

MINDSPEED TECHNOLOGIES, INC

Form 10-Q

February 06, 2013

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended December 28, 2012

OR

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

Commission file number: 001-31650

**MINDSPEED TECHNOLOGIES, INC.**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State of incorporation)

**01-0616769**  
(I.R.S. Employer  
Identification No.)

**4000 MacArthur Boulevard, East Tower**

**Newport Beach, California**  
(Address of principal executive offices)

**92660-3095**  
(Zip code)

**Registrant's telephone number, including area code:**

**(949) 579-3000**

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

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

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

Large accelerated filer  Accelerated filer

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

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

The number of outstanding shares of the Registrant's Common Stock as of January 25, 2013 was 42,177,885.

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**FORWARD-LOOKING STATEMENTS**

This Quarterly Report on Form 10-Q contains statements (including certain projections and business trends) relating to Mindspeed Technologies, Inc. that are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), and are subject to the safe harbor created by those sections. All statements included in this Quarterly Report on Form 10-Q, other than those that are purely historical, are forward-looking statements. Words such as expect, believe, anticipate, outlook, could, target, project, intend, plan, seek, estimate, assume and continue, as well as variations of such words and similar expressions, also identify forward-looking statements. Forward-looking statements in this Quarterly Report on Form 10-Q include, without limitation, statements regarding:

our belief that the resolution of certain legal proceedings will not have a material adverse effect on our financial condition, results of operations or cash flows;

the ability of our relationships with leading network infrastructure original equipment manufacturers to facilitate early adoption of our products, enhance our ability to obtain design wins and encourage adoption of our technology in the industry;

the growth prospects for the network infrastructure equipment and communications semiconductors markets, including increased demand for network capacity, the upgrade and expansion of existing networks and the build-out of networks in developing countries;

our belief that our diverse portfolio of semiconductor solutions, combined with our expertise in low-power semiconductor hardware and software and communication systems engineering, has positioned us to capitalize on some of the most significant trends in telecommunications spending;

our belief that we are well-situated in China and that fiber deployments are being rolled out by the country's major telecommunications carriers;

our plans to make substantial investments in research and development and participate in the formulation of industry standards;

our belief that we can maximize our return on our research and development spending by focusing our investment in what we believe are key growth markets;

the increasing trend toward industry consolidation and the effect it could have on our operating results;

the sufficiency of our existing sources of liquidity to fund our operations, research and development efforts, earnout payments, anticipated capital expenditures, working capital and other financing requirements, including interest payments on debt obligations, for at least the next 12 months, and to fund the \$15.0 million principal payment of our 6.50% convertible senior notes due in August 2013;

our restructuring plans, including timing, expected workforce reductions, the expected cost savings under our restructuring plans and the uses of those savings, the timing and amount of payments, the impact on our business, the amounts of future charges to complete our restructuring plans, including any future plans to reduce operating expenses and/or increase revenue;

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our intention to continue to expand our international business activities, including expansion of design and operations centers abroad, and the challenges associated with such expansion;

our expectations regarding the cyclical nature of the semiconductor industry; and

the impact of recent accounting pronouncements and the adoption of new accounting standards.

Our expectations, beliefs, anticipations, objectives, intentions, plans and strategies regarding the future are not

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guarantees of future performance and are subject to risks and uncertainties that could cause actual results, and actual events that occur, to differ materially from results contemplated by the forward-looking statement. These risks and uncertainties include, but are not limited to:

worldwide political and economic uncertainties and specific conditions in the markets we address;

fluctuations in our operating results and future operating losses;

cash requirements and terms and availability of financing;

successful and timely development and introduction of competitive new products;

the adverse effect our debt obligations may have on our financial condition;

constraints in the supply of wafers and other product components from our third-party manufacturers;

significant fluctuations in the price of our common stock;

pricing pressures and other competitive factors;

loss of or diminished demand from one or more key customers or distributors;

our acquisition of picoChip Inc. and its wholly owned subsidiaries;

doing business internationally and our ability to successfully and cost effectively establish and manage operations in foreign jurisdictions;

maintaining compliance with applicable governmental regulations;

the expense of and our ability to defend our intellectual property against infringement claims by others;

our ability to attract and retain qualified personnel;

substantial sales of the shares of our common stock issuable upon conversion of our convertible senior notes, exercise of outstanding warrants or shares issued in connection with the picoChip acquisition, could adversely affect our stock price or our ability to raise additional financing;

lengthy sales cycles;

order and shipment uncertainty;

our ability to obtain design wins and develop revenue from them;

product defects and bugs;

business acquisitions and investments; and

our ability to utilize our net operating loss carryforwards and certain other tax attributes.

The forward-looking statements in this report are subject to additional risks and uncertainties, including those set forth in Part II, Item 1A Risk Factors and those detailed from time to time in our other filings with the Securities and Exchange Commission, or the SEC. These forward-looking statements are made only as of the date hereof and, except as required by law, we undertake no obligation to update or revise any of them, whether as a result of new information, future events or otherwise.

Mindspeed® and Mindspeed Technologies® are registered trademarks of Mindspeed Technologies, Inc. Other brands, names and trademarks contained in this report are the property of their respective owners.

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****MINDSPEED TECHNOLOGIES, INC.****CONSOLIDATED CONDENSED BALANCE SHEETS****(unaudited, in thousands)**

	December 28, 2012	September 28, 2012
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 51,137	\$ 49,098
Receivables, net of allowance for doubtful accounts of \$328 at December 28, 2012 and \$356 at September 28, 2012	16,649	14,527
Inventories	9,199	10,482
Prepaid expenses and other current assets	5,300	10,497
<b>Total current assets</b>	<b>82,285</b>	<b>84,604</b>
Property, plant and equipment, net	17,510	16,031
Intangible assets, net	36,165	35,351
Goodwill	57,110	57,110
Other assets	4,190	4,000
<b>Total assets</b>	<b>\$ 197,260</b>	<b>\$ 197,096</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 8,371	\$ 9,262
Accrued compensation and benefits	5,363	6,401
Deferred income on sales to distributors	3,606	4,396
Deferred revenue	1,661	2,338
Line of credit - short term	5,521	5,511
Short term debt	15,866	15,384
Contingent consideration	1,866	1,876
Other current liabilities	9,589	10,661
<b>Total current liabilities</b>	<b>51,843</b>	<b>55,829</b>
Line of credit - long-term	8,000	8,000
Long-term debt	44,470	44,765
Other liabilities	6,853	6,767
<b>Total liabilities</b>	<b>111,166</b>	<b>115,361</b>
Commitments and contingencies (Note 7)		
<b>Stockholders Equity</b>		
Preferred stock, \$0.01 par value: 25,000 shares authorized; no shares issued or outstanding		
Common stock, \$0.01 par value, 100,000 shares authorized; 42,172 (December 28, 2012) and 41,551 (September 28, 2012) issued and outstanding shares		
	423	416
Additional paid-in capital	375,186	371,949



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Accumulated deficit	(289,437)	(290,507)
Accumulated other comprehensive loss	(78)	(123)
Total stockholders' equity	86,094	81,735
Total liabilities and stockholders' equity	\$ 197,260	\$ 197,096

See accompanying notes to consolidated condensed financial statements.

**Table of Contents****MINDSPEED TECHNOLOGIES, INC.****CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS****(unaudited, in thousands, except per share amounts)**

	Three Months Ended	
	December 28, 2012	December 30, 2011
Net revenue:		
Products	\$ 38,394	\$ 33,842
Intellectual property	6,000	90
Total net revenue	44,394	33,932
Cost of goods sold	15,094	14,219
Gross margin	29,300	19,713
Operating expenses:		
Research and development	15,597	15,008
Selling, general and administrative	9,610	10,130
Restructuring charges	1,572	
Total operating expenses	26,779	25,138
Operating income/(loss)	2,521	(5,425)
Interest expense	(1,389)	(387)
Other income, net	16	302
Income/(loss) before income taxes	1,148	(5,510)
Provision for income taxes	71	88
Net income/(loss)	\$ 1,077	\$ (5,598)
Net income/(loss) per share:		
Basic	\$ 0.03	\$ (0.17)
Diluted	\$ 0.03	\$ (0.17)
Weighted-average number of shares used in per share computation:		
Basic	39,497	32,900
Diluted	40,058	32,900

See accompanying notes to consolidated condensed financial statements.

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**MINDSPEED TECHNOLOGIES, INC.**

**CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME/(LOSS)**

**(in thousands)**

	Three Months Ended	
	December 28, 2012	December 30, 2011
Net income/(loss)	\$ 1,077	\$ (5,598)
Other comprehensive income/(loss):		
Foreign currency translation adjustments	45	(110)
Comprehensive income/(loss)	\$ 1,122	\$ (5,708)

See accompanying notes to consolidated condensed financial statements.

**Table of Contents****MINDSPEED TECHNOLOGIES, INC.****CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS****(unaudited, in thousands)**

	Three Months Ended	
	December 28, 2012	December 30, 2011
<b>Cash Flows From Operating Activities</b>		
Net income/(loss)	\$ 1,077	\$ (5,598)
Adjustments required to reconcile net income/(loss) to net cash provided by operating activities:		
Depreciation and amortization of property, plant and equipment	1,553	1,513
Amortization of license agreements	659	643
Amortization of intangibles	351	
Restructuring charges	1,471	
Stock-based compensation	2,671	2,150
Inventory provisions	367	699
Amortization of debt discount on convertible debt	244	144
Other non-cash items, net	125	(93)
Changes in assets and liabilities, net of acquisitions:		
Receivables	(2,193)	(590)
Inventories	916	2,428
Other assets, net	4,207	854
Accounts payable	(909)	(1,009)
Deferred income on sales to distributors	(790)	8
Restructuring charges	(909)	(528)
Accrued compensation and benefits	(1,134)	(2,481)
Accrued expenses and other current liabilities	(1,667)	1,627
Other liabilities, net	182	(113)
Net cash provided by/(used in) operating activities	6,221	(346)
<b>Cash Flows From Investing Activities</b>		
Purchases of property, plant and equipment	(2,227)	(1,570)
Payments under license agreements	(2,477)	(1,111)
Net cash used in investing activities	(4,704)	(2,681)
<b>Cash Flows From Financing Activities</b>		
Payments made on capital lease obligations	(67)	(173)
Borrowings under line of credit	1,250	
Payments made on line of credit	(1,240)	
Repurchase of restricted stock for income tax withholding	(216)	(264)
Proceeds from equity compensation programs	770	992
Net cash provided by financing activities	497	555
Effect of foreign currency exchange rates on cash	25	6
Net (decrease)/increase in cash and cash equivalents	2,039	(2,466)
Cash and cash equivalents at beginning of period	49,098	45,227
Cash and cash equivalents at end of period	\$ 51,137	\$ 42,761

See accompanying notes to consolidated condensed financial statements.

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(unaudited)

**1. Basis of Presentation and Significant Accounting Policies**

Mindspeed Technologies, Inc. (Mindspeed or the Company) designs, develops and sells semiconductor solutions for communications applications in the wireline and wireless network infrastructure equipment, which includes broadband access networks (fixed and mobile), enterprise networks and metropolitan and WAN (fixed and mobile) networks.

*Basis of Presentation* The consolidated condensed financial statements, prepared in accordance with generally accepted accounting principles (GAAP) in the United States of America, include the accounts of Mindspeed and each of its subsidiaries. All intercompany accounts and transactions among Mindspeed and its subsidiaries have been eliminated in consolidation. In the opinion of management, the accompanying consolidated condensed financial statements contain all adjustments, consisting of adjustments of a normal recurring nature and restructuring charges (Note 8), necessary to present fairly the Company's financial position, results of operations and cash flows in accordance with GAAP. The results of operations for interim periods are not necessarily indicative of the results that may be expected for a full year. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 28, 2012.

*Fiscal Periods* The Company's interim fiscal quarters end on the thirteenth Friday of each quarter. The first quarter of fiscal 2012 and 2011 ended on December 28, 2012 and December 30, 2011, respectively.

*Recent Accounting Standards* In October 2012, the FASB issued accounting guidance covering a wide range of Topics in the Accounting Standards Codification. These amendments include technical corrections and improvements to the Accounting Standards Codification and conforming amendments related to fair value measurements. The amendments in this update will be effective for fiscal periods beginning after December 15, 2012. The Company does not expect the adoption of this guidance to have a material impact on its financial position or results of operations.

*Significant Accounting Policies* There were no significant changes to the Company's significant accounting policies disclosed in its Annual Report on Form 10-K, filed on December 12, 2012, for the fiscal year ended September 28, 2012.

**2. Supplemental Financial Statement Data*****Inventories***

Inventories consisted of the following:

	December 28, 2012	September 28, 2012
	(in thousands)	
Work-in-process	\$ 3,321	\$ 3,957
Finished goods	5,878	6,525
<b>Total inventories</b>	<b>\$ 9,199</b>	<b>\$ 10,482</b>

***Intangible Assets, Net***

Intangible assets, net, consisted of licensed and acquired intangibles.

***Licensed Intangibles***

Licensed intangibles consisted mainly of licenses of intellectual property.

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	December 28, 2012 (in thousands)	September 28, 2012
Licensed intangibles	\$ 30,074	\$ 28,145
Accumulated amortization	(7,050)	(6,286)
<b>Licensed intangibles, net</b>	<b>\$ 23,024</b>	<b>\$ 21,859</b>
Weighted-average remaining life	65 months	59 months

Amortization of licensed intangible assets included in costs of goods sold was as follows:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
<b>Amortization expense of licensed intangibles</b>	<b>\$ 659</b>	<b>\$ 643</b>

Estimated future amortization of existing licensed intangible assets, is as follows:

	Licensed Intangible Assets Amortization by Fiscal Year						Total
	remainder of 2013	2014	2015	2016	2017	Thereafter	
	(in thousands)						
<b>Cost of goods sold</b>	<b>\$ 2,486</b>	<b>\$ 4,524</b>	<b>\$ 4,622</b>	<b>\$ 3,728</b>	<b>\$ 3,728</b>	<b>\$ 3,936</b>	<b>\$ 23,024</b>

*Acquired Intangibles*

Acquired intangibles consisted of the following:

	December 28, 2012			Weighted-Average Useful Life (in years)
	Gross	Accumulated Amortization (in thousands)	Net	
Trade names and trademarks	\$ 310	\$ (188)	\$ 122	1.5
Developed technology	11,800	(889)	10,911	12
Customer relationships	1,500	(192)	1,308	7
In-process research and development	800		800	Indefinite
	<b>\$ 14,410</b>	<b>\$ (1,269)</b>	<b>\$ 13,141</b>	



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	September 28, 2012			Weighted-Average Useful Life (in years)
	Gross	Accumulated Amortization (in thousands)	Net	
Trade names and trademarks	\$ 310	\$ (136)	\$ 174	1.5
Developed technology	11,800	(643)	11,157	12
Customer relationships	1,500	(139)	1,361	7
In-process research and development	800		800	Indefinite
	\$ 14,410	\$ (918)	\$ 13,492	

Amortization of acquired intangible assets included in the costs of goods sold and operating expense categories was as follows:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
Cost of goods sold	\$ 247	
Selling, general and administrative	104	
	\$ 351	

Estimated future amortization of existing acquired intangible assets, excluding IPR&D, is as follows:

	Acquired Intangible Assets Amortization by Fiscal Year						Total
	remainder of 2013	2014	2015	2016	2017	Thereafter	
	(in thousands)						
Cost of goods sold	\$ 736	\$ 983	\$ 983	\$ 983	\$ 983	\$ 6,242	\$ 10,910
Selling, general and administrative	284	214	214	214	214	291	1,431
	\$ 1,020	\$ 1,197	\$ 1,197	\$ 1,197	\$ 1,197	\$ 6,533	\$ 12,341

**Goodwill**

There was no change in the carrying amount of goodwill from September 28, 2012.

