SIGMA DESIGNS INC
Form 10-Q
December 09, 2015
**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

*(MARK ONE)*

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

**For the quarterly period ended October 31, 2015**

**or**

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

**For the transition period from ______ to**

**Commission file number 001-32207**

**Sigma Designs, Inc.**

*(Exact name of registrant as specified in its charter)*

| | |
|---|---|
| **California** | **94-2848099** |
| *(State or other jurisdiction of* | *(I.R.S. Employer* |

*incorporation or organization) Identification No.)*

**47467 Fremont Boulevard,**

**Fremont, California 94538**

*(Address of principal executive offices including Zip Code)*

**(510) 897-0200**

*(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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No**

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

| | | | |
|---|---|---|---|
| **Large accelerated filer** | **Accelerated filer** | **Non-accelerated filer**<br>**(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**

As of December 2, 2015, the Company had 36,451,927 shares of Common Stock outstanding.

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**SIGMA DESIGNS, INC.**

**QUARTERLY REPORT ON FORM 10-Q**

**FOR THE THREE MONTHS ENDED OCTOBER 31, 2015**

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**PART I. FINANCIAL INFORMATION**

**ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**SIGMA DESIGNS, INC.**

**UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

**(In thousands, except per share data)**

| | **October 31, 2015** | **January 31, 2015** |
|---|---|---|
| **ASSETS** | | |
| **Current assets** | | |
| Cash and cash equivalents | $67,164 | $83,502 |
| Short-term marketable securities | 24,528 | 6,347 |
| Restricted cash | 400 | 400 |
| Accounts receivable, net of allowances of $2,229 as of October 31, 2015 and $1,502 as of January 31, 2015 | 30,971 | 26,415 |
| Inventory | 27,953 | 20,445 |
| Deferred tax assets | 3,259 | 3,319 |
| Prepaid expenses and other current assets | 11,704 | 8,805 |
| **Total current assets** | 165,979 | 149,233 |
| | | |
| Long-term marketable securities | 3,537 | 4,249 |
| Software, equipment and leasehold improvements, net | 16,638 | 21,594 |
| Intangible assets, net | 24,318 | 24,642 |
| Deferred tax assets, net of current portion | 645 | 687 |
| Long-term investments, net of current portion | 3,132 | 3,267 |
| Other non-current assets | 7,586 | 1,661 |
| **Total assets** | $221,835 | $205,333 |
| | | |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| **Current liabilities** | | |
| Accounts payable | $26,664 | $21,207 |
| Accrued compensation and related benefits | 8,684 | 6,806 |
| Accrued liabilities | 12,451 | 22,894 |
| **Total current liabilities** | 47,799 | 50,907 |

| | | |
|---|---|---|
| Income taxes payable | 10,475 | 7,573 |
| Long-term deferred tax liabilities | 423 | 741 |
| Other long-term liabilities | 6,439 | 2,822 |
| **Total liabilities** | 65,136 | 62,043 |
| | | |
| Commitments and contingencies (Note 9) | | |
| | | |
| **Shareholders' equity** | | |
| Preferred stock; no par value, authorized 2,000,000 shares, none issued and outstanding | - | - |
| Common stock and additional paid-in capital; no par value; 100,000,000 shares authorized; 41,016,710 issued and 36,357,567 outstanding as of October 31, 2015 and 39,973,689 issued and 35,314,546 outstanding as of January 31, 2015 | 501,101 | 493,550 |
| Treasury stock, at cost, 4,659,143 shares as of October 31, 2015 and January 31, 2015 | (88,198 ) | (88,198 ) |
| Accumulated other comprehensive loss | (1,602 ) | (1,111 ) |
| Accumulated deficit | (254,602) | (260,951) |
| **Total shareholders' equity** | 156,699 | 143,290 |
| **Total liabilities and shareholders' equity** | $221,835 | $205,333 |

**See the accompanying Notes to Unaudited Condensed Consolidated Financial Statements**

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**SIGMA DESIGNS, INC.**

**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

**(In thousands, except per share data)**

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | October 31, | November 1, | October 31, | November 1, |
| | 2015 | 2014 | 2015 | 2014 |
| **Net revenue** | $61,581 | $ 53,784 | $175,800 | $ 133,467 |
| Cost of revenue | 30,794 | 27,272 | 87,141 | 64,841 |
| **Gross profit** | 30,787 | 26,512 | 88,659 | 68,626 |
| | | | | |
| **Operating expenses** | | | | |
| Research and development | 17,339 | 16,603 | 49,754 | 50,158 |
| Sales and marketing | 5,875 | 5,559 | 16,940 | 16,484 |
| General and administrative | 5,314 | 4,808 | 16,091 | 14,394 |
| Restructuring costs | - | (18) | 9 | 1,002 |
| Impairment of IP, mask sets and design tools | 795 | 856 | 1,783 | 2,122 |
| Total operating expenses | 29,323 | 27,808 | 84,577 | 84,160 |
| **Income (loss) from operations** | 1,464 | (1,296) | 4,082 | (15,534) |
| Gain on sale of development project | 7,551 | - | 7,551 | - |
| Interest and other income, net | 37 | 188 | 821 | 508 |
| **Income (loss) before income taxes** | 9,052 | (1,108) | 12,454 | (15,026) |
| Provision for (benefit from) income taxes | 2,617 | (551) | 6,105 | 3,065 |
| **Net income (loss)** | $6,435 | $ (557) | $6,349 | $ (18,091) |
| | | | | |
| **Net income (loss) per common share**: | | | | |
| Basic | $0.18 | $ (0.02) | $0.18 | $ (0.52) |
| Diluted | $0.17 | $ (0.02) | $0.17 | $ (0.52) |
| | | | | |
| **Shares used in computing net income (loss) per share:** | | | | |
| Basic | 36,046 | 34,790 | 35,670 | 34,578 |
| Diluted | 36,785 | 34,790 | 36,515 | 34,578 |

