

MoSys, Inc.
Form 10-Q
November 09, 2011
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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, DC 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended September 30, 2011

OR

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

For the transition period from to

Commission file number 000-32929

MOSYS, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
of Incorporation or organization)

77-0291941
(I.R.S. Employer
Identification Number)

3301 Olcott Street

Santa Clara, California, 95054

(Address of principal executive office and zip code)

(408) 418-7500

(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 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 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

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As of November 1, 2011, 38,345,877 shares of the Registrant's common stock, \$0.01 par value, were outstanding.

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MOSYS, INC.

FORM 10-Q
September 30, 2011

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****MOSYS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)****(In thousands, except par value)**

| | September 30, 2011 | December 31, 2010 |
|---|-----------------------|----------------------|
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | \$ 5,781 | \$ 14,340 |
| Short-term investments | 12,524 | 15,011 |
| Accounts receivable, net | 602 | 1,079 |
| Unbilled contracts receivable | 107 | 202 |
| Prepaid expenses and other current assets | 2,985 | 3,377 |
| Total current assets | 21,999 | 34,009 |
| Long-term investments | 8,061 | 8,193 |
| Property and equipment, net | 1,654 | 2,160 |
| Goodwill | 23,134 | 23,134 |
| Intangible assets, net | 4,274 | 6,238 |
| Other assets | 348 | 232 |
| Total assets | \$ 59,470 | \$ 73,966 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities | | |
| Accounts payable | \$ 1,114 | \$ 839 |
| Accrued expenses and other liabilities | 2,232 | 2,623 |
| Accrued acquisition-related liabilities | 500 | 1,500 |
| Deferred revenue | 1,212 | 1,801 |
| Total current liabilities | 5,058 | 6,763 |
| Long-term liabilities | 108 | 146 |
| Commitments and contingencies (Note 4) | | |
| Stockholders equity | | |
| Preferred stock, \$0.01 par value; 20,000 shares authorized; none issued and outstanding | | |
| Common stock, \$0.01 par value; 120,000 shares authorized; 38,307 shares and 37,225 shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively | 383 | 372 |
| Additional paid-in capital | 149,131 | 143,336 |
| Accumulated other comprehensive income (loss) | (11) | 4 |

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| | | | | |
|--|----|----------|----|----------|
| Accumulated deficit | | (95,199) | | (76,655) |
| Total stockholders' equity | | 54,304 | | 67,057 |
| Total liabilities and stockholders' equity | \$ | 59,470 | \$ | 73,966 |

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

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MOSYS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands, except per share data)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|------------|------------------------------------|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| Net revenue | | | | |
| Licensing | \$ 756 | \$ 1,494 | \$ 3,319 | \$ 5,060 |
| Royalty | 1,351 | 2,282 | 5,619 | 6,535 |
| Total net revenue | 2,107 | 3,776 | 8,938 | 11,595 |
| Cost of net revenue | | | | |
| Licensing | 356 | 735 | 1,515 | 2,058 |
| Total cost of net revenue | 356 | 735 | 1,515 | 2,058 |
| Gross profit | 1,751 | 3,041 | 7,423 | 9,537 |
| Operating expenses | | | | |
| Research and development | 6,648 | 6,779 | 19,369 | 19,456 |
| Selling, general and administrative | 1,952 | 2,435 | 6,583 | 7,541 |
| Total operating expenses | 8,600 | 9,214 | 25,952 | 26,997 |
| Loss from operations | (6,849) | (6,173) | (18,529) | (17,460) |
| Other income and expense, net | 10 | 8 | 44 | 200 |
| Loss before income taxes | (6,839) | (6,165) | (18,485) | (17,260) |
| Income tax provision | 24 | 33 | 59 | 91 |
| Net loss | \$ (6,863) | \$ (6,198) | \$ (18,544) | \$ (17,351) |
| Net loss per share | | | | |
| Basic and diluted | \$ (0.18) | \$ (0.19) | \$ (0.49) | \$ (0.55) |
| Shares used in computing net loss per share | | | | |
| Basic and diluted | 38,090 | 31,946 | 37,700 | 31,616 |

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

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MOSYS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

| | Nine Months Ended September 30, | |
|---|------------------------------------|-------------|
| | 2011 | 2010 |
| Cash flows from operating activities: | | |
| Net loss | \$ (18,544) | \$ (17,351) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization | 839 | 740 |
| Stock-based compensation | 2,474 | 2,296 |
| Amortization of intangible assets | 1,964 | 2,147 |
| Provision for doubtful accounts | 106 | |
| Other non-cash items | 18 | 48 |
| Changes in assets and liabilities, net of business acquired: | | |
| Accounts receivable | 371 | (54) |
| Unbilled contracts receivable | 95 | 1,063 |
| Prepaid expenses and other assets | 1,031 | 1,043 |
| Deferred revenue | (589) | (1,101) |
| Accounts payable | (355) | 1,352 |
| Accrued expenses and other liabilities | (289) | (763) |
| Net cash used in operating activities | (12,879) | (10,580) |
| Cash flows from investing activities: | | |
| Purchases of property and equipment | (349) | (1,274) |
| Net cash paid for purchase of Prism Circuits, Inc. and MagnaLynx, Inc. | (1,000) | (7,936) |
| Proceeds from sales and maturities of marketable securities | 30,314 | 49,786 |
| Purchases of marketable securities | (27,712) | (32,968) |
| Net cash provided by investing activities | 1,253 | 7,608 |
| Cash flows from financing activities: | | |
| Proceeds from issuance of common stock | 3,207 | 1,800 |
| Payments on capital lease obligations | (140) | (61) |
| Net cash provided by financing activities | 3,067 | 1,739 |
| Net decrease in cash and cash equivalents | (8,559) | (1,233) |
| Cash and cash equivalents at beginning of period | 14,340 | 7,123 |
| Cash and cash equivalents at end of period | \$ 5,781 | \$ 5,890 |

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

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MOSYS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. The Company and Summary of Significant Accounting Policies

The Company

MoSys, Inc. (the Company) was incorporated in California in September 1991, and reincorporated in September 2000 in Delaware. The Company designs, develops, markets and licenses high-performance semiconductor memory and high-speed parallel and serial interface intellectual property (IP) used by the semiconductor industry and communications, networking and storage equipment manufacturers. In February 2010, the Company announced the commencement of a new product initiative to develop a family of integrated circuit (IC) products under the Bandwidth Engine product name. Bandwidth Engine ICs combine the Company's high-density embedded memory with its high-speed 10 Gigabits per second interface (I/O) technology and are initially being marketed to networking systems companies and designers of advanced systems on chips designs. To date, the Company has not generated any revenue from the sale of Bandwidth Engine ICs.

The accompanying condensed consolidated financial statements of the Company have been prepared without audit in accordance with the rules and regulations of the Securities and Exchange Commission (SEC). The condensed consolidated balance sheet at December 31, 2010 has been derived from the audited consolidated financial statements at that date. Certain information and disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) have been condensed or omitted in accordance with these rules and regulations. The information in this report should be read in conjunction with the Company's consolidated financial statements and notes thereto included in its most recent annual report on Form 10-K filed with the SEC.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary to summarize fairly the Company's financial position, results of operations and cash flows for the interim periods presented. The operating results for the three and nine months ended September 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011 or for any other future period.

Basis of Presentation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation. The Company's fiscal year is the calendar year.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues recognized under the percentage of completion method and expenses recognized during the reported period. Actual results could differ from those estimates.

Cash Equivalents and Investments

The Company has invested its excess cash in money market accounts, certificates of deposit, corporate debt, government agency and municipal debt securities and considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Investments with original maturities greater than three months and remaining maturities less than one year are classified as short-term investments. Investments with remaining maturities greater than one year are classified as long-term investments. Management generally determines the appropriate classification of securities at the time of purchase. All securities are classified as available-for-sale. The Company's available-for-sale short-term and long-term investments are carried at fair value, with the unrealized holding gains and losses reported in accumulated other comprehensive income (loss). Realized gains and losses and declines in the value judged to be other than temporary are included in the other income and expense, net line item in the condensed consolidated statements of operations. The cost of securities sold is based on the specific identification method.