**Deferred Income on Sales to Distributors**

Deferred income on sales to distributors was as follows:

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	December 28, 2012	September 28, 2012
	(in thousands)	
Deferred revenue on shipments to distributors	\$ 3,947	\$ 4,722
Deferred cost of goods sold on shipments to distributors	(377)	(362)
Reserves	36	36
Deferred income on sales to distributors	\$ 3,606	\$ 4,396

**Other Liabilities**

Details of other liabilities were as follows:

	December 28, 2012	September 28, 2012
	(in thousands)	
<i>Current</i>		
Deferred rent	\$ 48	\$ 53
Capital lease obligations	264	321
Accrued royalties	364	379
Accrued license fees	486	860
Accrued income taxes	652	707
Restructuring	892	427
Accrued interest	683	913
Escrow payable	3,491	3,491
Accrued professional fees	900	837
Other	1,809	2,673
Total other current liabilities	9,589	\$ 10,661
<i>Long-term</i>		
Deferred rent	4,979	\$ 5,044
Capital lease obligations	58	68
Licensed intangibles payable	713	699
Other	1,103	956
Total other liabilities	\$ 6,853	\$ 6,767

**Computation of Net Income/(Loss) Per Share**

The following table presents the computation of net income/(loss) per share:

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	Three Months Ended	
	December 28, 2012	December 30, 2011
Earnings per share - basic		
Net income/(loss)	\$ 1,077	\$ (5,598)
Basic weighted average common shares outstanding	39,497	32,900
Earnings/(loss) per share - basic	\$ 0.03	\$ (0.17)
Basic weighted average common shares outstanding	\$ 39,497	\$ 32,900
Effect of dilutive securities:		
Convertible senior notes		
Dilutive stock awards	546	
Dilutive employee stock purchase plan shares	15	
Diluted weighted average common shares outstanding	40,058	32,900
Earnings/(loss) per share - diluted	\$ 0.03	\$ (0.17)

The following table presents the number of potentially dilutive shares of the Company's common stock excluded from the computation of diluted net income/(loss) per share as their effect would have been anti-dilutive:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
6.75% convertible senior notes	8,205	
6.50% convertible senior notes	3,165	3,165
Stock awards	3,728	3,140
Employee stock purchase plan shares		27
Warrants	6,109	6,109
Anti-dilutive weighted average common shares	21,207	12,441

**Net Revenue by Product Line**

Net revenue by new product lines was as follows:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
High-performance analog	\$ 19,190	\$ 14,344
Communication processors	14,630	19,226
Wireless infrastructure	4,574	272
Intellectual property	6,000	90
Total net revenue	\$ 44,394	\$ 33,932

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Net revenue by historical product lines was as follows:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
High-performance analog products	\$ 19,190	\$ 14,344
Communications convergence processing products	14,051	14,989
WAN communications products	5,153	4,509
Intellectual property	6,000	90
<b>Total net revenue</b>	<b>\$ 44,394</b>	<b>\$ 33,932</b>

In previous reporting periods, the Company reported the following three product lines: communications convergence processing, high-performance analog and WAN communications. As previously reported, communications convergence processing included small cell wireless equipment. Beginning this quarter, to better align with its investment focus and provide greater transparency into the execution of its growth business, the Company is reporting small cell wireless infrastructure revenues as a standalone category. The Company is also combining the communications convergence processing, excluding small cell wireless infrastructure revenues, and WAN businesses into communications processors. High-performance analog will remain unchanged. Therefore, the Company's three new product lines will be wireless infrastructure, communications processors and high-performance analog.

**Net Revenue by Geographic Area**

Revenue by geographic area, based upon country of destination, was as follows:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
Americas	\$ 11,510	\$ 5,516
Asia-Pacific	29,430	26,558
Europe, Middle East and Africa	3,454	1,858
<b>Total net revenue</b>	<b>\$ 44,394</b>	<b>\$ 33,932</b>

The Company believes a substantial portion of the products sold to original equipment manufacturers (OEMs) and third-party manufacturing service providers in the Asia-Pacific region are ultimately shipped to end-markets in the Americas and Europe.

**Research and Development Expenses**

The Company receives certain reimbursements from its customers related to the development of certain products or product features. In the first quarter of fiscal 2013, the Company offset \$252,000 in development expenses related to these services. The cost reduction is recognized when services are performed and customer acceptance has been received.

**Supplemental Cash Flow Information**

Non-cash investing and financing activities consisted of the following:

Three Months Ended

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	December 28, 2012	December 30, 2011
	(in thousands)	
Interest paid	\$ 1,329	\$
Income taxes paid, net of refunds received	125	41
Purchase of property and equipment on account	47	264
License of intellectual property on account	23	4,428
Leasehold improvements paid by landlord	805	

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The following direct customers and/or distributors accounted for 10% or more of net revenue in the periods presented:

	Three Months Ended	
	December 28, 2012	December 30, 2011
Customer A	31%	21%
Customer B	16%	20%

The following direct customers and/or distributors accounted for 10% or more of total accounts receivable at each period end:

	December 28, 2012	September 28, 2012
	Customer A	28%
Customer B	16%	19%

**3. Business Combination**

On February 6, 2012, the Company completed the acquisition of picoChip, Inc. and its wholly owned subsidiaries (picoChip). picoChip is a supplier of integrated system-on-chip (SoC) solutions for small cell base stations. Pursuant to the terms of the acquisition agreement, all of picoChip's outstanding shares were converted into the right to receive consideration consisting of cash and shares of the Company's common stock.

The acquisition-date fair value of the consideration transferred totaled \$64.3 million, which consisted of cash, common stock and contingent consideration. The cash consideration transferred upon the close of the acquisition was \$20.5 million, of which, \$14.3 million was deposited into an escrow account and a majority of the remaining \$6.2 million was used to pay the remainder of picoChip's outstanding debt. Claims against the escrow account can be made until June 30, 2013, which is subject to extension if outstanding claims against the escrow remain unresolved at that date. Due to the nature of the escrow account, the cash portion of the consideration transferred has been determined only provisionally and is subject to change pending the outcome of potential escrow claims. The accounting for such changes and the finalization of the net asset adjustment are discussed below.

The acquisition agreement contained provisions for additional earnout payments, contingent on the achievement of milestones relating to: (i) revenue associated with sales of certain picoChip products for the period beginning on the closing of the acquisition and ending on December 31, 2012; and (ii) product and business development milestones. The revenue milestone was not met and therefore the related liability was reduced to zero. The business development milestone was not achieved and therefore the earnout's fair value was reduced to zero. Although one of the product development milestones was achieved, the second product development milestone was not achieved within the required timeframe and therefore the product development earnouts' fair value was reduced from a total of \$4.5 million to \$2.5 million in the fourth quarter of fiscal 2012.

The Company has the right to offset its earnout payments, if any, with certain employee termination liabilities incurred subsequent to the close of the acquisition. The estimated employee termination liabilities have been discounted at a risk-free rate because the Company will not realize the benefit of these reductions to earnout payments until the earnout payments have been made. As of December 28, 2012, the offsetting employee termination expenses were estimated to be \$634,000, reducing the net contingent consideration liability from \$2.5 million to \$1.9 million, and are not included in the quantitative information tables in Note 4.

As discussed above, the cash portion of the purchase price has not been finalized. In particular, the acquisition agreement stipulates that the purchase price is to be reduced if the actual net assets as defined in the agreement are determined to be less than the estimated net assets. The Company and the picoChip selling shareholders' representative have not reached agreement on the amount of the actual net assets as of the acquisition date. Under generally accepted accounting principles, the measurement period for making adjustments to the purchase price allocation for business combinations ends one year after the acquisition date. Accordingly, any adjustment resulting from the resolution of this matter would be recorded in the Company's results of operations.



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**4. Fair Value Measurements**

ASC 820 defines fair value as the price that would be received from the sale of an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 establishes a three-level hierarchy for disclosure that is based on the extent and level of judgment used to estimate the fair value of assets and liabilities.

**Level 1** uses unadjusted quoted prices that are available in active markets for identical assets or liabilities. The Company's Level 1 assets include investments in money market funds.

**Level 2** uses inputs other than quoted prices included in Level 1 that are either directly or indirectly observable through correlation with market data. These include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; and inputs to valuation models or other pricing methodologies that do not require significant judgment because the inputs used in the model, such as interest rates and volatility, can be corroborated by readily observable market data.

**Level 3** uses one or more significant inputs that are unobservable and supported by little or no market activity, and reflect the use of significant management judgment. Level 3 assets and liabilities include those whose fair value measurements are determined using pricing models, discounted cash flow methodologies or similar valuation techniques and significant management judgment or estimation.

The following table represents financial assets and liabilities that the Company measured at fair value. The Company has classified these assets and liabilities in accordance with the fair value hierarchy set forth in ASC 820:



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	Fair Value as of December 28, 2012	Fair Value Measurements at December 28, 2012 Using Fair Value Hierarchy		
		Level 1 (in thousands)	Level 2	Level 3
<b>Assets</b>				
Money market fund	\$ 20,046	\$ 20,046	\$	\$
<b>Assets at fair value</b>	<b>\$ 20,046</b>	<b>\$ 20,046</b>	<b>\$</b>	<b>\$</b>
<b>Liabilities</b>				
Contingent consideration	\$ 1,866	\$	\$	\$ 1,866
<b>Liabilities at fair value</b>	<b>\$ 1,866</b>	<b>\$</b>	<b>\$</b>	<b>\$ 1,866</b>

	Fair Value as of September 28, 2012	Fair Value Measurements at September 28, 2012 Using Fair Value Hierarchy		
		Level 1 (in thousands)	Level 2	Level 3
<b>Assets</b>				
Money market fund	\$ 20,040	\$ 20,040	\$	\$
<b>Assets at fair value</b>	<b>\$ 20,040</b>	<b>\$ 20,040</b>	<b>\$</b>	<b>\$</b>
<b>Liabilities</b>				
Contingent consideration	\$ 1,876	\$	\$	\$ 1,876
<b>Liabilities at fair value</b>	<b>\$ 1,876</b>	<b>\$</b>	<b>\$</b>	<b>\$ 1,876</b>

The following table presents a reconciliation of the beginning and ending balances of the Company's liabilities measured and recorded at fair value on a recurring basis using significant unobservable inputs (Level 3) at December 28, 2012:

Balance as of September 28, 2012	Contingent Consideration (in thousands)	\$ 1,876
Additions		
Change in fair value of contingent consideration		(10)
Balance as of December 28, 2012		\$ 1,866

The fair value measurements of the contingent consideration discussed above were based primarily on significant inputs not observable in the market and thus represent a Level 3 measurement as defined in ASC 820. The key assumptions were as follows:

**Table of Contents**Quantitative Information about Level 3 Fair Value Measurements as of December 28, 2012  
Valuation

Liability	Fair Value	Technique (in thousands, except percentages)	Unobservable Inputs	Selected Input (Range)
Revenue Earnout	\$	N/A	Probability of Achieving	0.0%
Business Development Earnout	\$	N/A	Probability of Achieving	0.0%
Product Development Earnout (1 of 2)	\$	Income Approach	Probability of Achieving	0.0%
Product Development Earnout (2 of 2)	\$ 2,500	Income Approach	Probability of Achieving	100.0% (90.0% - 100.0%)

Quantitative Information about Level 3 Fair Value Measurements as of September 28, 2012  
Valuation

Liability	Fair Value	Technique (in thousands, except percentages)	Unobservable Inputs	Selected Input (Range)
Revenue Earnout	\$	N/A	Probability of Achieving	0.00%
Business Development Earnout	\$	N/A	Probability of Achieving	0.00%
Product Development Earnout (1 of 2)	\$	Income Approach	Probability of Achieving	0.00%
Product Development Earnout (2 of 2)	\$ 2,500	Income Approach	Probability of Achieving	100.0% (90.0% - 100.0%)

As of December 28, 2012, the offsetting employee termination expenses and costs expected to be incurred to achieve the product development earnout were estimated to be \$634,000 and are not included in the above tables.

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Intangible asset valuations completed in connection with the Company's acquisition of picoChip have been based on level 3 inputs. The following table represents the Company's acquired intangible assets subject to fair value measurements that were based primarily on significant inputs not observable in the market and thus represent a Level 3 measurement as defined in ASC 820:

Quantitative Information about Level 3 Fair Value Measurements as of February 6, 2012				
Asset	Fair Value	Valuation		
		Technique (in thousands, except percentages)	Unobservable Inputs	Selected Input (Range)
Trade Names and Trademarks	\$ 310	Relief from Royalty	Revenue Projections	12.5% Market Share
Developed Technology	\$ 11,800	Relief from Royalty	Estimated Useful Life	2 years (1 year - 3 years)
			Revenue Attrition	5.0% - 10.0% (5.0% - 10.0%)
IPR&D	\$ 800	Income Approach	Core Revenue Attributable	25.0% (15.0% - 35.0%)
			Base Revenue Projections	12.5% Market Share
			Revenue Attrition	5.0% (5.0% - 10.0% per Year)
			Expected Product Cycle	5 Years (3 Years to 7 Years)
Customer Relationships	\$ 1,500	Multi-Period Excess Earnings	Base Revenue Projections	12.5% Market Share
			Revenue Attrition	20.0% (19.3% - 20.8% per Year)
			Base Revenue Projections	12.5% Market Share
			Margin Improvement	80.0% (60.0% - 90.0% of Sales and Executive Professional Time)
			Estimated Useful Life	7 Years (5 Years to 10 Years)

**5. Stock-Based Compensation**

The Company has stock-based incentive plans in effect that provide for the grant of stock options, unrestricted stock, restricted stock units and other stock-awards to employees and non-employee directors. These stock-based incentive plans include inducement grants that are occasionally made to new employees of the Company. The Company also provides an employee stock purchase plan for all eligible employees. The fair value of stock-based awards are estimated on the date of grant and recognized as an expense ratably over the requisite service period.

The following table presents stock-based compensation by functional line item presented on the unaudited consolidated condensed statements of operations:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
Cost of goods sold	\$ 45	\$ (43)
Research and development	913	652
Selling, general and administrative	1,713	1,541
Total stock-based compensation	\$ 2,671	\$ 2,150

A management bonus accrual of \$380,000 was recorded during the three months ended December 28, 2012. The Company expects to pay 75% of the bonus in cash and 25% in equity awards. The equity award portion of the bonus is included in the selling, general and administrative line item in the above table.

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Stock option grant date fair value was estimated using the Black-Scholes pricing model with the following weighted-average assumptions:

	Three Months Ended	
	December 28, 2012	December 30, 2011
<b>Weighted-average assumptions:</b>		
Expected option life	*	3.5 years
Risk-free interest rate	*	0.6%
Expected volatility	*	91%
Dividend yield	*	
Weighted-average grant date fair value per share	*	\$ 3.26

\* No stock options were granted during the period.

*Stock Option Awards*

The following tables summarize stock option activity:

	Number of Shares (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding at September 28, 2012	2,375	\$ 6.71	5.1 years	\$ 648
Granted				
Exercised	(73)	2.10		
Forfeited or expired	(143)	9.27		
Outstanding at December 28, 2012	2,159	\$ 6.69	5.2 years	\$ 998
Vested and expected to vest	2,085	\$ 6.69	5.2 years	\$ 991
Exercisable at December 28, 2012	1,330	\$ 6.61	4.3 years	\$ 920

Vesting Condition	Remaining Unrecognized Compensation Cost (in thousands)	Remaining Years to Vest
Service-based	\$ 2,245	0.9

*Stock Awards*

The following tables summarize stock award activity:

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	Number of Shares  (in thousands)	Weighted- Average Grant Date Fair Value	Fair Value of Shares Vested (in thousands)
Outstanding at September 28, 2012	2,620	\$ 6.29	
Granted	344	3.63	
Vested	(225)	6.99	\$ 774
Forfeited	(167)	8.22	
Outstanding at December 28, 2012	2,572	\$ 6.09	
		Remaining Unrecognized Compensation Cost (in thousands)	Remaining Years to Vest
Vesting Condition			
Service-based		11,447	0.9
Market-based		5	0.1
Stock awards		11,452	

**6. Revolving Credit Facilities and Long-Term Debt****6.75% Convertible Senior Notes**

On June 19, 2012, the Company sold \$32.0 million in aggregate principal amount of its 6.75% Convertible Senior Notes due 2017, or the 6.75% convertible notes, for net proceeds of \$30.6 million. Interest on the 6.75% convertible notes will be paid semi-annually in arrears in cash at a rate of 6.75% per year on the principal amount, accruing from June 19, 2012. The 6.75% convertible notes will mature on June 15, 2017, unless earlier repurchased, redeemed or converted. The 6.75% convertible notes are fully and unconditionally guaranteed on a senior, unsecured basis by certain of the Company's subsidiaries.

The 6.75% convertible notes are convertible at an initial conversion rate of 256.4103 shares of the Company's common stock per \$1,000 principal amount of 6.75% convertible notes, subject to adjustment in certain circumstances. This is equivalent to an initial conversion price of \$3.90 per share of common stock. Holders may convert the 6.75% convertible notes at any time prior to the close of business on the second scheduled trading day immediately preceding June 15, 2017. If the Company undergoes certain fundamental changes prior to maturity of the notes, including a change of control, sale of all or substantially all of the assets of the Company, a liquidation or dissolution of the Company, the failure of the common stock to be listed or quoted on any of The New York Stock Exchange, The NASDAQ Global Select Market or The NASDAQ Global Market, and certain other events as more fully described in the indenture relating to the 6.75% convertible notes, a holder thereof will have the option to require the Company to repurchase for cash all or any portion of such notes at a repurchase price equal to 100% of the principal amount of the notes being repurchased, plus accrued and unpaid interest (including additional interest, if any) to, but excluding, the repurchase date.

On or after June 15, 2013, in the event that the last reported price of the Company's common stock exceeds the conversion price then in effect for 20 or more trading days during any 30 consecutive trading day period ending within five trading days prior to the date the Company receives a notice of conversion, the Company will, in addition to delivering shares upon conversion of the 6.75% convertible notes (and cash in lieu of fractional shares), make a make-whole premium payment in cash, shares of Company common stock or a combination thereof, subject to certain limitations, at the option of the Company, equal to the sum of the remaining scheduled payments of interest that would have been made on the 6.75% convertible notes to be converted had such notes remained outstanding through the earlier of the date that is three years after the date the Company receives the notice of conversion and June 15, 2017. If the Company elects to pay some or all of the make-whole premium in shares of the Company's common stock, then the

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number of shares of common stock a holder will receive will be that number of shares that have a value equal to the amount of the make-whole premium payment to be paid to such holder in shares, divided by the product of 0.97 and the average of the last reported sale prices of the common stock for the five trading days immediately preceding, and including, the third trading day immediately prior to the conversion date; provided that in no event will such price be less than \$3.00.