**SIGMA DESIGNS, INC.**

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

**(In thousands)**

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | October 31, 2015 | November 1, 2014 | October 31, 2015 | November 1, 2014 |
| Net income (loss) | $6,435 | $ (557 ) | $6,349 | $ (18,091 ) |
| Other comprehensive loss: | | | | |
| Currency translation adjustments, net of $0 tax during the three and nine months ended October 31, 2015 and November 1, 2014 | (100 ) | (606 ) | (388 ) | (701 ) |
| Unrealized loss on marketable securities, net of $0 tax during the three and nine months ended October 31, 2015 and November 1, 2014 | (24 ) | (33 ) | (103 ) | (124 ) |
| Other comprehensive loss | (124 ) | (639 ) | (491 ) | (825 ) |
| Comprehensive income (loss) | $6,311 | $ (1,196 ) | $5,858 | $ (18,916 ) |

**See the accompanying Notes to Unaudited Condensed Consolidated Financial Statements**

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**SIGMA DESIGNS, INC.**

**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(In thousands)**

| | **Nine Months Ended** | |
|---|---|---|
| | **October 31, 2015** | **November 1, 2014** |
| **Cash flows from operating activities:** | | |
| Net income (loss) | $6,349 | $ (18,091 ) |
| Adjustments to reconcile net income (loss) to net cash used in (provided by) operating activities: | | |
| Depreciation and amortization | 15,691 | 16,153 |
| Stock-based compensation | 4,880 | 4,578 |
| Provision for excess and obsolete inventory | 2,252 | 2,397 |
| Provision for sales returns, discounts and doubtful accounts | 727 | 368 |
| Deferred income taxes | (216 ) | (3,123 ) |
| Impairment of IP, mask sets and design tools | 1,783 | 2,122 |
| Tax effect related to share awards | 81 | (620 ) |
| Excess tax expense from stock-based compensation | (81 ) | 620 |
| Impairment of investment | 132 | 601 |
| Other non-cash activities | (267 ) | 70 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (5,283 ) | 1,313 |
| Inventory | (9,760 ) | (2,103 ) |
| Prepaid expenses and other current assets | 98 | 1,598 |
| Other non-current assets | (5,953 ) | 127 |
| Accounts payable | 4,321 | 4,141 |
| Accrued liabilities, compensation and related benefits | (4,482 ) | 5,310 |
| Income taxes payable | (1,425 ) | (273 ) |
| Other long-term liabilities | 910 | (2,428 ) |
| **Net cash provided by operating activities** | 9,757 | 12,760 |
| | | |
| **Cash flows from investing activities:** | | |
| Restricted cash | - | 275 |
| Purchases of marketable securities | (22,622) | (3,079 ) |
| Sales and maturities of marketable securities | 5,050 | 13,233 |
| Purchases of software, equipment and leasehold improvements | (5,551 ) | (5,161 ) |
| Purchases of IP | (2,750 ) | (2,443 ) |
| Issuance of short-term promissory notes | (2,710 ) | - |
| Repayment of note receivable | - | 230 |
| **Net cash (used in) provided by investing activities** | (28,583) | 3,055 |
| | | |
| **Cash flows from financing activities:** | | |
| Excess tax benefit from stock-based compensation | (81 ) | 36 |

| | | |
|---|---|---|
| Net proceeds from exercises of employee stock options and stock purchase rights | 2,752 | 1,270 |
| **Net cash provided by financing activities** | 2,671 | 1,306 |
| | | |
| Effect of foreign exchange rate changes on cash and cash equivalents | (183) | (151) |
| Net (decrease) increase in cash and cash equivalents | (16,338) | 16,970 |
| | | |
| **Cash and cash equivalents, beginning of period** | 83,502 | 64,326 |
| **Cash and cash equivalents, end of period** | $67,164 | $81,296 |
| | | |
| **Supplemental disclosure of cash flow information:** | | |
| | | |
| Cash paid for income taxes | $7,335 | $5,596 |

**See the accompanying Notes to Unaudited Condensed Consolidated Financial Statements**

**SIGMA DESIGNS, INC.**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Organization and summary of significant accounting policies**

**Organization and nature of operations:** Sigma Designs, Inc. (referred to collectively in these unaudited condensed consolidated financial statements as “Sigma,” “we,” “our”, “the Company” and “us”) is a provider of intelligent media platform for use in the home entertainment and control markets. Our goal is to ensure integrated semiconductor solutions serve as the foundation for some of the world’s leading consumer products, including televisions, set-top boxes, media connectivity and home control products. A majority of our primary products are semiconductors that are targeted toward end-product manufacturers, Original Equipment Manufacturers, or OEMs, and Original Design Manufacturers, or ODMs. We sell our products into four primary target markets which are the Smart TV, Set-top Box, Media Connectivity and Internet of Things (“IoT”) Devices markets. We derive a portion of our revenue from other products and services, including technology licenses, software development kits, engineering support services for hardware and software, engineering development for customization of chipsets and other accessories.

