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

FORM 10-Q

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

For the quarterly period ended September 30, 2014

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 001-33387

GSI Technology, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

77-0398779

(IRS Employer Identification No.)

1213 Elko Drive

Sunnyvale, California 94089

(Address of principal executive offices, zip code)

(408) 331-8800

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

The number of shares of the registrant's common stock outstanding as of October 31, 2014: 23,736,079

GSI TECHNOLOGY, INC.

FORM 10-Q FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2014

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PART I — FINANCIAL INFORMATION**Item 1. Financial Statements****GSI TECHNOLOGY, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

	September 30, 2014	March 31, 2014
	(In thousands, except share and per share amounts)	
ASSETS		
Cash and cash equivalents	\$ 34,760	\$ 41,520
Short-term investments	27,971	39,412
Accounts receivable, net	7,830	8,238
Inventories	9,240	8,185
Prepaid expenses and other current assets	5,471	5,152
Total current assets	85,272	102,507
Property and equipment, net	9,006	9,683
Long-term investments	19,011	28,819
Other assets	594	668
Total assets	<u>\$ 113,883</u>	<u>\$ 141,677</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable	\$ 3,724	\$ 4,870
Accrued expenses and other liabilities	4,244	4,444
Deferred revenue	3,100	2,523
Total current liabilities	11,068	11,837
Income taxes payable	1,492	1,462
Total liabilities	12,560	13,299
Commitments and contingencies (Note 6)		
Stockholders' equity:		
Preferred stock: \$0.001 par value authorized: 5,000,000 shares; issued and outstanding: none	—	—
Common Stock: \$0.001 par value authorized: 150,000,000 shares; issued and outstanding: 23,736,079 and 27,561,482 shares, respectively	24	28
Additional paid-in capital	31,780	56,399
Accumulated other comprehensive income (loss)	(3)	33
Retained earnings	69,522	71,918
Total stockholders' equity	101,323	128,378
Total liabilities and stockholders' equity	<u>\$ 113,883</u>	<u>\$ 141,677</u>

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

GSI TECHNOLOGY, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	<u>Three Months Ended September 30,</u>		<u>Six Months Ended September 30,</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
	(In thousands, except per share amounts)			
Net revenues	\$ 13,263	\$ 15,542	\$ 26,208	\$ 31,954
Cost of revenues	7,202	8,140	14,208	17,086
Gross profit	6,061	7,402	12,000	14,868
Operating expenses:				
Research and development	2,946	2,951	6,019	5,948
Selling, general and administrative	4,156	4,210	8,491	9,220
Total operating expenses	7,102	7,161	14,510	15,168
Income (loss) from operations	(1,041)	241	(2,510)	(300)
Interest income, net	78	95	174	199
Other income (expense), net	34	(10)	9	(3)
Income (loss) before income taxes	(929)	326	(2,327)	(104)
Provision (benefit) for income taxes	21	(60)	69	(49)
Net income (loss)	<u>\$ (950)</u>	<u>\$ 386</u>	<u>\$ (2,396)</u>	<u>\$ (55)</u>
Net income (loss) per share:				
Basic	<u>\$ (0.04)</u>	<u>\$ 0.01</u>	<u>\$ (0.09)</u>	<u>\$ —</u>
Diluted	<u>\$ (0.04)</u>	<u>\$ 0.01</u>	<u>\$ (0.09)</u>	<u>\$ —</u>
Weighted average shares used in per share calculations:				
Basic	25,540	27,631	26,512	27,407
Diluted	25,540	28,975	26,512	27,407

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

GSI TECHNOLOGY, INC.**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)****(Unaudited)**

	<u>Three Months Ended September 30,</u>		<u>Six Months Ended September 30,</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
	(In thousands)			
Net income (loss)	\$ (950)	\$ 386	\$ (2,396)	\$ (55)
Net unrealized gain (loss) on available-for-sale investments, net of tax	(40)	46	(36)	(39)
Total comprehensive income (loss)	<u>\$ (990)</u>	<u>\$ 432</u>	<u>\$ (2,432)</u>	<u>\$ (94)</u>

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

GSI TECHNOLOGY, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	<u>Six Months Ended September 30,</u>	
	<u>2014</u>	<u>2013</u>
	(In thousands)	
Cash flows from operating activities:		
Net loss	\$ (2,396)	\$ (55)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Allowance for sales returns, doubtful accounts and other	(5)	(14)
Provision for excess and obsolete inventories	622	526
Depreciation and amortization	931	998
Stock-based compensation	1,144	1,128
Deferred income taxes	—	102
Windfall tax benefits from stock options exercised	—	(403)
Amortization of bond premium on investments	340	439
Changes in assets and liabilities:		
Accounts receivable	413	445
Inventory	(1,677)	2,097
Prepaid expenses and other assets	(334)	(36)
Accounts payable	(1,146)	(63)
Accrued expenses and other liabilities	(175)	297
Deferred revenue	577	(449)
Net cash provided by (used in) operating activities	<u>(1,706)</u>	<u>5,012</u>
Cash flows from investing activities:		
Purchase of investments	(4,000)	(19,708)
Sales and maturities of short-term investments	24,873	20,111
Purchases of property and equipment	(160)	(138)
Net cash provided by investing activities	<u>20,713</u>	<u>265</u>
Cash flows from financing activities:		
Repurchase of common stock	(26,430)	—
Windfall tax benefits from stock options exercised	—	403
Proceeds from issuance of common stock under employee stock plans	663	2,021
Net cash provided by (used in) financing activities	<u>(25,767)</u>	<u>2,424</u>
Net increase (decrease) in cash and cash equivalents	(6,760)	7,701
Cash and cash equivalents at beginning of the period	41,520	41,120
Cash and cash equivalents at end of the period	<u>\$ 34,760</u>	<u>\$ 48,821</u>
Non-cash financing activities:		
Purchases of property and equipment through accounts payable and accruals	\$ 5	\$ —
Supplemental cash flow information:		
Net cash paid for income taxes	\$ 52	\$ 10

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

GSI TECHNOLOGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1—THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying unaudited condensed consolidated financial statements of GSI Technology, Inc. and its subsidiaries (“GSI” or the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission. Accordingly, the interim financial statements do not include all of the information and footnotes required by GAAP for annual financial statements. These interim financial statements contain all adjustments (which consist of only normal, recurring adjustments) that are, in the opinion of management, necessary to state fairly the interim financial information included therein. The Company believes that the disclosures are adequate to make the information not misleading. However, these financial statements should be read in conjunction with the audited consolidated financial statements and related notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

The consolidated results of operations for the three months and six months ended September 30, 2014 are not necessarily indicative of the results to be expected for the entire fiscal year.

Significant accounting policies

The Company’s significant accounting policies are disclosed in the Company’s Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

Litigation and settlement costs

From time to time, the Company is involved in legal actions. The Company currently is a party to pending legal proceedings which it is defending aggressively. See Note 6 for additional information regarding this pending litigation. There are many uncertainties associated with any litigation, and the Company may not prevail. The litigation, regardless of its eventual outcome, will be costly and time consuming and, should the outcome be adverse to the Company, could result in the Company being required to pay significant monetary damages. If that occurs, our business, financial condition and results of operations could be materially and adversely affected. If information becomes available that causes us to determine that a loss in any of our pending litigation, or the settlement of such litigation, is probable, and we can reasonably estimate the loss associated with such events, we will record the loss in accordance with GAAP. However, the actual liability in any such litigation may be materially different from our estimates, which could require us to record additional costs.

Recent accounting pronouncements

In July 2013, the Financial Accounting Standards Board (“FASB”) issued an Accounting Standards Update (“ASU”) on Income Taxes, to improve the presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance is expected to reduce diversity in practice and is expected to better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. Implementation of this guidance in the quarter ended June 30, 2014 did not have a material impact on the Company’s financial position or results of operations.

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In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." The new accounting standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The accounting standard is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016. Early adoption is not permitted. The Company is currently evaluating the impact of this accounting standard on its consolidated financial statements.

NOTE 2—NET INCOME (LOSS) PER COMMON SHARE

The Company uses the treasury stock method to calculate the weighted average shares used in computing diluted net income (loss) per share. The following table sets forth the computation of basic and diluted net income (loss) per share:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
	(In thousands, except per share amounts)			
Net income (loss)	\$ (950)	\$ 386	\$ (2,396)	\$ (55)
Denominators:				
Weighted average shares—Basic	25,540	27,631	26,512	27,407
Dilutive effect of employee stock options	—	1,331	—	—
Dilutive effect of employee stock purchase plan options	—	13	—	—
Weighted average shares—Dilutive	25,540	28,975	26,512	27,407
Net income (loss) per common share—Basic	\$ (0.04)	\$ 0.01	\$ (0.09)	\$ —
Net income (loss) per common share—Diluted	\$ (0.04)	\$ 0.01	\$ (0.09)	\$ —

The following shares of common stock underlying outstanding stock options, determined on a weighted average basis, were excluded from the computation of diluted net income (loss) per share as they had an anti-dilutive effect:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
	(In thousands)			
Shares underlying options	3,503	1,558	3,375	2,964

NOTE 3—BALANCE SHEET DETAIL

	September 30, 2014		March 31, 2014	
	(In thousands)			
Inventories:				
Work-in-progress	\$	2,852	\$	2,011
Finished goods		5,785		5,588
Inventory at distributors		603		586
	\$	9,240	\$	8,185

	September 30, 2014	March 31, 2014
	(In thousands)	
Accounts receivable, net:		
Accounts receivable	\$ 7,936	\$ 8,349
Less: Allowances for sales returns, doubtful accounts and other	(106)	(111)
	<u>\$ 7,830</u>	<u>\$ 8,238</u>

	September 30, 2014	March 31, 2014
	(In thousands)	
Prepaid expenses and other current assets:		
Prepaid tooling and masks	\$ 1,362	\$ 833
Prepaid income taxes	2,601	2,598
Other receivables	484	596
Other prepaid expenses	1,024	1,125
	<u>\$ 5,471</u>	<u>\$ 5,152</u>

	September 30, 2014	March 31, 2014
	(In thousands)	
Property and equipment, net:		
Computer and other equipment	\$ 16,942	\$ 16,990
Software	4,792	4,780
Land	3,900	3,900
Building and building improvements	2,256	2,256
Furniture and fixtures	110	110
Leasehold improvements	791	791
	<u>28,791</u>	<u>28,827</u>
Less: Accumulated depreciation and amortization	(19,785)	(19,144)
	<u>\$ 9,006</u>	<u>\$ 9,683</u>

Depreciation and amortization expense was \$377,000 and \$459,000, respectively, for the three months ended September 30, 2014 and 2013 and \$842,000 and \$908,000, respectively, for the six months ended September 30, 2014 and 2013.

	September 30, 2014	March 31, 2014
	(In thousands)	
Other assets:		
Non-current deferred income taxes	\$ 39	\$ 24
Intangibles, net	475	564
Deposits	80	80
	<u>\$ 594</u>	<u>\$ 668</u>

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The following table summarizes the components of intangible assets and related accumulated amortization balances at September 30, 2014 (in thousands):

	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
Intangible assets:			
Product designs	\$ 590	\$ 428	\$ 162
Patents	720	407	313
Software	80	80	—
Total	<u>\$ 1,390</u>	<u>\$ 915</u>	<u>\$ 475</u>

Amortization of intangible assets included in cost of revenues was \$44,000 and \$45,000, respectively, for the three months ended September 30, 2014 and 2013 and \$89,000 and \$90,000, respectively, for the six months ended September 30, 2014 and 2013.

	<u>September 30, 2014</u>	<u>March 31, 2014</u>
	(In thousands)	
Accrued expenses and other liabilities:		
Accrued compensation	\$ 2,134	\$ 2,330
Accrued professional fees	699	824
Accrued commissions	322	307
Other accrued expenses	1,089	983
	<u>\$ 4,244</u>	<u>\$ 4,444</u>

NOTE 4—INCOME TAXES

The current portion of the Company's unrecognized tax benefits was \$0 at both September 30, 2014 and March 31, 2014. The long-term portion at September 30, 2014 and March 31, 2014 was \$1,492,000 and \$1,462,000, respectively, of which the timing of the resolution is uncertain. As of September 30, 2014, \$1,122,000 of unrecognized tax benefits had been recorded as a reduction to net deferred tax assets. As of September 30, 2014 and March 31, 2014, the Company's net deferred tax assets of \$4.5 million and \$3.7 million, respectively, were subject to a full valuation allowance.

Management believes that it is reasonably possible that within the next twelve months the Company could have a reduction in uncertain tax benefits of up to \$775,000, including interest and penalties, related to positions taken with respect to credits and loss carryforwards on previously filed tax returns.

The Company's policy is to include interest and penalties related to unrecognized tax benefits within the provision for income taxes in the Condensed Consolidated Statements of Operations.

The Company is subject to taxation in the United States and various state and foreign jurisdictions. Fiscal years 2011 through 2014 remain open to examination by federal tax authorities, and fiscal years 2010 through 2014 remain open to examination by California tax authorities.