The Company can redeem all or any part of the 6.75% convertible notes for cash on or after June 15, 2015 if the last reported sale price of its common stock exceeds 150% of the conversion price then in effect for at least 20 trading days during any 30 consecutive trading day period ending within five trading days prior to the notice of redemption and certain other conditions are met (referred to as the provisional redemption). The redemption price will equal the principal amount of the convertible notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date, plus a make-whole premium payment in cash, shares of the Company's common stock or a combination thereof, subject to certain limitations, at the option of the Company, equal to the sum of the remaining scheduled payments of interest that would have been made on the 6.75% convertible notes to be redeemed had such notes remained outstanding from the redemption date to June 15, 2017. If the Company elects to pay some or all of the make-whole premium in shares of the Company's common stock, then the number of shares of common stock a holder will receive will be that number of shares that have a value equal to the amount of the make-whole premium payment to be paid to such holder in shares, divided by the product of 0.97 and the average of the last reported sale prices of the Company's common stock for the five trading days immediately preceding, and including, the third trading day immediately prior to the redemption date; provided that in no event will such price be less than \$3.00.

If there is an event of default under the notes, the principal of and premium, if any, on all the notes and the interest accrued thereon may be declared immediately due and payable, subject to certain conditions set forth in the indenture. Events of default under the indenture include, but are not limited to, the Company: (i) becoming delinquent in making certain payments due under the notes; (ii) failing to deliver shares of common stock or cash upon conversion of the notes; (iii) failing to deliver certain required notices under the notes; (iv) incurring certain events of default with respect to other indebtedness or obligations; (v) becoming subject to certain bankruptcy proceedings or orders; or (vi) failing to pay or the acceleration of other indebtedness. If the Company fails to file certain periodic reports with the SEC, it will be required to make additional interest payments. As of December 28, 2012, no events of default have occurred.

The indenture relating to the 6.75% convertible notes contains a covenant that limits the Company's ability to incur Indebtedness, as that term is defined in the indenture, secured by a lien on the Company's assets or any Indebtedness that is senior to, or pari passu to, the 6.75% convertible notes, or permit any subsidiary to do so, other than a senior secured credit facility financing in an aggregate principal amount not to exceed \$35 million, and any subsidiary guarantees required thereunder, or any other Indebtedness outstanding as of the date of the indenture.

For financial accounting purposes, the requirements for the Company to make additional interest payments in the event of early redemption by the Company and to make additional interest payments in the event that the Company does not timely file certain periodic reports with the SEC are embedded derivatives. As of December 28, 2012, the fair value of these embedded derivatives has been estimated and is not significant. The Company's contingent obligation to make an interest make-whole premium payment in the event of an early conversion by the holders of the notes is also an embedded derivative. As of December 28, 2012, the fair value of this contingent obligation has been estimated at \$253,000 and is recorded in other liabilities.

The estimated fair value of these notes as of December 28, 2012 was approximately \$40.6 million and was calculated using an option pricing model with Level 3 inputs. Key assumptions used in the calculation of this fair value include a volatility of 83.6%, based on the implied volatility of a Mindspeed publicly traded call option, a debt discount rate of 9.0% and discount for lack of marketability of 10.0%.

The Company incurred \$492,000 of debt issuance costs, which is being amortized to interest expense over the term of the convertible notes through June 15, 2017 using the effective interest method. At December 28, 2012, debt issuance costs of \$438,000, net of accumulated amortization, were included in other assets.

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The following table sets forth balance sheet information related to the 6.75% convertible senior notes:

	December 28, 2012	September 28, 2012
	(in thousands)	
Principal value of the liability component	\$ 32,000	\$ 32,000
Unamortized value of the debt discount	(1,405)	(1,484)
<b>Net carrying value of the liability component</b>	<b>\$ 30,595</b>	<b>\$ 30,516</b>

The following table sets forth interest expense information related to the 6.75% convertible senior notes:

	December 28, 2012	Three Months Ended December 30, 2011
	(in thousands)	
Interest expense - coupon	\$ 548	\$
Interest expense - debt discount amortization	80	
<b>Total</b>	<b>\$ 628</b>	<b>\$</b>
Effective interest rate on the liability for the period	7.85%	0.00%

**Loan and Security Agreement**

A loan and security agreement was entered into between the Company and Silicon Valley Bank (SVB) on February 6, 2012, as amended by that certain first amendment to the loan and security agreement entered into on June 12, 2012. The loan and security agreement includes: (i) a term loan facility of \$15.0 million; and (ii) a revolving credit facility of up to \$20.0 million. As of December 28, 2012, the outstanding balance on the term loan was \$15.0 million and the outstanding balance on the revolving credit facility was \$13.5 million. The obligations under the loan and security agreement are guaranteed by material subsidiaries of the Company and secured by a security interest in substantially all of the Company's assets and the Company's guarantors' assets, excluding intellectual property.

The principal on the term loan will be payable in quarterly installments beginning on March 31, 2013 and ending on the maturity date of the term loan, February 6, 2017. Quarterly principal payments of \$375,000 are due for each quarter during calendar year 2013, \$750,000 for each quarter during calendar year 2014, \$1.1 million for each quarter during calendar year 2015 and \$1.5 million for each quarter during calendar year 2016. Interest on the term loan will be paid quarterly beginning in calendar year 2012. The revolving credit facility also has a maturity date of February 6, 2017. Interest on the revolving credit facility will be paid quarterly beginning in calendar year 2012.

The total amount available under the revolving credit facility is \$20.0 million. The Company is eligible to borrow amounts against the revolving credit facility up to the amount allowable by the borrowing base. The borrowing base is calculated on a monthly basis and is based on the amount of the Company's eligible accounts receivable. At December 28, 2012, the Company's outstanding revolving credit facility balance of \$13.5 million totalled the entire amount of the eligible borrowing base. To the extent that the eligible borrowing base is reduced, the Company is required to pay down the outstanding revolving credit facility balance to the amount of the eligible borrowing base. During the next 12 months, the Company expects the borrowing base will be sufficient to maintain borrowings on the revolving credit facility at a minimum of \$8.0 million. Consequently, it has classified \$8.0 million of the revolving credit facility as a long-term liability.

The Company has the option to choose, with a few exceptions, whether the term loan facility and the revolving credit facility bear interest based on a base rate, which is the prime rate published in The Wall Street Journal, or a LIBOR rate, which has a floor of 0.75%. A base rate facility will bear interest ranging from the base rate plus 1.25% to base rate plus 1.75%. A LIBOR rate facility will bear interest ranging from LIBOR rate plus 3.25% to LIBOR rate plus 3.75%. Both the base rate margin and LIBOR margin vary based upon the Company's liquidity ratio. As of December 28, 2012, the interest rate on both the term loan facility and the revolving credit facility was 4.25%. Total interest expense incurred on the term loan facility and revolving credit facility was \$306,000 for the three months ended December 28, 2012.





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The revolving credit facility is subject to an unused line of credit fee. This fee is payable quarterly in an amount equal to 0.25% - 0.50% of the average daily unused portion of the credit facility. The unused line fee will vary based upon the Company's liquidity ratio.

The loan and security agreement requires the Company to meet certain requirements relating to a liquidity ratio and minimum cash and cash equivalent levels. If the Company fails to maintain the liquidity ratio and cash and cash equivalent levels within certain targets, the Company will be required to maintain covenants relating to adjusted EBITDA and a fixed charge coverage ratio.

The Company incurred approximately \$537,000 of debt issuance costs related to the loan and security agreement, which are being amortized to interest expense over the term of the facility through February 6, 2017 using the effective interest method. At December 28, 2012, debt issuance costs of \$422,000, net of accumulated amortization, were included in other assets.

**6.50% Convertible Senior Notes**

On July 30, 2008, the Company entered into separate exchange agreements with certain holders of its previously outstanding 3.75% convertible senior notes, pursuant to which holders of an aggregate of \$15.0 million of the notes agreed to exchange their notes for \$15.0 million in aggregate principal amount of a new series of 6.50% convertible senior notes due in August 2013 (the Exchange Offer). The Exchange Offer closed on August 1, 2008. The Company paid at the closing an aggregate of approximately \$100,000 in accrued and unpaid interest on the 3.75% convertible senior notes that were exchanged for the 6.50% convertible senior notes, as well as approximately \$900,000 in transaction fees.

The 6.50% convertible senior notes are convertible at the option of the holders, at any time on or prior to maturity, into shares of the Company's common stock at a conversion rate initially equal to approximately \$4.74 per share of common stock, which is subject to adjustment in certain circumstances. Upon conversion of the notes, the Company generally has the right to deliver to the holders thereof, at the Company's option: (i) cash; (ii) shares of the Company's common stock; or (iii) a combination thereof. The initial conversion price of the 6.50% convertible senior notes will be adjusted to reflect stock dividends, stock splits, issuances of rights to purchase shares of the Company's common stock, and upon other events. If the Company undergoes certain fundamental changes prior to maturity of the notes, the holders thereof will have the right, at their option, to require it to repurchase for cash some or all of their 6.50% convertible senior notes at a repurchase price equal to 100% of the principal amount of the notes being repurchased, plus accrued and unpaid interest (including additional interest, if any) to, but not including, the repurchase date, or convert the notes into shares of its common stock and, under certain circumstances, receive additional shares of its common stock in the amount provided in the indenture.

The estimated fair value of these notes as of December 28, 2012 was approximately \$15.2 million and was calculated using an option pricing model with Level 3 inputs. Key assumptions used in the calculation of this fair value include a volatility of 60.6%, based on the implied volatility of a Mindspeed publicly traded call option, a debt discount rate of 9.0% and discount for lack of marketability of 10.0%.

The Company's contingent obligation to issue additional shares or make additional cash payment upon conversion following a fundamental change is considered an embedded derivative. As of December 28, 2012, the liability under the fundamental change adjustment has been recorded at its estimated fair value and is not significant.

The following table sets forth balance sheet information related to the 6.50% convertible senior notes:

	December 28, 2012	September 28, 2012
	(in thousands)	
Principal value of the liability component	\$ 15,000	\$ 15,000
Unamortized value of the debt discount	(259)	(366)
Net carrying value of the liability component	\$ 14,741	\$ 14,634

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The following table sets forth interest expense information related to the 6.50% convertible senior notes:

	Three Months Ended	
	December 28, 2012	December 30, 2011
	(in thousands)	
Interest expense - coupon	\$ 244	\$ 245
Interest expense - debt discount amortization	106	102
<b>Total</b>	<b>\$ 350</b>	<b>\$ 347</b>
Effective interest rate on the liability for the period	9.33%	9.25%

**7. Commitments and Contingencies**

Various lawsuits, claims and proceedings have been or may be instituted or asserted against the Company, including those pertaining to product liability, intellectual property, environmental, safety and health and employment matters. As is common in the industry, the Company currently has in effect a number of agreements in which it has agreed to defend, indemnify and hold harmless certain of its suppliers and customers from damages and costs which may arise from the infringement by the Company's products of third-party patents, trademarks or other proprietary rights. The Company has not incurred significant costs to defend lawsuits or settle claims related to these indemnification agreements.

The outcome of litigation cannot be predicted with certainty and some lawsuits, claims or proceedings may be determined unfavorably against the Company. Based on its evaluation of matters which are pending or asserted, while there can be no assurance, management of the Company believes the disposition of such matters will not have a material adverse effect on the financial condition or results of operations of the Company.

**8. Restructuring Charges**

The Company has, and may in the future, commit to restructuring plans to help manage the costs of the Company or to help implement strategic initiatives, among other reasons.

*Fourth Quarter of Fiscal 2012 Restructuring Plan* In the fourth quarter of fiscal 2012, the Company committed to the implementation of a restructuring plan, which consisted primarily of a headcount reduction in the Company's research and development functions and selling, general and administrative functions. The restructuring plan is expected to be substantially completed during the fourth quarter of fiscal 2013. The Company made the decision to implement the restructuring in furtherance of its efforts to reduce operating expenses and cash consumption. Approximately \$2.3 million in charges were incurred through the first quarter of fiscal 2013 related to this plan. Of the amounts incurred, \$2.1 million related to severance costs for affected employees and approximately \$206,000 related to contractual obligations on vacated office space. The Company currently expects to incur total charges ranging from approximately \$4.0 million to \$5.0 million, including cash expenditures ranging from approximately \$3.5 million to \$4.5 million, each primarily related to severance costs for affected employees.

Activity and liability balances related to the Company's fourth quarter of fiscal 2012 restructuring plan from September 28, 2012 through December 28, 2012 were as follows:

	Workforce Reductions (in thousands)	Facilities and Other (in thousands)	Total (in thousands)
Restructuring balance, September 28, 2012	\$ 382	\$	\$ 382
Charges to costs and expenses	1,362	210	1,572
Cash payments	(993)		(993)
Non-cash adjustments	(97)	(4)	(101)

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Restructuring balance, December 28, 2012	\$	654	\$	206	\$	860
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The remaining accrued restructuring balance principally represents employee severance costs and contractual obligations on vacated office space. The Company expects to pay these remaining employee severance obligations through the fourth quarter of fiscal 2013 and the remaining contractual obligations on vacated office space through the second quarter of fiscal 2015, the end of the related lease term.

*Fourth Quarter of Fiscal 2011 Restructuring Plan* In the fourth quarter of fiscal 2011, the Company implemented a restructuring plan, which consisted primarily of a targeted headcount reduction in the selling, general and administrative functions and WAN product line, which is new part of the communications processors product line. The Company incurred \$1.2 million of charges related to severance costs for the affected employees. The restructuring plan was substantially completed during the fourth quarter of fiscal 2011.

Activity and liability balances related to the Company's fourth quarter of fiscal 2011 restructuring plan from September 28, 2012 through December 28, 2012 were as follows:

	Workforce Reductions (in thousands)
Restructuring balance, September 28, 2012	\$ 45
Cash payments	(13)
Restructuring balance, December 28, 2012	\$ 32

The remaining accrued restructuring balance principally represents employee severance costs. The Company expects to pay these remaining obligations through the third quarter of fiscal 2013.

**9. Income Taxes**

The Company utilizes the liability method of accounting for income taxes. The federal statutory rate was 34% for all periods. The difference between the Company's effective tax rate and the federal statutory rate for fiscal 2012 is primarily due to the full valuation allowance offsetting any current period benefit from operating losses and the effect of foreign earnings taxed at rates differing from the federal statutory rate. The difference between the Company's effective tax rate and the federal statutory rate for fiscal 2013 is primarily due to a change in the Company's valuation allowance offsetting any current period liability from operating gains and the effect of foreign earnings taxed at rates differing from the federal statutory rate.

**10. Related Party Transactions**

In June 2011, the Company entered into an agreement to license certain intellectual property from a related party. The licensor is a related party because one of the Company's directors also serves as a director of the licensor and one of the Company's members of management serves on the licensor's technical advisory board. Pursuant to terms of the license agreement, the Company will pay an aggregate of \$6.3 million upon the completion of certain milestones, including the delivery of licensed intellectual property. In addition, the Company is obligated to pay royalties not to exceed an additional \$2.2 million for products sold that include the licensed intellectual property. As of December 28, 2012, the Company has paid \$3.5 million in related license fees.

**11. Subsequent Events**

In January 2013, Clark Leips, a purported shareholder of the Company, filed a lawsuit against the Company and its board of directors in the United States District Court for the District of Delaware alleging, among other things, that the compensation and management development committee of the board of directors breached its fiduciary duties in each of calendar years 2009, 2010, 2011 and 2012 by approving equity incentive grants for the Company's chief executive officer that exceeded the respective sub-limitations under Section 5 of the Company's 2003 long-term incentives plan for grants to a single participant in any calendar year. Plaintiff also alleged that the disclosures in the proxy statement for the Company's 2013 annual meeting of stockholders are inadequate. The plaintiff seeks, among other things, injunctive relief, damages, rescission of the excess grants, disgorgement and attorney's fees. Plaintiff filed a motion to enjoin the Company's 2013 annual meeting of stockholders until the Company issued additional disclosures to supplement the proxy statement. On January 22, 2013, the Company filed a supplement to the proxy statement. The motion for an injunction was then withdrawn by the plaintiff. Management does not believe the resolution of this matter will result in a material adverse impact on the Company's financial position, results of operations or cash flows.



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

This information should be read in conjunction with our unaudited consolidated condensed financial statements and the notes thereto included in this Quarterly Report on Form 10-Q and our audited consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for our fiscal year ended September 28, 2012.

#### **Overview**

Mindspeed Technologies, Inc. designs, develops and sells semiconductor solutions for communications applications in wireline and wireless network infrastructure equipment, which includes broadband access networks (fixed and mobile), enterprise and metropolitan and wide area networks (WAN) (fixed and mobile). In previous reporting periods, we had organized our solutions for these interrelated and rapidly converging networks into three product lines: communications convergence processing, high-performance analog and WAN communications. As previously reported, communications convergence processing included small cell wireless equipment. Beginning this quarter, to better align with our investment focus and provide greater transparency into the execution of our growth business, we are reporting small cell wireless infrastructure revenues as a standalone category. We are also combining the communications convergence processing, excluding small cell wireless infrastructure revenues, and WAN businesses into communications processors. High-performance analog will remain unchanged. Therefore, our three product lines will be wireless infrastructure, communications processors and high-performance analog. Our wireless infrastructure products include ultra-low-power, multi-core digital signal processor (DSP) system-on-chip (SoC) products for the mobile (3G/4G) carrier infrastructure, including residential, and enterprise platforms. Our communications processors products include ultra-low-power, multi-core digital signal processor (DSP) system-on-chip (SoC) products for the fixed carrier infrastructure platforms and WAN communication products that help optimize today's circuit-switched networks that furnish much of the Internet's underlying long-distance infrastructure. Our high-performance analog products include high-density crosspoint switches, optical drivers, equalization and signal-conditioning solutions that solve difficult switching, timing and synchronization challenges in next-generation optical networking, enterprise storage and broadcast video transmission applications.