**Basis of presentation:** The unaudited condensed consolidated financial statements include the accounts of Sigma Designs, Inc. and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated upon consolidation. We operate and report quarterly financial results that consist of 13 weeks and end on the last Saturday of the period. The third quarter of fiscal 2016 and fiscal 2015 ended on October 31, 2015 (91 days) and November 1, 2014 (91 days), respectively.

The unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“US GAAP”) for interim financial information and the rules and regulations of the Securities and Exchange Commission (“SEC”). They do not include all disclosures required by US GAAP for complete financial statements. Therefore, these financial statements should be read in conjunction with our audited consolidated financial statements and notes thereto for the year ended January 31, 2015, included in our fiscal 2015 Annual Report on Form 10-K, as filed with the SEC on April 15, 2015, referred to as our fiscal 2015 Annual Report.

The condensed consolidated financial statements included herein are unaudited; however, they contain all normal recurring accruals and adjustments that, in our opinion, are necessary to present fairly our consolidated financial position at October 31, 2015 and January 31, 2015, the consolidated results of our operations for the three and nine months ended October 31, 2015 and November 1, 2014, and the consolidated cash flows for the nine months ended October 31, 2015 and November 1, 2014. The results of operations for the three and nine months ended October 31, 2015 are not necessarily indicative of the results to be expected for future quarters or the full year.

There have been no significant changes in our critical accounting policies during the nine months ended October 31, 2015, as compared to the critical accounting policies described in our Annual Report on Form 10-K for the year ended January 31, 2015. For a complete summary of our significant accounting policies, refer to Note 1, "Organization and Summary of Significant Accounting Policies”, in Part II, Item 8 of our fiscal 2015 Annual Report.

**Recent accounting pronouncements**

Recent accounting pronouncements expected to impact our operations that are not yet effective are summarized as follows:

In November 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update No. 2015-17, *Balance Sheet Classification of Deferred Taxes* (“ASU 2015-17”), which simplifies the presentation of deferred income taxes by eliminating the need for entities to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. ASU 2015-17 is effective for us beginning in the first quarter of 2018 with early application permitted as of the beginning of an interim or annual reporting period. We are currently evaluating the timing of its application. The adoption of this standard is not expected to have a material impact on our consolidated financial statements.

In July 2015, the FASB issued Accounting Standards Update No. 2015-11, *Simplifying the Measurement of Inventory* (“ASU 2015-11”), which changes guidance for subsequent measurement of inventory within the scope of the Update from the lower of cost or market to the lower of cost and net realizable value. ASU 2015-11 is effective for us beginning in the first quarter of 2018 with early adoption permitted. The adoption of this standard is not expected to have a material impact on our consolidated financial statements.

**SIGMA DESIGNS, INC.**

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

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern* ("ASU 2014-15"), to provide guidance on management's responsibility in evaluating whether there is substantial doubt about a company's ability to continue as a going concern and to provide related footnote disclosures. ASU 2014-15 is effective for us beginning in the first quarter of 2016 with early adoption permitted. The adoption of this standard is not expected to have a material impact on our consolidated financial statements.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers* (Topic 606) ("ASU 2014-09"), which amends the existing accounting standards for revenue recognition. ASU 2014-09 is based on principles that govern the recognition of revenue at an amount an entity expects to be entitled when products are transferred to customers. The original effective date for ASU 2014-09 would have required us to adopt this standard beginning in our first quarter of 2018. In July 2015, the FASB voted to amend ASU 2014-09 by approving a one-year deferral of the effective date as well as providing the option to early adopt the standard on the original effective date. Accordingly, we may adopt the standard in either our first quarter of 2018 or 2019. The new revenue standard may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. We are currently evaluating the timing of its adoption and the impact of adopting the new revenue standard on our consolidated financial statements.

**2. Cash, cash equivalents and marketable securities**

As of October 31, 2015 and January 31, 2015, we had $0.4 million of restricted cash related to an office-space operating lease and other transactions, which is not included in the amounts below. Cash, cash equivalents and marketable securities consist of the following (in thousands):

| | October 31, 2015 | | | January 31, 2015 | | |
|---|---|---|---|---|---|---|
| | Book Value | Net Unrealized Gains (Losses) | Fair Value | Book Value | Net Unrealized Gains (Losses) | Fair Value |
| Certificate of deposits | $15,509 | $ - | $15,509 | $- | $ - | $- |
| Corporate bonds | 11,205 | 66 | 11,271 | 9,130 | 153 | 9,283 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Money market funds | 5,235 | | - | 5,235 | 7,650 | | - | | 7,650 |
| Fixed income mutual funds | 1,259 | | 26 | 1,285 | 1,324 | | (11 | ) | 1,313 |
| **Total cash equivalents and marketable securities** | $33,208 | $ | 92 | 33,300 | $18,104 | $ | 142 | | 18,246 |

| | | |
|---|---|---|
| Cash on hand held in the United States | 9,455 | 12,042 |
| Cash on hand held overseas | 52,474 | 63,810 |
| **Total cash on hand** | 61,929 | 75,852 |
| **Total cash, cash equivalents and marketable securities** | $95,229 | $94,098 |
| | | |
| **Reported as:** | | |
| Cash and cash equivalents | $67,164 | $83,502 |
| Short-term marketable securities | 24,528 | 6,347 |
| Long-term marketable securities | 3,537 | 4,249 |
| | $95,229 | $94,098 |