The Company's estimated annual effective income tax rate was approximately 4.5% and (3.6)% as of September 30, 2014 and 2013, respectively. The annual effective tax rate as of September 30, 2014 varies from the United States statutory income tax rate primarily due to valuation allowances in the United States whereby pre-tax losses do not result in the recognition of corresponding income tax benefits and expenses. The difference between the effective income tax rate and the applicable United States statutory income tax rate as of September 30, 2013 was primarily due to the effects of tax credits, foreign tax rate differentials and tax free interest income, offset by stock-based compensation expense.

NOTE 5—FINANCIAL INSTRUMENTS

Fair value measurements

The authoritative accounting guidance for fair value measurements provides a framework for measuring fair value and related disclosures. The guidance applies to all financial assets and financial liabilities that are measured on a recurring basis. The guidance requires fair value measurement to be classified and disclosed in one of the following three categories:

Level 1: Valuations based on quoted prices in active markets for identical assets and liabilities. The fair value of available-for-sale securities included in the Level 1 category is based on quoted prices that are readily and regularly available in an active market. As of September 30, 2014, the Level 1 category included money market funds of \$1.1 million, which were included in cash and cash equivalents in the Condensed Consolidated Balance Sheet.

Level 2: Valuations based on observable inputs (other than Level 1 prices), such as quoted prices for similar assets at the measurement date; quoted prices in markets that are not active; or other inputs that are observable, either directly or indirectly. The fair value of available-for-sale securities included in the Level 2 category is based on the market values obtained from an independent pricing service that were evaluated using pricing models that vary by asset class and may incorporate available trade, bid and other market information and price quotes from well established independent pricing vendors and broker-dealers. As of September 30, 2014, the Level 2 category included short-term investments of \$28.0 million and long-term investments of \$19.0 million, which were comprised of certificates of deposit, corporate debt securities and government and agency securities.

Level 3: Valuations based on inputs that are unobservable and involve management judgment and the reporting entity's own assumptions about market participants and pricing. As of September 30, 2014, the Company had no Level 3 financial assets measured at fair value in the Condensed Consolidated Balance Sheet.

As of September 30, 2014, there were no liabilities measured at fair value on a recurring basis.

The fair value of financial assets measured on a recurring basis is as follows (in thousands):

	Fair Value Measurements at Reporting Date Using			
		Quoted Prices in Active Markets for Identical Assets and Liabilities	Significant Other Observable Inputs	Significant Unobservable Inputs
	September 30, 2014	(Level 1)	(Level 2)	(Level 3)
Assets:				
Money market funds	\$ 1,135	\$ 1,135	\$ —	\$ —
Marketable securities	46,982	—	46,982	—
Total	\$ 48,117	\$ 1,135	\$ 46,982	\$ —

	Fair Value Measurements at Reporting Date Using			
		Quoted Prices in Active Markets for Identical Assets and Liabilities	Significant Other Observable Inputs	Significant Unobservable Inputs
	March 31, 2014	(Level 1)	(Level 2)	(Level 3)
Assets:				
Money market funds	\$ 3,852	\$ 3,852	\$ —	\$ —
Marketable securities	68,231	—	68,231	—
Total	\$ 72,083	\$ 3,852	\$ 68,231	\$ —

Short-term and long-term investments

All of the Company's short-term and long-term investments are classified as available-for-sale. Available-for-sale debt securities with maturities greater than twelve months are classified as long-term investments when they are not intended for use in current operations. Investments in available-for-sale securities are reported at fair value with unrecognized gains (losses), net of tax, as a component of accumulated other comprehensive income in the Condensed Consolidated Balance Sheets. The Company had money market funds of \$1.1 million and \$3.9 million at September 30, 2014 and March 31, 2014, respectively, included in cash and cash equivalents in the Condensed Consolidated Balance Sheet. The Company monitors its investments for impairment periodically and records appropriate reductions in carrying values when declines are determined to be other-than-temporary.

The following table summarizes the Company's available-for-sale investments:

	September 30, 2014			
	Cost	Gross	Gross	Fair Value
		Unrealized Gains	Unrealized Losses	
(In thousands)				
Short-term investments:				
State and municipal obligations	\$ 11,581	\$ 4	\$ —	\$ 11,585
Corporate notes	7,366	12	—	7,378
Agency bonds	1,001	1	—	1,002
Certificates of deposit	8,000	6	—	8,006
Total short-term investments	\$ 27,948	\$ 23	\$ —	\$ 27,971
Long-term investments:				
State and municipal obligations	\$ 1,074	\$ 5	\$ —	\$ 1,079
Corporate notes	3,017	9	—	3,026
Certificates of deposit	10,250	—	(12)	10,238
Agency bonds	3,008	—	(9)	2,999
International government obligations	1,676	—	(7)	1,669
Total long-term investments	\$ 19,025	\$ 14	\$ (28)	\$ 19,011

	March 31, 2014			
	Cost	Gross	Gross	Fair Value
		Unrealized Gains	Unrealized Losses	
(In thousands)				
Short-term investments:				
State and municipal obligations	\$ 8,336	\$ 4	\$ —	\$ 8,340
Corporate notes	5,023	12	—	5,035
Agency bonds	3,523	2	—	3,525
Certificates of deposit	14,997	6	—	15,003
International government obligations	7,507	2	—	7,509
Total short-term investments	\$ 39,386	\$ 26	\$ —	\$ 39,412
Long-term investments:				
State and municipal obligations	\$ 8,227	\$ 10	\$ —	\$ 8,237
Corporate notes	6,392	16	—	6,408
Certificates of deposit	10,500	—	(2)	10,498
Agency bonds	2,011	—	(5)	2,006
International government obligations	1,670	—	—	1,670
Total long-term investments	\$ 28,800	\$ 26	\$ (7)	\$ 28,819

The Company's investment portfolio consists of both corporate and governmental securities that have a maximum maturity of three years. All unrealized gains are due to changes in interest rates and bond yields. Subject to normal credit risks, the Company has the ability to realize the full value of all these investments upon maturity.

The deferred tax liability related to unrecognized gains and losses on short-term and long-term investments was \$0 and \$11,000 at September 30, 2014 and March 31, 2014, respectively.

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As of September 30, 2014, contractual maturities of the Company’s available-for-sale non-equity investments were as follows:

	Cost	Fair Value
	(In thousands)	
Maturing within one year	\$ 27,948	\$ 27,971
Maturing in one to three years	19,025	19,011
Maturing in more than three years	—	—
	<u>\$ 46,973</u>	<u>\$ 46,982</u>

The Company classifies its short-term investments as “available-for-sale” as they are intended to be available for use in current operations.

NOTE 6—COMMITMENTS AND CONTINGENCIES

Indemnification obligations

The Company is a party to a variety of agreements pursuant to which it may be obligated to indemnify the other party with respect to certain matters. Typically, these obligations arise in the context of contracts entered into by the Company, under which the Company agrees to hold the other party harmless against losses arising from a breach of representations and covenants related to such matters as title to assets sold and certain intellectual property rights. In each of these circumstances, the Company’s indemnification obligations are conditioned on the other party making a claim pursuant to the procedures specified in the particular contract, which procedures typically allow the Company to challenge the other party’s claims. Further, the Company’s obligations under these agreements may be limited in terms of time and/or amount, and in some instances, the Company may have recourse against third parties for certain payments made by it under these agreements.

It is not possible to predict the maximum potential amount of future payments that may be required under these or similar agreements due to the conditional nature of the Company’s obligations and the unique facts and circumstances involved in each particular agreement. Historically, payments made by the Company under these agreements have not had a material effect on its business, financial condition, cash flows or results of operations.

Product warranties

The Company warrants its products to be free of defects generally for a period of three years. The Company estimates its warranty costs based on historical warranty claim experience and includes such costs in cost of revenues. Warranty costs were not significant for the three months or six months ended September 30, 2014 or 2013.

Legal proceedings

In March 2011, Cypress Semiconductor Corporation, a semiconductor manufacturer, filed a lawsuit against the Company in the United States District Court for the District of Minnesota alleging that the Company’s products, including its SigmaDDR and SigmaQuad families of Very Fast SRAMs, infringe five patents held by Cypress. The complaint seeks unspecified damages for past infringement and a permanent injunction against future infringement.

On June 10, 2011, Cypress filed a complaint against the Company with the United States International Trade Commission (the “ITC”). The ITC complaint, as subsequently amended, alleged infringement by the Company of three of the five patents involved in the District Court case and one additional patent and also alleged infringement by three of our distributors and 11 of our customers who allegedly incorporate the Company’s SRAMs in their products. The ITC complaint sought a limited exclusion order excluding the allegedly infringing SRAMs, and products containing them, from entry into the United States and permanent orders directing the Company and the other respondents to cease and desist from selling or distributing such products in the United States. On July 21,

2011, the ITC formally instituted an investigation in response to Cypress’s complaint. On June 7, 2013, the ITC announced that the full Commission had affirmed the determination of Chief Administrative Judge Charles E. Bullock that GSI’s SRAM devices, and products containing them, do not infringe the Cypress patents and that Cypress had failed to establish existence of a domestic industry that practices the patents. Moreover, the Commission reversed a portion of Judge Bullock’s determination with respect to the validity of the patents, finding the asserted claims of one of the patents to have been anticipated by prior art and, therefore, invalid. The Commission ordered the investigation terminated, and Cypress did not appeal the ruling.

The Minnesota District Court case had been stayed pending the conclusion of the ITC proceeding. Following the termination of the ITC investigation, the stay was lifted. On May 1, 2013, Cypress filed an additional lawsuit in the United States District Court for the Northern District of California alleging infringement by our products of five additional Cypress patents. Like the Minnesota case, the complaint in the California lawsuit seeks unspecified damages for past infringement and a permanent injunction against future infringement. The Company filed answers in both cases denying liability and asserting affirmative defenses. On August 7, 2013, the parties stipulated that the claims in the Minnesota case with respect to three of the asserted patents would be dismissed without prejudice and that the claims with respect to the remaining two patents would be transferred to, and consolidated with, the California case. On August 20, 2013, the Court in the California case ordered the cases consolidated. Discovery in the case is proceeding.

The Company believes that it has strong defenses against Cypress’ patent infringement claims and intends to continue to defend itself vigorously. However, the litigation process is inherently uncertain, and the Company may not prevail. Patent litigation is particularly complex and can extend for a protracted period of time, which can substantially increase the cost of such litigation. The Company has not recorded any loss contingency during fiscal 2012, fiscal 2013, fiscal 2014 or fiscal 2015 in connection with these legal proceedings as the Company cannot predict their outcome and cannot estimate the likelihood or potential dollar amount of any adverse results. However, an unfavorable outcome in these proceedings could have a material adverse impact on the Company’s financial position, results of operations or cash flows for the period in which the outcome occurs and in future periods.

NOTE 7—STOCK-BASED COMPENSATION

As of September 30, 2014, 6,396,356 shares of common stock were available for grant under the Company’s 2007 Equity Incentive Plan.

The following table summarizes the Company’s stock option activities for the six months ended September 30, 2014:

	Shares Available for Grant	Number of Shares Underlying Options Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Intrinsic Value
Balance at March 31, 2014	5,585,500	6,143,980		5.13	
Options reserved	1,377,699	—		—	
Granted	(575,043)	575,043		5.29	
Exercised	—	(105,725)		4.04	\$ 224,178
Forfeited	8,200	(8,200)		5.97	
Balance at September 30, 2014	<u>6,396,356</u>	<u>6,605,098</u>		\$ 5.16	
Options vested and exercisable		<u>4,188,255</u>	4.45	\$ 4.83	<u>\$ 3,742,830</u>
Options vested and expected to vest		<u>6,556,577</u>	5.87	\$ 5.16	<u>\$ 4,300,040</u>

The weighted average fair value per underlying share of options granted during the three months ended September 30, 2014 and 2013 was \$2.14 and \$2.93, respectively, and for the six months ended September 30, 2014 and 2013 was \$2.16 and \$2.72, respectively.

