GSI TECHNOLOGY INC
Form 10-Q
August 08, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2016

or

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

For the transition period from to

Commission File Number 001-33387

GSI Technology, Inc.

(Exact name of registrant as specified in its charter)

Delaware	77-0398779
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

1213 Elko Drive

Sunnyvale, California 94089

(Address of principal executive offices, zip code)

(408) 331-8800

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company

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

The number of shares of the registrant’s common stock outstanding as of July 31, 2016: 20,549,058

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GSI TECHNOLOGY, INC.

FORM 10-Q FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2016

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PART I — FINANCIAL INFORMATION

Item 1.Financial Statements

GSI TECHNOLOGY, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

	June 30, 2016	March 31, 2016
ASSETS		
Cash and cash equivalents	$ 28,237	$ 31,963
Short-term investments	21,727	23,149
Accounts receivable, net	9,180	7,478
Inventories	7,583	7,174
Prepaid expenses and other current assets	2,392	2,198
Total current assets	69,119	71,962
Property and equipment, net	8,464	8,653
Long-term investments	9,404	11,148
Goodwill	8,030	8,030
Intangible assets, net	3,551	3,651
Other assets	3,239	3,086
Total assets	$ 101,807	$ 106,530
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable	$ 2,067	$ 2,514
Accrued expenses and other liabilities	4,411	4,398
Deferred revenue	1,976	2,330
Total current liabilities	8,454	9,242
Income taxes payable	251	116
Long-term deferred income taxes	—	811
Other accrued expenses	6,156	6,492

Total liabilities	14,861	16,661
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock: $0.001 par value authorized: 5,000,000 shares; issued and outstanding: none	-	-
Common Stock: $0.001 par value authorized: 150,000,000 shares; issued and outstanding: 20,838,246 and 21,716,364 shares, respectively	21	22
Additional paid-in capital	21,861	25,050
Accumulated other comprehensive income	34	27
Retained earnings	65,030	64,770
Total stockholders' equity	86,946	89,869
Total liabilities and stockholders' equity	$ 101,807	$ 106,530

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

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GSI TECHNOLOGY, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended June 30, 2016	2015
Net revenues	$ 12,946	$ 14,025
Cost of revenues	6,224	6,730
Gross profit	6,722	7,295
Operating expenses:		
Research and development	3,499	2,998
Selling, general and administrative	2,834	5,305
Total operating expenses	6,333	8,303
Income (loss) from operations	389	(1,008)
Interest income, net	77	79
Other income (expense), net	65	37
Income (loss) before income taxes	531	(892)
Provision for income taxes	271	25
Net income (loss)	$ 260	$ (917)
Net income (loss) per share:		
Basic	$ 0.01	$ (0.04)
Diluted	$ 0.01	$ (0.04)
Weighted average shares used in per share calculations:		
Basic	21,299	22,943
Diluted	21,526	22,943

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

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GSI TECHNOLOGY, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	Three Months Ended June 30,	
	2016	2015
Net income (loss)	$ 260	$ (917)
Net unrealized gain (loss) on available-for-sale investments, net of tax	7	(5)
Total comprehensive income (loss)	$ 267	$ (922)

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

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GSI TECHNOLOGY, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended June 30, 2016	2015
	(In thousands)	
Cash flows from operating activities:		
Net income (loss)	$ 260	$ (917)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Allowance for sales returns, doubtful accounts and other	1	3
Provision for excess and obsolete inventories	85	388
Depreciation and amortization	424	333
Stock-based compensation	443	474
Amortization of premium on investments	25	93
Changes in assets and liabilities:		
Accounts receivable	(1,703)	(1,169)
Inventory	(494)	(650)
Prepaid expenses and other assets	(347)	(908)
Accounts payable	(447)	1,534
Accrued expenses and other liabilities	(999)	(1,845)
Deferred revenue	(354)	207
Net cash used in operating activities	(3,106)	(2,457)
Cash flows from investing activities:		
Sales and maturities of short-term investments	3,148	7,000
Purchases of property and equipment	(135)	(6)
Net cash provided by investing activities	3,013	6,994
Cash flows from financing activities:		
Repurchase of common stock	(3,906)	(2,453)
Proceeds from issuance of common stock under employee stock plans	273	316
Net cash used in financing activities	(3,633)	(2,137)
Net increase (decrease) in cash and cash equivalents	(3,726)	2,400
Cash and cash equivalents at beginning of the period	31,963	36,776
Cash and cash equivalents at end of the period	$ 28,237	$ 39,176

Supplemental cash flow information:		
Net cash paid (received) for income taxes	$ 1,256	$ (132)

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

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GSI TECHNOLOGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1—THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying unaudited condensed consolidated financial statements of GSI Technology, Inc. and its subsidiaries (“GSI” or the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission. Accordingly, the interim financial statements do not include all of the information and footnotes required by GAAP for annual financial statements. These interim financial statements contain all adjustments (which consist of only normal, recurring adjustments) that are, in the opinion of management, necessary to state fairly the interim financial information included therein. The Company believes that the disclosures are adequate to make the information not misleading. However, these financial statements should be read in conjunction with the audited consolidated financial statements and related notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

The consolidated results of operations for the three months ended June 30, 2016 are not necessarily indicative of the results to be expected for the entire fiscal year.