**SIGMA DESIGNS, INC.**

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

The amortized cost and estimated fair value of cash equivalents and marketable securities, by contractual maturity, are as follows (in thousands):

| | **October 31, 2015** | | **January 31, 2015** | |
|---|---|---|---|---|
| | **Book Value** | **Fair Value** | **Book Value** | **Fair Value** |
| Due in one year or less | $29,669 | $29,763 | $13,995 | $13,997 |
| Due in greater than one year | 3,539 | 3,537 | 4,109 | 4,249 |
| **Total** | $33,208 | $33,300 | $18,104 | $18,246 |

## 3. Fair values of assets and liabilities

Fair value is defined as, "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price)." The accounting standards establish a consistent framework for measuring fair value and disclosure requirements about fair value measurements and among other things, require us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

*Fair value hierarchy*

The accounting standards discuss valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost). The standards utilize a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

**Level 1** - Valuation is based upon quoted prices for identical instruments traded in active markets.

**Level 2** - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

**Level 3** - Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our estimate of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of option pricing models, discounted cash flow models, and similar techniques.

*Determination of fair value*

Our cash equivalents and marketable securities are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. The types of marketable securities valued based on quoted market prices in active markets include most U.S. government and agency securities, sovereign government obligations, money market securities and certain corporate obligations with high credit ratings and an ongoing trading market.

The tables below present the balances of our assets and liabilities measured at fair value on a recurring basis as of October 31, 2015 and January 31, 2015 (in thousands):

| | **October 31, 2015** | | | |
|---|---|---|---|---|
| | **Fair Value** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** |
| Certificate of deposits | $15,509 | $ 15,509 | $ - | $ - |
| Corporate bonds | 11,271 | 11,271 | - | - |
| Money market funds | 5,235 | 5,235 | - | - |
| Fixed income mutual funds | 1,285 | 1,285 | - | - |
| **Total cash equivalents and marketable securities** | 33,300 | 33,300 | - | - |
| Restricted cash | 400 | 400 | - | - |
| **Total assets measured at fair value** | $33,700 | $ 33,700 | $ - | $ - |

**SIGMA DESIGNS, INC.**

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

| | **January 31, 2015** | | | |
|---|---|---|---|---|
| | **Fair Value** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** |
| Corporate bonds | $9,283 | $ 9,283 | $ - | $ - |
| Money market funds | 7,650 | 7,650 | - | - |
| Fixed income mutual funds | 1,313 | 1,313 | - | - |
| **Total cash equivalents and marketable securities** | 18,246 | 18,246 | - | - |
| Restricted cash | 400 | 400 | - | - |
| **Total assets measured at fair value** | $18,646 | $ 18,646 | $ - | $ - |

*Assets measured and recorded at fair value on a non-recurring basis*

Our non-marketable preferred stock investments in privately-held venture capital funded technology companies are recorded at cost and are adjusted to fair value only in the event that they become other-than-temporarily impaired. As of October 31, 2015, we held equity investments in three privately-held venture capital funded technology companies and an equity investment in one joint venture, with an aggregate carrying value of $3.1 million. In the fourth quarter of fiscal 2014, the second quarter of fiscal 2015 and the second quarter of fiscal 2016, we recorded impairment charges of $0.3 million, $0.6 million and $0.1 million, respectively, on an investment as we concluded the impairment to be other-than-temporary, effectively nullifying any value from this investment as of October 31, 2015. We did not identify any other events or changes in circumstances that may have had a significant adverse effect on the fair value of these investments during the three and nine months ended October 31, 2015 and November 1, 2014. Each of these equity investments in privately-held companies constituted less than a 20% ownership position. Furthermore, we do not believe that we have the ability to exert significant influence over any of these companies.

## 4. Investments in privately held companies

The following table sets forth the value of investments in and notes receivable from privately-held companies (in thousands):

| **Equity investments:** | **October 31, 2015** | **January 31, 2015** |
|---|---|---|
| Issuer A | $ 2,000 | $ 2,000 |
| Issuer B | 1,000 | 1,000 |
| Issuer C | - | 129 |
| Issuer D | 132 | 138 |
| **Total equity investments** | $ 3,132 | $ 3,267 |

During fiscal 2009, we purchased shares of preferred stock in a privately-held venture capital funded technology company ("Issuer A") at a total investment cost of $1.0 million. In the fourth quarter of fiscal 2010, we purchased additional shares of preferred stock in Issuer A at a cost of $1.0 million. In November 2010, we loaned $1.0 million to Issuer A and received a secured promissory note. During the second quarter of fiscal 2015, the note receivable from Issuer A was fully repaid.

In the third quarter of fiscal 2011, we purchased shares of preferred stock in another privately-held technology company ("Issuer B") at a total investment cost of $1.0 million.