Fair Value Measurements

The Company measures the fair value of financial instruments using a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels, as follows:

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Level 1 Inputs used to measure fair value are unadjusted quoted prices that are available in active markets for the identical assets or liabilities as of the reporting date.

Level 2 Pricing is provided by third party sources of market information obtained through the Company's investment advisors rather than models. The Company does not adjust for or apply any additional assumptions or estimates to the pricing information it receives from advisors. The Company's Level 2 securities include cash equivalents and available-for-sale securities, which consist primarily of certificates of deposit, corporate debt, and government agency and municipal debt securities from issuers with high quality credit ratings. The Company's investment advisors obtain pricing data from independent sources, such as Standard & Poor's, Bloomberg and Interactive Data Corporation, and rely on comparable pricing of other securities because the Level 2 securities it holds are not actively traded and have fewer observable transactions. The Company considers this the most reliable information available for the valuation of the securities.

Level 3 Unobservable inputs that are supported by little or no market activity and reflect the use of significant management judgment are used to measure fair value. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions. The determination of fair value for Level 3 investments and other financial instruments involves the most management judgment and subjectivity.

Allowance for Doubtful Accounts

The Company establishes an allowance for doubtful accounts to ensure that its trade receivables balances are not overstated due to uncollectibility. The Company performs ongoing customer credit evaluations within the context of the industry in which it operates. A specific allowance of up to 100% of the invoice value is provided for any problematic customer balances. Delinquent account balances are written off after management has determined that the likelihood of collection is remote. The Company performs ongoing credit evaluations of its customers financial condition and generally does not require collateral from its customers. The Company grants credit only to customers deemed creditworthy in the judgment of management. The Company maintains an allowance for doubtful accounts receivable based upon the expected collectibility of all accounts receivable. The allowance for doubtful accounts was \$194,000 and \$125,000 at September 30, 2011 and December 31, 2010, respectively.

Revenue Recognition

General

The Company generates revenue from the licensing of its IP, and customers pay fees for licensing, development services, royalties and maintenance and support. The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery or performance has occurred, the sales price is fixed or determinable, and collectibility is reasonably assured. Evidence of an arrangement generally consists of signed agreements. When sales arrangements contain multiple deliverables (e.g., license and services), the Company reviews each deliverable to determine the separate units of accounting that exist within the agreement. If more than one unit of accounting exists, the consideration payable to the Company under the agreement is allocated to each unit of accounting using the relative fair value method. Revenue is recognized for each unit of accounting when the revenue recognition criteria have been met for that unit of accounting.

Licensing

Licensing revenue consists of fees earned from license agreements, development services and support and maintenance. For stand-alone license agreements or license deliverables in multi-deliverable arrangements that do not require significant development, modification or customization, revenue is recognized when all revenue recognition criteria have been met. Delivery of the licensed technology is typically the final revenue recognition criterion met, at which time revenue is recognized. If any of the criteria are not met, revenue recognition is deferred until such time as all criteria have been met.

Effective with the first quarter of 2011, the Company allocates revenue among license deliverables in multi-deliverable arrangements using the relative selling price method. Revenue allocated to each element is recognized when the basic revenue recognition criteria is met for each element. Under GAAP, the Company is required to apply a hierarchy to determine the selling price to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third-party evidence of selling price (TPE) and (iii) best estimate of the selling price (ESP). In general, the Company is unable to establish VSOE or TPE for its license fees and development services; therefore, revenue is allocated to these elements based on the Company's ESP, which the Company determines after considering multiple factors such as management approved pricing guidelines, geographic differences, market conditions, competitor pricing strategies, internal costs and gross margin objectives. These factors may vary over time depending upon the unique facts and circumstances related to each deliverable. If the facts and circumstances underlying the factors considered change or should future facts and circumstances lead the Company to consider additional factors, the Company's ESP for license fee and development services could change. If the Company's arrangements entered into or materially modified on or after

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January 1, 2011 were subject to the previous accounting guidance, the reported net revenue amount would have remained consistent with reported amounts for the three and nine months ended September 30, 2011.

For license agreements involving deliverables that do require significant production, modification or customization, and where the Company has significant experience in meeting the design specifications in the contract and the direct labor hours related to services under the contract can be reasonably estimated, the Company recognizes revenue over the period in which the contract services are performed. For these arrangements, the Company recognizes revenue using the percentage of completion method. Under this method, revenue recognized in any period depends on the Company's progress toward completion of projects in progress. Significant management judgment and discretion are used to estimate total direct labor hours. These judgmental elements include determining that the Company has the experience to meet the design specifications and estimating the total direct labor hours to perform the contract services, based on experience in developing prior licensee's designs. The direct labor hours for the development of the licensee's design are estimated at the beginning of the contract. As the direct labor hours are incurred, they are used as a measure of progress towards completion. During the contract performance period, the Company reviews estimates of direct labor hours to complete the contracts and will revise its estimates of revenue and gross profit under the contract if it revises the estimations of the direct labor hours to complete. The Company's policy is to reflect any revision in the contract gross profit estimate in reported income or loss in the period in which the facts giving rise to the revision become known. Under the percentage of completion method, provisions for estimated losses on uncompleted contracts are recorded in the period in which such losses are determined to be likely. If the amount of revenue recognized under the percentage of completion accounting method exceeds the amount of billings to a customer, the excess amount is recorded as an unbilled contracts receivable.

For contracts involving design specifications that the Company has not previously met or if inherent risks make estimates doubtful, the contract is accounted for under the completed contract method. Under this method, the Company defers the recognition of all revenue until the design meets the contractual design specifications, and the cost of revenue is expensed as incurred. When the Company has experience in meeting design specifications but the lack of significant experience or inherent risks prevent the Company from reasonably estimating the direct labor hours related to services to meet a design specification, the Company defers the recognition of revenue.

The Company provides support and maintenance under many of its license agreements. Under these arrangements, the Company provides unspecified upgrades, design rule changes and technical support. No other upgrades, products or other post-contract support are provided. Support and maintenance revenue is recognized at its fair value established by VSOE, ratably over the period during which the obligation exists, typically 12 months. These arrangements are generally renewable annually by the customer.

Under limited circumstances, the Company also recognizes prepaid pre-production royalties as licensing revenue. These are lump sum payments made when the Company enters into licensing agreements that cover future shipments of a product that is not commercially available from the licensee. The Company characterizes such payments as licensing revenue because they are paid as part of the initial license fee and not with respect to products being produced by the licensee. These payments are non-cancelable and non-refundable.

Royalty

The Company's licensing contracts typically also provide for royalties based on licensee's use of the Company's memory technology in their currently shipping commercial products. The Company recognizes revenue on royalties in the quarter in which it receives the licensee's report. Under limited circumstances, the Company may also recognize prepaid post-production royalties as revenue upon execution of the contract, which are paid in a lump sum after the licensee commences production of the royalty-bearing product and applied against future unit shipments regardless of the actual level of shipments by the licensee. The criteria for revenue recognition of prepaid royalties are that a formal agreement

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with the licensee is executed, no deliverables, development or support services related to prepaid royalties are required, the fees are non-refundable and not contingent upon future product shipments by the licensee, and the fees are payable by the licensee in a time period consistent with the Company's normal billing terms. If any of these criteria are not met, the Company defers revenue recognition until such time as all criteria have been met.

Cost of Revenue

Cost of licensing revenue consists primarily of engineering personnel and overhead allocation costs directly related to development services specified in agreements. These services typically include customization of the Company's technologies for the licensee's particular IC design and may include engineering support to assist in the commencement of production of a licensee's products. The Company recognizes cost of licensing revenue in the following manner:

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- If licensing revenue is recognized using the percentage of completion method, the associated cost of licensing revenue is recognized in the period in which the Company incurs the engineering costs. If revenue is deferred, the corresponding costs are capitalized in other current assets and charged to cost of licensing revenue when the related revenue is recognized.
- If licensing revenue is recognized using the completed contract method, to the extent that the amount of engineering cost does not exceed the amount of the related licensing revenue, the cost of licensing revenue is deferred on a contract-by-contract basis from the time the Company has established technological feasibility of the product to be developed under the license contract. Technological feasibility is established when the Company has completed all activities necessary to demonstrate that the licensee's product can be produced to meet the performance specifications when incorporating its technology. Deferred costs are capitalized in other current assets and charged to cost of licensing revenue when the related revenue is recognized.