Options outstanding by exercise price at September 30, 2014 were as follows:

Exercise Price	Number of Shares Underlying Options Outstanding	Options Outstanding		Options Exercisable	
		Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Number Vested and Exercisable	Weighted Average Exercise Price
\$ 2.43 - 3.43	917,384	\$ 3.16	4.35	917,384	\$ 3.16
\$ 3.75 - 4.00	812,779	\$ 3.96	4.46	812,779	\$ 3.96
\$ 4.17 - 4.81	812,205	\$ 4.39	5.85	419,494	\$ 4.39
\$ 4.90 - 5.23	789,563	\$ 5.11	8.84	132,396	\$ 4.90
\$ 5.41	30,000	\$ 5.41	9.88	—	\$ —
\$ 5.50	783,433	\$ 5.50	2.13	783,433	\$ 5.50
\$ 5.59 - 5.76	675,410	\$ 5.70	7.02	259,146	\$ 5.69
\$ 6.00 - 6.54	798,358	\$ 6.32	6.66	384,692	\$ 6.19
\$ 6.61 - 6.86	666,153	\$ 6.77	8.39	210,023	\$ 6.78
\$ 7.00 - 9.20	319,813	\$ 7.78	6.02	268,908	\$ 7.51
	<u>6,605,098</u>	\$ 5.16	5.89	<u>4,188,255</u>	4.83

The following table summarizes stock-based compensation expense by line item in the Condensed Consolidated Statements of Operations, all relating to employee stock plans:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
	(In thousands)			
Cost of revenues	\$ 104	\$ 102	\$ 204	\$ 196
Research and development	248	232	489	490
Selling, general and administrative	219	229	451	442
Total	\$ 571	\$ 563	\$ 1,144	\$ 1,128

As stock-based compensation expense recognized in the Condensed Consolidated Statement of Operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures in accordance with authoritative guidance. The Company estimates forfeitures at the time of grant and revises the original estimates, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

The Company recognized related income tax benefits of \$0 and \$29,000, respectively, for the three months ended September 30, 2014 and 2013, and \$0 and \$46,000, respectively, for the six months ended September 30, 2014, and 2013. Windfall tax benefits realized from exercised stock options were \$0, and \$226,000, respectively, for the three months ended September 30, 2014 and 2013 and \$0 and \$403,000, respectively for the six months ended September 30, 2014 and 2013. Compensation cost capitalized within inventory at September 30, 2014 was insignificant. As of September 30, 2014, the Company's total unrecognized compensation cost was \$3.9 million, which will be recognized over a weighted average period of 2.14 years. The Company calculated the fair value of stock-based awards in the periods presented using the Black-Scholes option pricing model and the following weighted average assumptions:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
	(In thousands)		(In thousands)	
Stock Option Plans:				
Risk-free interest rate	1.70 %	1.51 %	1.66 - 1.70 %	0.91 - 1.51 %
Expected life (in years)	5.00	5.00	5.00	5.00
Volatility	44.8 %	47.6 %	44.5 - 44.8 %	47.6 - 48.4 %
Dividend yield	— %	— %	— %	— %
Employee Stock Purchase Plan:				
Risk-free interest rate	— %	— %	0.05 %	0.09 %
Expected life (in years)	—	—	0.50	0.50
Volatility	%	— %	30.8 %	30.4 %
Dividend yield	— %	— %	-%	— %

NOTE 8—SEGMENT AND GEOGRAPHIC INFORMATION

Based on its operating management and financial reporting structure, the Company has determined that it has one reportable business segment: the design, development and sale of integrated circuits.

The following is a summary of net revenues by geographic area based on the location to which product is shipped:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
	(In thousands)			
United States	\$ 4,777	\$ 4,414	\$ 8,394	\$ 10,385
China	3,708	2,794	7,239	6,271
Malaysia	1,098	3,208	2,700	5,555
Singapore	1,833	1,613	3,500	3,065
Netherlands	456	1,879	1,471	3,412
Rest of the world	1,391	1,634	2,904	3,266
	<u>\$ 13,263</u>	<u>\$ 15,542</u>	<u>\$ 26,208</u>	<u>\$ 31,954</u>

All sales are denominated in United States dollars.

NOTE 9—MODIFIED DUTCH AUCTION TENDER OFFER

On July 9, 2014 the Company announced that it had commenced a modified “Dutch auction” self-tender offer to repurchase for cash shares of its common stock for an aggregate purchase price of up to \$25 million. Under the terms of the tender offer, the Company’s stockholders had the opportunity to tender some or all of their shares at a price within the range of \$6.50 to \$6.70 per share.

The tender offer expired on August 6, 2014. The Company accepted for purchase an aggregate of 3,846,153 shares of its common stock at a final purchase price of \$6.50 per share, for an aggregate cost of approximately \$25 million, excluding fees and expenses related to the tender offer. A total of 10,466,830 shares were properly tendered and not properly withdrawn at a price of \$6.50 per share. Since the offer was oversubscribed, the number of shares that the Company accepted for purchase from tendering stockholders was prorated, based upon

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the proration procedures described in the offer to purchase (other than shares tendered by “odd lot” holders, which were not subject to proration and were accepted in full).

The aggregate number of shares purchased by the Company in the tender offer represented approximately 14.0 percent of its issued and outstanding shares of common stock as of August 8, 2014. Following settlement of the tender offer, the Company had approximately 23.7 million shares of its common stock outstanding.

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

This Quarterly Report on Form 10-Q, and in particular the following Management’s Discussion and Analysis of Financial Condition and Results of Operations, includes “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 (the “Exchange Act”). These forward-looking statements involve risks and uncertainties. Forward-looking statements are identified by words such as “anticipates,” “believes,” “expects,” “intends,” “may,” “will,” and other similar expressions. In addition, any statements which refer to expectations, projections, or other characterizations of future events, or circumstances, are forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of a number of factors, including those set forth in this report under “Risk Factors,” those described elsewhere in this report, and those described in our other reports filed with the Securities and Exchange Commission (“SEC”). We caution you not to place undue reliance on these forward-looking statements, which speak only as of the date of this report, and we undertake no obligation to update these forward-looking statements after the filing of this report. You are urged to review carefully and consider our various disclosures in this report and in our other reports publicly disclosed or filed with the SEC that attempt to advise you of the risks and factors that may affect our business.

Overview

We are a fabless semiconductor company that designs, develops and markets static random access memories, or SRAMs, that operate at speeds of less than 10 nanoseconds, which we refer to as Very Fast SRAMs, and low latency dynamic random access memories, or LLDRAMs, primarily for the networking and telecommunications markets. We are subject to the highly cyclical nature of the semiconductor industry, which has experienced significant fluctuations, often in connection with fluctuations in demand for the products in which semiconductor devices are used. Our revenues have been substantially impacted by significant fluctuations in sales to Cisco Systems, historically our largest customer, and we expect that future direct and indirect sales to Cisco Systems will continue to fluctuate significantly on a quarterly basis. The worldwide financial crisis and the resulting economic impact on the end markets we serve have adversely impacted our financial results since the second half of fiscal 2009, and we expect that the unsettled global economic environment will continue to affect our operating results in future periods. However, with no debt, substantial liquidity and a history of positive cash flows from operations, we believe we are in a better financial position than many other companies of our size.

Revenues. Our revenues are derived primarily from sales of our Very Fast SRAM products. Sales to networking and telecommunications original equipment manufacturers, or OEMs, accounted for 73% to 79% of our net revenues during our last three fiscal years. We also sell our products to OEMs that manufacture products for defense applications such as radar and guidance systems, for professional audio applications such as sound mixing systems, for test and measurement applications such as high-speed testers, for automotive applications such as smart cruise control and voice recognition systems, and for medical applications such as ultrasound and CAT scan equipment.

As is typical in the semiconductor industry, the selling prices of our products generally decline over the life of the product. Our ability to increase net revenues, therefore, is dependent upon our ability to increase unit sales volumes of existing products and to introduce and sell new products with higher average selling prices in quantities sufficient to compensate for the anticipated declines in selling prices of our more mature products. Although we expect the average selling prices of individual products to decline over time, we believe that, over the next several quarters, our overall average selling prices will increase due to a continuing shift in product mix to a higher percentage of higher price, higher density products. Our ability to increase unit sales volumes is dependent primarily upon increases in customer demand but, particularly in periods of increasing demand, can also be affected by our ability to increase production through the availability of increased wafer fabrication capacity from Taiwan Semiconductor Manufacturing Company, or TSMC, and Powerchip, our wafer suppliers, and our ability to increase the number of good integrated circuit die produced from each wafer through die size reductions and yield enhancement activities.

We may experience fluctuations in quarterly net revenues for a number of reasons. Historically, orders on hand at the beginning of each quarter are insufficient to meet our revenue objectives for that quarter and are generally cancelable up to 30 days prior to scheduled delivery. Accordingly, we depend on obtaining and shipping

orders in the same quarter to achieve our revenue objectives. In addition, the timing of product releases, purchase orders and product availability could result in significant product shipments at the end of a quarter. Failure to ship these products by the end of the quarter may adversely affect our operating results. Furthermore, our customers may delay scheduled delivery dates and/or cancel orders within specified timeframes without significant penalty.

We sell our products through our direct sales force, international and domestic sales representatives and distributors. Revenues from product sales, except for sales to distributors, are generally recognized upon shipment, net of sales returns and allowances. Sales to consignment warehouses, who purchase products from us for use by contract manufacturers, are recorded upon delivery to the contract manufacturer. Sales to distributors are recorded as deferred revenues for financial reporting purposes and recognized as revenues when the products are resold by the distributors to the OEM. Sales to distributors are made under agreements allowing for returns or credits under certain circumstances. We therefore defer recognition of revenue on sales to distributors until products are resold by the distributor.

Cisco Systems, historically our largest OEM customer, purchases our products primarily through its consignment warehouse, SMART Modular Technologies, and also purchases some products through its contract manufacturers and directly from us. Historically, purchases by Cisco Systems have fluctuated from period to period. Based on information provided to us by Cisco Systems' consignment warehouses and contract manufacturers, purchases by Cisco Systems represented approximately 14%, 19%, 29% and 41% of our net revenues in the six months ended September 30, 2014 and in fiscal 2014, 2013 and 2012, respectively. Alcatel-Lucent was our largest customer in fiscal 2014. Alcatel-Lucent purchases products directly from us and through contract manufacturers and distributors. Purchases by Alcatel-Lucent represented approximately 24%, 19%, 12% and 9% of our net revenues in the six months ended September 30, 2014 and in fiscal 2014, 2013 and 2012, respectively. Our revenues have been substantially impacted by significant fluctuations in sales to Cisco Systems and Alcatel-Lucent, and we expect that future direct and indirect sales to these two customers will continue to fluctuate substantially on a quarterly basis and that such fluctuations may significantly affect our operating results in future periods. To our knowledge, none of our other OEM customers accounted for more than 10% of our net revenues in fiscal 2014, 2013 or 2012.

Cost of Revenues. Our cost of revenues consists primarily of wafer fabrication costs, wafer sort, assembly, test and burn-in expenses, the amortized cost of production mask sets, stock-based compensation and the cost of materials and overhead from operations. All of our wafer manufacturing and assembly operations, and a significant portion of our wafer sort testing operations, are outsourced. Accordingly, most of our cost of revenues consists of payments to TSMC, Powerchip and independent assembly and test houses. Because we do not have long-term, fixed-price supply contracts, our wafer fabrication and other outsourced manufacturing costs are subject to the cyclical fluctuations in demand for semiconductors. Cost of revenues also includes expenses related to supply chain management, quality assurance, and final product testing and documentation control activities conducted at our headquarters in Sunnyvale, California and our branch operations in Taiwan.

Gross Profit. Our gross profit margins vary among our products and are generally greater on our higher density products and, within a particular density, greater on our higher speed and industrial temperature products. We expect that our overall gross margins will fluctuate from period to period as a result of shifts in product mix, changes in average selling prices and our ability to control our cost of revenues, including costs associated with outsourced wafer fabrication and product assembly and testing.

Research and Development Expenses. Research and development expenses consist primarily of salaries and related expenses for design engineers and other technical personnel, the cost of developing prototypes, stock-based compensation and fees paid to consultants. We charge all research and development expenses to operations as incurred. We charge mask costs used in production to cost of revenues over a 12-month period. However, we charge costs related to pre-production mask sets, which are not used in production, to research and development expenses at the time they are incurred. These charges often arise as we transition to new process technologies and, accordingly, can cause research and development expenses to fluctuate on a quarterly basis. We believe that continued investment in research and development is critical to our long-term success, and we expect to continue to devote significant resources to product development activities. Accordingly, we expect that our research and development expenses will increase in future periods, although such expenses as a percentage of net revenues may fluctuate.

Selling, General and Administrative Expenses. Selling, general and administrative expenses consist primarily of commissions paid to independent sales representatives, salaries, stock-based compensation and related expenses for personnel engaged in sales, marketing, administrative, finance and human resources activities, professional fees, costs associated with the promotion of our products and other corporate expenses. We expect that our sales and marketing expenses will increase in absolute dollars in future periods if we are able to grow and expand our sales force but that, to the extent our revenues increase in future periods, these expenses will generally decline as a percentage of net revenues. We also expect that, in support of any future growth that we are able to achieve, general and administrative expenses will generally increase in absolute dollars. General and administrative expenses increased significantly beginning in fiscal 2012 as a result of substantial legal expenses related to our pending patent infringement and antitrust litigation with Cypress Semiconductor Corporation. These expenses have varied significantly from quarter to quarter thereafter, depending on the relative level of activity in the Cypress litigation. They were substantially reduced during the six months ended September 30, 2012 while the issuance of the initial determination in the ITC proceeding was pending, although they increased again in the following quarters as the parties filed and responded to petitions for review of the initial determination, which was issued on October 25, 2012, activities related to our pending antitrust litigation with Cypress entered the discovery phase and activity resumed in the federal court patent litigation that had been stayed pending the conclusion of the ITC proceeding. Whatever the outcome of our pending litigation with Cypress, we expect to continue to incur additional legal expenses as we pursue our two lawsuits against Cypress and other pending litigation. These expenses are likely to continue to fluctuate significantly from quarter to quarter and to be substantial during some quarters over the next one to two years.