In the fourth quarter of fiscal 2011, we purchased shares of preferred stock in another privately-held technology company ("Issuer C") at a total investment cost of $1.0 million. In the fourth quarter of fiscal 2014, the second quarter of fiscal 2015 and the second quarter of fiscal 2016, we recorded impairment charges of $0.3 million, $0.6 million and $0.1 million, respectively, on this investment as we concluded the impairment to be other-than-temporary, effectively nullifying any value from this investment as of October 31, 2015.

In the third quarter of fiscal 2012, we made an equity investment of $0.1 million in a privately-held joint venture ("Issuer D").

**SIGMA DESIGNS, INC.**

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

We made the aforementioned investments because we viewed the issuer as either having strategic technology or a business that would complement our technological capabilities or help create an opportunity for us to sell our chipset solutions. We analyze each investment quarterly for evidence of impairment.

Our President and Chief Executive Officer is a member of the Board of Directors of both Issuer A and Issuer B. In the case of Issuer B, the investment transaction was negotiated without the personal involvement of the executive officer who had a personal interest in the transaction.

## 5. Supplemental financial information

Inventory consists of the following (in thousands):

| | **October 31, 2015** | **January 31, 2015** |
|---|---|---|
| Wafers and other purchased materials | $16,417 | $8,420 |
| Work-in-process | 1,950 | 3,045 |
| Finished goods | 9,586 | 8,980 |
| **Total inventory** | $27,953 | $20,445 |

Prepaid expenses and other current assets consist of the following (in thousands):

| | **October 31, 2015** | **January 31, 2015** |
|---|---|---|
| Deposits | $3,221 | $ 3,124 |
| Short-term promissory notes | 2,710 | - |
| Prepayments for inventory | 1,685 | 1,670 |
| Prepayments for royalties | 741 | 659 |

| | | |
|---|---|---|
| R&D credit receivable | 576 | 583 |
| Other current assets | 2,771 | 2,769 |
| **Total prepaid expenses and other current assets** | $11,704 | $ 8,805 |

Software, equipment and leasehold improvements consist of the following (in thousands):

| | **Estimated Useful Lives (years)** | **October 31, 2015** | **January 31, 2015** |
|---|---|---|---|
| Software | 2 | $40,271 | $41,069 |
| Equipment | 1 - 5 | 22,698 | 22,168 |
| Office equipment and furniture | 2 | 7,934 | 8,693 |
| Leasehold improvements | 1 - 6 | 1,800 | 2,874 |
| **Total** | | 72,703 | 74,804 |
| Less: Accumulated depreciation and amortization | | (56,065) | (53,210) |
| **Total software, equipment and leasehold improvements, net** | | $16,638 | $21,594 |

Software, equipment and leasehold improvement depreciation and amortization expense was $3.3 million and $3.1 million for the three months ended October 31, 2015 and November 1, 2014, respectively, and was $9.2 million for both the nine months ended October 31, 2015 and November 1, 2014. We recorded impairment charges for mask sets and design tools associated with discontinued products for the three and nine months ended October 31, 2015 of $0.4 million and $1.4 million, respectively, and for the three and nine months ended November 1, 2014 of $0.7 million and $1.5 million, respectively, which was recorded in operating expenses in the accompanying condensed consolidated statement of operations.

**SIGMA DESIGNS, INC.**

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

Accrued liabilities consist of the following (in thousands):

| | **October 31, 2015** | **January 31, 2015** |
|---|---|---|
| License fees | $4,795 | $4,286 |
| Rebates | 2,287 | 9,599 |
| Royalties | 1,804 | 880 |
| Income taxes payable, current portion | 998 | 5,326 |
| Warranties | 983 | 864 |
| Deferred revenue | 492 | 372 |
| Other accrued liabilities | 1,092 | 1,567 |
| **Total accrued liabilities** | $12,451 | $22,894 |

The following table summarizes activity related to accrued rebates (in thousands):

| | **Three Months Ended** | | **Nine Months Ended** | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **October 31, 2015** | **November 1, 2014** |
| Beginning balance | $4,918 | $ 3,903 | $9,599 | $ 3,587 |
| Charged as a reduction of revenue | 2,596 | 6,399 | 9,147 | 12,463 |
| Reversal of unclaimed rebates | - | - | (1,028) | - |
| Payments | (5,227) | (3,526) | (15,431) | (9,274) |
| Ending balance | $2,287 | $ 6,776 | $2,287 | $ 6,776 |

**6. Intangible assets**

The tables below present the balances of our intangible assets (in thousands, except for years):

**October 31, 2015**

| | Gross Value | Impairment | Accumulated Amortization and Effect of Currency Translation | Net Value | Weighted Average Remaining Amortization Period (Years) |
|---|---|---|---|---|---|
| Acquired intangible assets: | | | | | |
| Developed technology | $76,628 | $ (24,614) | $ (47,595) | $4,419 | 1.3 |
| Customer relationships | 50,704 | (30,486) | (19,145) | 1,073 | 1.0 |
| Trademarks and other | 5,478 | - | (5,110) | 368 | 3.2 |
| Purchased IP - amortizing | 32,002 | (5,516) | (17,567) | 8,919 | 2.9 |
| **Total amortizing** | 164,812 | (60,616) | (89,417) | 14,779 | 2.3 |
| Purchased IP - not yet deployed | 13,677 | (4,138) | - | 9,539 | |
| **Total intangibles** | $178,489 | $ (64,754) | $ (89,417) | $24,318 | |