Significant accounting policies

The Company’s significant accounting policies are disclosed in the Company’s Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

Recent accounting pronouncements

In March 2016, the Financial Accounting Standards Board ("FASB") issued ASU 2016-09, "Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting." ASU 2016-09 simplifies several aspects of the accounting for share-based payments transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This accounting standard update will be effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods, and early adoption is permitted. The Company is currently evaluating the methods and impact of adopting the new accounting standard on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)." The core principle of Topic 842 is that a lessee should recognize the assets and liabilities that arise from leases. All leases create an asset and a liability for the lessee in accordance with FASB Concepts Statement No. 6, "Elements of Financial Statements," and, therefore, recognition of those lease assets and lease liabilities represents a change of previous GAAP, which did not require lease assets and lease liabilities to be recognized for most leases. This ASU is effective for annual and interim periods beginning after December 15, 2018. Early adoption is permitted. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have not significantly changed from previous GAAP. The Company is currently evaluating the impact the pronouncement will have on its consolidated financial statements and related disclosures.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Assets." ASU 2016-01 requires equity investments to be measured at fair value with changes in fair value recognized in net income and simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. The accounting standard update also updates certain presentation and disclosure requirements. This accounting standard update will be effective for fiscal years beginning after December 15, 2017, including

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interim periods within those fiscal years, and early adoption is permitted. The Company is currently evaluating the impact of this accounting standard update on its consolidated financial statements.

In September 2015, the FASB issued a new accounting standard that eliminates the requirement to restate prior period financial statements for measurement period adjustments following a business combination. The new guidance requires that the cumulative impact of a measurement period adjustment including the impact on prior periods be recognized in the reporting period in which the adjustment is identified along with additional disclosures. The new guidance will be effective for the Company beginning in the first quarter of fiscal 2017. The new guidance is required to be adopted prospectively with early adoption permitted for financial statements that have not yet been made available for issuance. The new guidance is not expected to have a material impact on the Company’s consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, "Simplifying the Measurement of Inventory.” This standard update intends to simplify the subsequent measurement of inventory, excluding inventory accounted for under the last-in, first-out or the retail inventory methods. The update replaces the current lower of cost or market test with a lower of cost and net realizable value test. Under the current guidance, market could be replacement cost, net realizable value or net realizable value less an approximately normal profit margin. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The update is effective for reporting periods beginning after December 15, 2016, with early adoption permitted. The Company is currently evaluating the impact of this accounting standard on its consolidated financial statements.

In August 2014, the FASB issued new guidance related to the Company’s responsibility to evaluate whether there is substantial doubt about its ability to continue ongoing business operations and to provide relevant footnote disclosures. The new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. Early adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company’s consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." The new accounting standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The accounting standard is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2017. Early adoption is permitted for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016. ASU No. 2014-09 provides for one of two methods of transition: retrospective application to each prior period presented; or recognition of the cumulative effect of retrospective application of the new standard in the period of initial application. The Company is currently evaluating the impact of this accounting standard on its consolidated financial statements. In March, April and May 2016, the FASB issued additional updates to the new revenue standard relating to reporting revenue on a gross versus net basis, identifying performance obligations and licensing arrangements, and narrow-scope improvements and practical expedients, respectively. The Company is in the process of assessing the impact this additional guidance is expected to have upon adoption, including determining the adoption method.

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NOTE 2—NET INCOME (LOSS) PER COMMON SHARE

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

	Three Months Ended June 30,	
	2016	2015
Net income (loss)	$ 260	$ (917)
Denominators:		
Weighted average shares—Basic	21,299	22,943
Dilutive effect of employee stock options	223	—
Dilutive effect of employee stock purchase plan options	4	—
Weighted average shares—Dilutive	21,526	22,943
Net income (loss) per common share—Basic	$ 0.01	(0.04)
Net income (loss) per common share—Diluted	$ 0.01	(0.04)

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

	Three Months Ended June 30,	
	2016	2015
Shares underlying options	6,666	4,782

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NOTE 3—BALANCE SHEET DETAIL

	June 30, 2016	March 31, 2016
	(In thousands)	
Inventories:		
Work-in-progress	$ 2,000	$ 1,697
Finished goods	5,266	5,011
Inventory at distributors	317	466
	$ 7,583	$ 7,174