Goodwill

The Company reviews goodwill for impairment on an annual basis or whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable. The Company uses a two-step impairment test. In the first step, the Company compares the fair value of the reporting unit to its carrying value. The fair value of the reporting unit is determined using the market approach. If the fair value of the reporting unit exceeds the carrying value of net assets of the reporting unit, goodwill is not impaired, and the Company is not required to perform further testing. If the carrying value of the net assets of the reporting unit exceeds the fair value of the reporting unit, then the Company must perform the second step in order to determine the implied fair value of the reporting unit's goodwill and compare it to the carrying value of the reporting unit's goodwill. If the carrying value of a reporting unit's goodwill exceeds its implied fair value, then the Company must record an impairment charge equal to the difference. The Company has determined that it has a single reporting unit for purposes of performing its goodwill impairment test. The Company performed the annual impairment test in September 2011, and the test did not indicate impairment of goodwill, as the fair value exceeded the carrying value of the reporting unit by approximately 61%. As the Company used the market approach to assess impairment, the price of its common stock is an important component of the fair value calculation. If the Company's stock price continues to experience significant price and volume fluctuations, this will impact the fair value of the reporting unit, which can lead to potential impairment in future periods. As of September 30, 2011, the Company had not identified any factors to indicate there was an impairment of its goodwill and determined that no additional impairment analysis was required.

Purchased Intangible Assets

Intangible assets acquired in business combinations are accounted for based on the fair value of assets purchased and are amortized over the period in which economic benefit is estimated to be received. Identifiable intangible assets relating to business combinations were as follows (dollar amounts in thousands):

| | | September 30, 2011 | | |
|------------------------|-----------------|-----------------------------|-----------------------------|--------------------------|
| | Life (years) | Gross Carrying Amount | Accumulated Amortization | Net Carrying Value |
| Developed technology | 3-5 | \$ 9,240 | \$ 5,054 | \$ 4,186 |
| Customer relationships | 3 | 390 | 302 | 88 |
| Contract backlog | 1 | 750 | 750 | |
| Non-compete agreements | 1.5 | 140 | 140 | |

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| | | | | | | |
|-------|----|--------|----|-------|----|-------|
| Total | \$ | 10,520 | \$ | 6,246 | \$ | 4,274 |
|-------|----|--------|----|-------|----|-------|

| | | December 31, 2010 | | |
|------------------------|-----------------|-----------------------------|-----------------------------|--------------------------|
| | Life (years) | Gross Carrying Amount | Accumulated Amortization | Net Carrying Value |
| Developed technology | 3-5 | \$ 9,240 | \$ 3,188 | \$ 6,052 |
| Customer relationships | 3 | 390 | 204 | 186 |
| Contract backlog | 1 | 750 | 750 | |
| Non-compete agreements | 1.5 | 140 | 140 | |
| Total | | \$ 10,520 | \$ 4,282 | \$ 6,238 |

The related amortization expense was \$0.7 million and \$2.0 million for the three and nine months ended September 30, 2011, respectively. The amortization expense was \$0.7 million and \$2.1 million for the three and nine months ended September 30, 2010, respectively. Amortization expense has been included in research and development expense in the condensed consolidated statements

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of operations. The estimated aggregate amortization expense to be recognized in the future is approximately \$0.7 million for the remainder of 2011, \$1.6 million for 2012, \$0.9 million for 2013, \$0.9 million for 2014 and \$0.2 million for 2015.

Per Share Amounts

Basic net loss per share is computed by dividing net loss for the period by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per share gives effect to all potentially dilutive common shares outstanding during the period. Potentially dilutive common shares consist of incremental shares of common stock issuable upon the exercise of stock options, vesting of stock awards and purchases under the employee stock purchase plan. As of September 30, 2011 and 2010, stock awards to purchase approximately 10,129,000 and 10,699,000 shares, respectively, were excluded from the computation of diluted net loss per share as their inclusion would be anti-dilutive.

Comprehensive Loss

Comprehensive loss, as defined, includes all changes in equity (net assets) during a period from non-owner sources. The components of comprehensive loss for the three and nine months ended September 30, 2011 and 2010 were as follows (in thousands):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|------------|------------------------------------|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| Net loss | \$ (6,863) | \$ (6,198) | \$ (18,544) | \$ (17,351) |
| Change in net unrealized gains (losses) on available-for-sale securities | (23) | 14 | (15) | (21) |
| Comprehensive loss | \$ (6,886) | \$ (6,184) | \$ (18,559) | \$ (17,372) |

Recent Accounting Pronouncements

In September 2011, the Financial Accounting Standards Board (FASB) issued ASU No. 2011-08, *Intangibles-Goodwill and Other - Testing Goodwill for Impairment*. Under this updated guidance, an entity is permitted to first assess qualitative factors to determine whether it is more-likely-than-not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The effective date of this guidance is for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The Company does not believe the adoption of this guidance will have a material effect on its consolidated financial statements.

Note 2. Fair Value of Financial Instruments

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The estimated fair values of financial instruments outstanding were as follows (in thousands):

| | Cost | September 30, 2011 | | Fair Value |
|---------------------------------|-----------|--------------------|-------------------|------------|
| | | Unrealized Gains | Unrealized Losses | |
| Cash and cash equivalents | \$ 5,781 | \$ | \$ | \$ 5,781 |
| Short-term investments: | | | | |
| U.S. government debt securities | \$ 8,763 | \$ 1 | \$ | \$ 8,764 |
| Corporate notes | 3,037 | 4 | (1) | 3,040 |
| Certificates of deposit | 720 | | | 720 |
| Total short-term investments | \$ 12,520 | \$ 5 | \$ (1) | \$ 12,524 |
| Long-term investments: | | | | |
| U.S. government debt securities | \$ 3,000 | \$ | \$ (1) | \$ 2,999 |
| Corporate notes | 3,876 | | (14) | 3,862 |
| Certificates of deposit | 1,200 | 1 | (1) | 1,200 |
| Total long-term investments | \$ 8,076 | \$ 1 | \$ (16) | \$ 8,061 |

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| | Cost | December 31, 2010 | | Fair Value |
|---------------------------------|-----------|-------------------|-------------------|------------|
| | | Unrealized Gains | Unrealized Losses | |
| Cash and cash equivalents | \$ 14,340 | \$ | \$ | \$ 14,340 |
| Short-term investments: | | | | |
| U.S. government debt securities | \$ 8,711 | \$ 1 | \$ (2) | \$ 8,710 |
| Corporate notes | 5,115 | 6 | (5) | 5,116 |
| Certificates of deposit | 1,185 | | | 1,185 |
| Total short-term investments | \$ 15,011 | \$ 7 | \$ (7) | \$ 15,011 |
| Long-term investments: | | | | |
| U.S. government debt securities | \$ 6,204 | \$ | \$ (2) | \$ 6,202 |
| Corporate notes | 1,507 | 6 | | 1,513 |
| Certificates of deposit | 480 | | (2) | 478 |
| Total long-term investments | \$ 8,191 | \$ 6 | \$ (4) | \$ 8,193 |

As of September, 30, 2011 and December 31, 2010, all of the available-for-sale securities with unrealized losses had been in a loss position for less than 12 months. Total fair value of available-for-sale securities with unrealized losses was \$11.7 million at September 30, 2011.