**SIGMA DESIGNS, INC.**

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

| | January 31, 2015 | | | | |
|---|---|---|---|---|---|
| | **Gross Value** | **Impairment** | **Accumulated Amortization and Effect of Currency Translation** | **Net Value** | **Weighted Average Remaining Amortization Period (Years)** |
| Acquired intangible assets: | | | | | |
| Developed technology | $76,628 | $ (24,614) | $ (44,604) | $7,410 | 2.0 |
| Customer relationships | 50,704 | (30,486) | (18,313) | 1,905 | 1.7 |
| Trademarks and other | 4,078 | - | (3,621) | 457 | 3.9 |
| Purchased IP - amortizing | 23,398 | (5,516) | (15,162) | 2,720 | 1.0 |
| **Total amortizing** | 154,808 | (60,616) | (81,700) | 12,492 | 1.8 |
| Purchased IP - not yet deployed | 15,877 | (3,727) | - | 12,150 | |
| **Total intangibles** | $170,685 | $ (64,343) | $ (81,700) | $24,642 | |

Acquired intangible assets represent intangible assets acquired through business combinations. Purchased intellectual property (“Purchased IP”) represents intangible assets acquired through direct purchases of licensed technology from vendors which is incorporated into our products.

Purchased IP – not yet deployed relates to Purchased IP from third parties for our products that are currently in development. We begin amortizing such intellectual property upon the earlier of the beginning of the term of the license agreement, as appropriate, or at the time we begin shipment of the associated products into which such intellectual property is incorporated.

The following table presents the amortization of intangible assets in the accompanying condensed consolidated statements of operations (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **October 31, 2015** | **November 1, 2014** |

| | | | | |
|---|---|---|---|---|
| Cost of revenue | $1,585 | $ 2,000 | $5,467 | $ 5,924 |
| Operating expenses | 349 | 354 | 1,049 | 1,064 |
| **Total intangibles amortization expense** | $1,934 | $ 2,354 | $6,516 | $ 6,988 |

As of October 31, 2015, we expect amortization expense in future periods to be as follows (in thousands):

| **Fiscal year** | **Total** |
|---|---|
| 2016 (remaining three months) | $2,255 |
| 2017 | 7,252 |
| 2018 | 2,972 |
| 2019 | 1,621 |
| 2020 | 679 |
| **Total** | $14,779 |

**7. Restructuring costs**

In fiscal 2013, as a result of significant expansion in our infrastructure and operational activities in connection with purchases and acquisitions that took place between fiscal years 2008 and 2013, and in response to certain redundancies, underperforming operations and delays in programs and product releases, we implemented a restructuring program to realign our global operating expenses with our new business conditions, and to improve efficiency, competitiveness and profitability. Costs relating to facilities closure or lease commitment are recognized when the facility has been exited. Termination costs are recognized when the costs are deemed both probable and estimable and after notification to impacted employees has occurred.

**SIGMA DESIGNS, INC.**

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

During the first quarter of fiscal 2016, we incurred restructuring charges of less than $0.1 million, substantially all of which was related to facility exit cost adjustments, which was reflected in operating expenses. During the second and third quarters of fiscal 2016, we incurred no restructuring charges.

In the first quarter of fiscal 2015, we incurred restructuring charges of $1.0 million, all of which was related to workforce reductions of 29 employees across several geographic regions, the majority of which were in our operations in Israel. Of the total restructuring charges recorded in the first fiscal quarter, approximately $0.1 million was reflected in cost of revenue and $0.9 million was reflected in operating expenses. During the second and third quarters of fiscal 2015, we incurred less than $0.1 million of restructuring charges.

Expenses recognized for restructuring activities impacting our operating expenses are included in "Restructuring costs" in the condensed consolidated statements of operations. Our restructuring measures could negatively impact our revenue and results of operations in the future as a result of less employees developing future products and working to sell our products.

A combined summary of the recent activity of the restructuring plans initiated by us is as follows (in thousands):

| | Workforce Reduction | Asset Impairment | Facility Exit Costs | Total | Cumulative Restructuring Costs |
|---|---|---|---|---|---|
| Liability, February 1, 2014 | $ 363 | $ - | $ 2 | $ 365 | $ 5,570 |
| Charges in fiscal 2015 | 1,083 | - | (20) | 1,063 | 1,063 |
| Cash payments | (1,382) | - | 8 | (1,374) | - |
| Non-cash items | 38 | - | 10 | 48 | - |
| Liability, January 31, 2015 | 102 | - | - | 102 | 6,633 |
| Charges for the nine months ended October 31, 2015 | 3 | - | 6 | 9 | 9 |
| Cash payments | (3) | - | (7) | (10) | - |
| Non-cash items | - | | 1 | 1 | - |
| Liability, October 31, 2015 | $ 102 | $ - | $ - | $ 102 | $ 6,642 |

**8. Sale of development project**

On March 8, 2013, we entered into an Asset Purchase Agreement with a third party (the “Buyer”) to sell certain development projects (intellectual property) and long-lived assets (the “Connectivity Assets”) related to the connectivity technology over coaxial cable market, including the transfer of 21 employees (the “Connectivity Employees”) to the Buyer. The aggregate carrying amount of the Connectivity Assets ultimately transferred was approximately $0.6 million and were classified as assets held for sale in prepaid expenses and other current assets in the consolidated balance sheet at February 2, 2013. We received an initial payment of $2.0 million in cash at the closing of the transaction and a payroll expense reimbursement payment of $0.6 million (as described more fully below). Under the terms of the Asset Purchase Agreement, if certain technical milestones were met by September 30, 2013 as a result of further development of the transferred technology by the Buyer, we were to be paid an additional $5.0 million in cash.