Our products are sold to original equipment manufacturers (OEMs) for use in a variety of network infrastructure equipment, including:

*Wireless Infrastructure* 3G/4G long-term evolution (LTE) wireless small cell base stations in the carrier infrastructure, including residential and enterprise;

*Communications Processors* triple-play access gateways for Voice-over-Internet Protocol (VoIP) and data processing platforms; broadband customer premises equipment (CPE) gateways and other equipment that carriers use to deliver voice, data and video services to residential subscribers; Internet Protocol (IP) private branch exchange (PBX) equipment and security appliances used in the enterprise and circuit-switched networking equipment that implements asynchronous transfer mode (ATM) and T1/E1 and T3/E3 communications protocols; and

*High-Performance Analog* next-generation fiber access network equipment (including passive optical networking, or PON, systems); switching and signal conditioning products supporting fiber-to-the-premise, optical transport networks (OTN), storage and server systems and broadcast video, inclusive of routers and other systems that are driving the migration to 3G high-definition (HD) transmission.

Our customers include Alcatel-Lucent SA, Cisco Systems, Inc., Huawei Technologies Co. Ltd., Hitachi Ltd., LM Ericsson Telephone Company, Mitsubishi Electric Corporation, Nokia Siemens Networks and Zhongxing Telecom Equipment Corp., among others.

#### **Trends and Factors Affecting Our Business**

Our products are components of network infrastructure equipment. As a result, we rely on network infrastructure OEMs to select our products from among alternative offerings to be designed into their equipment. These design wins

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are an integral part of the long sales cycle for our products. Our customers may need six months or longer to test and evaluate our products and an additional six months or more to begin volume production of equipment that incorporates our products. We believe our close relationships with leading network infrastructure OEMs facilitate early adoption of our products during development of their products, enhance our ability to obtain design wins and encourage adoption of our technology by the industry. We believe our diverse portfolio of semiconductor solutions has us well positioned to capitalize on some of the most significant trends in telecommunications spending, including: next generation network convergence; VoIP/fiber access deployment in developing and developed markets; 3G/4G wireless infrastructure build-out; the adoption of higher speed interconnectivity solutions; and the migration of broadcast video to HD.

We market and sell our semiconductor products directly to network infrastructure OEMs. We also sell our products indirectly through electronic component distributors and third-party electronic manufacturing service providers, who manufacture products incorporating our semiconductor networking solutions for OEMs. Sales to distributors accounted for approximately 63% of our net revenue for the first three months of fiscal 2013. Our revenue is well diversified globally, with 86% of net revenue for the first three months of fiscal 2013 coming from outside of the Americas. We believe a portion of the products we sell to OEMs and third-party manufacturing service providers in the Asia-Pacific region is ultimately shipped to end markets in the Americas and Europe. We believe we are well-situated in China, where fiber deployments are being rolled out by the country's major telecommunications carriers. Through our OEM customers, we are shipping into the fiber-to-the-building (FTTB) deployments of China Telecom, China Unicom and China Mobile. Approximately 29% of our net revenue for the first three months of fiscal 2013 was derived from customers in China.

We have significant research, development, engineering and product design capabilities. Our success depends to a substantial degree upon our ability to develop and introduce in a timely fashion new products and enhancements to our existing products that meet changing customer requirements and emerging industry standards. We have made, and plan to make, substantial investments in research and development and to participate in the formulation of industry standards. We spent approximately \$15.6 million on research and development in the first three months of fiscal 2013. We seek to maximize our return on our research and development spending by focusing our research and development investment in what we believe are key growth markets, including wireless infrastructure solutions for small cell base station processing, communications processors for VoIP and other high-bandwidth multiservice access applications, and high-performance analog applications such as optical networking and broadcast-video transmission. We have completed a series of cost reduction actions, which have improved our operating cost structure, and we will continue to perform additional actions, when necessary.

We are dependent upon third parties for the development, manufacturing, assembly and testing of our products. Our ability to bring new products to market, to fulfill orders and to achieve long-term revenue growth is dependent upon our ability to obtain sufficient external manufacturing capacity, including wafer fabrication capacity. Periods of upturn in the semiconductor industry may be characterized by rapid increases in demand and a shortage of capacity for wafer fabrication and assembly and test services. In such periods, we may experience longer lead times or indeterminate delivery schedules, which may adversely affect our ability to fulfill orders for our products. During periods of capacity shortages for manufacturing, assembly and testing services, our primary foundries and other suppliers may devote their limited capacity to fulfill the requirements of their other customers that are larger than we are, or who have superior contractual rights to enforce manufacture of their products, including to the exclusion of producing our products. The foundries and other suppliers on whom we rely may experience financial difficulties or suffer disruptions in their operations due to causes beyond our control, including deteriorations in general economic conditions, labor strikes, work stoppages, electrical power outages, fire, earthquake, flooding or other natural disasters. We may also incur increased manufacturing costs, including costs of finding acceptable alternative foundries or assembly and test service providers. In order to achieve sustained profitability and positive cash flows from operations, we may need to further reduce operating expenses and/or increase our revenue.

Our ability to achieve revenue growth will depend on increased demand for network infrastructure equipment that incorporates our products, which in turn depends primarily on the level of capital spending by communications service providers, the level of which may decrease due to general economic conditions and uncertainty, over which we have no control. We believe the market for network infrastructure equipment in general, and for communications semiconductors in particular, offers attractive long-term growth prospects due to increasing demand for network capacity, the continued upgrading and expansion of existing networks and the build-out of telecommunication networks in developing countries. However, the semiconductor industry is highly cyclical and is characterized by constant and rapid technological change, rapid product obsolescence and price erosion, evolving technical standards, short product life cycles and wide fluctuations in product supply and demand. In addition, there has been an increasing trend toward industry consolidation,

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particularly among major network equipment and telecommunications companies. Consolidation in the industry has generally led to pricing pressure and loss of market share. These factors have caused substantial fluctuations in our revenue and our results of operations in the past, and we may experience cyclical fluctuations in our business in the future.

**Critical Accounting Policies and Estimates**

The accounting policies that have the greatest impact on our financial condition and results of operations and that require the most judgment are those relating to inventories, stock-based compensation, revenue recognition, deferred income taxes and uncertain tax positions, business combinations, goodwill and other long-lived assets, and impairment of goodwill and other long-lived assets. These policies are described in further detail in our Annual Report on Form 10-K for the fiscal year ended September 28, 2012. There have been no significant changes in our critical accounting policies and estimates during the fiscal quarter ended December 28, 2012 as compared to what was previously disclosed in our Annual Report on Form 10-K for the fiscal year ended September 28, 2012.

**Recent Accounting Pronouncements**

In October 2012, the FASB issued accounting guidance covering a wide range of topics in the Accounting Standards Codification. These amendments include technical corrections and improvements to the Accounting Standards Codification and conforming amendments related to fair value measurements. The amendments in this update will be effective for fiscal periods beginning after December 15, 2012. We do not expect the adoption of this guidance to have a material impact on our financial position or results of operations.

**Results of Operations****Net Revenue by Product Line**

The following table summarizes fiscal quarter net revenue by our new product lines:

	December 28, 2012	Three Months Ended		December 30, 2011	% of Net Revenue	Change \$	%
		% of Net Revenue	% of Net Revenue				
			(in thousands, except percentages)				
High-performance analog	\$ 19,190	44%	\$ 14,344	42%	\$ 4,846	33.8%	
Communications processors	14,630	33%	19,226	57%	(4,596)	-23.9%	
Wireless infrastructure	4,574	9%	272	1%	4,302	1581.6%	
Total net product revenue	38,394	86%	33,842	100%	4,552	13.5%	
Intellectual property	6,000	14%	90	0%	5,910		
Net revenue	\$ 44,394	100%	\$ 33,932	100%	\$ 10,462	30.8%	



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The following table summarizes fiscal quarter net revenue by the historical product lines:

	December 28, 2012	Three Months Ended		December 30, 2011	% of Net Revenue	Change \$	% 
		% of Net Revenue	% of Net Revenue				
(in thousands, except percentages)							
High-performance analog products	\$ 19,190	43%	\$ 14,344	43%	\$ 4,846	33.8%	
Communications convergence processing products	14,051	32%	14,989	44%	(938)	-6.3%	
WAN communications products	5,153	11%	4,509	13%	644	14.3%	
Total net product revenue	38,394	86%	33,842	100%	4,552	13.5%	
Intellectual property	6,000	14%	90	0%	5,910		
Net revenue	\$ 44,394	100%	\$ 33,932	100%	\$ 10,462	30.8%	

Net revenue from high-performance analog products increased in the first quarter of fiscal 2013 when compared to the first quarter of fiscal 2012 due to increased demand for crosspoint switches and optical physical media devices. Net revenue from wireless infrastructure products also increased in the first quarter of fiscal 2013 when compared to the first quarter of fiscal 2012 due to increased shipments of our system-on-chip (SoC) products for small cell base stations. These increases were partially offset by a decrease in sales in communications processors products. Net revenue from our communications processors products decreased in the first quarter of fiscal 2013 when compared to the first quarter of fiscal 2012, despite a slight increase in Ethernet products for wide area networks. The decline is due to a slowdown in the infrastructure voice market, as well as a decrease in shipments of CPE products, which are used in broadband CPE gateways and other equipment that service providers are deploying in order to deliver voice, data and video services to residential subscribers.

In the first fiscal quarter of 2013, we also sold \$6.0 million in intellectual property compared to \$90,000 in intellectual property sales in the first fiscal quarter of 2012. We have developed and maintain a broad intellectual property portfolio, and we may periodically enter into strategic arrangements to leverage our portfolio by licensing or selling our intellectual property.

The demand environment was dynamic throughout the first quarter of fiscal 2013. Certain customers increased or accelerated product orders to earn financial incentives, while other customers requested product shipments that could not be supported due to standard manufacturing lead times exceeding the time between orders being placed and requested delivery dates. The net impact of these activities was an increase to net revenue of \$2.1 million for the three months ended December 28, 2012.

**Gross Margin**

Gross margin represents net revenue less cost of goods sold. As a fabless semiconductor company, we use third parties, including Taiwan Semiconductor Manufacturing Co., Ltd. (TSMC), Amkor Technology, Inc., Unisem, Inc. and Advanced Semiconductor Engineering, Inc. (ASE), for wafer fabrication and assembly and test services. Cost of goods sold primarily consisted of: purchased finished wafers; assembly and test services; royalty and other intellectual property costs; labor and overhead costs associated with product procurement; asset impairments; amortization of the cost of mask sets purchased; and sustaining engineering expenses pertaining to products sold.

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The following table presents fiscal quarter gross margin:

	December 28, 2012		Three Months Ended December 30, 2011		Change	
	\$	% of Net Revenue	\$	% of Net Revenue	\$	%
Gross margin	\$ 29,300	66%	\$ 19,713	58%	\$ 9,587	48.6%

(in thousands, except percentages)

Gross margin increased for the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 by approximately \$9.6 million due to a \$4.6 million, or 13.5%, increase in product revenue and a \$5.9 million increase in intellectual property revenue. The increase in our gross margin as a percent of net revenue for the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 was driven primarily by a change in product mix, as well as an increase in intellectual property revenue, which had no associated cost. These increases in gross margin as a percent of net revenue were partially offset by the amortization of acquired intangible assets related to the picoChip acquisition.

**Research and Development**

Research and development (R&D) expenses consisted primarily of: direct personnel costs, including stock-based compensation; photomasks; electronic design automation tools; and pre-production evaluation and test costs.

The following table presents details of fiscal quarter R&D expenses:

	December 28, 2012		Three Months Ended December 30, 2011		Change	
	\$	% of Net Revenue	\$	% of Net Revenue	\$	%
Personnel-related costs	\$ 9,473		\$ 8,965		\$ 508	5.7%
Stock-based compensation	913		652		261	40.0%
Design & development costs	2,117		2,954		(837)	-28.3%
Facilities	2,097		1,362		735	54.0%
Depreciation	765		592		173	29.2%
Other	232		483		(251)	-52.0%
Research and development	\$ 15,597	35%	\$ 15,008	44%	\$ 589	3.9%

(in thousands, except percentages)

R&D expenses increased modestly for the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 due to an increase in personnel-related costs. This increase was primarily due to the addition of personnel costs related to the picoChip R&D employees obtained during the second quarter of fiscal 2012. R&D expense also increased due to increased facilities and depreciation expense related to the additional facilities and property, plant and equipment obtained through the acquisition of picoChip. These increases were mostly offset by design and development cost reductions, as part of the restructuring plan we undertook in fiscal 2012.

**Selling, General and Administrative**

Our selling, general and administrative (SG&A) expenses include personnel costs, independent sales representative commissions and product marketing, applications engineering and other marketing costs. Our SG&A expenses also include costs of corporate functions, including accounting, finance, legal, human resources, information systems and communications.

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The following table presents details of fiscal quarter SG&A expenses:

	December 28,	Three Months Ended		Change		
	2012	% of Net Revenue	December 30, 2011	% of Net Revenue	\$	%
	(in thousands, except percentages)					
Personnel-related costs	\$ 5,051		\$ 5,056		\$ (5)	-0.1%
Stock-based compensation	1,713		1,541		172	11.2%
Professional fees & outside services	1,061		1,870		(809)	-43.3%
Facilities	508		781		(273)	-35.0%
Depreciation	166		186		(20)	-10.8%
Other	1,111		696		415	59.6%
Selling, general and administrative	\$ 9,610	22%	\$ 10,130	30%	\$ (520)	-5.1%

SG&A expenses decreased for the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 primarily due to a reduction in professional fees and outside services. In the first quarter of fiscal 2012, professional fees and outside services included approximately \$800,000 in expenses incurred related to the acquisition of picoChip which closed on February 6, 2012.

**Restructuring Charges**

We have, and may in the future, commit to restructuring plans to help manage our costs or to help implement strategic initiatives, among other reasons.

*Fourth Quarter of Fiscal 2012 Restructuring Plan* In the fourth quarter of fiscal 2012, we committed to the implementation of a restructuring plan, which consisted primarily of a headcount reduction in our research and development functions and selling, general and administrative functions. The restructuring plan is expected to be substantially completed during the fourth quarter of fiscal 2013. We made the decision to implement the restructuring in furtherance of our efforts to reduce operating expenses and cash consumption. Approximately \$2.3 million in net charges were incurred through the first quarter of fiscal 2013 related to this plan. Of the amounts incurred, \$2.1 million related to severance costs for affected employees and approximately \$206,000 related to contractual obligations on vacated office space.

Activity and liability balances related to our fourth quarter of fiscal 2012 restructuring plan from September 28, 2012 through December 28, 2012 were as follows:

	Workforce Reductions (in thousands)	Facilities and Other (in thousands)	Total (in thousands)
Restructuring balance, September 28, 2012	\$ 382	\$	\$ 382
Charges to costs and expenses	1,362	210	1,572
Cash payments	(993)		(993)
Non-cash adjustments	(97)	(4)	(101)
Restructuring balance, December 28, 2012	\$ 654	\$ 206	\$ 860

The remaining accrued restructuring balance principally represents employee severance costs and contractual obligations on vacated office space. We expect to pay these remaining employee severance obligations through the third quarter of fiscal 2013 and the remaining contractual obligations on vacated office space through the second quarter of fiscal 2015, the end of the related lease term.

*Fourth Quarter of Fiscal 2011 Restructuring Plan* In the fourth quarter of fiscal 2011, we implemented a restructuring plan, which consisted primarily of a targeted headcount reduction in the selling, general and administrative functions and (WAN) product line, which is now part of the communications processors product line. We incurred \$1.1



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million of charges related to severance costs for the affected employees during the fourth quarter of fiscal 2011. The restructuring plan was substantially completed during the fourth quarter of fiscal 2011. An additional \$138,000 of charges was incurred related to severance costs for the affected employees during the third quarter of fiscal 2012.

Activity and liability balances related to our fourth quarter of fiscal 2011 restructuring plan from September 28, 2012 through December 28, 2012 were as follows:

	Workforce Reductions (in thousands)
Restructuring balance, September 28, 2012	\$ 45
Cash payments	(13)
<b>Restructuring balance, December 28, 2012</b>	<b>\$ 32</b>

The remaining accrued restructuring balance principally represents employee severance costs. We expect to pay these remaining obligations through the third quarter of fiscal 2013.

**Interest Expense**

The following tables present details of fiscal quarter interest expense:

	December 28, 2012		Three Months Ended December 30, 2011		Change	
	\$	% of Net Revenue	\$	% of Net Revenue	\$	%
Interest expense	\$ 1,389	3%	\$ 387	1%	\$ 1,002	258.9%

(in thousands, except percentages)

In the first quarter of fiscal 2013, interest expense consisted of interest on our 6.75% convertible senior notes, our loan and security agreement and our 6.50% convertible senior notes. In the first quarter of fiscal 2012, interest expense primarily consisted of interest on our 6.50% convertible senior notes.