	June 30, 2016	March 31, 2016
	(In thousands)	
Accounts receivable, net:		
Accounts receivable	$ 9,281	$ 7,578
Less: Allowances for sales returns, doubtful accounts and other	(101)	(100)
	$ 9,180	$ 7,478

	June 30, 2016	March 31, 2016
	(In thousands)	
Prepaid expenses and other current assets:		
Prepaid tooling and masks	$ 860	$ 1,224
Prepaid income taxes	43	—
Escrow deposit	484	—
Other receivables	358	230
Other prepaid expenses and other current assets	647	744
	$ 2,392	$ 2,198

	June 30, 2016	March 31, 2016
	(In thousands)	
Property and equipment, net:		
Computer and other equipment	$ 18,520	$ 18,394
Software	4,793	4,793
Land	3,900	3,900
Building and building improvements	2,256	2,256
Furniture and fixtures	110	114
Leasehold improvements	696	687
	30,275	30,144
Less: Accumulated depreciation	(21,811)	(21,491)
	$ 8,464	$ 8,653

Depreciation expense was $324,000 and $292,000, respectively, for the three months ended June 30, 2016 and 2015.

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	June 30, 2016	March 31, 2016
	(In thousands)	
Other assets:		
Escrow deposit	$ 2,500	$ 2,984
Non-current deferred income taxes	35	—
Prepaid income taxes	585	—
Deposits	119	102
	$ 3,239	$ 3,086

The escrow deposits at June 30, 2016 and March 31, 2016 include approximately $2.5 million and $3.0 million respectively, placed in escrow in connection with the Company's acquisition of MikaMonu Group Ltd. on November 23, 2015. See Note 10— Acquisition for more information.

The following tables summarize the components of intangible assets and related accumulated amortization balances at June 30, 2016 and March 31, 2016 (in thousands):

	As of June 30, 2016		
	Gross Carrying Amount	Accumulated amortization	Net Carrying Amount
Intangible assets:			
Product designs	$ 590	$ (576)	$ 14
Patents	4,220	(683)	3,537
Software	80	(80)	—
Total	$ 4,890	$ (1,339)	$ 3,551

	As of March 31, 2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets:			

Product designs	$ 590	$ (555)	$ 35
Patents	4,220	(604)	3,616
Software	80	(80)	—
Total	$ 4,890	$ (1,239)	$ 3,651

Amortization of intangible assets included in cost of revenues was $100,000 and $41,000, respectively, for the three months ended June 30, 2016 and 2015.

As of June 30, 2016, the estimated future amortization expense of intangible assets in the table above is as follows (in thousands):

Three Months Ended June 30,	
2017	$ 327
2018	313
2019	247
2020	233
2021	233
Thereafter	2,198
Total	$ 3,551

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	June 30, 2016	March 31, 2016
	(In thousands)	
Accrued expenses and other liabilities:		
Accrued compensation	$ 2,369	$ 3,082
Escrow indemnity accrual	484	—
Accrued professional fees	173	83
Accrued commissions	363	284
Accrued income taxes	373	15
Other accrued expenses	649	934
	$ 4,411	$ 4,398

	June 30, 2016	March 31, 2016
	(In thousands)	
Other accrued expenses:		
Contingent consideration	$ 5,895	$ 5,856
Escrow indemnity accrual	—	484
Other long-term accrued liabilities	261	152
	$ 6,156	$ 6,492

NOTE 4—GOODWILL

Goodwill represents the difference between the purchase price and the estimated fair value of the identifiable assets acquired and liabilities assumed in a business combination. The Company tests for goodwill impairment on an annual basis, or more frequently if events or changes in circumstances indicate that the asset is more likely than not impaired. The Company has one reporting unit. The Company assesses goodwill for impairment on an annual basis on the last day of February in the fourth quarter of its fiscal year.

As of March 31, 2016 and June 30, 2016, the Company had a goodwill balance of $8.0 million. The goodwill resulted from the acquisition of MikaMonu Group Ltd. (“MikaMonu”) in fiscal 2016.

The Company utilized a two-step quantitative analysis to complete its annual impairment test during the fourth quarter of fiscal 2016 and concluded that there was no impairment, as the fair value of its sole reporting unit exceeded its carrying value. The Company determined that the second step of the impairment test was not necessary. No triggering event took place subsequent to the fiscal 2016 annual assessment that necessitated a quantitative impairment analysis for the Company’s one reporting unit. However, there continues to be a risk that a sustained decline in the Company’s stock price could constitute a triggering event that would require assessment for potential goodwill impairment in fiscal 2017.