In April 2013, upon receiving the closing consideration of $2.0 million, we recorded a gain of $1.1 million, net of the carrying value of the Connectivity Assets and fees for legal and bank services of approximately $0.4 million. The gain is included in “Gain on sale of development project” in the consolidated statements of operations for fiscal 2014. Additionally, in April 2013, in connection with the Asset Purchase Agreement, the Buyer reimbursed us for payroll expenses related to the employees transferred to the Buyer for the period from February 1, 2013 through the actual payroll transfer, totaling $0.6 million. As the contingent consideration was uncertain at the time of the initial sale, we did not recognize the contingent payment.

**SIGMA DESIGNS, INC.**

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

The Buyer advised us that it did not believe the milestones had been met by the deadline of September 30, 2013. On May 19, 2014, the parties amended the Asset Purchase Agreement to require the use of Judicial Arbitration and Mediations Services ("JAMS") for arbitration to settle the dispute between the parties. We pursued our rights to the milestone consideration payment through the alternative dispute resolution provisions set forth in the amendment. On September 5, 2014, the Buyer filed counterclaims in response to our claims arising from the Asset Purchase Agreement. Arbitration regarding this dispute took place on June 1, 2015. In August 2015, we prevailed on all of the claims we asserted against the Buyer, and all of the Buyer's counterclaims against us were denied. We were awarded $5.0 million plus reimbursement of reasonable legal and other associated costs and interest. We have recovered $2.6 million in legal costs, interest and other associated expenses to date from the Buyer, for a total recovery of $7.6 million, which was recorded as other income in our condensed consolidated statements of operations in its entirety.

## 9. Commitments and contingencies

***Commitments***

*Product warranty*

In general, we sell products with up to a one-year limited warranty that our products will be free from defects in materials and workmanship. Warranty cost is estimated at the time revenue is recognized based on historical activity, and additionally, for any specific known product warranty issues. Accrued warranty cost includes hardware repair and/or replacement and is included in accrued liabilities in the accompanying condensed consolidated balance sheets.

Details of the change in accrued warranty as of October 31, 2015 and November 1, 2014 are as follows (in thousands):

| Three Months Ended | Balance Beginning of Period | Additions and Adjustments | Deductions | Balance End of Period |
|---|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| October 31, 2015 | $ 874 | $ 321 | $ (212 ) | $ 983 |
| November 1, 2014 | $ 640 | $ 342 | $ (128 ) | $ 854 |

| **Nine Months Ended** | **Balance Beginning of Period** | **Additions and Adjustments** | **Deductions** | **Balance End of Period** |
|---|---|---|---|---|
| October 31, 2015 | $ 864 | $ 610 | $ (491 ) | $ 983 |
| November 1, 2014 | $ 620 | $ 584 | $ (350 ) | $ 854 |

*Purchase commitments*

We place non-cancelable orders to purchase semiconductor products from our suppliers on an eight to twelve week lead-time basis.  As of October 31, 2015, the total amount of outstanding non-cancelable purchase orders was approximately $28.2 million.

*Design Tools*

We entered into an agreement with a vendor to purchase $12.9 million of design tools. Payments under this agreement are being made on a quarterly basis from June 2013 through March 2016. As of October 31, 2015, the remaining payments under this agreement totaled $2.7 million. In addition to this agreement, we have entered into other purchase arrangements for certain design tools which totaled $3.1 million. Payments under these arrangements are being made through fiscal 2017. We have fully accrued these amounts as of October 31, 2015.

*Royalties*

We pay royalties for the right to sell certain products under various license agreements. During the three and nine months ended October 31, 2015, we recorded gross royalty expense of $1.2 million and $3.3 million, respectively, and $0.8 million and $1.9 million for the three and nine months ended November1, 2014, respectively, in cost of revenue in the condensed consolidated statements of operations.

**SIGMA DESIGNS, INC.**

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

Our wholly owned subsidiary, Sigma Designs Israel SDI Ltd. (formerly Coppergate Communications, Ltd.), participated in programs sponsored by the Office of the Chief Scientist of Israel's Ministry of Industry, Trade and Labor, or the OCS, for the support of research and development activities that we conducted in Israel. Through October 31, 2015, we had obtained grants from the OCS aggregating to $5.2 million of our research and development projects in Israel. We completed the most recent of these projects in 2013. We are obligated to pay royalties to the OCS, amounting up to 4.5% of the sales of certain products up to an amount equal to the grants received, plus LIBOR-based interest. As of October 31, 2015, our remaining potential obligation under these programs was approximately $1.1 million.