Cost and fair value of investments based on two maturity groups were as follows (in thousands):

| | Cost | September 30, 2011 | | Fair Value |
|-------------------|-----------|--------------------|-------------------|------------|
| | | Unrealized Gains | Unrealized Losses | |
| Due within 1 year | \$ 12,520 | \$ 5 | \$ (1) | \$ 12,524 |
| Due in 1-2 years | 8,076 | 1 | (16) | 8,061 |
| Total | \$ 20,596 | \$ 6 | \$ (17) | \$ 20,585 |

| | Cost | December 31, 2010 | | Fair Value |
|-------------------|-----------|-------------------|-------------------|------------|
| | | Unrealized Gains | Unrealized Losses | |
| Due within 1 year | \$ 15,011 | \$ 7 | \$ (7) | \$ 15,011 |
| Due in 1-2 years | 8,191 | 6 | (4) | 8,193 |
| Total | \$ 23,202 | \$ 13 | \$ (11) | \$ 23,204 |

The following table represents the Company's fair value hierarchy for its financial assets (cash equivalents and investments) as of September 30, 2011 (in thousands):

| | Fair Value | September 30, 2011 | | |
|-------------------------|------------|--------------------|---------|---------|
| | | Level 1 | Level 2 | Level 3 |
| Money market funds | \$ 5,321 | \$ 5,321 | \$ | \$ |
| Certificates of deposit | 1,920 | | 1,920 | |
| Corporate notes | 6,902 | | 6,902 | |

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| | | | | | |
|---------------------------------|----|--------|----|-------|-----------|
| U.S. government debt securities | | 11,763 | | | 11,763 |
| Total assets | \$ | 25,906 | \$ | 5,321 | \$ 20,585 |

There were no transfers in or out of Level 1 and Level 2 securities during the three and nine months ended September 30, 2011. There were no Level 3 financial assets as of September 30, 2011.

Note 3. Acquisitions

MagnaLynx

In March 2010, the Company acquired all of the outstanding stock of MagnaLynx, Inc. (MagnaLynx), a provider of semiconductor interface technology. Under the terms of the merger agreement, the Company paid approximately \$2.2 million to settle debt and certain other liabilities of MagnaLynx and approximately \$1.2 million to MagnaLynx shareholders. An additional \$0.5 million, referred to as the indemnification holdback, is payable 18 months after the closing, net of any costs related to indemnification claims that may arise during such 18 month period. The full amount of the indemnification holdback was paid in October 2011. In addition, the Company paid an additional \$1.0 million to the former shareholders of MagnaLynx in the second quarter of 2011, as earn-out consideration based on MagnaLynx meeting certain contractually agreed-upon development milestones. This earn-out consideration was included in the acquisition price because the Company expected that it was more likely than not that the objectives related to this earn-out would be met.

The Company recorded a total acquisition price as follows (in thousands):

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| | | |
|------------------------------|----|-------|
| Cash | \$ | 3,355 |
| Acquisition-related earn-out | | 1,000 |
| Indemnification holdback | | 500 |
| Liabilities assumed by MoSys | | 32 |
| Total acquisition price | \$ | 4,887 |

The allocation of the acquisition price for net tangible and intangible assets was as follows (in thousands):

| | | |
|---|----|-------|
| Net tangible assets | \$ | 100 |
| Intangible asset - developed technology | | 4,440 |
| Goodwill | | 347 |
| Total acquisition price | \$ | 4,887 |

Goodwill represents the excess of the acquisition price of an acquired business over the fair value of the underlying net tangible and intangible assets. Included in the goodwill amount is the value of the acquired workforce, which has significant expertise in low-power interface IP. The goodwill recognized is expected to be deductible for income tax purposes.

The value of the identifiable intangible asset was determined by using future cash flow assumptions. The intangible asset, which is considered developed technology, is being amortized on a straight-line basis over its estimated life of five years.

Note 4. Commitments and Contingencies*Indemnifications*

In the ordinary course of business, the Company enters into contractual arrangements under which it may agree to indemnify the counterparties from any losses incurred relating to breach of representations and warranties, failure to perform certain covenants, or claims and losses arising from certain events as outlined within the particular contract, which may include, for example, losses arising from litigation or claims relating to past performance. Such indemnification clauses may not be subject to maximum loss clauses. The Company has entered into indemnification agreements with its officers and directors. No material amounts were reflected in the Company's condensed consolidated financial statements for the three and nine months ended September 30, 2011 or 2010 related to these indemnifications.

The Company has not estimated the maximum potential amount of indemnification liability under these agreements due to the limited history of prior claims and the unique facts and circumstances applicable to each particular agreement. To date, the Company has not made any material payments related to these indemnification agreements.

Legal Matters

The Company is not a party to any material legal proceeding that the Company believes is likely to have a material adverse effect on its consolidated financial position or results of operations. From time to time, the Company may be subject to legal proceedings and claims in the ordinary course of business. These claims, even if not meritorious, could result in the expenditure of significant financial resources and diversion of management efforts.

Note 5. Business Segments and Significant Customers

The Company operates in one business segment and uses one measurement of profitability for its business. Revenue attributed to the United States and to all foreign countries is based on the geographical location of the customer.

The Company recognized revenue from licensing of its technologies to customers in North America, Asia and Europe as follows (in thousands):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---------------|-------------------------------------|----------|------------------------------------|-----------|
| | 2011 | 2010 | 2011 | 2010 |
| United States | \$ 638 | \$ 1,519 | \$ 3,072 | \$ 4,529 |
| Japan | 511 | 1,394 | 2,721 | 4,900 |
| Taiwan | 785 | 760 | 2,422 | 2,042 |
| Europe | 173 | | 715 | |
| Other Asia | | 103 | 8 | 124 |
| Total | \$ 2,107 | \$ 3,776 | \$ 8,938 | \$ 11,595 |

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Customers who accounted for at least 10% of total revenues were as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------|-------------------------------------|------|------------------------------------|------|
| | 2011 | 2010 | 2011 | 2010 |
| Customer A | 37% | 20% | 27% | 17% |
| Customer B | 17% | 9% | 14% | 9% |
| Customer C | 13% | 1% | 5% | 2% |
| Customer D | % | 23% | 14% | 21% |
| Customer E | % | 13% | 3% | 5% |

Five customers accounted for 100% of net accounts receivable at September 30, 2011. Four customers accounted for 99% of net accounts receivable at December 31, 2010.

Note 6. Income Tax Provision

The Company determines deferred tax assets and liabilities based upon the differences between the financial statement and tax bases of the Company's assets and liabilities using tax rates in effect for the year in which the Company expects the differences to affect taxable income. A valuation allowance is established for any deferred tax assets for which it is more likely than not that all or a portion of the deferred tax assets will not be realized.

The Company files U.S. federal and state and foreign income tax returns in jurisdictions with varying statutes of limitations. The Company is not currently under any tax jurisdiction examination. The 2003 through 2010 tax years generally remain subject to examination by federal, state and foreign tax authorities. As of September 30, 2011, the Company did not have any unrecognized tax benefits or recognize any interest or penalties related to unrecognized tax benefits.

Note 7. Stock-Based Compensation

The Company recorded \$0.9 million and \$0.8 million of stock-based compensation expense for the three months ended September 30, 2011 and 2010, respectively. The Company recorded \$2.5 million and \$2.3 million of stock-based compensation expense for the nine months ended September 30, 2011 and 2010, respectively. The expense relating to stock-based awards is recognized on a straight-line basis over the requisite service period, usually the vesting period, based on the grant-date fair value. The unamortized compensation cost, net of expected forfeitures, as of September 30, 2011 was \$4.4 million and is expected to be recognized as expense over a weighted average period of approximately 2.17 years.

The Company presents the tax benefits resulting from tax deductions in excess of the compensation cost recognized from the exercise of stock options as financing cash flows in the condensed consolidated statements of cash flows. For the three and nine months ended September 30, 2011 and 2010, there were no such tax benefits associated with the exercise of stock options due to the Company's loss position.