**Other Income, Net**

Other income, net, principally consisted of the change in fair value of contingent consideration, income from reimbursable foreign R&D incentives, foreign exchange gains and losses and other non-operating gains and losses. The following table presents details of fiscal quarter other income, net:

	December 28, 2012		Three Months Ended December 30, 2011		Change	
	\$	% of Net Revenue	\$	% of Net Revenue	\$	%
Other Income/(Expense), Net	\$ 16	0%	\$ 302	1%	\$ (286)	-94.7%

(in thousands, except percentages)

The decrease in other income, net, in the first quarter of fiscal 2013 compared to the first quarter of fiscal 2012 reflected a \$230,000 increase in net foreign exchange losses and a \$70,000 increase in the fair value of a contingent obligation on our 6.75% convertible senior notes.

**Income Taxes**

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Our provision for income taxes for the first quarter of fiscal 2013 and 2012 principally consisted of income taxes incurred by our foreign subsidiaries. As a result of our history of operating losses and the uncertainty of future operating results, we determined that it is more likely than not that the U.S. federal and state income tax benefits (principally net operating losses we can carry forward to future years) will not be realized. Based on available objective evidence, we

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believe it is more likely than not that our deferred tax assets will not be realized. Accordingly, we continue to provide a full valuation allowance against our U.S. federal and state net deferred tax assets at December 28, 2012. Should sufficient positive objectively verifiable evidence of the realization of our net deferred tax assets exist at a future date, we would reverse any remaining valuation allowance to the extent supported by estimates of future taxable income at that time.

**Liquidity and Capital Resources**

Our principal source of liquidity is our existing cash and cash equivalent balance.

In order to sustain profitability and positive cash flows from operations, we may need to further reduce operating expenses, increase our gross margin and/or increase revenue. We have recently completed a series of cost reduction actions, which have improved our operating expense structure, and we will continue to perform additional actions, if necessary. In addition, we may commit to additional restructurings to help implement strategic initiatives. These restructurings and other cost saving measures alone may not allow us to achieve profitability. Our ability to maintain, or increase, current revenue levels to achieve and sustain profitability will depend on demand for network infrastructure equipment that incorporates our products, which in turn depends primarily on the level of capital spending by communications service providers and enterprises, the level of which may decrease due to general economic conditions, and uncertainty, over which we have no control. We may be unable to increase current revenue levels or sustain past and future expense reductions in subsequent periods. We may not be able to achieve sustained profitability.

We are obligated to make an earnout payment, contingent upon the achievement of certain milestones, to the shareholders of picoChip. As of December 28, 2012, the estimated amount payable as a result of the achievement of these milestones was \$1.9 million. The earnout payment will be paid in the first quarter of calendar 2013. The payment may be made in the form of cash, stock or any combination thereof. We are also obligated to make a payment of approximately \$3.5 million to the picoChip escrow account related to a research and development tax credit.

We believe that our existing cash balances, cash expected to be generated from operations and our revolving credit facility will be sufficient to fund our operations, anticipated capital expenditures, working capital and other financing requirements, including interest payments on debt obligations, for at least the next 12 months. We have principal payments of \$375,000 due each quarter during calendar 2013 on our term loan with Silicon Valley Bank and \$15.0 million of principal payments due in August 2013 on our 6.50% convertible notes. We have no other principal payments on debt obligations for the next 12 months. We may acquire our debt securities through privately negotiated transactions, tender offers, exchange offers (for new debt or other securities), redemptions or otherwise, upon such terms and at such prices as we may determine appropriate. We will need to continue a focused program of capital expenditures to meet our research and development and corporate requirements. We may also consider acquisition opportunities to extend our technology portfolio and design expertise and to expand our product offerings. In order to fund capital expenditures, increase our working capital, re-pay debt or complete any acquisitions, we may seek to obtain additional debt or equity financing. We may also need to seek to obtain additional debt or equity financing if we experience downturns or cyclical fluctuations in our business that are more severe or longer than anticipated or if we fail to achieve anticipated revenue and expense levels. However, we cannot assure you that such financing will be available to us on favorable terms, or at all, particularly in light of recent economic conditions in the capital markets.

The following table presents details of our working capital and cash and cash equivalents:

	December 28, 2012	September 28, 2012 (in thousands)	Increase/ (Decrease)
Working capital	\$ 30,442	\$ 28,775	\$ 1,667
Cash and cash equivalents	\$ 51,137	\$ 49,098	\$ 2,039

Cash and cash equivalents increased as a result of cash provided by operating activities. The cash provided by operating activities was partially offset by cash used in our investing activities.

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The following table presents the major components of the consolidated statements of cash flows:

	Three Months Ended	
	December 28, 2012	December 30 2011
	(in thousands)	
Net cash provided by/(used in):		
Net income	\$ 1,077	\$ (5,598)
Non-cash operating expenses, net	7,441	5,056
Changes in operating assets and liabilities:		
Receivables	(2,193)	(590)
Inventories	916	2,428
Other assets, net	4,207	854
Accounts payable	(909)	(1,009)
Deferred income on sales to distributors	(790)	8
Restructuring charges	(909)	(528)
Accrued compensation and benefits	(1,134)	(2,481)
Accrued expenses and other current liabilities	(1,667)	1,627
Other liabilities, net	182	(113)
Net cash provided by operating activities	6,221	(346)
Net cash used in investing activities	(4,704)	(2,681)
Net cash provided by financing activities	497	555
Effect of foreign exchange rate changes on cash	25	6
Increase/(decrease) in cash and cash equivalents	\$ 2,039	\$ (2,466)

Operating activities generated cash for the first quarter of fiscal 2013 due to our net income and cash provided by net non-cash operating adjustments, partially offset by changes in operating assets and liabilities. Significant non-cash adjustments included stock-based compensation expense, restructuring charges, depreciation and amortization. Net income was also adjusted for a decrease in prepaid and other current assets due to the receipt of an international tax receivable related to our picoChip acquisition, as well as the collection of our tenant improvement incentives from the new operating lease of our corporate headquarters. Cash outflows related to an increase in our accounts receivable balance due to the timing of sales and the timing of cash collections. Cash outflows also related to a decrease in accrued restructuring charges due to payments made mainly on the restructuring plan implemented in the fourth quarter of fiscal 2012 and a decrease in accrued compensation and benefits mainly due to the timing of our payroll calendar.

Operating activities used cash for the first quarter of fiscal 2012 due to our net loss, partially offset by net non-cash operating activities and net cash provided by changes in operating assets and liabilities. Significant non-cash operating expenses included stock-based compensation expense, depreciation and amortization and amortization of licensed and purchased intangibles. The changes in operating assets and liabilities that had a significant impact on cash used in operating activities included cash provided by a decrease in inventories resulting from the sale of inventory purchased in prior periods in an effort to mitigate the effect of the natural disasters in Japan and an increase in accrued expenses and other current liabilities mainly due to accrued acquisition related costs. These cash inflows were mostly offset by a decrease in accounts payable due to the timing of payments and a decrease in accrued compensation and benefits due to the payment of bonuses under our fiscal 2011 cash bonus plan in the first quarter of fiscal 2012.

*Investing Activities*

Investing activities used cash for the first quarter of fiscal 2013 due to payments under license agreements of \$2.5 million and the purchase of property, plant and equipment of \$2.2 million.

Investing activities used cash for the first quarter of fiscal 2012 due to payments under licensed and purchased intangibles of \$1.1 million and the purchase of property, plant and equipment of \$1.6 million.





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*Financing Activities*

Financing activities provided cash for the first quarter of fiscal 2013 due to \$770,000 in proceeds from equity compensation programs. This cash inflow was partially offset by \$216,000 in payments made related to shares of our common stock withheld from, or delivered by, employees in order to satisfy applicable tax withholding obligations in connection with the vesting of restricted stock and \$67,000 in payments made on capital lease obligations.

Financing activities provided cash for the first quarter of fiscal 2012 due to \$1.0 million in proceeds from equity compensation programs, partially offset by \$264,000 in payments made related to shares of our common stock withheld from, or delivered by, employees in order to satisfy applicable tax withholding obligations in connection with the vesting of restricted stock and \$173,000 in payments made on capital lease obligations.

***Revolving Credit Facilities and Long-Term Debt***

*6.75% Convertible Senior Notes*

On June 19, 2012, we sold \$32.0 million in aggregate principal amount of our 6.75% convertible senior notes due 2017 for net proceeds of \$30.6 million. Interest on the 6.75% convertible notes is payable semi-annually on June 15 and December 15 in arrears in cash at a rate of 6.75% per year on the principal amount, accruing from June 19, 2012. The 6.75% convertible notes will mature on June 15, 2017, unless earlier repurchased, redeemed or converted. The 6.75% convertible notes are fully and unconditionally guaranteed on a senior, unsecured basis by certain of our subsidiaries. The effective interest rate was 7.85% for the first quarter of fiscal 2013. The interest expense for the \$32.0 million convertible debt for the first quarter of fiscal 2013 was \$628,000.

The 6.75% convertible notes are convertible at an initial conversion rate of 256.4103 shares of our common stock per \$1,000 principal amount of 6.75% convertible notes, subject to adjustment in certain circumstances. This is equivalent to an initial conversion price of \$3.90 per share of common stock. Holders may convert the 6.75% convertible notes at any time prior to the close of business on the second scheduled trading day immediately preceding June 15, 2017. If we undergo certain fundamental changes prior to maturity of the notes, including a change of control, sale of all or substantially all of our assets, our liquidation or dissolution, the failure of our common stock to be listed or quoted on any of The New York Stock Exchange, The NASDAQ Global Select Market or The NASDAQ Global Market, and certain other events as more fully described in the indenture relating to the 6.75% convertible notes, a holder thereof will have the option to require us to repurchase for cash all or any portion of such notes at a repurchase price equal to 100% of the principal amount of the notes being repurchased, plus accrued and unpaid interest (including additional interest, if any) to, but excluding, the repurchase date.

On or after June 15, 2013, in the event that the last reported price of our common stock exceeds the conversion price then in effect for 20 or more trading days during any 30 consecutive trading day period ending within five trading days prior to the date we receive a notice of conversion, we will, in addition to delivering shares upon conversion of the 6.75% convertible notes (and cash in lieu of fractional shares), make a make-whole premium payment in cash, shares of our common stock or a combination thereof, subject to certain limitations, at our option, equal to the sum of the remaining scheduled payments of interest that would have been made on the 6.75% convertible notes to be converted had such notes remained outstanding through the earlier of the date that is three years after the date we receive the notice of conversion and June 15, 2017. If we elect to pay some or all of the make-whole premium in shares of our common stock, then the number of shares of common stock a holder will receive will be that number of shares that have a value equal to the amount of the make-whole premium payment to be paid to such holder in shares, divided by the product of 0.97 and the average of the last reported sale prices of the common stock for the five trading days immediately preceding, and including, the third trading day immediately prior to the conversion date; provided that in no event will such price be less than \$3.00.

We can redeem all or any part of the 6.75% convertible notes for cash on or after June 15, 2015 if the if the last reported sale price of our common stock exceeds 150% of the conversion price then in effect for at least 20 trading days during any 30 consecutive trading day period ending within five trading days prior to the notice of redemption and certain other conditions are met (referred to as the provisional redemption). The redemption price will equal the principal amount of the convertible notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date, plus a make-whole premium payment in cash, shares of our common stock or a combination thereof, subject to certain limitations, at our option, equal to the sum of the remaining scheduled payments of interest that would have been made on the 6.75% convertible notes to be redeemed had such notes remained outstanding from the redemption date to June

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15, 2017. If we elect to pay some or all of the make-whole premium in shares of our common stock, then the number of shares of common stock a holder will receive will be that number of shares that have a value equal to the amount of the make-whole premium payment to be paid to such holder in shares, divided by the product of 0.97 and the average of the last reported sale prices of our common stock for the five trading days immediately preceding, and including, the third trading day immediately prior to the redemption date; provided that in no event will such price be less than \$3.00.

If there is an event of default under the notes, the principal of and premium, if any, on all the notes and the interest accrued thereon may be declared immediately due and payable, subject to certain conditions set forth in the indenture. An event of default under the indenture will occur if we: (i) are delinquent in making certain payments due under the notes; (ii) fail to deliver shares of common stock or cash upon conversion of the notes; (iii) fail to deliver certain required notices under the notes; (iv) incur certain events of default with respect to other indebtedness or obligations; (v) are subject to certain bankruptcy proceedings or orders; or (vi) fail to pay or the acceleration of other indebtedness. If we fail to file certain periodic reports with the SEC, we will be required to make additional interest payments. As of December 28, 2012, no events of default have occurred.

For financial accounting purposes, the requirements for us to make additional interest payments in the event of early redemption by us and to make additional interest payments in the event that we do not timely file certain periodic reports with the SEC are embedded derivatives. As of December 28, 2012, the fair value of these embedded derivatives has been estimated and is not significant. Our contingent obligation to make an interest make-whole premium payment in the event of an early conversion by the holders of the notes is also an embedded derivative. As of December 28, 2012, the fair value of this contingent obligation has been estimated at \$253,000 and is recorded in other liabilities.

We incurred \$492,000 of debt issuance costs, which is being amortized to interest expense over the term of the convertible notes through June 15, 2017 using the effective interest method. At December 28, 2012, debt issuance costs of \$438,000, net of accumulated amortization, was included in other assets.

*Loan and Security Agreement*

On February 6, 2012, we entered into a loan and security agreement between us and Silicon Valley Bank, as amended by that certain first amendment to the loan and security agreement entered into on June 12, 2012. The loan and security agreement includes: (i) a term loan facility of \$15.0 million; and (ii) a revolving credit facility of up to \$20.0 million. As of December 28, 2012, the outstanding balance on the term loan was \$15.0 million and the outstanding balance on the revolving credit facility was \$13.5 million. The obligations under the loan and security agreement are guaranteed by our material subsidiaries and secured by a security interest in substantially all of our assets and guarantors' assets, excluding intellectual property.

The principal on the term loan will be payable in quarterly installments beginning on March 31, 2013 and ending on the maturity date of the term loan, February 6, 2017. Quarterly principal payments of \$375,000 are due for each quarter during calendar year 2013, \$750,000 for each quarter during calendar year 2014, \$1.1 million for each quarter during calendar year 2015 and \$1.5 million for each quarter during calendar year 2016. Interest on the term loan will be paid quarterly beginning in calendar year 2012. The revolving credit facility also has a maturity date of February 6, 2017. Interest on the revolving credit facility is paid quarterly.

The total amount available under the revolving credit facility is \$20.0 million. We are eligible to borrow amounts against the revolving credit facility up to the amount allowable by the borrowing base. The borrowing base is calculated on a monthly basis and is based on the amount of our eligible accounts receivable. At December 28, 2012, we had an outstanding revolving credit facility balance of \$13.5 million and the amount of the eligible borrowing base was \$13.5 million. To the extent that the eligible borrowing base is reduced, we are required to pay down the outstanding revolving credit facility balance to the amount of the eligible borrowing base. During the next 12 months, we expect the borrowing base will be sufficient to maintain borrowings on the revolving credit facility at a minimum of \$8.0 million. Consequently, we have classified \$8.0 million of the revolving credit facility as a long-term liability.

We have the option to choose, with a few exceptions, whether the term loan facility and revolving credit facility bear interest based on a base rate, which is the prime rate published in The Wall Street Journal, or a LIBOR rate, which has a floor of 0.75%. A base rate facility will bear interest ranging from the base rate plus 1.25% to base rate plus 1.75%. A LIBOR rate facility will bear interest ranging from LIBOR rate plus 3.25% to LIBOR rate plus 3.75%. Both the base rate margin and LIBOR margin vary based upon our liquidity ratio. As of December 28, 2012, the interest rate on both the term loan facility and the revolving credit facility was 4.25%. Total interest expense incurred on the term loan facility and revolving credit facility was \$306,000 for the first quarter of fiscal 2013.



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The revolving credit facility is subject to an unused line of credit fee. This fee is payable quarterly in an amount equal to 0.25% - 0.50% of the average daily unused portion of the credit facility. The unused line fee will vary based upon our liquidity ratio.

The loan and security agreement requires us to meet certain requirements relating to a liquidity ratio and minimum cash and cash equivalent levels. If we fail to maintain the liquidity ratio and cash and cash equivalent levels within certain targets, we will be required to maintain covenants relating to adjusted EBITDA and a fixed charge coverage ratio. As of December 28, 2012, we have maintained the required liquidity ratio and cash and cash equivalent levels.

We incurred approximately \$537,000 of debt issuance costs related to the loan and security agreement, which is being amortized to interest expense over the term of the facility through February 6, 2017 using the effective interest method. At December 28, 2012, debt issuance costs of approximately \$422,000, net of accumulated amortization, was included in other assets.

*6.50% Convertible Senior Notes due 2013*

On July 30, 2008, we entered into separate exchange agreements with certain holders of our previously outstanding 3.75% convertible senior notes, pursuant to which holders of an aggregate of \$15.0 million of the notes agreed to exchange their notes for \$15.0 million in aggregate principal amount of a new series of 6.50% convertible senior notes due 2013. The exchange offer closed on August 1, 2008. We paid at the closing an aggregate of approximately \$100,000 in accrued and unpaid interest on the 3.75% convertible senior notes that were exchanged for the 6.50% convertible senior notes, as well as approximately \$900,000 in transaction fees.