Results of Operations

The following table sets forth statement of operations data as a percentage of net revenues for the periods indicated:

	<u>Three Months Ended September 30,</u>		<u>Six Months Ended September 30,</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Net revenues	100.0 %	100.0 %	100.0 %	100.0 %
Cost of revenues	54.3	52.4	54.2	53.5
Gross profit	45.7	47.6	45.8	46.5
Operating expenses:				
Research and development	22.2	19.0	23.0	18.6
Selling, general and administrative	31.4	27.1	32.4	28.9
Total operating expenses	53.6	46.1	55.4	47.5
Income (loss) from operations	(7.9)	1.5	(9.6)	(1.0)
Interest and other income (expense), net	0.8	0.5	0.7	0.6
Income (loss) before income taxes	(7.1)	2.0	(8.9)	(0.4)
Provision (benefit) for income taxes	0.1	(0.4)	0.2	(0.2)
Net income (loss)	(7.2)	2.4	(9.1)	(0.2)

Net Revenues. Net revenues decreased by 14.7% from \$15.5 million in the three months ended September 30, 2013 to \$13.3 million in the three months ended September 30, 2014 and by 18.0% from \$32.0 million in the six months ended September 30, 2013 to \$26.2 million in the six months ended September 30, 2014. The reduction in both periods reflects the continuing weakness in the global networking and telecommunications markets and, in particular, continued weakness in Asia. Direct and indirect sales to Alcatel-Lucent, currently our largest customer, were unchanged at \$3.2 million in each of the three month periods ended September 30, 2013 and September 30, 2014 and \$6.4 million in each of the six month periods ended September 30, 2013 and September 30, 2014. Direct and indirect sales to Cisco Systems decreased by \$1.5 million from \$3.4 million in the three months ended September 30, 2013 to \$1.9 million in the three months ended September 30, 2014 and by \$2.5 million from \$6.2 million in the six months ended September 30, 2013 to \$3.7 million in the six months ended September 30, 2014. We believe that our net revenues in each of these periods were also negatively impacted by uncertainty regarding the outcome of our pending patent litigation with Cypress Semiconductor. We believe that the Commission's favorable final determination in the ITC proceeding has reduced this market uncertainty, although

some design-in losses that we suffered during the pendency of the ITC proceeding will continue to adversely affect our revenues throughout the life of the related products. Shipments of our SigmaQuad product line accounted for 40.6% of total shipments in the six months ended September 30, 2014 compared to 41.9% of total shipments in the nine months ended September 30, 2013.

Cost of Revenues. Cost of revenues decreased by 11.5% from \$8.1 million in the three months ended September 30, 2013 to \$7.2 million in the three months ended September 30, 2014 and by 16.8% from \$17.1 million in the six months ended September 30, 2013 to \$14.2 million in the six months ended September 30, 2014. The decreases in both periods were primarily due to the corresponding decreases in net revenues. Cost of revenues included stock-based compensation expense of \$104,000 and \$102,000, respectively, for the three months ended September 30, 2014 and 2013 and \$204,000 and \$196,000, respectively, for the six months ended September 30, 2014 and 2013.

Gross Profit. Gross profit decreased by 18.1% from \$7.4 million in the three months ended September 30, 2013 to \$6.1 million in the three months ended September 30, 2014 and by 19.3% from \$14.9 million in the six months ended September 30, 2013 to \$12.0 million in the six months ended September 30, 2014. Gross margin decreased from 47.6% in the three months ended September 30, 2013 to 45.7% in the three months ended September 30, 2014 and from 46.5% in the six months ended September 30, 2013 to 45.8% in the six months ended September 30, 2014. The changes in gross profit and gross margin were primarily related to the corresponding decreases in net revenues and changes in the mix of products and customers.

Research and Development Expenses. Research and development expenses were essentially unchanged at \$3.0 million in the three months ended September 30, 2013 and \$2.9 million in the three months ended September 30, 2014. An increase of \$83,000 in payroll related expenses was more than offset by decreases in maintenance and repair expenses and depreciation expense. Research and development expenses included stock-based compensation expense of \$248,000 and \$232,000, respectively, for the three months ended September 30, 2014 and 2013. Research and development expenses increased 1.2% from \$5.9 million in the six months ended September 30, 2013 to \$6.0 million in the six months ended September 30, 2014. This increase was primarily due to increases of \$135,000 in payroll related expenses and \$36,000 in patent-related legal expenses, partially offset by decreases in maintenance and repair expenses and depreciation expense. Research and development expenses included stock-based compensation expense of \$489,000 and \$490,000, respectively, for the six months ended September 30, 2014 and 2013.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were essentially unchanged at \$4.2 million in both the three months ended September 30, 2013 and in the three months ended September 30, 2014. Decreases in legal expenses, depreciation expense, independent sales representative commissions and payroll related expenses were offset by increases in other professional fees and travel related expenses. Selling, general and administrative expenses included stock-based compensation expense of \$219,000 and \$229,000, respectively, for the three months ended September 30, 2014 and 2013. Selling, general and administrative expenses decreased 7.9% from \$9.2 million in the six months ended September 30, 2013 to \$8.5 million in the six months ended September 30, 2014. This decrease was primarily related to a decrease of \$626,000 in legal fees related to the pending patent infringement and antitrust litigation involving Cypress Semiconductor and other pending litigation and lesser decreases in independent sales representative commissions and payroll related expenses, partially offset by increases in other professional fees and travel related expenses. Selling, general and administrative expenses included stock-based compensation expense of \$451,000 and \$442,000, respectively, for the six months ended September 30, 2014 and 2013.

Interest and Other Income (Expense), Net. Interest and other income (expense), net increased 31.8%, from income of \$85,000 in the three months ended September 30, 2013 to \$112,000 in the three months ended September 30, 2014. Interest income decreased by \$17,000 due to lower interest rates received on our cash and short-term and long-term investments and a lesser total cash and investments balance. However, the decline in interest income was offset by a foreign exchange gain of \$34,000 for the three months ended September 30, 2014 compared to an exchange loss of \$10,000 for the three months ended September 30, 2013. Interest and other income (expense), net decreased 6.6% from income of \$196,000 in the six months ended September 30, 2013 to \$183,000 in the six months ended September 30, 2014. Interest income decreased by \$26,000 due to lower interest rates received on our cash and short-term and long-term investments on a lesser total cash and investments balance. The decline in

interest income was partially offset by an exchange gain of \$9,000 for the six months ended September 30, 2014 compared to an exchange loss of \$4,000 for the six months ended September 30, 2013. The exchange gains and losses in each period were related to our Taiwan branch operations.

Provision (Benefit) for Income Taxes. The benefit for income taxes of \$60,000 in the three months ended September 30, 2013 compared to a provision of \$21,000 in the three months ended September 30, 2014, and the benefit of \$49,000 in the six months ended September 30, 2013 compared to a provision of \$69,000 in the six months ended September 30, 2014. These changes were due to fluctuations in the relative mix of income within operating jurisdictions.

Net Loss. Net income decreased from \$386,000 in the three months ended September 30, 2013 to a net loss of \$950,000 in the three months ended September 30, 2014. A net loss of \$55,000 in the six months ended September 30, 2013 increased to a net loss of \$2.4 million in the six months ended September 30, 2014. These increases were primarily due to the decreases in net revenues, gross profit and the changes in operating expenses discussed above.

Liquidity and Capital Resources

As of September 30, 2014, our principal sources of liquidity were cash, cash equivalents and short-term investments of \$62.7 million compared to \$80.9 million as of March 31, 2014.

Net cash used by operating activities was \$1.7 million for the six months ended September 30, 2014 compared to net cash provided by operating activities of \$5.0 million for the three months ended September 30, 2013. The primary uses of cash in the current six month period were a decrease of \$1.1 million in accounts payable, and increases of \$1.7 million in inventories and \$334,000 in prepaid expenses and other assets, partially offset by non-cash stock-based compensation expense of \$1.1 million, depreciation and amortization expense of \$931,000 and an increase in deferred revenue of \$577,000. The decreases in accounts payable and accrued expenses and other liabilities are primarily related to the decrease in legal expenses related to the pending patent infringement and antitrust litigation involving Cypress Semiconductor Corporation and other pending litigation in the quarter ended September 30, 2014 compared to the quarter ended March 31, 2014 and the payment of cash-based incentive compensation in the six month period ended September 30, 2014. The primary sources of cash in the six month period ended September 30, 2013 were a reduction in inventory of \$2.1 million and adjustments for stock-based compensation expense, depreciation expense and a provision for excess and obsolete inventory, partially offset by a decrease in deferred revenue. We allowed inventory levels to decrease in response to the slowdown in our business during fiscal 2013 and the first six months of the fiscal 2014.

Net cash provided by investing activities was \$20.7 million in the six months ended September 30, 2014 compared to \$265,000 in the six months ended September 30, 2013. Investment activities in the six months ended September 30, 2014 consisted primarily of the sale and maturity of corporate notes and certificates of deposits of \$24.9 million, partially offset by the purchase of investments of \$4 million. Investment activities in the six months ended September 30, 2013 consisted primarily of the sale and maturities of investments of \$20.1 million, partially offset by the purchase of state and municipal obligations, corporate notes and certificates of deposit of \$19.7 million.

Net cash used by financing activities in the six months ended September 30, 2014 primarily consisted of the repurchase of an aggregate of \$26.4 million of our common stock at an average purchase price of \$6.51, including shares purchased for \$25 million in our modified "Dutch" tender offer that settled in August 2014. Cash used for the repurchase of our common stock was partially offset by the net proceeds from the sale of common stock pursuant to our employee stock plans. Net cash provided by financing activities in the six months ended September 30, 2013 primarily consisted of the net proceeds from the sale of common stock pursuant to our employee stock plans.

We believe that our existing balances of cash, cash equivalents and short-term investments, and cash flow expected to be generated from our future operations will be sufficient to meet our cash needs for working capital and capital expenditures for at least the next 12 months, although we could be required, or could elect, to seek additional funding prior to that time. Our future capital requirements will depend on many factors, including revenue growth, if any, that we experience, the extent to which we utilize subcontractors, the levels of inventory and accounts

receivable that we maintain, the timing and extent of spending to support our product development efforts and the expansion of our sales and marketing efforts and the extent of legal expenses that we incur in connection with pending litigation. Additional capital may also be required for the consummation of any acquisition of businesses, products or technologies that we may undertake. We cannot assure you that additional equity or debt financing, if required, will be available on terms that are acceptable or at all.

Contractual Obligations

The following table describes our contractual obligations as of September 30, 2014:

	Payments due by period				Total
	Up to 1 year	1 - 3 years	3 - 5 years	More than 5 years	
Facilities and equipment leases	\$ 286,000	\$ 490,000		\$ —	\$ 776,000
Wafer, test and mask purchase obligations	3,585,000	607,000			4,192,000
	<u>\$ 3,871,000</u>	<u>\$ 1,097,000</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 4,968,000</u>

As of September 30, 2014, the current portion of our unrecognized tax benefits was \$0, and the long-term portion was \$1,492,000. The unrecognized tax benefits balance of \$2,466,000 as of September 30, 2014 would affect our effective tax rate if recognized. As of September 30, 2014, \$1,122,000 of unrecognized tax benefits have been recorded as a reduction of net deferred tax assets.

Critical Accounting Policies and Estimates

Our critical accounting policies and estimates are disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

Off-Balance Sheet Arrangements

At September 30, 2014, we did not have any off-balance sheet arrangements or relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Accordingly, we are not exposed to the type of financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

Recent Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board ("FASB") issued an Accounting Standards Update ("ASU") on Income Taxes, to improve the presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance is expected to reduce diversity in practice and is expected to better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. Implementation of this guidance in the quarter ended June 30, 2014 did not have a material impact on our financial position or results of operations.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." The new accounting standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The accounting standard is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016. Early adoption is not permitted. We are currently evaluating the impact of this accounting standard on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

Foreign Currency Exchange Risk. Our revenues and expenses, except those expenses related to our operations in Taiwan, including subcontractor manufacturing expenses, are denominated in U.S. dollars. As a result, we have relatively little exposure for currency exchange risks, and foreign exchange gains and losses have been minimal to date. We do not currently enter into forward exchange contracts to hedge exposure denominated in foreign currencies or any other derivative financial instruments for trading or speculative purposes. In the future, if we feel our foreign currency exposure has increased, we may consider entering into hedging transactions to help mitigate that risk.

Interest Rate Sensitivity. We had cash, cash equivalents, short-term investments and long-term investments totaling \$81.7 million at September 30, 2014. These amounts were invested primarily in money market funds, state and municipal obligations, corporate notes, certificates of deposit, government agency bonds and international government obligations. The cash, cash equivalents and short-term marketable securities are held for working capital purposes. We do not enter into investments for trading or speculative purposes. Due to the short-term nature of these investments, we believe that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates. We believe a hypothetical 100 basis point increase or decrease in interest rates would not materially affect the fair value of our interest-sensitive financial instruments. Declines in interest rates, however, will reduce future investment income.