Common Stock Options and Restricted Stock

A summary of the option and restricted stock unit activity under the Company's Amended and Restated 2000 Stock Option and Equity Incentive Plan (Amended 2000 Plan) and 2010 Equity Incentive Plan (2010 Plan), referred to collectively as the Plans, is presented below (in thousands, except exercise price):

| | Available for Grant | Number of Shares | Options Outstanding Weighted Average Exercise Prices | |
|--|------------------------|---------------------|--|------|
| Balance at December 31, 2010 | 3,650 | 5,594 | \$ | 4.64 |
| Additional shares authorized under the 2010 Plan | 500 | | | |
| Options granted | (120) | 120 | \$ | 5.94 |
| Options cancelled | 2 | (323) | \$ | 3.86 |
| Options exercised | | (200) | \$ | 3.51 |
| Balance at March 31, 2011 | 4,032 | 5,191 | \$ | 4.76 |
| Options granted | (334) | 334 | \$ | 5.92 |
| Options cancelled | | (242) | \$ | 7.67 |
| Options exercised | | (251) | \$ | 3.62 |
| Balance at June 30, 2011 | 3,698 | 5,032 | \$ | 4.75 |
| Options granted | (121) | 121 | \$ | 5.18 |
| Options cancelled | 3 | (90) | \$ | 6.64 |
| Options exercised | | (55) | \$ | 1.67 |
| Balance at September 30, 2011 | 3,580 | 5,008 | \$ | 4.76 |

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On June 30, 2011, the Company's executive vice president of engineering resigned from the Company and agreed to act as a consultant for an indefinite period. As compensation for the consulting services, an option to purchase 675,000 shares of the Company's common stock granted to the executive vice president on June 26, 2009, of which the unvested and unexercised portion would have otherwise terminated by its terms following the termination of employment with the Company, will remain in effect and continue to vest in accordance with its vesting terms during the term of the consulting agreement. The Company accounts for this option as a variable award and the fair value compensation expense will be recognized each period over the remaining vesting term of the option. As a result of the option modification, the Company recognized \$0.2 million of stock-based compensation expense during the quarter and nine months ended September 30, 2011.

A summary of restricted stock award and restricted stock unit activity for grants outside of the Plans is presented below (in thousands, except fair value):

| | Number of Shares | | Weighted Average Grant-Date Fair Value |
|---|---------------------|----|---|
| Non-vested shares at March 31, 2011 and December 31, 2010 | 31 | \$ | 1.60 |
| Vested | (16) | \$ | 1.60 |
| Non-vested shares at September 30, 2011 and June 30, 2011 | 15 | \$ | 1.60 |

The Company also has awarded shares to new employees outside the Plans and may continue to do so outside the 2010 Plan, as a material inducement to the acceptance of employment with the Company. These grants must be approved by the compensation committee of the board of directors, a majority of the independent directors or an authorized executive officer, as specified under the Listing Rules of the Nasdaq Stock Market.

A summary of the inducement grant option activity is presented below (in thousands, except exercise price):

| | Number of Shares | | Options Outstanding Weighted Average Exercise Prices |
|-------------------------------|---------------------|----|--|
| Balance at December 31, 2010 | 4,812 | \$ | 2.92 |
| Exercised | (52) | \$ | 1.55 |
| Balance at March 31, 2011 | 4,760 | \$ | 2.93 |
| Granted | 400 | \$ | 6.06 |
| Cancelled | (2) | \$ | 1.50 |
| Exercised | (152) | \$ | 1.55 |
| Balance at June 30, 2011 | 5,006 | \$ | 3.22 |
| Cancelled | (36) | \$ | 1.55 |
| Exercised | (47) | \$ | 1.54 |
| Balance at September 30, 2011 | 4,923 | \$ | 3.25 |

The following table summarizes significant ranges of outstanding and exercisable options and inducement grants, excluding restricted stock award and restricted stock unit activity, as of September 30, 2011 (in thousands, except contractual life and exercise price):

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| Range of Exercise Price | Number Outstanding | Options Outstanding | | | Options Exercisable | | | |
|-------------------------|--------------------|--|---------------------------------|---------------------------|---------------------|--|---------------------------------|---------------------------|
| | | Weighted Average Remaining Contractual Life (in Years) | Weighted Average Exercise Price | Aggregate Intrinsic value | Number Exercisable | Weighted Average Remaining Contractual Life (in Years) | Weighted Average Exercise Price | Aggregate Intrinsic value |
| \$1.50 - \$2.50 | 3,656 | 3.43 | \$ 1.69 | \$ 7,208 | 1,766 | 3.42 | \$ 1.69 | \$ 3,484 |
| \$2.51 - \$5.00 | 2,935 | 4.01 | \$ 4.18 | 224 | 1,818 | 3.69 | \$ 4.11 | 102 |
| \$5.01 - \$7.50 | 2,693 | 4.70 | \$ 5.87 | | 1,606 | 4.16 | \$ 5.86 | |
| \$7.51 - \$15.00 | 647 | 1.42 | \$ 8.63 | | 647 | 1.42 | \$ 8.63 | |
| | 9,931 | 3.81 | \$ 4.01 | \$ 7,432 | 5,837 | 3.49 | \$ 4.36 | \$ 3,586 |

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As of September 30, 2011, the Company had 9.3 million shares subject to outstanding options fully vested and expected to vest, after estimated forfeitures, with a remaining contractual life of 3.77 years, weighted average exercise price of \$4.03 and aggregate intrinsic value of \$6.9 million.

The total fair value of shares subject to outstanding options vested during the nine months ended September 30, 2011 and 2010 calculated using the Black-Scholes valuation method was \$1.2 million and \$1.3 million, respectively. The total intrinsic value of employee stock options exercised during the nine months ended September 30, 2011 and 2010 was \$2.2 million and \$1.8 million, respectively.

Options to purchase 5.8 million and 5.0 million shares with weighted average exercise prices of \$4.36 and \$4.84 per share were exercisable at September 30, 2011 and 2010, respectively.

Valuation Assumptions and Expense Information

The fair value of the Company's share-based payment awards for the three and nine months ended September 30, 2011 and 2010 was estimated on the grant date using a Black-Scholes valuation method and an option-pricing model with the following assumptions:

| | Three Months Ended September 30, | | | | Nine Months Ended September 30, | | | |
|--------------------------------|-------------------------------------|-------|-------|-------|------------------------------------|-------|-------|-------|
| | 2011 | | 2010 | | 2011 | | 2010 | |
| Employee stock options: | | | | | | | | |
| Risk-free interest rate | 0.2% | 0.7% | 1.3% | 1.4% | 0.2% | 1.7% | 1.3% | 2.1% |
| Volatility | 40.7% | 61.3% | 63.4% | 63.5% | 40.7% | 63.8% | 63.0% | 72.7% |
| Expected life (years) | 4.0 | | 4.0 | | 4.0 | | 4.0 | |
| Dividend yield | 0% | | 0% | | 0% | | 0% | |

The risk-free interest rate was derived from the Daily Treasury Yield Curve Rates as published by the U.S. Department of the Treasury as of the grant date for terms equal to the expected terms of the options. The expected volatility was based on the combination of: 1) four-year historical volatility and 2) implied volatility of the Company's stock price. The expected term of options granted was derived from historical data based on employee exercises and post-vesting employment termination behavior. A dividend yield of zero is applied because the Company has never paid dividends and has no intention to pay dividends in the near future.

The stock-based compensation expense recorded is adjusted based on estimated forfeiture rates. An annualized forfeiture rate has been used as a best estimate of future forfeitures based on the Company's historical forfeiture experience. The stock-based compensation expense will be adjusted in later periods if the actual forfeiture rate is different from the estimate.

Employee Stock Purchase Plan

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In June 2010, the Company's stockholders approved the 2010 Employee Stock Purchase Plan (ESPP). A total of 2.0 million shares of common stock have been reserved for issuance under the ESPP. The ESPP, which is intended to qualify under Section 423 of the Internal Revenue Code, is administered by the board of directors or the compensation committee of the board of directors. The ESPP provides that eligible employees may purchase up to \$25,000 worth of the Company's common stock annually over the course of two six-month offering periods. The purchase price to be paid by participants is 85% of the price per share of the Company's common stock either at the beginning or the end of each six-month offering period, whichever is less. On September 1, 2010, the Company commenced the first six month offering period under the ESPP. On February 29, 2011, approximately 149,000 shares of common stock were issued at an aggregate purchase price of \$581,000 under the ESPP. On August 31, 2011, approximately 164,000 shares of common stock were issued at an aggregate purchase price of \$558,000 under the ESPP.

Note 8. Subsequent Events

The Company has evaluated subsequent events through the date the preparation of these unaudited condensed consolidated financial statements was complete and did not identify any material recognizable subsequent events.