We issued our 6.50% convertible senior notes due in August 2013 pursuant to an indenture, dated as of August 1, 2008, between us and Wells Fargo Bank, N.A., as trustee.

The 6.50% convertible senior notes are unsecured senior indebtedness and bear interest at a rate of 6.50% per annum. Interest is payable on February 1 and August 1 of each year. The notes mature on August 1, 2013. At maturity, we will be required to repay the outstanding principal amount of the notes. At December 28, 2012, \$15.0 million in aggregate principal amount of our 6.50% convertible senior notes were outstanding.

The 6.50% convertible senior notes are convertible at the option of the holders, at any time on or prior to maturity, into shares of our common stock at a conversion rate equal to approximately \$4.74 per share of common stock, which is subject to adjustment in certain circumstances. Upon conversion of the notes, we generally have the right to deliver to the holders thereof, at our option: (i) cash; (ii) shares of our common stock; or (iii) a combination thereof. The initial conversion price of the notes will be adjusted to reflect stock dividends, stock splits, issuances of rights to purchase shares of our common stock, and upon other events. If we undergo certain fundamental changes prior to maturity of the notes, the holders thereof will have the right, at their option, to require us to repurchase for cash some or all of their 6.50% convertible senior notes at a repurchase price equal to 100% of the principal amount of the notes being repurchased, plus accrued and unpaid interest (including additional interest, if any) to, but not including, the repurchase date, or convert the notes into shares of our common stock and, under certain circumstances, receive additional shares of our common stock in the amount provided in the indenture.

For financial accounting purposes, our contingent obligation to issue additional shares or make additional cash payment upon conversion following a fundamental change is an embedded derivative. At December 28, 2012, the liability under the fundamental change adjustment has been recorded at its estimated fair value and is not significant.

If there is an event of default under the 6.50% convertible senior notes, the principal of and premium, if any, on all the notes and the interest accrued thereon may be declared immediately due and payable, subject to certain conditions set forth in the indenture. An event of default under the indenture will occur if we: (i) are delinquent in making certain payments due under the notes; (ii) fail to deliver shares of common stock or cash upon conversion of the notes; (iii) fail to deliver certain required notices under the notes; (iv) fail, following notice, to cure a breach of a covenant under the notes or the indenture; (v) incur certain events of default with respect to other indebtedness; or (vi) are subject to certain bankruptcy proceedings or orders. If we fail to deliver certain SEC reports to the trustee in a timely manner as required

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by the indenture: (x) the interest rate applicable to the notes during the delinquency will be increased by 0.25% or 0.50%, as applicable (depending on the duration of the delinquency); and (y) if the required reports are not delivered to the trustee within 180 days after their due date under the indenture, a holder of the notes will generally have the right, subject to certain limitations, to require us to repurchase all or any portion of the notes then held by such holder. As of December 28, 2012, no events of default have occurred.

## **Contractual Obligations**

There have been no material changes to the amounts in our contractual obligations as of December 28, 2012, as previously disclosed in our Annual Report on Form 10-K for the fiscal year ended September 28, 2012.

## **Off-Balance Sheet Arrangements**

We have made guarantees and indemnities, under which we may be required to make payments to a guaranteed or indemnified party, in relation to certain transactions. In connection with a June 2003 distribution to stockholders of our former parent company of all outstanding shares of common stock of Mindspeed, we generally assumed responsibility for all contingent liabilities and then-current and future litigation against our former parent company or its subsidiaries related to our business. In connection with certain facility leases, we have indemnified our lessors for certain claims arising from the facility or the lease. We indemnify our directors, officers, employees and agents to the maximum extent permitted under the laws of the State of Delaware. The duration of the guarantees and indemnities varies, and in many cases is indefinite. The majority of our guarantees and indemnities do not provide for any limitation of the maximum potential future payments we could be obligated to make. We have not recorded any liability for these guarantees and indemnities in the accompanying unaudited consolidated condensed balance sheets.

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### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We do not use derivative instruments for speculative or investment purposes.

#### **Interest Rate Risk**

Our cash and cash equivalents are not subject to significant interest rate risk. As of December 28, 2012, the carrying value of our cash and cash equivalents approximated fair value.

At December 28, 2012, our debt consisted of a revolving credit facility, a term loan facility and short-term and long-term convertible senior notes. Our revolving credit facility and term loan facility carry variable interest rates and the interest payments are therefore subject to interest rate risk, while the principal is not subject to interest rate risk. We have the option to choose, with a few exceptions, whether the term loan facility and revolving credit facility bear interest based on a base rate, which is the prime rate published in The Wall Street Journal, or a LIBOR rate, which has a floor of 0.75%. If the prime rate or LIBOR rate changed by 1.0%, thereby changing our effective borrowing rate by the same amount, cash interest expense related to the credit facility and term loan facility would change by approximately \$300,000, annually. Our convertible senior notes bear interest at a fixed rate of 6.50% and 6.75% per annum. Consequently, our results of operations and cash flows are not subject to any significant interest rate risk relating to our convertible senior notes. The fair value of the debt could increase or decrease if interest rates decrease or increase, respectively, and that could impact our ability and cost to negotiate a settlement of such notes prior to maturity.

#### **Foreign Exchange Risk**

We transact business in various foreign currencies and we face foreign exchange risk on assets and liabilities that are denominated in foreign currencies. Currently, our foreign exchange risks are not hedged; however, from time to time, we may utilize foreign currency forward exchange contracts to hedge a portion of our exposure to foreign exchange risk.

These hedging transactions are intended to offset the gains and losses we experience on foreign currency transactions with gains and losses on the forward contracts, so as to mitigate our overall risk of foreign exchange gains and losses. We do not enter into forward contracts for speculative or trading purposes. At December 28, 2012, we held no foreign currency forward exchange contracts. Based on our overall currency rate exposure at December 28, 2012, a 10% change in currency rates would not have a material effect on our consolidated financial position, results of operations or cash flows.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### **Evaluation of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our chief executive officer and our chief financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of December 28, 2012. Disclosure controls and procedures are defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act), as controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within required time periods, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow for timely decisions regarding required disclosure. Based upon that evaluation, our chief executive officer and our chief financial officer have concluded that, as of December 28, 2012, these disclosure controls and procedures were effective.

#### **Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting, as defined in Rule 13a-15(f) of the Exchange Act, during the fiscal quarter ended December 28, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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### **PART II. OTHER INFORMATION**

#### **ITEM 1. LEGAL PROCEEDINGS**

In January 2013, Clark Leips, a purported shareholder of ours, filed a lawsuit against us and our board of directors in the United States District Court for the District of Delaware alleging, among other things, that the compensation and management development committee of the board of directors breached its fiduciary duties in each of calendar years 2009, 2010, 2011 and 2012 by approving equity incentive grants for our chief executive officer that exceeded the respective sub-limitations under Section 5 of our 2003 long-term incentives plan for grants to a single participant in any calendar year. The plaintiff also alleged that the disclosures in the proxy statement for our 2013 annual meeting of stockholders are inadequate. The plaintiff seeks, among other things, injunctive relief, damages, rescission of the excess grants, disgorgement and attorney's fees. The plaintiff filed a motion to enjoin our 2013 annual meeting of stockholders until we issued additional disclosures to supplement the proxy statement. On January 22, 2013, we filed a supplement to the proxy statement. The motion for an injunction was then taken off calendar. We do not believe the resolution of this matter will result in a material adverse impact on our financial position, results of operations or cash flows.

In addition, we are, from time to time, subject to legal proceedings and claims that arise in the normal course of our business. We do not believe that the ultimate outcome of any such currently pending matters, if any, arising in the normal course of business will have a material adverse effect on our financial position, results of operations or cash flows.

#### **ITEM 1A. RISK FACTORS**

We have revised the risk factors that relate to our business, as set forth below. These risks include any material changes to and supersede the risks previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended September 28, 2012. We encourage investors to review these risk factors, as well as those contained under "Forward-Looking Statements" preceding Part I of this Quarterly Report on Form 10-Q.

Our business, financial condition and operating results can be affected by a number of factors, including those listed below, any one of which could cause our actual results to vary materially from recent results or from our anticipated future results. Any of these risks could also materially and adversely affect our business, financial condition or the price of our common stock or other securities.

*Our operating results may be adversely impacted by worldwide economic uncertainties and specific conditions in the markets we address, including the cyclical nature of and volatility in the semiconductor industry.*

We operate in the semiconductor industry, which is cyclical and subject to rapid change and evolving industry standards. From time to time, the semiconductor industry has experienced significant downturns characterized by decreases in product demand, excess customer inventories and accelerated erosion of prices. The semiconductor industry also periodically experiences increased demand and production capacity constraints, which may affect our ability to ship products. Furthermore, during challenging economic times, our customers and vendors may face issues gaining timely access to sufficient credit, which could impact their ability to make timely payments to us. As a result, we may experience growth patterns that are different than the end demand for products, particularly during periods of high volatility. Accordingly, our operating results may vary significantly as a result of the general conditions in the semiconductor industry, which could cause large fluctuations in our stock price.

We cannot predict the timing, strength or duration of any economic slowdown or the impact it will have on our customers, our vendors or us. The combination of our lengthy sales cycle coupled with challenging macroeconomic conditions could have a compound impact on our business. The impact of market volatility is not limited to revenue, but may also affect our product gross margins and other financial metrics. Any downturns in the semiconductor industry could be severe and prolonged, and any failure of the industry or wired and wireless communications markets to fully recover from downturns could seriously impact our revenue and harm our business, financial condition and results of operations.



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*Our operating results are subject to substantial quarterly and annual fluctuations.*

We have incurred significant losses in prior periods. Our net revenue and operating results have fluctuated in the past and may fluctuate in the future and we may incur losses and negative cash flows in future periods. These fluctuations are due to a number of factors, many of which are beyond our control. These factors include, among others:

changes in end-user demand for the products manufactured and sold by our customers;

customers could accelerate their demand to earn financial incentives;

the effects of competitive pricing pressures, including decreases in average selling prices of our products;

the gain or loss of significant customers;

market acceptance of our products and our customers' products;

our ability to timely develop, introduce, market and support new products and technologies;

availability and cost of products from our suppliers;

intellectual property disputes;

the timing of receipt, reduction or cancellation of significant orders by customers;

fluctuations in the levels of component inventories held by our customers and changes in our customers' inventory management practices;

shifts in our product mix and the effect of maturing products;

the timing and extent of product development costs;

new product and technology introductions by us or our competitors;

fluctuations in manufacturing yields; and

significant warranty claims, including those not covered by our suppliers.

The foregoing factors are difficult to forecast, and these, as well as other factors, could materially and adversely affect our quarterly or annual operating results.

***We have substantial cash requirements to fund our operations, research and development efforts and capital expenditures. Our capital resources are limited and capital needed for our business may not be available when we need it.***

We have used significant cash to fund our operating activities. Our principal sources of liquidity are our existing cash balances, cash generated from product sales and our revolving credit facility with Silicon Valley Bank (SVB). We believe that our existing cash balances, along with cash expected to be generated from operations and our revolving credit facility, will be sufficient to fund our operations, research and development efforts, anticipated capital expenditures, working capital and other financing requirements, including interest payments on our debt obligations, for at least the next 12 months. We have completed transactions that involved the issuance of equity and the issuance or incurrence of indebtedness, including credit facilities. Even after completing these transactions, we may need additional capital in the future and may not have access to additional sources of capital on favorable terms or at all. If we raise additional funds through the issuance of equity, equity-based or debt securities, such securities may have rights, preferences or privileges senior to those of our common stock and our stockholders may experience dilution of their ownership interests. In addition, there can be no assurance that we will continue to benefit from the sale or licensing of intellectual property as we have in previous periods.

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***Our success depends on our ability to timely develop competitive new products and keep abreast of the rapid technological changes in our market.***

Our operating results will depend largely on our ability to continue to timely introduce new and enhanced semiconductor products, as well as our ability to keep abreast of rapid technological changes in our markets. Our products could become obsolete sooner than we expect because of faster than anticipated, or unanticipated, changes in one or more of the technologies related to our products. The introduction of new technology representing a substantial advance over current technology could adversely affect demand for our existing products. Currently accepted industry standards are also subject to change, which may also contribute to the obsolescence of our products. If we are unable to develop and introduce new or enhanced products in a timely manner, our business may be adversely affected.

Successful product development and introduction depends on numerous factors, including, among others:

our ability to anticipate customer and market requirements and changes in technology and industry standards;

our ability to accurately define new products;

our ability to complete development of new products, and bring our products to market, on a timely basis;

our ability to differentiate our products from offerings of our competitors; and

overall market acceptance of our products.

We may not have sufficient resources to make the substantial investment in research and development in order to develop and bring to market new and enhanced products, particularly if we are required to take further cost reduction actions. Furthermore, we are required to continually evaluate expenditures for planned product development and to choose among alternative technologies based on our expectations of future market growth. We may be unable to timely develop and introduce new or enhanced products, our products may not satisfy customer requirements or achieve market acceptance, or we may be unable to anticipate new industry standards and technological changes. We also may not be able to respond successfully to new product announcements and introductions by competitors.

Research and development projects may experience unanticipated delays related to our internal design efforts. New product development also requires the production of photomask sets and the production and testing of sample devices. In the event we experience delays in obtaining these services from the wafer fabrication and assembly and test vendors on whom we rely, our product introductions may be delayed and our revenue and results of operations may be adversely affected.

***Our debt obligations could adversely affect our financial condition.***

In recent periods, our debt obligations have increased. As of December 28, 2012, we had \$47.0 million in aggregate principal amount of convertible senior notes outstanding. In addition, our loan and security agreement with SVB includes: (i) a term loan facility of \$15.0 million; and (ii) a revolving credit facility of up to \$20.0 million. As of December 28, 2012, the outstanding balance on the term loan was \$15.0 million and the outstanding balance on the revolving credit facility was \$13.5 million. Our debt obligations may adversely impact our financial condition. For example, our debt obligations may:

require us to use a large portion of our cash flow to repay our indebtedness thereunder if we fail to comply with the restrictive financial and operating covenants in the loan and security agreement or if other events of default occur, which may have a material adverse effect on our liquidity and will reduce the availability of our cash flow to fund working capital, capital expenditures, acquisitions or strategic business opportunities, research and development expenditures and other general business activities;

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limit our future ability to raise funds for working capital, capital expenditures, acquisitions or strategic business opportunities, research and development expenditures and other general business activities; and

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contribute to a future downgrade of our credit rating, which could increase future borrowing costs.

Our ability to meet our payment obligations under our debt obligations depends on our ability to generate significant cash flow in the future. We believe our existing and expected cash balances will be sufficient to fund the \$15.0 million principal payment of our 6.50% convertible senior notes due in August 2013. However, there can be no assurance that our business will generate cash flow from operations, or that additional capital will be available to us, in an amount sufficient to enable us to meet our payment obligations under our debt obligations and to fund our other liquidity needs. If we are unable to generate sufficient cash flow to service our debt obligations, we may need to refinance or restructure our debt, sell assets, reduce or delay capital investments, or seek to raise additional capital. If we were unable to implement one or more of these alternatives, we may be unable to meet our debt payment obligations.

*We are entirely dependent upon third parties for the manufacture of our products and are vulnerable to their capacity constraints during times of increasing demand for semiconductor products.*

We are entirely dependent upon outside wafer fabrication facilities, known as foundries, for wafer fabrication services. Our principal suppliers of wafer fabrication services are TSMC and Jazz Semiconductor, Inc. We are also dependent upon third parties, including Amkor and ASE, for the assembly and testing of all of our products. Under our fabless business model, our long-term revenue growth is dependent on our ability to obtain sufficient external manufacturing capacity, including wafer production capacity. Periods of upturns in the semiconductor industry may be characterized by rapid increases in demand and a shortage of capacity for wafer fabrication and assembly and test services.

The risks associated with our reliance on third parties for manufacturing services include:

the lack of assured supply, potential shortages and higher prices;

the effects of disputes or litigation involving our third-party foundries;

increased lead times;

limited control over delivery schedules, manufacturing yields, production costs and product quality; and

the unavailability of, or delays in obtaining, products or access to key process technologies.

Our standard lead time, or the time required to manufacture our products (including wafer fabrication, assembly and testing), is typically 12 to 16 weeks. During periods of manufacturing capacity shortages, the foundries and other suppliers on whom we rely may devote their limited capacity to fulfill the production requirements of other customers that are larger or better financed than we are, or who have superior contractual rights to enforce the manufacture of their products, including to the exclusion of producing our products.

Additionally, if we are required to seek alternative foundries or assembly and test service providers, we would be subject to longer lead times, indeterminate delivery schedules and increased manufacturing costs, including costs to find and qualify acceptable suppliers. For example, if we choose to use a new foundry, the qualification process may take as long as six months over the standard lead time before we can begin shipping products from the new foundry. Such delays could negatively affect our relationships with our customers.

Wafer fabrication processes are subject to obsolescence, and foundries may discontinue a wafer fabrication process used for certain of our products. In such event, we generally offer our customers a last-time buy program to satisfy their anticipated requirements for our products. Any unanticipated discontinuation of a wafer fabrication process on which we rely may adversely affect our revenue and our customer relationships.