Item 4. Controls and Procedures

Management's Evaluation of Disclosure Controls and Procedures

Based on their evaluation of 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) as of September 30, 2014, our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report for the purpose of ensuring that the information required to be disclosed by us in this report is made known to them by others on a timely basis, and that the information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, in order to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized, and reported by us within the time periods specified in the SEC's rules and instructions for Form 10-Q.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the quarter ended September 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

Item 1. Legal Proceedings

In March 2011, Cypress Semiconductor Corporation, a semiconductor manufacturer, filed a lawsuit against us in the United States District Court for the District of Minnesota alleging that our products, including our SigmaDDR and SigmaQuad families of Very Fast SRAMs, infringe five patents held by Cypress. The complaint seeks unspecified damages for past infringement and a permanent injunction against future infringement.

On June 10, 2011, Cypress filed a complaint against us with the United States International Trade Commission (the "ITC"). The ITC complaint, as subsequently amended, alleged infringement by GSI of three of the five patents involved in the District Court case and one additional patent and also alleged infringement by three of our distributors and 11 of our customers who allegedly incorporate our SRAMs in their products. The ITC complaint sought a limited exclusion order excluding the allegedly infringing SRAMs, and products containing them, from entry into the United States and permanent orders directing GSI and the other respondents to cease and desist from selling or distributing such products in the United States. On July 21, 2011, the ITC formally instituted

an investigation in response to Cypress's complaint. On June 7, 2013, the ITC announced that the full Commission had affirmed the determination of Chief Administrative Law Judge Charles E. Bullock that GSI's SRAM devices, and products containing them, do not infringe the Cypress patents and that Cypress had failed to establish the existence of a domestic industry that practices the patents. Moreover, the Commission reversed a portion of Judge Bullock's determination with respect to the validity of the patents, finding the asserted claims of one of the patents to have been anticipated by prior art and, therefore, invalid. The Commission ordered the investigation terminated, and Cypress did not appeal the ruling.

The Minnesota District Court case had been stayed pending the conclusion of the ITC proceeding. Following the termination of the ITC proceeding, the stay was lifted. On May 1, 2013, Cypress filed an additional lawsuit in the United States District Court for the Northern District of California alleging infringement by our products of five additional Cypress patents. Like the Minnesota case, the complaint in the California lawsuit seeks unspecified damages for past infringement and a permanent injunction against future infringement. We filed answers in both cases denying liability and asserting affirmative defenses. On August 7, 2013, the parties stipulated that the claims in the Minnesota case with respect to three of the asserted patents would be dismissed without prejudice and that the claims with respect to the remaining two patents would be transferred to the Northern District of California and consolidated with the pending California case. On August 20, 2013, the Court in the California case ordered the cases consolidated.

In connection with the pending litigation, we filed petitions with the Patent Trial and Appeal Board of the United States Patent and Trademark Office (the "PTAB") seeking *inter partes* review of certain claims of five of the seven Cypress patents that remain at issue in the California District Court litigation. The PTAB granted our petitions with respect to four of the patents and instituted a review of those patents. Our petition with respect to the other patent was denied. On October 7, 2014, the Court in the California District Court case granted our motion for a stay of the proceedings in that case with respect to the four patents under review by the PTAB pending a final resolution of that review. Accordingly, the case is currently proceeding with respect to only three of the ten patents initially asserted by Cypress.

On July 22, 2011, we filed a complaint against Cypress in the United States District Court for the Northern District of California. Our complaint alleges that Cypress has conducted an unlawful combination and conspiracy to monopolize the market for certain high-performance SRAM devices, known as fast synchronous Quad Data Rate (or QDR) SRAMs and Double Data Rate (or DDR) SRAMs. The complaint alleges that the anti-competitive, collusive and conspiratorial conduct of Cypress and certain co-conspirators has violated Section 1 of the Sherman Act and also constitutes unlawful restraint of trade and unfair competition under applicable provisions of California law. The complaint seeks treble damages, in an amount to be determined at trial, a preliminary and permanent injunction prohibiting the continuation of the unfair and illegal business practices and recovery of GSI's attorneys' fees and costs. On July 6, 2012, the Court denied Cypress' motion to dismiss the complaint, upholding the sufficiency of the antitrust claims asserted. Discovery in the case is proceeding, and trial has been set for February and March 2015.

We believe that we have strong defenses against Cypress' infringement claims in the remaining California District Court case. We intend to continue to defend ourselves vigorously in that proceeding while vigorously continuing to prosecute our antitrust claims against Cypress. However, the litigation process is inherently uncertain, and we may not prevail. Patent litigation is particularly complex and can extend for a protracted period of time, which can substantially increase the cost of such litigation. We have incurred and expect to continue to incur substantial legal fees and expenses in connection with the Cypress patent and antitrust litigation, and we also expect the litigation to continue to divert the efforts and attention of some of our key management and technical personnel. As a result, the litigation has been, and will continue to be, costly and time consuming. In addition, we believe that uncertainty regarding the outcome of the litigation has caused some of our customers and potential customers to reduce purchases of our products and/or seek second sources of supply, which adversely affected our revenues during the past three fiscal years. We believe that the Commission's favorable final determination in the ITC proceeding has reduced this market uncertainty, although some design-in losses that we suffered during the pendency of the ITC proceeding will continue to adversely affect our revenues throughout the life cycle of the related products.

Should the outcome of the patent litigation be adverse to us, we could be required to pay significant monetary damages to Cypress and could be enjoined from selling those of our products found to infringe Cypress's patents unless and until we are able to negotiate a license from Cypress. Any such license arrangement with Cypress would likely require the payment of royalties which would increase our cost of revenues and reduce our gross profit. If we are required to pay significant monetary damages, are enjoined from selling any of our products or are required to make substantial royalty payments pursuant to any such license arrangement, our business would be significantly harmed.

Item 1A. Risk Factors

Our future performance is subject to a variety of risks. If any of the following risks actually occur, our business, financial condition and results of operations could suffer and the trading price of our common stock could decline. Additional risks that we currently do not know about or that we currently believe to be immaterial may also impair our business operations. You should also refer to other information contained in this report, including our condensed consolidated financial statements and related notes. With the exception of the new item entitled "Use of our cash reserves to repurchase shares of our common stock presents potential risks and disadvantages to us and our continuing stockholders", the risk factors described below do not contain any material changes from those previously disclosed in Item 1A of our Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

Unpredictable fluctuations in our operating results could cause our stock price to decline.

Our quarterly and annual revenues, expenses and operating results have varied significantly and are likely to vary in the future. For example, in the ten fiscal quarters ended September 30, 2014, we recorded net revenues of as much as \$17.5 million and as little as \$12.8 million and quarterly operating income of as much as \$1.5 million and, in five quarters, operating losses, including an operating loss of \$3.6 million in the quarter ended March 31, 2014. We therefore believe that period-to-period comparisons of our operating results are not a good indication of our future performance, and you should not rely on them to predict our future performance or the future performance of our stock price. In future periods, we may not have any revenue growth, or our revenues could decline. Furthermore, if our operating expenses exceed our expectations, our financial performance could be adversely affected. Factors that may affect periodic operating results in the future include:

- our ability to anticipate and conform to new industry standards.
- unpredictability of the timing and size of customer orders, since most of our customers purchase our products on a purchase order basis rather than pursuant to a long-term contract;
- changes in our customers' inventory management practices;
- fluctuations in availability and costs associated with materials needed to satisfy customer requirements;
- manufacturing defects, which could cause us to incur significant warranty, support and repair costs, lose potential sales, harm our relationships with customers and result in write-downs;
- changes in our product pricing policies, including those made in response to new product announcements and pricing changes of our competitors;
- fluctuations in our quarterly operating expenses due to substantial litigation-related expenses in some quarters; and
- our ability to address technology issues as they arise, improve our products' functionality and expand our product offerings.

Our expenses are, to a large extent, fixed, and we expect that these expenses will increase in the future. We will not be able to adjust our spending quickly if our revenues fall short of our expectations. If this were to occur, our operating results would be harmed. If our operating results in future quarters fall below the expectations of market analysts and investors, the price of our common stock could fall.

Our two largest OEM customers account for a significant percentage of our net revenues. If either of these customers, or any of our other major customers, reduce the amount they purchase or stop purchasing our products, our operating results will suffer.

Alcatel-Lucent, currently our largest customer, purchases our products directly from us and through contract manufacturers and distributors. Purchases by Alcatel-Lucent represented approximately 24%, 19%, 12% and 9% of our net revenues in the six months ended September 30, 2014 and in fiscal 2014, 2013 and 2012, respectively. Cisco Systems, historically our largest OEM customer, purchases our products through its consignment warehouses and its contract manufacturers and directly from us. Purchases by Cisco Systems represented approximately 14%, 19%, 29% and 41% of our net revenues in the six months ended September 30, 2014 and in fiscal 2014, 2013 and 2012, respectively. We expect that our operating results in any given period will continue to depend significantly on orders from our key OEM customers, particularly Alcatel-Lucent and Cisco Systems, and our future success is dependent to a large degree on the business success of these OEMs over which we have no control. We do not have long-term contracts with Alcatel-Lucent and Cisco Systems or any of our other major OEM customers, distributors or contract manufacturers that obligate them to purchase our products. We expect that future direct and indirect sales to Cisco Systems will continue to fluctuate significantly on a quarterly basis and that such fluctuations may substantially affect our operating results in future periods. If we fail to continue to sell to our key OEM customers, distributors or contract manufacturers in sufficient quantities, our business could be harmed.

We have incurred significant losses in prior periods and may incur losses in the future.

We have incurred significant losses in prior periods. We incurred a loss of \$6.2 million during fiscal 2014, and in fiscal 2003 and 2004, we incurred losses of \$7.4 million and \$670,000, respectively. Although we have operated profitably during nine of the last ten fiscal years, there can be no assurance that our Very Fast SRAMs will continue to receive broad market acceptance or that we will be able to achieve sustained revenue growth. Our failure to do so may result in additional losses in the future. In addition, we expect our operating expenses to increase as we expand our business. If our revenues do not grow to offset these expected increased expenses, our business will suffer.

We depend upon the sale of our Very Fast SRAMs for most of our revenues, and a downturn in demand for these products could significantly reduce our revenues and harm our business.

We derive most of our revenues from the sale of Very Fast SRAMs, and we expect that sales of these products will represent the substantial majority of our revenues for the foreseeable future. Our business depends in large part upon continued demand for our products in the markets we currently serve, and adoption of our products in new markets. Market adoption will be dependent upon our ability to increase customer awareness of the benefits of our products and to prove their high-performance and cost-effectiveness. We may not be able to sustain or increase our revenues from sales of our products, particularly if the networking and telecommunications markets were to experience another significant downturn in the future. Any decrease in revenues from sales of our products could harm our business more than it would if we offered a more diversified line of products.

If we do not successfully develop new products to respond to rapid market changes due to changing technology and evolving industry standards, particularly in the networking and telecommunications markets, our business will be harmed.

If we fail to offer technologically advanced products and respond to technological advances and emerging standards, we may not generate sufficient revenues to offset our development costs and other expenses, which will hurt our business. The development of new or enhanced products is a complex and uncertain process that requires the accurate anticipation of technological and market trends. In particular, the networking and telecommunications markets are rapidly evolving and new standards are emerging. We are vulnerable to advances in technology by competitors, including new SRAM architectures, new forms of DRAM and the emergence of new memory

technologies that could enable the development of products that feature higher performance or lower cost. We may experience development, marketing and other technological difficulties that may delay or limit our ability to respond to technological changes, evolving industry standards, competitive developments or end-user requirements. For example, because we have limited experience developing integrated circuits, or IC, products other than Very Fast SRAMs, our efforts to introduce new products may not be successful and our business may suffer. Other challenges that we face include:

- our products may become obsolete upon the introduction of alternative technologies;
- we may incur substantial costs if we need to modify our products to respond to these alternative technologies;
- we may not have sufficient resources to develop or acquire new technologies or to introduce new products capable of competing with future technologies;
- new products that we develop may not successfully integrate with our end-users' products into which they are incorporated;
- we may be unable to develop new products that incorporate emerging industry standards;
- we may be unable to develop or acquire the rights to use the intellectual property necessary to implement new technologies; and
- when introducing new or enhanced products, we may be unable to manage effectively the transition from older products.

We are subject to the highly cyclical nature of the networking and telecommunications markets.

Our products are incorporated into routers, switches, wireless local area network infrastructure equipment, wireless base stations and network access equipment used in the highly cyclical networking and telecommunications markets. For example, our operating results declined sharply in fiscal 2002 and 2003 as a result of the severe contraction in demand for networking and telecommunications equipment in which our products are incorporated. Prior to this period of contraction, the networking and telecommunications markets experienced a period of rapid growth, which resulted in a significant increase in demand for our products. We expect that the networking and telecommunications markets will continue to be highly cyclical, characterized by periods of rapid growth and contraction. Our business and our operating results are likely to fluctuate, perhaps quite severely, as a result of this cyclicity.

The market for Very Fast SRAMs is highly competitive.