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the accompanying condensed consolidated financial statements and notes included in this report. This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which include, without limitation, statements about the market for our technology, our strategy, competition, expected financial performance, all information disclosed under Item 3 of this Part I, and other aspects of our business identified in our most recent annual report on Form 10-K filed with the Securities and Exchange Commission on March 15, 2011 and in other reports that we file from time to time with the Securities and Exchange Commission. Any statements about our business, financial results, financial condition and operations contained in this Form 10-Q that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes, anticipates, expects, intends, plans, projects, or similar expressions are intended to identify forward-looking statements. Our actual results could differ materially from those expressed or implied by these forward-looking statements as a result of various factors, including the risk factors described below in Risk Factors and elsewhere in this report and under Item 1A of our annual report on Form 10-K for the year ended December 31, 2010. We undertake no obligation to update publicly any forward-looking statements for any reason, except as required by law, even as new information becomes available or events occur in the future.

Overview

To date, our primary business has been defining, designing, marketing and licensing differentiated embedded memory and high-speed parallel and serial interface (I/O), intellectual property (IP), for advanced Systems on Chips (SOCs), designs. The 1T-SRAM is our high-density, high-performance patented memory solution that represents an alternative to traditional volatile embedded memory. Our I/O IP includes physical layer (PHY) circuitry that allows integrated circuits (ICs) to communicate with one another in the networking, storage, computer and consumer market segments. Our PHY IP supports serial interface technologies, such as 10G Base KR, XAUI, PCI Express and SATA, as well as parallel interfaces like DDR3. Our IP customers typically include fabless semiconductor companies, integrated device manufacturers (IDMs) and foundries. We generate revenue from the licensing of our IP, and our customers pay us fees for one or more of the following: licensing, development services, royalties and/or maintenance and support. Royalty revenues are typically earned under our memory license agreements when our licensees manufacture or sell products that incorporate any of our memory technologies.

In February 2010, we announced a new product initiative to develop a family of integrated circuit products under the Bandwidth Engine product name. Our Bandwidth Engine family of ICs combines our 1T-SRAM high-density embedded memory with our high-speed 10 Gigabits per second (Gbps) serial I/O technology and is initially being marketed to networking systems companies. Bandwidth Engine ICs have been designed to increase system performance by using a serial I/O to increase the accesses per second between the processor and memory components in networking systems. Since the beginning of 2010, we have invested a significant amount of our financial and engineering resources towards the development of our Bandwidth Engine family of ICs. We shipped initial samples of our first Bandwidth Engine ICs to prospective customers in December 2010, and, in November 2011, we announced two design wins for low volume applications.

Our strategy and primary business objective is to become a fabless semiconductor company focused on the development and sale of Bandwidth Engine ICs to the networking equipment systems providers and their subsystem and component vendors. Our future success and ability to achieve and maintain profitability will be dependent on our success in developing a market for our Bandwidth Engine ICs. We have begun to dedicate more of our engineering resources and the engineering budget to our integrated circuit efforts and expect that this trend will continue as we place more emphasis on integrated circuit product sales as opposed to IP sales. As a result, we have begun placing less emphasis on IP licensing and deploying more resources for our IC product development and marketing efforts, and our competitiveness and the demand for our IP have declined since the beginning of the year. We do not expect to generate significant revenue from our Bandwidth Engine ICs until the second half of 2012 or later and believe that IC revenues are not likely to approximate the revenues generated from licensing and royalties until

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at least 2013. As a result of our reduced licensing activities, it will be challenging for us to grow or maintain our licensing revenue at current levels, and we do not expect our royalty revenue to grow in future periods, and we believe that our licensing revenues in future periods are likely to be lower than they were in 2011.

Sources of Revenue

We currently generate two types of IP revenue: licensing and royalties.

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Licensing. Licensing revenue consists of fees earned from license agreements, development services, prepaid pre-production royalties, and support and maintenance. Our license agreements involve long sales cycles, which make it difficult to predict when the agreements will be signed. In addition, our licensing revenue fluctuates from period to period, and it is difficult for us to predict the timing and magnitude of such revenue from quarter to quarter. Moreover, we believe that the amount of licensing revenue for any period is not necessarily indicative of results in any future period.

Our licensing revenue consists primarily of fees for providing circuit design, layout and design verification and granting licenses to customers that embed our technology into their products. License fees generally range from \$100,000 to several million dollars per contract, depending on the scope and complexity of the development project, and the extent of the licensee's rights. The vast majority of our contracts allow for milestone billing based on work performed. Fees billed prior to revenue recognition are recorded as deferred revenue.

Royalty. Royalty revenue represents amounts earned under provisions in our memory licensing contracts that require our licensees to report royalties and make payments at a stated rate based on actual units manufactured or sold by licensees for products that include our memory IP. We recognize royalties in the quarter in which we receive the licensee's report.

Royalty-bearing license agreements provide for royalty payments at a stated rate. We negotiate royalty rates by taking into account such factors as the anticipated volume of the licensee's sales of products utilizing our technologies and the cost savings to be achieved by the licensee through the use of our technology. Our license agreements require the licensee to report the manufacture or sale of products that include our technology after the end of the quarter in which the sale or manufacture occurs.

As with our licensing revenue, the timing and level of royalties are difficult to predict. They depend on the licensee's ability to market, produce and sell products incorporating our technology. Many of the products of our licensees that are currently subject to licenses from us are used in consumer products, such as electronic game consoles, for which demand can be seasonal.

Critical Accounting Policies and Use of Estimates

The discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make certain estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis we make these estimates based on our historical experience and on assumptions that we consider reasonable under the circumstances. Actual results may differ from these estimates, and reported results could differ under different assumptions or conditions. Our significant accounting policies and estimates are disclosed in Note 1 of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2010. As of September 30, 2011, there have been no material changes to our significant accounting policies and estimates, with the exception of our accounting policy for revenue recognition as described in Note 1 of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report under the heading Revenue Recognition.

Results of Operations

Revenue.

| | September 30, 2011 | September 30, 2010 | Change 2010 to 2011 | |
|---------------------------------|-------------------------------|-----------------------|------------------------|-------|
| | (dollar amounts in thousands) | | | |
| Licensing three months ended | \$ 756 | \$ 1,494 | \$ (738) | (49)% |
| Percentage of total net revenue | 36% | 40% | | |
| Licensing nine months ended | \$ 3,319 | \$ 5,060 | \$ (1,741) | (34)% |
| Percentage of total net revenue | 37% | 44% | | |

Licensing revenue decreased for the three and nine months ended September 30, 2011, compared with the same periods of 2010, primarily due a decreased level of licensing activity compared to the prior periods due to weaker global economic conditions, increased competition, and delays in proving our SerDes IP at more advanced foundry process nodes, which have reduced new license fee engagements with customers since the end of the second quarter. We experienced delays in customer acceptance of IP delivered under license agreements entered into in prior periods, which resulted in lower revenue recognition. Also, in the fourth quarter of 2009 and second quarter of 2010, technology agreements were signed with customers, which resulted in significant revenue recognition in the comparable prior periods.

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| | | 2011 | September 30, 2010 | (dollar amounts in thousands) | | Change 2010 to 2011 |
|---------------------------------|----|-------|-----------------------|-------------------------------|----|------------------------|
| Royalty three months ended | \$ | 1,351 | \$ | 2,282 | \$ | (931) (41)% |
| Percentage of total net revenue | | 64% | | 60% | | |
| Royalty nine months ended | \$ | 5,619 | \$ | 6,535 | \$ | (916) (14)% |
| Percentage of total net revenue | | 63% | | 56% | | |

Royalty revenue decreased for the three and nine months ended September 30, 2011, compared with the same period of 2010, primarily due to a decrease in shipments by an IDM licensee whose product is used in the Nintendo Wii® game console combined with lower shipments by other licensees. Specifically, we believe this significant decrease in royalties in the third quarter of 2011 from this IDM licensee was attributable to an inventory correction. We believe this inventory correction is complete, and we expect royalty revenues will increase in the fourth quarter of 2011. The decrease in royalty revenue for the nine months ended September 30, 2011, was partially offset by an increase in royalties received from a major foundry partner and a fabless semiconductor company.