The foundries and other suppliers on whom we rely may experience financial difficulties or suffer disruptions in their operations due to causes beyond our control, including deteriorations in general economic conditions, labor strikes, work stoppages, electrical power outages, fire, earthquake, flooding or other natural disasters. Certain of our suppliers' manufacturing facilities are located near major earthquake fault lines in the Asia-Pacific region and in California. Due to cross dependencies, supply chain disruptions could negatively impact demand of our products, including, for example, if



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our customers are unable to obtain sufficient supply of other components required for their end product. In the event of a disruption of the operations of one or more of our suppliers, we may not have an alternate source immediately available. Such an event could cause significant delays in shipments until we are able to shift the products from an affected facility or supplier to another facility or supplier. The manufacturing processes we rely on are specialized and are available from a limited number of suppliers. Alternate sources of manufacturing capacity, particularly wafer production capacity, may not be available to us on a timely basis. Even if alternate manufacturing capacity is available, we may not be able to obtain it on favorable terms, or at all. Difficulties or delays in securing an adequate supply of our products on favorable terms, or at all, could impair our ability to meet our customers' requirements and have a material adverse effect on our operating results.

In addition, the highly complex and technologically demanding nature of semiconductor manufacturing has caused foundries to experience, from time to time, lower than anticipated manufacturing yields, particularly in connection with the introduction of new products and the installation and start-up of new process technologies. Lower than anticipated manufacturing yields may affect our ability to fulfill our customers' demands for our products on a timely basis. Moreover, lower than anticipated manufacturing yields may adversely affect our gross margin and our results of operations.

### ***The price of our common stock may fluctuate significantly.***

The price of our common stock is volatile and may fluctuate significantly. There can be no assurance as to the prices at which our common stock will trade or that an active trading market in our common stock will be sustained in the future. The market price at which our common stock trades may be influenced by many factors, including:

our operating and financial performance and prospects, including our ability to achieve sustained profitability;

the depth and liquidity of the market for our common stock which can impact, among other things, the volatility of our stock price and the availability of market participants to borrow shares;

investor perception of us and the industry in which we operate;

the recently completed acquisition of picoChip may not be accretive and may cause dilution to our earnings per share;

the level of research coverage of our common stock;

changes in earnings estimates or buy/sell recommendations by analysts;

the issuance and sale of additional shares of common stock;

the recently completed sale and issuance of convertible senior notes;

limitations placed on our investors by our stockholders rights agreement, which is designed to protect our net operating loss carryforwards;

general financial and other market conditions; and

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domestic and international economic conditions.

In addition, public stock markets have experienced, and may in the future experience, extreme price and trading volume volatility, particularly in the technology sectors of the market. This volatility has significantly affected the market prices of securities of many technology companies for reasons frequently unrelated to or disproportionately impacted by the operating performance of these companies. These broad market fluctuations may adversely affect the market price of our common stock. If we do not meet the requirements for continued quotation on the Nasdaq Global Select Market (NASDAQ), our common stock could be delisted which would adversely affect the ability of investors to sell shares of our common stock and could otherwise adversely affect our business.



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### ***We are subject to intense competition.***

The communications semiconductor industry in general, and the markets in which we compete in particular, are intensely competitive. We compete worldwide with a number of U.S. and international semiconductor manufacturers that are both larger and smaller than we are in terms of resources and market share. We currently face significant competition in our markets and expect that intense price and product competition will continue. This competition has resulted, and is expected to continue to result, in declining average selling prices for our products.

Many of our current and potential competitors have certain advantages over us, including:

stronger financial position and liquidity;

longer, or stronger, presence in key markets;

greater name recognition;

more secure supply chain;

lower cost alternatives to our products;

access to larger customer bases; and

significantly greater sales and marketing, manufacturing, distribution, technical and other resources.

As a result, these competitors may be able to adapt more quickly to new or emerging technologies and changes in customer requirements or may be able to devote greater resources to the development, promotion and sale of their products than we can. Moreover, we have incurred substantial operating losses and we may in the future incur losses in future periods. We believe that financial stability of suppliers is an important consideration in our customers' purchasing decisions. If our OEM customers perceive that we lack adequate financial stability, they may choose semiconductor suppliers that they believe have a stronger financial position or liquidity.

Current and potential competitors also have established or may establish financial or strategic relationships among themselves or with our existing or potential customers, resellers or other third parties. These relationships may affect customers' purchasing decisions. Accordingly, it is possible that new competitors or alliances among competitors could emerge and rapidly acquire significant market share. We may not be able to compete successfully against current and potential competitors.

***The loss of one or more key customers or distributors, or the diminished demand for our products from a key customer could significantly reduce our net revenue, gross margin and results of operations.***

A relatively small number of end customers and distributors have accounted for a significant portion of our net revenue in any particular period. There has been an increasing trend toward industry consolidation in our markets in recent years, particularly among major network equipment and telecommunications companies. Industry consolidation could decrease the number of significant customers for our products thereby increasing our reliance on key customers. In addition, industry consolidation has generally led, and may continue to lead, to pricing pressures and loss of market share. We have no long-term volume purchase commitments from our key customers. One or more of our key customers or distributors may discontinue operations as a result of consolidation, financial instability, liquidation or otherwise. Reductions, delays and cancellation of orders from our key customers or the loss of one or more key customers could significantly reduce our net revenue and results of operations. We cannot assure you that our current customers will continue to place orders with us, that orders by existing customers will continue at current or historical levels or that we will be able to obtain orders from new customers.



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*Our acquisition of picoChip Inc. and its wholly owned subsidiaries on February 6, 2012 has exposed us to risks arising from the acquisition and could have a material adverse effect on our financial position, results of operations and/or cash flows.*

Acquisition transactions are subject to inherent risks and uncertainties, including, among others, risks associated with the successful integration of geographically separate organizations; the ability to integrate the companies' technologies; and the potential for key employee attrition. Acquisition transactions could also result in large one-time write-offs, amortization expenses related to intangible assets, limitations on our ability to use our net operating loss carryforwards, litigation or other claims in connection with the acquired company and the diversion of management's time and attention from operating our business to acquisition integration challenges. Litigation or other claims may arise relating to certain terms and conditions of the acquisition agreement, such as earnout payments or closing net asset adjustments, which are currently in dispute. Operationally, the business of picoChip has depended on key customer and supplier relationships, and we will need to maintain those relationships. If we fail to maintain those relationships, it would have an adverse effect on our operating objectives and could have an adverse effect on our future operating results. Integration of our respective operations, including technology integration and integration of financial and administrative functions, may not proceed as we currently anticipate and could result in presently unanticipated costs or expenses (including unanticipated capital expenditures) that could have an adverse effect on our future operating results. We may also incur liability for activities of picoChip and its subsidiaries prior to the acquisition, including patent and trademark infringement claims, violations of laws, commercial disputes, tax liabilities and other known and unknown liabilities. In addition, we have no recent experience operating our business in the United Kingdom and lack familiarity with local laws, regulations and business practices. We cannot provide any assurances that we will achieve our business and financial objectives in connection with the acquisition of picoChip.

The cash payment of the initial purchase price for the acquisition of picoChip was financed in part with bank debt and through the issuance of shares of our common stock that resulted in dilution to our existing stockholders. We will be required to service this additional indebtedness and cannot provide assurances that picoChip's business will generate sufficient net cash flows, if any, to permit us to service the indebtedness without relying on cash flows, if any, generated by our incumbent businesses. The benefits or synergies we may expect from the acquisition of picoChip may not be realized to the extent or in the time frame we initially anticipate, which may result in an adverse effect on our stock price or our ability to raise additional financing, either in the public capital markets or through further debt financing.

*We are subject to the risks of doing business internationally.*

A significant part of our strategy involves our continued pursuit of growth opportunities in a number of international markets. We market, sell, design and service our products internationally. Products shipped to international destinations, primarily in the Asia-Pacific region and Europe, were approximately 88% of our net revenue for the first quarter of fiscal 2013. China is a particularly important international market for us, as approximately 29% of our net revenue for the first quarter of fiscal 2013 came from customers in China. In addition, we have design centers, customer support centers and rely on suppliers, located outside the U.S., including foundries and assembly and test service providers located in the Asia-Pacific region. We intend to continue to expand our international business activities and may open other design centers and customer support centers abroad. Our international sales and operations are subject to a number of risks inherent in selling and operating abroad which could adversely impact our international sales and could make our international operations more expensive. These include, but are not limited to, risks regarding:

currency exchange rate fluctuations;

local economic and political conditions;

difficulties in staffing and managing foreign operations;

potential hostilities and changes in diplomatic and trade relationships;

tax laws;

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natural disasters, including earthquakes or flooding;

restrictive governmental actions (such as restrictions on the transfer or repatriation of funds and trade protection measures, including export duties and quotas and customs duties and tariffs);

changes in legal or regulatory requirements;

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difficulty in obtaining distribution and support;

disruptions of capital and trading markets;

acts of terrorism;

wage inflation;

greater difficulty in accounts receivable collection and longer payment cycles;

the laws and policies of the U.S. and other countries affecting trade, foreign investment and loans and import or export requirements, including the Foreign Corrupt Practices Act and similar rules and regulations;

government export regulations as they apply to the encryption or other features contained in some of our products, which could limit our ability to manufacture the affected products at foreign foundries or ship these products to certain customers;

tariffs, duties and other import or export restrictions imposed by foreign governments on components that we obtain from non-domestic supplier;

existing or future environmental laws and regulations governing, among other things, air emissions, wastewater discharges, the contents of our products, the use, handling and disposal of hazardous substances and wastes, soil and groundwater contamination and employee health and safety;

limitations on our ability under local laws to protect our intellectual property; and

cultural differences in the conduct of business.

Because most of our international sales are currently denominated in U.S. dollars, our products could become less competitive in international markets if the value of the U.S. dollar increases relative to foreign currencies. As we continue to shift a portion of our operations offshore, more of our expenses are incurred in currencies other than those in which we bill for the related services. An increase in the value of certain currencies, such as the Euro, Japanese yen, Ukrainian hryvnia and Indian rupee, against the U.S. dollar could increase costs of our offshore operations by increasing labor and other costs that are denominated in local currencies.

We may in the future enter into foreign currency forward exchange contracts to mitigate the risk of loss from currency exchange rate fluctuations for foreign currency commitments entered into in the ordinary course of business. We do not enter into foreign currency forward exchange contracts for other purposes. Our financial condition and results of operations could be adversely affected by currency fluctuations.

***Our business is subject to various governmental regulations, and compliance with these regulations may cause us to incur significant expenses. If we fail to maintain compliance with applicable regulations, we may be forced to recall products and cease their manufacture and distribution, and we could be subject to civil or criminal penalties.***

Our business is subject to various international and U.S. laws and other legal requirements, including packaging, product content, labor and import/export regulations. These regulations are complex, change frequently and have generally become more stringent over time. We may be required to incur significant costs to comply with these regulations or to remedy violations. Any failure by us to comply with applicable

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government regulations could result in cessation of our operations or portions of our operations, product recalls or impositions of fines and restrictions on our ability to conduct our operations. In addition, because many of our products are regulated or sold into regulated industries, we must comply with additional regulations in marketing our products.

Our products and operations are also subject to the rules of industrial standards bodies, like the International Standards Organization, as well as regulation by other agencies, such as the U.S. Federal Communications Commission. If we fail to adequately address any of these rules or regulations, our business could be harmed.

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For example, the SEC recently adopted a final rule to implement Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which requires new disclosures concerning the use of conflict minerals, generally tantalum, tin, gold, or tungsten, that originated in the Democratic Republic of the Congo or an adjoining country. These disclosures are required whether or not these products containing conflict minerals are manufactured by us or third parties. Verifying the source of any conflict minerals in our products will create additional costs in order to comply with the new disclosure requirements and we may not be able to certify that the metals in our products are conflict free, which may create issues with our customers. In addition, the new rule may affect the pricing, sourcing and availability of minerals used in the manufacture of our products.

We must conform the manufacture and distribution of our products to various laws and adapt to regulatory requirements in all countries as these requirements change. If we fail to comply with these requirements in the manufacture or distribution of our products, we could be required to pay civil penalties, face criminal prosecution and, in some cases, be prohibited from distributing our products in commerce until the products or component substances are brought into compliance.

***We may be subject to claims, or we may be required to defend and indemnify customers against claims, of infringement of third-party intellectual property rights or demands that we, or our customers, license third-party technology, which could result in significant expense.***

The semiconductor industry is characterized by vigorous protection and pursuit of intellectual property rights. From time to time, third parties have asserted and may in the future assert patent, copyright, trademark and other intellectual property rights against technologies that are important to our business. The resolution or compromise of any litigation or other legal process to enforce such alleged third party rights, including claims arising through our contractual indemnification of our customers, or claims challenging the validity of our patents, regardless of its merit or resolution, could be costly and divert the efforts and attention of our management and technical personnel.

We may not prevail in any such litigation or other legal process or we may compromise or settle such claims because of the complex technical issues and inherent uncertainties in intellectual property disputes and the significant expense in defending such claims. If litigation or other legal process results in adverse rulings, we may be required to:

pay substantial damages for past, present and future use of the infringing technology;

cease the manufacture, use or sale of infringing products;

discontinue the use of infringing technology;

expend significant resources to develop non-infringing technology;

pay substantial damages to our customers or end users to discontinue use or replace infringing technology with non-infringing technology;

license technology from the third party claiming infringement, which license may not be available on commercially reasonable terms, or at all; or

relinquish intellectual property rights associated with one or more of our patent claims, if such claims are held invalid or otherwise unenforceable.

***If we are not successful in protecting our intellectual property rights, it may harm our ability to compete.***

We rely primarily on patent, copyright, trademark and trade secret laws, as well as employee and third-party nondisclosure and confidentiality agreements and other methods, to protect our proprietary technologies and processes. We may be required to engage in litigation to enforce or

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protect our intellectual property rights, which may require us to expend significant resources and to divert the efforts and attention of our management from our business operations; in particular:

the steps we take to prevent misappropriation or infringement of our intellectual property may not be successful;



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any existing or future patents may be challenged, invalidated or circumvented; or

the measures described above may not provide meaningful protection.

Despite the preventive measures and precautions that we take, a third party could copy or otherwise obtain and use our technology without authorization, develop similar technology independently or design around our patents. We generally enter into confidentiality agreements with our employees, consultants and strategic partners. We also try to control access to and distribution of our technologies, documentation and other proprietary information. Despite these efforts, internal or external parties may attempt to copy, disclose, obtain or use our products, services or technology without our authorization. Also, former employees may seek employment with our business partners, customers or competitors, and the confidential nature of our proprietary information may not be maintained in the course of such future employment. Further, in some countries outside the U.S., patent protection is not available or not reliably enforced. Some countries that do allow registration of patents do not provide meaningful redress for patent violations. As a result, protecting intellectual property in those countries is difficult and competitors may sell products in those countries that have functions and features that infringe on our intellectual property.

***We may not be able to attract and retain qualified personnel necessary for the design, development, sale and support of our products. Our success could be negatively affected if key personnel leave.***

Our future success depends on our ability to attract, retain and motivate qualified personnel, including executive officers and other key management, technical and support personnel. As the source of our technological and product innovations, our key technical personnel represent a significant asset. The competition for such personnel can be intense in the semiconductor industry. We may not be able to attract and retain qualified management and other personnel necessary for the design, development, sale and support of our products.

In periods of poor operating performance, we have experienced, and may experience in the future, particular difficulty attracting and retaining key personnel. If we are not successful in assuring our employees of our financial stability and our prospects for success, our employees may seek other employment, which may materially and adversely affect our business. We intend to continue to expand our international business activities including expansion of design and operations centers abroad and may have difficulty attracting and maintaining international employees. The loss of the services of one or more of our key employees, including Raouf Y. Halim, our chief executive officer, or certain key design and technical personnel, or our inability to attract, retain and motivate qualified personnel could have a material adverse effect on our ability to operate our business.

Some of our engineers are foreign nationals working in the U.S. under work visas. The visas permit qualified foreign nationals working in specialty occupations, such as certain categories of engineers, to reside in the U.S. during their employment. The number of new visas approved each year may be limited and may restrict our ability to hire additional qualified technical employees. In addition, immigration policies are subject to change, and these policies have generally become more stringent since the events of September 11, 2001. Any additional significant changes in immigration laws, rules or regulations may further restrict our ability to retain or hire technical personnel.

***Because of the lengthy sales cycles of many of our products, we may incur significant expenses before we generate any revenue related to those products.***

Our customers generally need six months or longer to test and evaluate our products and an additional nine months or more to begin volume production of equipment that incorporates our products. These lengthy periods also increase the possibility that a customer may decide to cancel or change product plans, which could reduce or eliminate sales to that customer. As a result of this lengthy sales cycle, we may incur significant research and development and selling, general and administrative expenses before we generate any revenue from new products. We may never generate the anticipated revenue if our customers cancel or change their product plans as customers may increasingly do if economic conditions continue to deteriorate.

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*Substantial sales of the shares of our common stock issuable upon conversion of our convertible senior notes or exercise of our outstanding warrant and antidilution and other provisions in our outstanding warrant, or substantial sales of the shares of our common stock issued in connection with the picoChip acquisition could adversely affect our stock price or our ability to raise additional financing in the public capital markets.*

At December 28, 2012, we had \$47.0 million aggregate principal amount of convertible senior notes outstanding. These notes are convertible at any time, at the option of the holder, into a total of approximately 11.4 million shares of common stock. In connection with the acquisition of picoChip, we issued an aggregate of approximately 5.2 million shares of our common stock to the stockholders of picoChip. The conversion of the notes and subsequent sale of a substantial number of shares of our common stock related to the notes or the sale of a substantial number of the picoChip acquisition shares could also adversely affect demand for, and the market price of, our common stock. Each of these transactions could adversely affect our ability to raise additional financing by issuing equity or equity-based securities in the public capital markets.