The market for Very Fast SRAMs, which are used primarily in networking and telecommunications equipment, is characterized by price erosion, rapid technological change, cyclical market patterns and intense foreign and domestic competition. Several of our competitors offer a broad array of memory products and have greater financial, technical, marketing, distribution and other resources than we have. Some of our competitors maintain their own semiconductor fabrication facilities, which may provide them with capacity, cost and technical advantages over us. We cannot assure you that we will be able to compete successfully against any of these competitors. Our ability to compete successfully in this market depends on factors both within and outside of our control, including:

- real or perceived imbalances in supply and demand of Very Fast SRAMs;
- the rate at which OEMs incorporate our products into their systems;

- the success of our customers' products;
- our ability to develop and market new products; and
- the supply and cost of wafers.

In addition, we are vulnerable to advances in technology by competitors, including new SRAM architectures and new forms of DRAM, or the emergence of new memory technologies that could enable the development of products that feature higher performance, lower cost or lower power capabilities. Additionally, the trend toward incorporating SRAM into other chips in the networking and telecommunications markets has the potential to reduce future demand for Very Fast SRAM products. There can be no assurance that we will be able to compete successfully in the future. Our failure to compete successfully in these or other areas could harm our business.

We are subject to pending patent infringement litigation.

In March 2011, Cypress Semiconductor Corporation, a semiconductor manufacturer, filed a lawsuit against us in the United States District Court for the District of Minnesota alleging that our products, including our SigmaDDR and SigmaQuad families of Very Fast SRAMs, infringe five patents held by Cypress. The complaint seeks unspecified damages for past infringement and a permanent injunction against future infringement. The case was stayed pending the conclusion of an investigation by the International Trade Commission (the "ITC") in response to a complaint filed by Cypress. In July 2013, following a final ITC determination favorable to us and the termination of the ITC investigation, the stay was lifted. On May 1, 2013, Cypress filed a lawsuit in the United States District Court for the Northern District of California alleging infringement by our products of five additional Cypress patents. Like the Minnesota case, the complaint in the California lawsuit sought unspecified damages for past infringement and a permanent injunction against future infringement. In August 2013, the Minnesota case was transferred to the Northern District of California and consolidated with the pending California case.

On July 22, 2011, we filed a complaint against Cypress in the United States District Court for the Northern District of California. Our complaint alleges that Cypress has conducted an unlawful combination and conspiracy to monopolize the market for certain high-performance SRAM devices, known as fast synchronous Quad Data Rate (or QDR) SRAMs and Double Data Rate (or DDR) SRAMs. The complaint alleges that the anti-competitive, collusive and conspiratorial conduct of Cypress and certain co-conspirators has violated Section 1 of the Sherman Act and also constitutes unlawful restraint of trade and unfair competition under applicable provisions of California law. The complaint seeks treble damages, in an amount to be determined at trial, a preliminary and permanent injunction prohibiting the continuation of the unfair and illegal business practices and recovery of GSI's attorneys' fees and costs. On July 6, 2012, the Court denied Cypress' motion to dismiss the complaint, upholding the sufficiency of the antitrust claims asserted, and discovery in the case is proceeding.

We believe that we have strong defenses against Cypress' patent infringement claims in the remaining California District Court case. We intend to continue to defend ourselves vigorously in that proceeding while vigorously continuing to prosecute our antitrust claims against Cypress. However, the litigation process is inherently uncertain, and we may not prevail. Patent litigation is particularly complex and can extend for a protracted period of time, which can substantially increase the cost of such litigation. We have incurred and expect to continue to incur substantial legal fees and expenses in connection with the Cypress patent and antitrust litigation. These expenses are likely to continue to fluctuate significantly from quarter to quarter and to be substantial in some quarters over the next one to two years. We also expect the litigation to continue to divert the efforts and attention of some of our key management and technical personnel. As a result, the litigation will be costly and time consuming. In addition, we believe that uncertainty regarding the outcome of the litigation has caused some of our customers and potential customers to reduce purchases of our products and/or seek second sources of supply, which adversely affected our revenues during the past three fiscal years.

Should the outcome of the patent litigation be adverse to us, we could be required to pay significant monetary damages to Cypress and could be enjoined from selling those of our products found to infringe Cypress's

patents unless and until we are able to negotiate a license from Cypress. Any such license arrangement with Cypress would likely require the payment of royalties which would increase our cost of revenues and reduce our gross profit. If we are required to pay significant monetary damages, are enjoined from selling any of our products or are required to make substantial royalty payments pursuant to any such license arrangement, our business would be significantly harmed.

The average selling prices of our products are expected to decline, and if we are unable to offset these declines, our operating results will suffer.

Historically, the average unit selling prices of our products have declined substantially over the lives of the products, and we expect this trend to continue. A reduction in overall average selling prices of our products could result in reduced revenues and lower gross margins. Our ability to increase our net revenues and maintain our gross margins despite a decline in the average selling prices of our products will depend on a variety of factors, including our ability to introduce lower cost versions of our existing products, increase unit sales volumes of these products, and introduce new products with higher prices and greater margins. If we fail to accomplish any of these objectives, our business will suffer. To reduce our costs, we may be required to implement design changes that lower our manufacturing costs, negotiate reduced purchase prices from our independent foundries and our independent assembly and test vendors, and successfully manage our manufacturing and subcontractor relationships. Because we do not operate our own wafer foundry or assembly facilities, we may not be able to reduce our costs as rapidly as companies that operate their own foundries or facilities.

Current unfavorable economic and market conditions, domestically and internationally, may adversely affect our business, financial condition, results of operations and cash flows.

We have significant customer sales both in the United States and internationally. We are also reliant upon U.S. and international suppliers, manufacturing partners and distributors. We are therefore susceptible to adverse U.S. and international economic and market conditions, including the challenging economic conditions that have prevailed and continue to prevail in the United States and worldwide. The recent turmoil in the financial markets has resulted in higher borrowing costs and tightened credit markets which have made it more difficult (in some cases, prohibitively so) for many companies to fund their working capital obligations. If any of our manufacturing partners, customers, distributors or suppliers experiences serious financial difficulties or ceases operations, our business could be adversely affected. The adverse impact of the credit crisis on consumers, including higher unemployment rates, is also adversely impacting consumer spending, which adversely impacts demand for consumer products, including certain end products in which our SRAMs are embedded. In addition, ongoing economic turmoil has recently had an adverse affect on capital expenditures for network equipment, particularly in Europe and Asia, which has impacted sales to some of our largest customers. The difficulty that businesses (including our customers) may have in obtaining credit, the decreased consumer spending resulting from the credit market crisis, high unemployment rates and continued global economic and market turmoil are likely to continue to have an adverse impact on our business, financial condition, results of operations and cash flows, at least over the near term.

We are dependent on a number of single source suppliers, and if we fail to obtain adequate supplies, our business will be harmed and our prospects for growth will be curtailed.

We currently purchase several key components used in the manufacture of our products from single sources and are dependent upon supply from these sources to meet our needs. If any of these suppliers cannot provide components on a timely basis, at the same price or at all, our ability to manufacture our products will be constrained and our business will suffer. Most significantly, we obtain wafers for our Very Fast SRAM products from a single foundry, TSMC, and most of them are packaged at ASE. Wafers for our LLDRAM products are obtained exclusively from Powerchip. If we are unable to obtain an adequate supply of wafers from TSMC or Powerchip or find alternative sources in a timely manner, we will be unable to fulfill our customer orders and our operating results will be harmed. We do not have supply agreements with TSMC, Powerchip, ASE or any of our other independent assembly and test suppliers, and instead obtain manufacturing services and products from these suppliers on a purchase-order basis. Our suppliers, including TSMC and Powerchip, have no obligation to supply products or services to us for any specific product, in any specific quantity, at any specific price or for any specific time period.

As a result, the loss or failure to perform by any of these suppliers could adversely affect our business and operating results.

Should any of our single source suppliers experience manufacturing failures or yield shortfalls, be disrupted by natural disaster or political instability, choose to prioritize capacity or inventory for other uses or reduce or eliminate deliveries to us, we likely will not be able to enforce fulfillment of any delivery commitments and we would have to identify and qualify acceptable replacements from alternative sources of supply. In particular, if TSMC is unable to supply us with sufficient quantities of wafers to meet all of our requirements, we would have to allocate our products among our customers, which would constrain our growth and might cause some of them to seek alternative sources of supply. Since the manufacturing of wafers and other components is extremely complex, the process of qualifying new foundries and suppliers is a lengthy process and there is no assurance that we would be able to find and qualify another supplier without materially adversely affecting our business, financial condition and results of operations

Because we outsource our wafer manufacturing and independent wafer foundry capacity is limited, we may be required to enter into costly long-term supply arrangements to secure foundry capacity.

We do not have long-term supply agreements with TSMC or Powerchip, but instead obtain our wafers on a purchase order basis. In order to secure future wafer supply from TSMC or Powerchip or from other independent foundries, we may be required to enter into various arrangements with them, which could include:

- contracts that commit us to purchase specified quantities of wafers over extended periods;
- investments in and joint ventures with the foundries; or
- non-refundable deposits with or prepayments or loans to foundries in exchange for capacity commitments.

We may not be able to make any of these arrangements in a timely fashion or at all, and these arrangements, if any, may not be on terms favorable to us. Moreover, even if we are able to secure independent foundry capacity, we may be obligated to use all of that capacity or incur penalties. These penalties may be expensive and could harm our financial results.

If we are unable to offset increased wafer fabrication costs by increasing the average selling prices of our products, our gross margins will suffer.

If there is a significant upturn in the networking and telecommunications markets that results in increased demand for our products and competing products, the available supply of wafers may be limited. As a result, we could be required to obtain additional manufacturing capacity in order to meet increased demand. Securing additional manufacturing capacity may cause our wafer fabrication costs to increase. If we are unable to offset these increased costs by increasing the average selling prices of our products, our gross margins will decline.

We rely heavily on distributors and our success depends on our ability to develop and manage our indirect distribution channels.

A significant percentage of our sales are made to distributors and to contract manufacturers who incorporate our products into end products for OEMs. For example, in the six months ended September 30, 2014 and in fiscal 2014, 2013 and 2012, our distributor Avnet Logistics accounted for 34.9%, 30.3%, 26.5% and 20.1%, respectively, of our net revenues. Avnet Logistics and our other existing distributors may choose to devote greater resources to marketing and supporting the products of other companies. Since we sell through multiple channels and distribution networks, we may have to resolve potential conflicts between these channels. For example, these conflicts may result from the different discount levels offered by multiple channel distributors to their customers or, potentially, from our direct sales force targeting the same equipment manufacturer accounts as our indirect channel distributors. These conflicts may harm our business or reputation.

We may be unable to accurately predict future sales through our distributors, which could harm our ability to efficiently manage our resources to match market demand.

Our financial results, quarterly product sales, trends and comparisons are affected by fluctuations in the buying patterns of the OEMs that purchase our products from our distributors. While we attempt to assist our distributors in maintaining targeted stocking levels of our products, we may not consistently be accurate or successful. This process involves the exercise of judgment and use of assumptions as to future uncertainties, including end user demand. Inventory levels of our products held by our distributors may exceed or fall below the levels we consider desirable on a going-forward basis. This could result in distributors returning unsold inventory to us, or in us not having sufficient inventory to meet the demand for our products. If we are not able to accurately predict sales through our distributors or effectively manage our relationships with our distributors, our business and financial results will suffer.

A small number of customers generally account for a significant portion of our accounts receivable in any period, and if any one of them fails to pay us, our financial position and operating results will suffer.

At September 30, 2014, three customers accounted for 23%, 20%, and 18% of our accounts receivable, respectively. If any of these customers do not pay us, our financial position and operating results will be harmed. Generally, we do not require collateral from our customers.

We have disclosed a material weakness in our internal control over financial reporting relating to the evaluation and calculation of our inventory reserve. Our failure to remediate this material weakness or to otherwise maintain effective internal control over financial reporting and disclosure controls and processes could adversely affect our ability to report our financial condition and results of operations accurately and on a timely basis.

In connection with the completion of our 2014 third fiscal quarter-end closing and review procedures certain errors were identified in the evaluation and calculation of our inventory write-down for the quarter and nine month periods ended December 31, 2013 that were the result of a material weakness in our internal control over financial reporting. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis.

During our 2014 third fiscal quarter-end closing and review procedures our management determined that we had not designed and maintained effective controls over the review of supporting information to confirm the completeness and accuracy of our calculations for the write-down of excess or obsolete inventory, thereby affecting the valuation of our inventory as of December 31, 2013. Specifically, quarterly controls, including procedures for monitoring older product inventory, did not fully take into account the fact that management's prior expectations of increasing demand for our products during the balance of fiscal 2014 following the favorable ITC ruling on June 7, 2013 and the exit of a competitor from the SRAM market in December 2012 did not materialize and were not sufficiently precise to identify all potentially excess or obsolete inventory, taking into account reduced materiality thresholds following declines in our revenues and income (loss) before tax. Consequently we did not initially write down the full amount of excess or obsolete inventory, and additional adjustments were recorded to increase the inventory write-downs and to increase cost of sales by \$985,000 for the quarter and nine months ended December 31, 2013. While this control deficiency did not result in any material misstatement of our historical financial statements, it did result in adjustments identified by our auditors as part of their quarterly review process, and require corrections after our initial estimate of excess and obsolete inventory write-downs for the three month period ended December 31, 2013.