Cost of Net Revenue and Gross Profit.

| | | 2011 | September 30, 2010 | (dollar amounts in thousands) | | Change 2010 to 2011 |
|--|----|-------|-----------------------|-------------------------------|----|------------------------|
| Cost of net revenue three months ended | \$ | 356 | \$ | 735 | \$ | (379) (52)% |
| Percentage of total net revenue | | 17% | | 19% | | |
| Cost of net revenue nine months ended | \$ | 1,515 | \$ | 2,058 | \$ | (543) (26)% |
| Percentage of total net revenue | | 17% | | 18% | | |

| | | 2011 | September 30, 2010 | (dollar amounts in thousands) | | Change 2010 to 2011 |
|---------------------------------|----|-------|-----------------------|-------------------------------|----|------------------------|
| Gross profit three months ended | \$ | 1,751 | \$ | 3,041 | \$ | (1,290) (42)% |
| Percentage of total net revenue | | 83% | | 81% | | |
| Gross profit nine months ended | \$ | 7,423 | \$ | 9,537 | \$ | (2,114) (22)% |
| Percentage of total net revenue | | 83% | | 82% | | |

Cost of net revenue consists of personnel costs for engineers assigned to revenue-generating licensing arrangements and related overhead allocation costs.

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Cost of net revenue decreased in absolute dollars and as a percentage of total net revenue for the three and nine months ended September 30, 2011, compared with the same period of 2010, primarily due to a fewer number of projects requiring customization. Cost of net revenue included stock-based compensation expense of \$30,000 and \$76,000 for the three months ended September 30, 2011 and 2010, respectively, and \$137,000 and \$246,000 for the nine months ended September 30, 2011 and 2010, respectively.

Gross profit decreased by \$1.3 million and \$2.1 million for the three and nine months ended September 30, 2011, respectively, primarily due to the decrease in our revenue. Gross margin percentage increased by 2% and 1% for the three and nine months ended September 30, 2011, respectively, from the year ago periods primarily due to the decrease in projects requiring customization.

Research and Development.

| | | | | | | | |
|---|----|--------|----|--------|----|-------|------|
| | | | | | | | |
| Research and development three months ended | \$ | 6,648 | \$ | 6,779 | \$ | (131) | (2)% |
| Percentage of total net revenue | | 316% | | 180% | | | |
| Research and development nine months ended | \$ | 19,369 | \$ | 19,456 | \$ | (87) | |
| Percentage of total net revenue | | 217% | | 168% | | | |

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Our research and development expenses include development and design of variations of our 1T-SRAM and I/O technologies for use in different manufacturing processes used by licensees, costs related to the development of the Bandwidth Engine IC and amortization of intangible assets. We expense research and development costs as they are incurred.

The \$0.1 million decrease for the three months ended September 30, 2011, compared with the same period a year ago, was primarily due to the decrease in mask costs related to the Bandwidth Engine product and personnel-related costs, partially offset by increases in software tool costs, capitalized development costs and stock-based compensation expense.

Research and development expenses included stock-based compensation expense of \$0.6 million and \$0.4 million for the three months ended September 30, 2011 and 2010, respectively.

The \$0.1 million decrease for the nine months ended September 30, 2011 compared with the same period a year ago, primarily due to the decrease in mask costs related to the Bandwidth Engine product and contingent compensation charges related to our acquisitions of Prism Circuits in 2009 and MagnaLynx in 2010, partially offset by increases in software tool costs, capitalized development costs and stock-based compensation expense.

Research and development expenses included stock-based compensation expense of \$1.4 million and \$1.1 million for the nine months ended September 30, 2011 and 2010, respectively.

We expect that research and development expenses will increase in absolute dollars and as a percentage of total net revenues as we invest in new product development for our embedded memory and I/O technologies and development of future versions of our Bandwidth Engine IC products.

Selling, General and Administrative (SG&A).

| | | September 30, | | September 30, | | Change | |
|---------------------------------|------|---------------|-------------------------------|---------------|------|--------------|-------|
| | 2011 | | 2010 | | 2010 | 2010 to 2011 | |
| | | | (dollar amounts in thousands) | | | | |
| SG&A three months ended | \$ | 1,952 | \$ | 2,435 | \$ | (483) | (20)% |
| Percentage of total net revenue | | 93% | | 64% | | | |
| SG&A nine months ended | \$ | 6,583 | \$ | 7,541 | \$ | (958) | (13)% |
| Percentage of total net revenue | | 74% | | 65% | | | |

SG&A expenses consist primarily of personnel and related overhead costs for sales, marketing, IP application engineering, finance, human resources and general management.

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The \$0.5 million decrease for the three months ended September 30, 2011, compared with the same period a year ago, was primarily due to the following:

- \$0.2 million decrease in personnel costs; and
- \$0.3 million decrease in individually minor items.

The \$1.0 million decrease for the nine months ended September 30, 2011, compared with the same period a year ago, was primarily due to the following:

- \$0.6 million decrease in personnel costs; and
- \$0.6 million decrease in professional service costs; partially offset by
- \$0.2 million increase in individually minor items.

Selling, general and administrative expenses included stock-based compensation expense of \$0.3 million for each of the three months ended September 30, 2011 and 2010. Selling, general and administrative expenses included stock-based compensation expense of \$1.0 million for each of the nine months ended September 30, 2011 and 2010.

We expect total selling, general and administrative expenses to increase in absolute dollars due to an increase in sales and marketing efforts related to developing a sales channel for our Bandwidth Engine IC product line.

Table of Contents*Other Income and Expense, net.*

| | | September 30, 2011 | September 30, 2010 | Change 2010 to 2011 | |
|---------------------------------|--------------------|-----------------------|-----------------------|------------------------|-------|
| (dollar amounts in thousands) | | | | | |
| Other income and expense, net | three months ended | \$ 10 | \$ 8 | \$ 2 | (25)% |
| Percentage of total net revenue | | | | | |
| Other income and expense, net | nine months ended | \$ 44 | \$ 200 | \$ (156) | (78)% |
| Percentage of total net revenue | | | 2% | | |

Other income and expense, net primarily consisted of interest income on our investments, which was \$0.1 million and \$0.2 million for the nine months ended September 30, 2011 and 2010, respectively. Interest income declined due to lower interest rates earned on investment balances compared to prior year periods. Interest income was partially offset by expenses including foreign exchange transaction losses and other non-operating expenses for the nine months ended September 30, 2011.

Income Tax Provision.

| | | September 30, 2011 | September 30, 2010 | Change 2010 to 2011 | |
|---------------------------------|--------------------|-----------------------|-----------------------|------------------------|-------|
| (dollar amounts in thousands) | | | | | |
| Income tax provision | three months ended | \$ 24 | \$ 33 | \$ (9) | (27)% |
| Percentage of total net revenue | | 1% | 1% | | |
| Income tax provision | nine months ended | \$ 59 | \$ 91 | \$ (32) | (35)% |
| Percentage of total net revenue | | 1% | 1% | | |

Our income tax provisions were primarily attributable to taxes payable in foreign jurisdictions.

We believe that, based on the history of our operating losses and other factors, the weight of available evidence indicates that it is more likely than not that we will not be able to realize the benefit of our net operating losses. Accordingly, a full valuation reserve has been recorded against our net deferred tax assets.

*Liquidity and Capital Resources; Changes in Financial Condition**Cash Flows*

As of September 30, 2011, we had cash, cash equivalents and long and short-term investments of \$26.4 million and had total working capital of \$16.9 million. Our primary capital requirements are to fund working capital, including the development and bringing to market of our Bandwidth Engine ICs. As of September 30, 2011, we had a total acquisition-related liability of \$0.5 million accrued on our condensed

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consolidated balance sheet as an indemnification holdback liability, which will be paid in the fourth quarter of 2011.

Net cash used in operating activities was \$12.9 million for the first nine months of 2011 and was primarily attributable to our net loss of \$18.5 million, partially offset by \$0.3 million in changes in assets and liabilities, non-cash charges, including stock-based compensation expense of \$2.5 million, depreciation and amortization expense of \$2.8 million and a provision for doubtful accounts of \$0.1 million. The changes in assets and liabilities primarily related to the timing of billing our customers, collection of receivables and payments to vendors.

Net cash used in operating activities was \$10.6 million for the first nine months of 2010 and was primarily attributable to our net loss of \$17.4 million, partially offset by non-cash charges, including stock-based compensation expense of \$2.3 million and depreciation and amortization expense of \$2.9 million.