A warrant is outstanding to acquire approximately 6.3 million shares of our common stock at a price of \$16.25 per share (adjusted to reflect a change in the number of shares and exercise price, which resulted from the offering of our 6.75% convertible seniors notes completed in the third quarter of fiscal 2012), exercisable through June 27, 2013, representing approximately 10% of our outstanding common stock on a fully diluted basis. The warrant may be transferred or sold in whole or part at any time. If the warrant holder sells the warrant or if it or a transferee of the warrant exercises the warrant and sells a substantial number of shares of our common stock in the future, or if investors perceive that these sales may occur, the market price of our common stock could decline or market demand for our common stock could be sharply reduced.

The warrant contains antidilution provisions that provide for adjustment of the warrant's exercise price, and the number of shares issuable under the warrant, upon the occurrence of certain events. If we issue, or are deemed to have issued, shares of our common stock, or securities convertible into our common stock, at prices below the current market price of our common stock (as defined in the warrant) at the time of the issuance of such securities, the warrant's exercise price will be reduced and the number of shares issuable under the warrant will be increased. The amount of such adjustment, if any, will be determined pursuant to a formula specified in the warrant and will depend on the number of shares issued, the offering price and the current market price of our common stock at the time of the issuance of such securities. Adjustments to the warrant pursuant to these antidilution provisions may result in significant dilution to the interests of our existing stockholders and may adversely affect the market price of our common stock. The antidilution provisions may also limit our ability to obtain additional financing on terms favorable to us.

Moreover, we may not realize any cash proceeds from the exercise of the warrant. The holder of the warrant may opt for a cashless exercise of all or part of the warrant. In a cashless exercise, the holder of the warrant would make no cash payment to us, and would receive a number of shares of our common stock having an aggregate value equal to the excess of the then-current market price of the shares of our common stock issuable upon exercise of the warrant over the exercise price of the warrant. Such an issuance of common stock would be immediately dilutive to the interests of other stockholders.

*Uncertainties involving the ordering and shipment of our products could adversely affect our business.*

Our sales are typically made pursuant to individual purchase orders and we generally do not have long-term supply arrangements with our customers. Generally, our customers may cancel orders until 30 days prior to shipment. In addition, we sell a substantial portion of our products through distributors, some of whom have a right to return unsold products to us. Sales to distributors accounted for approximately 63% of our revenue for the first quarter of fiscal 2013.

Because of the significant lead times for wafer fabrication and assembly and test services, we routinely purchase inventory based on estimates of end-market demand for our customers' products. End-market demand may be subject to dramatic changes and is difficult to predict. End-market demand is highly influenced by the timing and extent of carrier capital expenditures which may decrease due to general economic conditions, and uncertainty, over which we have no control. The difficulty in predicting demand may be compounded when we sell to OEMs indirectly through distributors or contract manufacturers, or both, as our forecasts of demand are then based on estimates provided by multiple parties. In addition, our customers may change their inventory practices on short notice for any reason. The cancellation or deferral of product orders, the return of previously sold products or overproduction due to the failure of anticipated orders to materialize could result in our holding excess or obsolete inventory, which could result in write-downs of inventory. Conversely, if we fail to anticipate inventory needs we may be unable to fulfill demand for our products, resulting in a loss of potential revenue.

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***If network infrastructure OEMs do not design our products into their equipment, we will be unable to sell those products. Moreover, a design win from a customer does not guarantee future sales to that customer.***

Our products are not sold directly to the end-user but are components of other products. As a result, we rely on network infrastructure OEMs to select our products from among alternative offerings to be designed into their equipment. We may be unable to achieve these design wins. Without design wins from OEMs, we would be unable to sell our products. Once an OEM designs another supplier's semiconductors into one of its product platforms, it is more difficult for us to achieve future design wins with that OEM's product platform because changing suppliers involves significant cost, time, effort and risk for the OEM. Achieving a design win with a customer does not ensure that we will receive significant revenue from that customer, and we may be unable to convert design wins into actual sales. Even after a design win, the customer is not obligated to purchase our products and can choose at any time to stop using our products if, for example, its own products are not commercially successful.

***The complexity of our products may lead to errors, defects and/or bugs, any of which could subject us to significant costs or damages and adversely affect market acceptance of our products.***

Although we, our customers and our suppliers rigorously test our products, our products are complex and may contain errors, defects or bugs when first introduced or as new versions are released. We have in the past experienced, and may in the future experience, errors, defects and bugs. If any of our products contain production defects or reliability, safety, quality or compatibility problems that are significant to our customers, our reputation may be damaged and customers may be reluctant to buy our products, which could adversely affect our ability to retain existing customers and attract new customers. In addition, these defects or bugs could interrupt or delay sales of affected products to our customers, which could adversely affect our results of operations.

If defects or bugs are discovered after commencement of commercial production of a new product, we may be required to make significant expenditures of capital and other resources to resolve the problems. This could result in significant additional development costs and the diversion of technical and other resources from our other development efforts. We could also incur significant costs to repair or replace defective products, and we could be subject to claims for damages by our customers or others against us. We could also be exposed to product liability claims or indemnification claims by our customers. These costs or damages could have a material adverse effect on our financial condition and results of operations.

***We may make business acquisitions or investments, which involve significant risk.***

In addition to the acquisition of picoChip, we may, from time to time, make acquisitions, enter into alliances or make investments in other businesses to complement our existing product offerings, augment our market coverage or enhance our technological capabilities. However, any such transactions could result in:

issuances of equity securities dilutive to our existing stockholders;

substantial cash payments;

the incurrence of substantial debt and assumption of unknown liabilities;

large one-time write-offs;

amortization expenses related to intangible assets;

a limitation on our ability to use our net operating loss carryforwards;

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the diversion of management's time and attention from operating our business to acquisition integration challenges;

adverse tax consequences; and

the potential loss of key employees, customers and suppliers of the acquired business.

Additionally, in periods subsequent to an acquisition, we must evaluate goodwill and acquisition-related intangible assets for impairment. If such assets are found to be impaired, they will be written down to estimated fair value, with a charge against earnings.

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Integrating acquired organizations and their products and services may be expensive, time-consuming and a strain on our resources and our relationships with employees, customers and suppliers, and ultimately may not be successful. The benefits or synergies we may expect from the acquisition of complementary or supplementary businesses may not be realized to the extent or in the time frame we initially anticipate. Some of the risks that may affect our ability to successfully integrate acquired companies include those associated with:

failure to successfully further develop the acquired products or technology;

conforming the acquired company's standards, policies, processes, procedures and controls with our operations;

coordinating new product and process development, especially with respect to highly complex technologies;

loss of key employees or customers of the acquired company;

hiring additional management and other critical personnel;

in the case of foreign acquisitions, the need to integrate operations across different cultures and languages and to address the particular economic, currency, political and regulatory risks associated with specific countries;

increasing the scope, geographic diversity and complexity of our operations;

consolidation of facilities, integration of the acquired company's accounting, human resource and other administrative functions and coordination of product, engineering and sales and marketing functions;

the geographic distance between the companies;

liability for activities of the acquired company before the acquisition, including patent and trademark infringement claims, violations of laws, commercial disputes, tax liabilities and other known and unknown liabilities; and

litigation or other claims in connection with the acquired company, including claims for terminated employees, customers, former stockholders or other third parties.

***Our ability to utilize our net operating loss carryforwards and certain other tax attributes may be limited.***

As of September 28, 2012, we had net operating loss carryforwards of approximately \$649.5 million for federal income tax purposes. Furthermore, we acquired additional net operating loss carryforwards upon the acquisition of picoChip. As of December 31, 2011, picoChip had net operating loss carryforwards for U.S. federal and California income tax purposes of \$1.5 million each and for U.K. corporation tax purposes of \$28.9 million. Under Section 382 of the Internal Revenue Code, if a corporation undergoes an ownership change, the corporation's ability to use its pre-change net operating loss carryforwards and other pre-change tax attributes to offset its post-change income may be significantly limited. An ownership change is generally defined as a greater than 50% change in equity ownership by value over a three-year period. In August 2009, our board of directors adopted a stockholders' rights agreement that is designed to help preserve our ability to utilize fully certain tax assets primarily associated with net operating loss carryforwards under Section 382 of the Internal Revenue Code. Even with this rights agreement in place, we may experience an ownership change in the future as a result of shifts in our stock ownership, including upon the

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issuance of our common stock, the exercise of stock options or warrants or as a result of any conversion of our convertible notes into shares of our common stock, among other things. If we were to trigger an ownership change in the future, our ability to use any net operating loss carryforwards existing at that time could be significantly limited.

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*Our results of operations could vary as a result of the methods, estimates and judgments we use in applying our accounting policies.*

The methods, estimates and judgments we use in applying our accounting policies have a significant impact on our results of operations (see Critical Accounting Policies and Estimates in Part I, Item 2 of this Quarterly Report on Form 10-Q). Such methods, estimates and judgments are, by their nature, subject to substantial risks, uncertainties and assumptions, and changes in rule making by various regulatory bodies. Factors may arise over time that lead us to change our methods, estimates and judgments. Changes in those methods, estimates and judgments could significantly affect our results of operations.

*Provisions in our organizational documents and stockholders rights agreements and Delaware law will make it more difficult for someone to acquire control of us.*

Our restated certificate of incorporation, our amended and restated bylaws, our stockholders rights agreements and the Delaware General Corporation Law contain several provisions that would make more difficult an acquisition of control of us in a transaction not approved by our board of directors. Our restated certificate of incorporation and amended and restated bylaws include provisions such as:

the division of our board of directors into three classes to be elected on a staggered basis, one class each year;

the exclusive responsibility of the board of directors to fill vacancies on the board of directors;

the ability of our board of directors to issue shares of our preferred stock in one or more series without further authorization of our stockholders;

a prohibition on stockholder action by written consent;

a requirement that stockholders provide advance notice of any stockholder nominations of directors or any proposal of new business to be considered at any meeting of stockholders;

a requirement that a supermajority vote be obtained to remove a director for cause or to amend or repeal certain provisions of our restated certificate of incorporation or amended and restated bylaws;

elimination of the right of stockholders to call a special meeting of stockholders; and

a fair price provision.

Our stockholders rights agreements give our stockholders certain rights that would substantially increase the cost of acquiring us in a transaction not approved by our board of directors.

In addition to the stockholders rights agreements and the provisions in our restated certificate of incorporation and amended and restated bylaws, Section 203 of the Delaware General Corporation Law generally provides that a corporation shall not engage in any business combination with any interested stockholder during the three-year period following the time that such stockholder becomes an interested stockholder, unless a majority of the directors then in office approves either the business combination or the transaction that results in the stockholder becoming an interested stockholder or specified stockholder approval requirements are met.





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## Issuer Purchases of Equity Securities

	Total Number of Shares (or Units) Purchased (a)	Average Price Paid per Share (or Unit)
September 29, 2012 to October 26, 2012	4,855	\$ 3.55
October 27, 2012 to November 23, 2012	50,627	3.45
November 24, 2012 to December 28, 2012	6,142	3.98
	61,624	\$ 3.51

- (a) Represents shares of our common stock withheld from, or delivered by, employees in order to satisfy applicable tax withholding obligations in connection with the vesting of restricted stock. These repurchases were not made pursuant to any publicly announced plan or program.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION**

None.

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- 2.1 Agreement and Plan of Merger, dated January 5, 2012, by and among the Registrant, Platinum Acquisition U.K. Limited, Platinum Acquisition Corporation, Picochip, LLC (formerly known as picoChip Inc.), Mindspeed Technologies U.K., Limited (formerly known as Picochip Ltd.) and Shareholder Representative Services LLC, as the stockholder representative, filed as Exhibit 2.1 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended March 30, 2012, is incorporated herein by reference (SEC File No. 001-31650).
- 3.1 Restated Certificate of Incorporation of the Registrant, filed as Exhibit 4.1 to the Registrant's Registration Statement on Form S-3 filed on June 16, 2003, is incorporated herein by reference (Registration Statement No. 333-106146).
- 3.2 Certificate of Amendment to the Restated Certificate of Incorporation of the Registrant, filed as Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on July 1, 2008, is incorporated herein by reference (SEC File No. 001-31650).
- 3.3 Certificate of Designation of Series B Junior Participating Preferred Stock, filed as Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on August 10, 2009, is incorporated herein by reference (SEC File No. 001-31650).
- 3.4 Amended and Restated Bylaws of the Registrant, filed as Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on May 27, 2011, is incorporated herein by reference (SEC File No. 001-31650).
- 4.1 Specimen certificate for the Registrant's Common Stock, par value \$.01 per share, filed as Exhibit 4.1 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended June 27, 2008, is incorporated herein by reference (SEC File No. 001-31650).
- 4.2 Rights Agreement dated as of June 26, 2003, by and between the Registrant and Mellon Investor Services LLC, as Rights Agent, filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on July 1, 2003, is incorporated herein by reference (SEC File No. 001-31650).
- 4.3 First Amendment to Rights Agreement, dated as of December 6, 2004, by and between the Registrant and Mellon Investor Services LLC, filed as Exhibit 4.4 to the Registrant's Current Report on Form 8-K filed on December 8, 2004, is incorporated herein by reference (SEC File No. 001-31650).
- 4.4 Second Amendment to Rights Agreement, dated as of June 16, 2008, by and between the Registrant and Mellon Investor Services LLC, filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on June 18, 2008, is incorporated herein by reference (SEC File No. 000-50499).
- 4.5 Section 382 Rights Agreement, dated as of August 9, 2009, between the Registrant and Mellon Investor Services LLC, filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on August 10, 2009, is incorporated herein by reference (SEC File No. 001-31650).
- 4.6 Amendment No. 1 to Section 382 Rights Agreement, dated as of August 9, 2012, between the Registrant and Computershare Shareowners Services LLC (as successor to Mellon Investor Services LLC) as Rights Agent, filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on August 9, 2012, is incorporated herein by reference (SEC File No. 001-31650).
- 4.7 Common Stock Purchase Warrant dated June 27, 2003, filed as Exhibit 4.5 to the Registrant's Registration Statement on Form S-3 filed on October 7, 2003, is incorporated herein by reference (Registration Statement No. 333-109523).
- 4.8 Registration Rights Agreement dated as of June 27, 2003, by and between the Registrant and Conexant Systems, Inc., filed as Exhibit 4.6 to the Registrant's Registration Statement on Form S-3 filed on October 7, 2003, is incorporated herein by reference (Registration Statement No. 333-109523).
- 4.9 Indenture, dated as of August 1, 2008, between the Registrant and Wells Fargo Bank, N.A., filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on August 4, 2008, is incorporated herein by reference (SEC File No. 001-31650).
- 4.10 Form of 6.50% Convertible Senior Notes due 2013, attached as Exhibit A to the Indenture (Exhibit 4.9 hereto), is incorporated herein by reference.
- 4.11 Declaration of Registration Rights, dated February 6, 2012, from the Registrant, filed as Exhibit 4.10 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended March 30, 2012, is incorporated herein by reference (SEC File No. 333-31650).

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4.12	Indenture, dated as of June 19, 2012, by and among the Registrant, certain Subsidiaries of the Registrant and Wells Fargo Bank, National Association, as trustee, filed as Exhibit 4.11 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended June 29, 2012, is incorporated herein by reference (SEC File No. 333-31650).
4.13	Form of 6.75% Convertible Senior Notes due 2017, attached as Exhibit A to the Indenture (Exhibit 4.12 hereto), is incorporated herein by reference.
+10.1	Mindspeed Technologies, Inc. Employee Stock Purchase Plan, as amended and restated.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
**32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
**32.2	Certification of 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 Document
***101.LAB	XBRL Taxonomy Extension Label Linkbase Document
***101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
+	Management contract or compensatory arrangement.
**	In accordance with Item 601(b)(32)(ii) of Regulation S-K and SEC Release No. 33-8238 and 34-47986, Final Rule: Management's Reports on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, the certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Form 10-Q and will not be deemed filed for purposes of Section 18 of the Exchange Act. Such certifications will not be deemed to be incorporated by reference into any filings under the Securities Act or the Exchange Act, except to the extent that the Registrant specifically incorporates it by reference.
***	Pursuant to applicable securities laws and regulations, the Registrant is deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and are not subject to liability under any anti-fraud provisions of the federal securities laws as long as the Registrant has made a good faith attempt to comply with the submission requirements and promptly amend the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. Users of this data are advised that, pursuant to Rule 406T, these interactive data files are deemed not filed and otherwise are not subject to liability. Confidential treatment has been granted with respect to certain portions of this exhibit. An unredacted copy of this exhibit has been filed separately with the SEC.

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**SIGNATURE**

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

MINDSPEED TECHNOLOGIES, INC.

(Registrant)

Date: February 6, 2013

By /s/ STEPHEN N. ANANIAS  
Stephen N. Ananias  
Senior Vice President and

Chief Financial Officer  
(principal financial officer)

Date: February 6, 2013

By /s/ JAMES M. WATKINS  
James M. Watkins  
Vice President and

Principal Accounting Officer  
(principal accounting officer)

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**EXHIBIT INDEX**

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