund capital expenditures and operating losses. Based on past performance and current expectations, we believe that our existing cash and cash equivalents, together with available financial resources from the revolving line of credit facility, will be sufficient to fund our operations and capital expenditures, and provide adequate working capital for the next twelve months.

After the next twelve months, our cash requirements will depend on many factors including our level of revenue and gross profit, the market acceptance of our existing and new products, the levels at which we maintain inventories and accounts receivable, costs of securing access to adequate manufacturing capacity, new product development efforts, capital expenditures and the level of our operating expenses. In order to satisfy our longer term liquidity requirements, we may be required to raise additional equity or debt financing at commercially acceptable terms.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

## Contractual Obligations and Commercial Commitments

The following table summarizes our contractual obligations and commercial commitments as of June 28, 2015 and the effect such obligations and commitments are expected to have on our liquidity and cash flows in future fiscal periods (in thousands):

	Payments Due by Period			
	Total	Less than 1 Year	1-3 Years	More than 3 Years
Contractual obligations:				
Operating leases	\$2,362	\$934	\$1,268	\$160
Wafer purchases <sup>(1)</sup>	913	913	—	—
Other purchase commitments	1,873	1,601	272	—
Total contractual cash obligations	5,148	3,448	1,540	160
Other commercial commitments <sup>(2)</sup> :				
Revolving line of credit	1,000	1,000	—	—
Capital lease obligations <sup>(3)</sup>	258	202	56	—
Total commercial commitments	1,258	1,202	56	—
Total contractual obligations and commercial commitments <sup>(4)</sup>	\$6,406	\$4,650	\$1,596	\$160

Certain of our wafer manufacturers require us to forecast wafer starts several months in advance. We are

<sup>(1)</sup> committed to take delivery of and pay for a portion of forecast wafer volume. Wafer and finished goods purchase commitments of \$913,000 include firm purchase commitments as of June 28, 2015.

<sup>(2)</sup> Other commercial commitments are included as liabilities on our balance sheet as of June 28, 2015.

<sup>(3)</sup> For a detailed explanation, see Note 5 of the Condensed Unaudited Consolidated Financial Statements.

<sup>(4)</sup> Does not include unrecognized tax benefits of \$52,000 as of June 28, 2015. See Note 10 of the Condensed Unaudited Consolidated Financial Statements.

## Concentration of Suppliers

We depend on a limited number of contract manufacturers, subcontractors, and suppliers for wafer fabrication, assembly, programming and testing of our devices, and for the supply of programming equipment. These services are typically provided by one supplier for each of our devices. We generally purchase these single or limited source services through standard purchase orders. Because we rely on independent subcontractors to perform these services, we cannot directly control product delivery schedules, costs or quality levels. Our future success also depends on the financial viability of our independent subcontractors. These subcontract manufacturers produce products for other companies and we must place orders up to several months in advance of expected delivery. As a result, we have only a limited ability to react to fluctuations in demand for our products, which could cause us to have an excess or a shortage of inventories of a particular product, and our ability to respond to changes in demand is limited by the ability of our suppliers to provide products with the quantity, quality, cost and timeliness that we require. The decision not to provide these services to us or the inability to supply these services to us, such as in the case of a natural or financial disaster, would have a significant impact on our business. Increased demand from other companies could result in these subcontract manufacturers allocating available capacity to customers that are larger or have long-term supply contracts in place and we may be unable to obtain adequate foundry and other capacity at acceptable prices, or we may experience delays or interruption in supply. Additionally, volatility of economic, market, social and political

conditions in countries where these suppliers operate may be unpredictable and could result in a reduction in product revenue or increase our cost of revenue and could adversely affect our business, financial condition and results of operations.

#### Off-Balance Sheet Arrangements

We do not maintain any off-balance sheet partnerships, arrangements or other relationships with unconsolidated entities or others, often referred to as structured finance or special purpose entities, which are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.



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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — (Continued)

Recently Issued Accounting Pronouncements

See Note 2 of the Condensed Unaudited Consolidated Financial Statements for a description of recent accounting pronouncements, including the respective dates of adoption and expected effects on results of operations and financial condition.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio and variable rate debt. We do not use derivative financial instruments to manage our interest rate risk. We are adverse to principal loss and ensure the safety and preservation of invested funds by limiting default, market risk and reinvestment risk. Our investment portfolio is generally comprised of investments that meet high credit quality standards and have active secondary and resale markets. Since these securities are subject to interest rate risk, they could decline in value if interest rates fluctuate or if the liquidity of the investment portfolio were to change. Due to the short duration and conservative nature of our investment portfolio, we do not anticipate any material loss with respect to our investment portfolio. A 10% move in interest rates as of the end of the second quarter of 2015 would have had an immaterial effect on our financial position, results of operations and cash flows.

Foreign Currency Exchange Rate Risk

All of our sales and costs of manufacturing are transacted in U.S. dollars. We conduct a portion of our research and development activities in Canada and India and have sales and marketing offices in several locations outside of the United States. We use the U.S. dollar as our functional currency. Most of the costs incurred at these international locations are in local currency. If these local currencies strengthen against the U.S. dollar, our payroll and other local expenses will be higher than we currently anticipate. Since our sales are transacted in U.S. dollars, this negative impact on expenses would not be offset by any positive effect on revenue. Operating expenses denominated in foreign currencies were approximately 16% and 19% of total operating expenses for the first six months of 2015 and 2014, respectively. A currency exchange rate fluctuation of 10% would have caused our operating expenses to change by approximately \$206,000 in the first six months of 2015.

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Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on management's evaluation as of June 28, 2015, our Chief Executive Officer and Principal Accounting Officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) were effective at the reasonable assurance level to ensure that the information required to be disclosed by us in this Quarterly Report on Form 10-Q was (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and regulations and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Principal Accounting Officer, to allow timely decisions regarding required disclosure.

Our management, including our Chief Executive Officer and Principal Accounting Officer, does not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all errors and frauds. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II. Other Information

Item 1. Legal Proceedings

See Note 13 of the Condensed Unaudited Consolidated Financial Statements for a description of legal proceedings.

Item 1A. Risk Factors

Our 2014 Annual Report on Form 10-K for the year ended December 28, 2014, filed with the SEC on March 5, 2015, includes a detailed discussion of our risk factors at Part I, Item 1A, Risk Factors, which discussion is hereby incorporated by reference into this Part II, Item 1A. Any information presented below updates and supplements, and should be read in conjunction with, the risk factors and information disclosed in that Form 10-K and in conjunction with any subsequent updates disclosed in our quarterly filings on Form 10-Q.

The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks not currently known to us or that we currently deem to be immaterial may also adversely affect our business and results from operations.

Item 4. Mine Safety Disclosures

Not applicable.

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Item 6. Exhibits

a. Exhibits

The following Exhibits are filed with this report:

Exhibit Number	Description
31.1	CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	PAO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	CEO and PAO Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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Signatures

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

Date: August 5, 2015

QUICKLOGIC  
CORPORATION

/s/ Suping (Sue) Cheung  
Suping (Sue) Cheung  
Principal Accounting Officer  
and Corporate Controller  
(as Principal Accounting and  
Financial Officer and on behalf  
of the Registrant)

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EXHIBIT INDEX

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