Net cash used in investing activities was \$1.3 million for the first nine months of 2011, and included net amounts transferred from cash to marketable securities of \$2.6 million that did not impact our liquidity, a \$1.0 million earn-out payment related to the MagnaLynx acquisition and \$0.3 million for purchases of fixed assets.

In the first nine months of 2010, we invested \$3.3 million of net cash in the acquisition of MagnaLynx in March 2010, paid out \$4.6 million in acquisition-related earn-out obligations to Prism Circuits and purchased \$1.3 million of fixed assets.

Our cash from financing activities for the first nine months of 2011 of \$3.1 million consisted primarily of the proceeds received from issuance of common stock related to the exercise of stock options and our employee stock purchase plan. Net cash provided by financing activities was \$1.7 million for the first nine months of 2010 primarily due to proceeds received from the issuance of common stock related to the exercise of stock options.

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Our future liquidity and capital requirements are expected to vary from quarter-to-quarter, depending on numerous factors, including:

- level and timing of licensing, royalty and IC product revenue;
- cost, timing and success of technology development efforts, including meeting customer design specifications;
- fabrication costs, including mask costs, of our Bandwidth Engine ICs currently under development;
- variations in manufacturing yields, materials costs and other manufacturing risks;
- costs of acquiring other businesses and integrating the acquired operations; and
- profitability of our business.

In order to become profitable or to achieve and sustain positive cash flows from operations in the future, we must significantly increase our revenues and reduce operating expenses. Our ability to achieve the necessary revenue growth will primarily depend on market acceptance of our Bandwidth Engine ICs and related product offerings; to obtain large volume orders for those products; to fulfill such orders; and to achieve acceptable IC manufacturing yields and obtain sufficiently high average selling prices for those products. We intend to continue to assess our cost structure in relationship to our revenue levels and to make appropriate adjustments to expense levels.

Although we expect our cash expenditures to continue to exceed receipts through 2012, as we continue our significant research and development efforts for our Bandwidth Engine IC product line, we expect our existing cash, cash equivalents and investments, along with our existing capital and cash generated from operations, if any, to be sufficient to meet our capital requirements for at least the next 12 months, including for existing contractual obligations during this period. Should our cash resources prove inadequate, we will have to obtain additional funding through public or private equity or debt financings or other capital-generating transactions, reduce spending, or some combination of the foregoing. We have a shelf registration allowing us to sell up to \$30 million of our securities (before reduction for expenses, underwriting discounts and commissions) from time to time prior to the third anniversary of the effective date of that registration statement. We also might decide to raise additional capital at such times and upon such terms as management considers favorable and in our interests, including, but not limited to, from the sale of our debt and/or equity securities under our existing shelf registration statement. There can be no assurance that such additional funding will be available to us on favorable terms, if at all. The failure to raise capital when needed could have a material adverse effect on our business and financial condition and result in us not achieving our longer term business objectives.

Contractual Obligations

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The impact that our contractual obligations as of September 30, 2011 are expected to have on our liquidity and cash flow in future periods is as follows (in thousands):

| | Payment Due by Period | | | | |
|----------------------|-----------------------|------------------|-----------|-----------|-------------------|
| | Total | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
| Operating Leases | \$ 6,652 | \$ 845 | \$ 1,592 | \$ 1,381 | \$ 2,834 |
| Purchase Commitments | 3,894 | 3,499 | 395 | | |
| Capital Lease | 202 | 186 | 16 | | |
| | \$ 10,748 | \$ 4,530 | \$ 2,003 | \$ 1,381 | \$ 2,834 |

As of September 30, 2011, we had purchase commitments primarily related to computer-aided design tools payable through March 2013 and capital lease obligations for testing equipment.

ITEM 3. Qualitative and Quantitative Disclosures about Market Risk

Our investment portfolio consists of money market accounts, certificates of deposit, corporate debt, government agency and municipal debt securities. The portfolio dollar-weighted average maturity of these investments is within 12 months. Our primary objective with this investment portfolio is to invest available cash while preserving principal and meeting liquidity needs. No single security should exceed 5% of the portfolio at the time of purchase. In accordance with our investment policy, we place investments with high credit quality issuers and limit the amount of credit exposure to any one issuer. These securities, which approximated \$25.6 million as of September 30, 2011 and earned an average annual interest rate of approximately 0.5% during the first nine months of

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2011, are subject to interest rate and credit risks. We do not have any investments denominated in foreign currencies, and, therefore, are not subject to foreign currency risk on such investments.

ITEM 4. Controls and Procedures

Disclosure Controls and Procedures. Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. Because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934. Based on this evaluation, our management concluded that as of September 30, 2011, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting. During the third quarter of 2011, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

The discussion of legal matters in Note 4 of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report under the heading "Legal Matters" is incorporated by reference in response to this Part II, Item 1.

ITEM 1A. Risk Factors

We face many significant risks in our business, some of which are unknown to us and not presently foreseen. These risks could have a material adverse impact on our business, financial condition and results of operations in the future. We have disclosed a number of material risks under Item 1A of our annual report on Form 10-K for the year ended December 31, 2010, which we filed with the Securities and Exchange Commission on March 15, 2011. The following discussion is of material changes to the risk factors disclosed in that report.

Our revenue has been highly concentrated among a small number of licensees and customers, and our results of operations could be harmed if we lose a key revenue source and fail to replace it.

Our overall revenue has been highly concentrated, with a few customers accounting for a significant percentage of our total revenue. For the three months ended September 30, 2011, three customers individually represented 37%, 17% and 13% of total revenue. For the nine months ended September 30, 2011, three customers individually represented 27%, 14% and 14% of total revenue. For the three months ended September 30, 2010, three customers individually represented 23%, 20% and 13% of total revenue. For the nine months ended September 30, 2010, two customers individually represented 21% and 17% of total revenue. We expect that a relatively small number of licensees will continue to account for a substantial portion of our revenue for the foreseeable future.

Our royalty revenue also has been highly concentrated among a few licensees, and we expect this trend to continue for the foreseeable future. In particular, a substantial portion of our licensing and royalty revenue has come from the licenses for integrated circuits used by one electronics manufacturing company. Royalties earned from the production of this company's gaming devices incorporating our 1T-SRAM technology represented 13% of total revenue for the nine months ended September 30, 2011, and 21% and 20% for the three and nine months ended September 30, 2010, respectively. This manufacturer faces intense competitive pressure in the video game market, which is characterized by extreme volatility, costly new product introductions and rapidly shifting consumer preferences, and we cannot be certain whether their sales of products incorporating our technology will increase or decrease beyond prior or current levels.

As a result of this revenue concentration, our results of operations could be impaired by the decision of a single key licensee or customer to cease using our technology or products or by a decline in the number of products that incorporate our technology that are sold by a single licensee or customer or by a small group of licensees or customers.

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Our revenue concentration may also pose credit risks, which could negatively affect our cash flow and financial condition.

We might also face credit risks associated with the concentration of our revenue among a small number of licensees and customers. As of September 30, 2011, five customers represented 100% of total trade receivables. Our failure to collect receivables from any customer that represents a large percentage of receivables on a timely basis, or at all, could adversely affect our cash flow or results of operations and might cause our stock price to fall.

ITEM 6. Exhibits

(a) Exhibits

- 31.1 Rule 13a-14 certification
- 31.2 Rule 13a-14 certification
- 32.1 Section 1350 certification
- 101 The following financial information from MoSys, Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 2011, filed with the SEC on November 9, 2011, formatted in Extensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2011 and 2010, (ii) the Condensed Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010, (iii) the Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 and 2010, and (iv) Notes to Condensed Consolidated Financial Statements.

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Signatures

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

Dated: November 9, 2011

MOSYS, INC.

By: /s/ Leonard Perham
Leonard Perham
President and Chief Executive Officer

By: /s/ James W. Sullivan
James W. Sullivan
Vice President of Finance and Chief Financial Officer
(Principal Financial Officer)

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EXHIBIT INDEX

| | |
|------|---|
| 31.1 | Rule 13a-14 certification |
| 31.2 | Rule 13a-14 certification |
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