A material weakness in our internal control over financial reporting could adversely impact our ability to provide timely and accurate financial information. Following the identification of the error in our third quarter financial statements and the material weakness that gave rise to the error, our management implemented a remediation plan which it believes fully remediated the material weakness. Should our remediation efforts prove to have been inadequate or should we otherwise fail to maintain effective internal control over financial reporting and disclosure controls and procedures, we could be unable to meet our reporting obligations accurately and on a timely

basis. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could adversely affect the trading price of our common stock.

Our acquisition of companies or technologies could prove difficult to integrate, disrupt our business, dilute stockholder value and adversely affect our operating results.

In August 2009, we consummated the acquisition of substantially all of the assets related to the SRAM memory device product line of Sony Corporation. In the future, we may make additional acquisitions or investments in companies, assets or technologies that we believe are complementary or strategic. Other than the Sony acquisition, we have not made any such acquisitions or investments, and therefore our experience as an organization in making such acquisitions and investments is limited. In connection with future acquisitions or investments we may make, we face numerous risks, including:

- difficulties in integrating operations, technologies, products and personnel;
- diversion of financial and managerial resources from existing operations;
- risk of overpaying for or misjudging the strategic fit of an acquired company, asset or technology;
- problems or liabilities stemming from defects of an acquired product or intellectual property litigation that may result from offering the acquired product in our markets;
- challenges in retaining key employees to maximize the value of the acquisition or investment;
- inability to generate sufficient return on investment;
- incurrence of significant one-time write-offs; and
- delays in customer purchases due to uncertainty.

If we proceed with additional acquisitions or investments, we may be required to use a considerable amount of our cash, or to finance the transaction through debt or equity securities offerings, which may decrease our financial liquidity or dilute our stockholders and affect the market price of our stock. As a result, if we fail to properly evaluate and execute acquisitions or investments, our business and prospects may be harmed.

Claims that we infringe third party intellectual property rights could seriously harm our business and require us to incur significant costs.

In recent years, there has been significant litigation in the semiconductor industry involving patents and other intellectual property rights. We are currently involved in patent infringement litigation. See "We are subject to pending patent infringement litigation" above. We could become subject to additional claims or litigation in the future as a result of allegations that we infringe others' intellectual property rights or that our use of intellectual property otherwise violates the law. Claims that our products infringe the proprietary rights of others would force us to defend ourselves and possibly our customers, distributors or manufacturers against the alleged infringement. Any such litigation regarding intellectual property could result in substantial costs and diversion of resources and could have a material adverse effect on our business, financial condition and results of operations. Similarly, changing our products or processes to avoid infringing the rights of others may be costly or impractical. If any claims received in the future were to be upheld, the consequences to us would be severe and could require us to:

- stop selling our products that incorporate the challenged intellectual property;
- obtain a license to sell or use the relevant technology, which license may not be available on reasonable terms or at all;

- pay damages; or
- redesign those products that use the disputed technology.

Although patent disputes in the semiconductor industry have often been settled through cross-licensing arrangements, we may not be able in any or every instance to settle an alleged patent infringement claim through a cross-licensing arrangement. We have a more limited patent portfolio than many of our competitors. If a successful claim is made against us or any of our customers and a license is not made available to us on commercially reasonable terms or we are required to pay substantial damages or awards, our business, financial condition and results of operations would be materially adversely affected.

Our business will suffer if we are unable to protect our intellectual property.

Our success and ability to compete depends in large part upon protecting our proprietary technology. We rely on a combination of patent, trade secret, copyright and trademark laws and non-disclosure and other contractual agreements to protect our proprietary rights. These agreements and measures may not be sufficient to protect our technology from third-party infringement, or to protect us from the claims of others. Monitoring unauthorized use of our products is difficult and we cannot be certain that the steps we have taken will prevent unauthorized use of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. Our attempts to enforce our intellectual property rights could be time consuming and costly. We are currently involved in litigation to enforce our intellectual property rights and to protect our trade secrets. Additional litigation of this type may be necessary in the future. Any such litigation could result in substantial costs and diversion of resources. If competitors are able to use our technology without our approval or compensation, our ability to compete effectively could be harmed.

We may experience difficulties in transitioning to smaller geometry process technologies and other more advanced manufacturing process technologies, which may result in reduced manufacturing yields, delays in product deliveries and increased expenses.

In order to remain competitive, we expect to continue to transition the manufacture of our products to smaller geometry process technologies. This transition will require us to migrate to new manufacturing processes for our products and redesign certain products. The manufacture and design of our products is complex, and we may experience difficulty in transitioning to smaller geometry process technologies or new manufacturing processes. These difficulties could result in reduced manufacturing yields, delays in product deliveries and increased expenses. We are dependent on our relationships with TSMC and Powerchip to transition successfully to smaller geometry process technologies and to more advanced manufacturing processes. We cannot assure you that TSMC or Powerchip will be able to effectively manage the transition or that we will be able to maintain our relationship with them. If we or TSMC or Powerchip experience significant delays in this transition or fail to implement these transitions, our business, financial condition and results of operations could be materially and adversely affected.

Manufacturing process technologies are subject to rapid change and require significant expenditures for research and development.

We continuously evaluate the benefits of migrating to smaller geometry process technologies in order to improve performance and reduce costs. Historically, these migrations to new manufacturing processes have resulted in significant initial design and development costs associated with pre-production mask sets for the manufacture of new products with smaller geometry process technologies. For example, in fiscal 2014, we incurred \$809,000 and \$648,000, respectively, in research and development expense associated with pre-production mask sets which were not later used in production as part of the transition to our new 40 nanometer SRAM process technology and 63 nanometer DRAM process technology, respectively. We will incur similar expenses in the future as we continue to transition our products to smaller geometry processes. The costs inherent in the transition to new manufacturing process technologies will adversely affect our operating results and our gross margin.

Our products are complex to design and manufacture and could contain defects, which could reduce revenues or result in claims against us.

We develop complex products. Despite testing by us and our OEM customers, design or manufacturing errors may be found in existing or new products. These defects could result in a delay in recognition or loss of revenues, loss of market share or failure to achieve market acceptance. These defects may also cause us to incur significant warranty, support and repair costs, divert the attention of our engineering personnel from our product development efforts, result in a loss of market acceptance of our products and harm our relationships with our OEM customers. Our OEM customers could also seek and obtain damages from us for their losses. A product liability claim brought against us, even if unsuccessful, would likely be time consuming and costly to defend.

Defects in wafers and other components used in our products and arising from the manufacturing of these products may not be fully recoverable from TSMC or our other suppliers. For example, in the quarter ended December 31, 2005, we incurred a charge of approximately \$900,000 related to the write-off of inventory resulting from an error in the assembly process at one of our suppliers. This write-off adversely affected our operating results for fiscal 2006.

Demand for our products may decrease if our OEM customers experience difficulty manufacturing, marketing or selling their products.

Our products are used as components in our OEM customers' products. For example, Cisco Systems, historically our largest OEM customer, incorporates our products in a number of its networking routers and switches. Accordingly, demand for our products is subject to factors affecting the ability of our OEM customers to successfully introduce and market their products, including:

- capital spending by telecommunication and network service providers and other end-users who purchase our OEM customers' products;
- the competition our OEM customers face, particularly in the networking and telecommunications industries;
- the technical, manufacturing, sales and marketing and management capabilities of our OEM customers;
- the financial and other resources of our OEM customers; and
- the inability of our OEM customers to sell their products if they infringe third-party intellectual property rights.

As a result, if OEM customers reduce their purchases of our products, our business will suffer.

Downturns in the semiconductor industry may harm our revenues and margins.

The semiconductor industry is highly cyclical. The industry has experienced significant downturns, often in connection with, or in anticipation of, maturing product cycles of both semiconductor companies' and their customers' products and declines in general economic conditions. These downturns have been characterized by production overcapacity, high inventory levels and accelerated erosion of average selling prices. From time to time, the semiconductor industry also has experienced periods of increased demand and production capacity constraints. Our operating results may suffer during the down portion of these cycles. Downturns in the semiconductor industry could cause our stock price to be volatile, and a prolonged decline in the industry could adversely affect our revenues. If we are unable to control our inventory levels or expenses adequately in response to reduced net sales, our results of operations would be negatively impacted.

Our products have lengthy sales cycles that make it difficult to plan our expenses and forecast results.

Our products are generally incorporated in our OEM customers' products at the design stage. However, their decisions to use our products often require significant expenditures by us without any assurance of success, and often precede volume sales, if any, by a year or more. If an OEM customer decides at the design stage not to incorporate our products into their products, we will not have another opportunity for a design win with respect to that customer's product for many months or years, if at all. Our sales cycle can take up to 24 months to complete, and because of this lengthy sales cycle, we may experience a delay between increasing expenses for research and development and our sales and marketing efforts and the generation of volume production revenues, if any, from these expenditures. Moreover, the value of any design win will largely depend on the commercial success of our OEM customers' products. There can be no assurance that we will continue to achieve design wins or that any design win will result in future revenues.

Any significant order cancellations or order deferrals could adversely affect our operating results.

We typically sell products pursuant to purchase orders that customers can generally cancel or defer on short notice without incurring a significant penalty. Any significant cancellations or deferrals in the future could materially and adversely affect our business, financial condition and results of operations. Cancellations or deferrals could cause us to hold excess inventory, which could reduce our profit margins, increase product obsolescence and restrict our ability to fund our operations. We generally recognize revenue upon shipment of products to a customer. If a customer refuses to accept shipped products or does not pay for these products, we could miss future revenue projections or incur significant charges against our income, which could materially and adversely affect our operating results.

If our business grows, such growth may place a significant strain on our management and operations and, as a result, our business may suffer.

We are endeavoring to resume the expansion of our business, and any growth that we are successful in achieving could place a significant strain on our management systems, infrastructure and other resources. To manage such growth of our operations and increases in the number of our personnel, we will need to invest the necessary capital to continue to improve our operational, financial and management controls and our reporting systems and procedures. Our controls, systems and procedures may prove to be inadequate should we experience significant growth. In addition, we may not have sufficient administrative staff to support our operations. For example, we currently have only five employees in our finance department in the United States, including our Chief Financial Officer. Furthermore, our officers have limited experience in managing large or rapidly growing businesses. If our management fails to respond effectively to changes in our business, our business may suffer.

Our international business exposes us to additional risks.

Products shipped to destinations outside of the United States accounted for 68.0%, 69.2%, 68.8% and 76.5% of our net revenues in the six months ended September 30, 2014 and in fiscal 2014, 2013 and 2012, respectively. Moreover, a substantial portion of our products is manufactured and tested in Taiwan. We intend to continue expanding our international business in the future. Conducting business outside of the United States subjects us to additional risks and challenges, including:

- heightened price sensitivity from customers in emerging markets;
- compliance with a wide variety of foreign laws and regulations and unexpected changes in these laws;
- legal uncertainties regarding taxes, tariffs, quotas, export controls, competition, export licenses and other trade barriers;

- political and economic instability in, or foreign conflicts that involve or affect, the countries in which we, our customers and our suppliers are located;
- difficulties in collecting accounts receivable and longer accounts receivable payment cycles;
- difficulties and costs of staffing and managing personnel, distributors and representatives across different geographic areas and cultures, including assuring compliance with the U. S. Foreign Corrupt Practices Act and other U. S. and foreign anti-corruption laws;
- limited protection for intellectual property rights in some countries; and
- fluctuations in freight rates and transportation disruptions.

Moreover, our reporting currency is the U.S. dollar. However, a portion of our cost of revenues and our operating expenses is denominated in currencies other than the U.S. dollar, primarily the New Taiwanese dollar. As a result, appreciation or depreciation of other currencies in relation to the U.S. dollar could result in transaction gains or losses that could impact our operating results. We do not currently engage in currency hedging activities to reduce the risk of financial exposure from fluctuations in foreign exchange rates.

TSMC and Powerchip, as well as our other independent suppliers and many of our OEM customers, have operations in the Pacific Rim, an area subject to significant earthquake risk and adverse consequences related to the potential outbreak of contagious diseases such as the H1N1 Flu.

The foundries that manufacture our Fast SRAM and LLDRAM products, TSMC and Powerchip, and all of the principal independent suppliers that assemble and test our products are located in Taiwan. Many of our customers are also located in the Pacific Rim. The risk of an earthquake in these Pacific Rim locations is significant. The occurrence of an earthquake or other natural disaster near the fabrication facilities of TSMC or our other independent suppliers could result in damage, power outages and other disruptions that impair their production and assembly capacity. Any disruption resulting from such events could cause significant delays in the production or shipment of our products until we are able to shift our manufacturing, assembling, packaging or production testing from the affected contractor to another third-party vendor. In such an event, we may not be able to obtain alternate foundry capacity on favorable terms, or at all.