NOTE 5—INCOME TAXES

The current portion of the Company’s unrecognized tax benefits was $0 at both June 30, 2016 and March 31, 2016. The long-term portion at June 30, 2016 and March 31, 2016 was $251,000 and $116,000, respectively, of which the timing of the resolution is uncertain. As of June 30, 2016, $2,011,000 of unrecognized tax benefits had been recorded as a reduction to net deferred tax assets. As of June 30, 2016 and March 31, 2016, the Company’s net deferred tax assets of $7.6 million and $6.4 million, respectively, were subject to a full valuation allowance.

The Company recorded a net deferred tax liability of $821,000 associated with the estimated fair value adjustments of the intangible assets acquired in its acquisition of MikaMonu in the quarter ended December 31, 2015. During the three months ended June 30, 2016, the Company reversed the deferred tax liability and recorded a prepaid tax asset of $636,000 associated the transfer of the acquired intangible assets out of Israel.

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During the three months ended June 30, 2016, the Company recorded a tax benefit of $71,000 that is included in the tax provision for the quarter then ended, to the reduction of uncertain tax benefits as a result of the lapse of applicable statutes of limitations.

Management believes that it is reasonably possible that within the next twelve months the Company could have a reduction in uncertain tax benefits of up to $438,000, including interest and penalties, related to positions taken with respect to credits and loss carryforwards on previously filed tax returns.

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

The Company is subject to taxation in the United States and various state and foreign jurisdictions. Fiscal years 2013 through 2016 remain open to examination by federal tax authorities, and fiscal years 2012 through 2016 remain open to examination by California tax authorities.

The Company’s estimated annual effective income tax rate was approximately (7.0%) and 2.6% as of June 30, 2016 and 2015, respectively. The annual effective tax rate as of June 30, 2016 and 2015 varies from the United States statutory income tax rate primarily due to valuation allowances in the United States, whereby pre-tax losses do not result in the recognition of corresponding income tax benefits and expenses, and the foreign tax differential.

NOTE 6—FINANCIAL INSTRUMENTS

Fair value measurements

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

Level 1: Valuations based on quoted prices in active markets for identical assets and liabilities. The fair value of available-for-sale securities included in the Level 1 category is based on quoted prices that are readily and regularly available in an active market. As of June 30, 2016, the Level 1 category included money market funds of $4.9 million, which were included in cash and cash equivalents on the Condensed Consolidated Balance Sheets.

Level 2: Valuations based on observable inputs (other than Level 1 prices), such as quoted prices for similar assets at the measurement date; quoted prices in markets that are not active; or other inputs that are observable, either directly or indirectly. The fair value of available-for-sale securities included in the Level 2 category is based on the market values obtained from an independent pricing service that were evaluated using pricing models that vary by asset class and may incorporate available trade, bid and other market information and price quotes from well established independent pricing vendors and broker-dealers. As of June 30, 2016, the Level 2 category included short-term investments of $21.7 million and long-term investments of $9.4 million, which were comprised of certificates of deposit, corporate debt securities and government and agency securities.

Level 3: Valuations based on inputs that are unobservable and involve management judgment and the reporting entity's own assumptions about market participants and pricing. As of June 30, 2016, the Company had no Level 3 financial assets and a Level 3 financial liability consisting of the contingent consideration liability for the acquisition of MikaMonu. See Note 10-Acquisition for more information.

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

		Fair Value Measurements at Reporting Date Using		
	June 30, 2016	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Money market funds	$ 4,914	$ 4,914	$ —	$ —
Marketable securities	31,131	—	31,131	—
Total	$ 36,045	$ 4,914	$ 31,131	$ —

		Fair Value Measurements at Reporting Date Using		
	March 31, 2016	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Money market funds	$ 6,611	$ 6,611	$ —	$ —
Marketable securities	34,297	—	34,297	—
Total	$ 40,908	$ 6,611	$ 34,297	$ —

Short-term and long-term investments

All of the Company's short-term and long-term investments are classified as available-for-sale. Available-for-sale debt securities with maturities greater than twelve months are classified as long-term investments when they are not intended for use in current operations. Investments in available-for-sale securities are reported at fair value with unrecognized gains (losses), net of tax, as a component of accumulated other comprehensive income (loss) in the Condensed Consolidated Balance Sheets. The Company had money market funds of $4.9 million and $6.6 million at

June 30, 2016 and March 31, 2016, respectively, included in cash and cash equivalents on the Condensed Consolidated Balance Sheets. The Company monitors its investments for impairment periodically and records appropriate reductions in carrying values when declines are determined to be other-than-temporary.

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

June 30, 2016		
	Gross Unrealized	Gross Unrealized