The outbreak of SARS in 2003 curtailed travel to and from certain countries, primarily in the Asia-Pacific region, and limited travel within those countries. If there were to be another outbreak of a contagious disease, such as the Ebola virus, SARS or the H1N1 Flu that significantly affected the Asia-Pacific region, the operations of our key suppliers could be disrupted. In addition, our business could be harmed if such an outbreak resulted in travel being restricted, as it was during parts of 2003, or if it adversely affected the operations of our suppliers or our OEM customers or the demand for our products or our OEM customers' products.

Changes in Taiwan's political, social and economic environment may affect our business performance.

Because much of the manufacturing and testing of our products is conducted in Taiwan, our business performance may be affected by changes in Taiwan's political, social and economic environment. For example, any political instability resulting from the relationship among the United States, Taiwan and the People's Republic of China could damage our business. Moreover, the role of the Taiwanese government in the Taiwanese economy is significant. Taiwanese policies toward economic liberalization, and laws and policies affecting technology companies, foreign investment, currency exchange rates, taxes and other matters could change, resulting in greater restrictions on our ability and our suppliers' ability to do business and operate facilities in Taiwan. If any of these changes were to occur, our business could be harmed and our stock price could decline.

We are substantially dependent on the continued services and performance of our senior management and other key personnel.

Our future success is substantially dependent on the continued services and continuing contributions of our senior management who must work together effectively in order to design our products, expand our business, increase our revenues and improve our operating results. Members of our senior management team have long-standing and important relationships with our key customers and suppliers. The loss of services of Lee-Lean Shu, our President and Chief Executive Officer, Robert Yau, our Vice President of Engineering, any other executive officer or other key employee could significantly delay or prevent the achievement of our development and strategic objectives. We do not have employment contracts with, nor maintain key person insurance on, any of our executive officers.

If we are unable to recruit or retain qualified personnel, our business and product development efforts could be harmed.

We must continue to identify, recruit, hire, train, retain and motivate highly skilled technical, managerial, sales and marketing and administrative personnel. Competition for these individuals is intense, and we may not be able to successfully recruit, assimilate or retain sufficiently qualified personnel. We may encounter difficulties in recruiting and retaining a sufficient number of qualified engineers, which could harm our ability to develop new products and adversely impact our relationships with existing and future end-users at a critical stage of development. The failure to recruit and retain necessary technical, managerial, sales, marketing and administrative personnel could harm our business and our ability to obtain new OEM customers and develop new products.

We may need to raise additional capital in the future, which may not be available on favorable terms or at all, and which may cause dilution to existing stockholders.

We may need to seek additional funding in the future. We do not know if we will be able to obtain additional financing on favorable terms, if at all. If we cannot raise funds on acceptable terms, if and when needed, we may not be able to develop or enhance our products, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements, and we may be required to reduce operating costs, which could seriously harm our business. In addition, if we issue equity securities, our stockholders may experience dilution or the new equity securities may have rights, preferences or privileges senior to those of our common stock.

Some of our products are incorporated into advanced military electronics, and changes in international geopolitical circumstances and domestic budget considerations may hurt our business.

Some of our products are incorporated into advanced military electronics such as radar and guidance systems. Military expenditures and appropriations for such purchases rose significantly in recent years. However, as the current conflicts in Afghanistan and Iraq wind down, demand for our products for use in military applications may decrease, and our operating results could suffer. Domestic budget considerations may also adversely affect our operating results. For example, if governmental appropriations for military purchases of electronic devices that include our products are reduced, our revenues will likely decline.

Our operations involve the use of hazardous and toxic materials, and we must comply with environmental laws and regulations, which can be expensive, and may affect our business and operating results.

We are subject to federal, state and local regulations relating to the use, handling, storage, disposal and human exposure to hazardous and toxic materials. If we were to violate or become liable under environmental laws in the future as a result of our inability to obtain permits, human error, accident, equipment failure or other causes, we could be subject to fines, costs, or civil or criminal sanctions, face property damage or personal injury claims or be required to incur substantial investigation or remediation costs, which could be material, or experience disruptions in our operations, any of which could have a material adverse effect on our business. In addition, environmental laws could become more stringent over time imposing greater compliance costs and increasing risks and penalties associated with violations, which could harm our business.

We also face increasing complexity in our product design as we adjust to new and future requirements relating to the materials composition of our products, including the restrictions on lead and other hazardous substances applicable to specified electronic products placed on the market in the European Union (Restriction on the Use of Hazardous Substances Directive 2002/95/EC, also known as the RoHS Directive). We also expect that our operations will be affected by other new environmental laws and regulations on an ongoing basis. Although we cannot predict the ultimate impact of any such new laws and regulations, they will likely result in additional costs, and could require that we change the design and/or manufacturing of our products, any of which could have a material adverse effect on our business.

The trading price of our common stock is subject to fluctuation and is likely to be volatile.

The trading price of our common stock may fluctuate significantly in response to a number of factors, some of which are beyond our control, including:

- actual or anticipated declines in operating results;
- changes in financial estimates or recommendations by securities analysts;
- the institution of legal proceedings against us or significant developments in such proceedings;
- announcements by us or our competitors of financial results, new products, significant technological innovations, contracts, acquisitions, strategic relationships, joint ventures, capital commitments or other events;
- changes in industry estimates of demand for Very Fast SRAM products;
- the gain or loss of significant orders or customers;
- recruitment or departure of key personnel; and
- market conditions in our industry, the industries of our customers and the economy as a whole.

In recent years the stock market in general, and the market for technology stocks in particular, have experienced extreme price fluctuations, which have often been unrelated to the operating performance of affected companies. The market price of our common stock might experience significant fluctuations in the future, including fluctuations unrelated to our performance. These fluctuations could materially adversely affect our business relationships, our ability to obtain future financing on favorable terms or otherwise harm our business. In addition, in the past, securities class action litigation has often been brought against a company following periods of volatility in the market price of its securities. This risk is especially acute for us because the extreme volatility of market prices of technology companies has resulted in a larger number of securities class action claims against them. Due to the potential volatility of our stock price, we may in the future be the target of similar litigation. Securities litigation could result in substantial costs and divert management's attention and resources. This could harm our business and cause the value of our stock to decline.

Use of a portion of our cash reserves to repurchase shares of our common stock presents potential risks and disadvantages to us and our continuing stockholders.

From November 2008 through September 2014, we repurchased and retired an aggregate of 8,048,851 shares of our common stock at a total cost of \$42.9 million, including 3,846,153 shares repurchased at a total cost of \$25 million pursuant to a modified "Dutch auction" tender offer that we completed in August 2014 and additional shares repurchased in the open market pursuant to our stock repurchase program. At September 30, 2014, we had outstanding authorization from our Board of Directors to purchase up to an additional \$12.1 million of our common

stock from time to time under our repurchase program. Although our Board has determined that these repurchases are in the best interests of our stockholders, they expose us to certain risks including:

- the risks resulting from a reduction in the size of our “public float,” which is the number of shares of our common stock that are owned by non-affiliated stockholders and available for trading in the securities markets, which may reduce the volume of trading in our shares and result in reduced liquidity and, potentially, lower trading prices;
- the risk that our stock price could decline and that we would be able to repurchase shares of our common stock in the future at a lower price per share than the prices we have paid in our tender offer and repurchase program; and
- the risk that the use of a portion of our cash reserves for this purpose has reduced the amount of cash that would otherwise have been available to pursue potential cash acquisitions or other strategic business opportunities.

Our executive officers, directors and entities affiliated with them hold a substantial percentage of our common stock.

As of September 30, 2014, our executive officers, directors and entities affiliated with them beneficially owned approximately 28% of our outstanding common stock. As a result, these stockholders will be able to exercise substantial influence over, and may be able to effectively control, matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, which could have the effect of delaying or preventing a third party from acquiring control over or merging with us.

The provisions of our charter documents might inhibit potential acquisition bids that a stockholder might believe are desirable, and the market price of our common stock could be lower as a result.

Our Board of Directors has the authority to issue up to 5,000,000 shares of preferred stock. Our Board of Directors can fix the price, rights, preferences, privileges and restrictions of the preferred stock without any further vote or action by our stockholders. The issuance of shares of preferred stock might delay or prevent a change in control transaction. As a result, the market price of our common stock and the voting and other rights of our stockholders might be adversely affected. The issuance of preferred stock might result in the loss of voting control to other stockholders. We have no current plans to issue any shares of preferred stock. Our charter documents also contain other provisions, which might discourage, delay or prevent a merger or acquisition, including:

- our stockholders have no right to remove directors without cause;
- our stockholders have no right to act by written consent;
- our stockholders have no right to call a special meeting of stockholders; and
- stockholders must comply with advance notice requirements to nominate directors or submit proposals for consideration at stockholder meetings.

These provisions could also have the effect of discouraging others from making tender offers for our common stock. As a result, these provisions might prevent the market price of our common stock from increasing substantially in response to actual or rumored takeover attempts. These provisions might also prevent changes in our management.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**Stock Repurchase Program**

On November 13, 2008, we announced that our Board of Directors had authorized us to repurchase, at management's discretion, shares of our common stock having an aggregate purchase price of up to \$10 million (the "Repurchase Program"). On January 26, 2012, we announced that the Board had increased the dollar value of shares that may be repurchased under the Repurchase Program by \$10 million, and, on August 21, 2013, we announced that the Board had further increased the dollar value by an additional \$10 million. Under the Repurchase Program, we may repurchase shares from time to time on the open market or in private transactions. The specific timing and amount of the repurchases are dependent on market conditions, securities law limitations and other factors. The Repurchase Program may be suspended or terminated at any time without prior notice.

On July 9, 2014, we announced the commencement of a modified "Dutch auction" self-tender offer to repurchase for cash shares of our common stock for an aggregate purchase price of up to \$25 million (the "Tender Offer"). The Tender Offer expired on August 6, 2014. On August 12, 2014, we announced that we had accepted for purchase under the Tender Offer an aggregate of 3,846,153 shares of our common stock at a final purchase price of \$6.50 per share.

Below is a summary of the repurchases of our common stock made during the quarter ended September 30, 2014:

Period	Shares Repurchased	Average Price per Share	Value of Shares That May Yet Be Repurchased Under the Repurchase Program or the Tender Offer
Beginning approximate dollar value available to be repurchased as of June 30, 2014			\$ 12,098,647 (1)
Additional dollar value of shares subject to the Tender Offer			\$ <u>25,000,000</u>
Dollar value available to be repurchased as of July 9, 2014			\$ 37,098,647
July 1 to July 31, 2014	—	\$ —	\$ 37,098,647
August 1 to August 31, 2014	3,846,153 (2)	\$ 6.50	\$ 12,098,647
September 1 to September 30, 2014	—	\$ —	\$ <u>12,098,647</u>
Total shares repurchased	<u>3,846,153</u>		
Ending approximate dollar value that may be repurchased as of September 30, 2014			\$ <u>12,098,647 (1)</u>

(1) Shares available for repurchase under the Repurchase Program.

(2) Shares repurchased pursuant to the Tender Offer.

Item 6. Exhibits

Exhibit Number	Name of Document
10.1	Factory lease agreement dated August 22, 2014 for 30 Tai Yuan Street, Chu-Pei City, Taiwan between Registrant, as lessee, and Tai Yuan Textile Co., Ltd., as lessor (Incorporated by reference to Exhibit 10.1 to Registrant's Current Report on Form 8-K filed on August 28, 2014)
10.2(1)	GSI Technology, Inc. Executive Retention and Severance Plan (Incorporated by reference to Exhibit 10.1 to Registrant's Current Report on 8-K filed on October 3, 2014)
31.1	Certification of Lee-Lean Shu, President and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Douglas M. Schirle, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Lee-Lean Shu, President and Chief Executive Officer, and Douglas M. Schirle, Chief Financial Officer, 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

(1) Compensatory plan or management contract

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: November 10, 2014

GSI Technology, Inc.

By: /s/ LEE-LEAN SHU
 Lee-Lean Shu
 President, Chief Executive Officer and Chairman

By: /s/ DOUGLAS M. SCHIRLE
 Douglas M. Schirle
 Chief Financial Officer

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(1) Compensatory plan or management contract

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT
TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Lee-Lean Shu, certify that:

1. I have reviewed this quarterly report on Form 10-Q of GSI Technology, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting, which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 10, 2014

/s/ LEE-LEAN SHU

Lee-Lean Shu

President and Chief Executive Officer

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT
TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Douglas M. Schirle, certify that:

1. I have reviewed this quarterly report on Form 10-Q of GSI Technology, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting, which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 10, 2014

/s/ DOUGLAS M. SCHIRLE

Douglas M. Schirle
Chief Financial Officer

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

In connection with the Quarterly Report of GSI Technology, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2014 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned officers of the Company, each certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 10, 2014

/s/ LEE-LEAN SHU

Lee-Lean Shu

President and Chief Executive Officer

/s/ DOUGLAS M. SCHIRLE

Douglas M. Schirle

Chief Financial Officer

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