***Contingencies***

*Litigation*

From time to time, we are involved in claims and legal proceedings that arise in the ordinary course of business. We expect that the number and significance of these matters will increase as our business expands. In particular, we could face an increasing number of patent and other intellectual property claims as the number of products and competitors in our industry grows. Any claims or proceedings against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time, result in the diversion of significant operational resources or cause us to enter into royalty or licensing agreements which, if required, may not be available on terms favorable to us. If an unfavorable outcome were to occur against us, there exists the possibility of a material adverse impact on our financial position and results of operations for the period in which the unfavorable outcome occurs and, potentially, in future periods.

On March 8, 2013, we entered into an Asset Purchase Agreement with a third party (the “Buyer”) to sell certain development projects (intellectual property) and long-lived assets (the “Connectivity Assets”) related to the connectivity technology over coaxial cable market, including the transfer of 21 employees (the “Connectivity Employees”) to the Buyer. Under the terms of the Asset Purchase Agreement, if certain technical milestones were met by September 30, 2013 as a result of further development of the transferred technology by the Buyer, we were to be paid an additional $5.0 million in cash. The Buyer advised us that it did not believe the milestones had been met by September 30, 2013. On May 19, 2014, the parties amended the Asset Purchase Agreement to require the use of JAMS for arbitration to settle the dispute between the parties. We pursued our rights to the milestone consideration payment through the alternative dispute resolution provisions set forth in the amendment. On September 5, 2014, the Buyer filed counterclaims in response to our claims arising from the Asset Purchase Agreement. Arbitration regarding this dispute took place on June 1, 2015. In August 2015, we prevailed on all of the claims we asserted against the Buyer, and all of the Buyer's counterclaims against us were denied. We were awarded $5.0 million plus reimbursement of reasonable legal costs, interest and other associated expenses. We have recovered $2.6 million in legal costs, interest and other associated expenses to date from the Buyer, for a total recovery of $7.6 million, which was recorded as other income in our condensed consolidated statements of operations in its entirety.

*Indemnifications*

In certain limited circumstances, we have agreed and may agree in the future to indemnify certain customers against patent infringement claims from third parties related to our intellectual property. In these limited circumstances, the terms and conditions of sale generally limit the scope of the available remedies to a variety of industry-standard methods including, but not limited to, a right to control the defense or settlement of any claim, procure the right for continued usage, and a right to replace or modify the infringing products to make them non-infringing. To date, we have not incurred or accrued any significant costs related to any claims under such indemnification provisions.

Our articles of incorporation and bylaws require that we indemnify our officers and directors against expenses, judgments, fines, settlements and other amounts actually and reasonably incurred in connection with any proceedings arising out of their services to us. In addition, we have entered into separate indemnification agreements with each of our directors and executive officers, which provide for indemnification of these individuals under similar circumstances and under additional circumstances. The indemnification obligations are more fully described in our charter documents and the form of indemnification agreement filed with our SEC reports. We purchase insurance to cover claims or a portion of the claims made against our directors and officers. Since a maximum obligation is not explicitly stated in our charter documents or in our indemnification agreements and will depend on the facts and circumstances that arise out of any future claims, the overall maximum amount of the obligations cannot be reasonably estimated. The fair value of these obligations was zero on our condensed consolidated balance sheet as of October 31, 2015.

**SIGMA DESIGNS, INC.**

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

*Third-party licensed technology*

We license technologies from various third parties and incorporate that technology into our products. Some of these licenses require us to pay royalties and others require us to report sales activities so that royalties may be collected from our customers. From time to time, we are audited by licensors of these technologies for compliance with the terms of these licenses. In the first quarter of fiscal 2015, we settled an audit through binding arbitration relating to a license agreement used in our Set-top Box business for $0.2 million, $0.1 million of which was incurred during the three months ending May 3, 2014 and was included in sales and marketing expenses for that period in the accompanying condensed consolidated statements of operations.

We could be required to make additional payments as a result of pending or future compliance audits. For license agreements where we have royalty obligations, we charge any settlement payments that we make in connection with audits to cost of revenue. For license agreements where we simply have reporting obligations, we treat any settlement payments as penalties and charge the amounts to operating expenses in sales and marketing. During the second quarter of fiscal 2015, we were notified by one of our licensors of their intent to audit for compliance with the terms of the license. As of October 31, 2015, the audit process has been completed for which the licensor concluded no further payments are required. Consequently, we reversed the previously accrued estimate of additional expenditures of $0.1 million in our condensed consolidated statement of operations during the three months ended October 31, 2015. We believe we are substantially in compliance with the terms of our licensing arrangements.

**10. Earnings per share**

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted-average number of common shares outstanding for the fiscal period. Diluted net loss per share is the same as basic net loss per share as the inclusion of potentially issuable shares is anti-dilutive. Diluted net income per share is computed by adjusting outstanding shares, assuming any dilutive effects of stock incentive awards calculated using the treasury stock method. Under the treasury stock method, an increase in the fair market value of our common stock results in a greater dilutive effect from outstanding stock options, restricted stock units and stock purchase rights. Additionally, the exercise of employee stock options and stock purchase rights and the vesting of restricted stock units results in a further dilutive effect on net income per share.

The following table sets forth the basic and diluted net income (loss) per share computed for the three and nine months ended October 31, 2015 and November 1, 2014 (in thousands, except per share amounts):

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | October 31, 2015 | November 1, 2014 | October 31, 2015 | November 1, 2014 |
| Numerator: | | | | |
| Net income (loss), as reported | $6,435 | $ (557 ) | $6,349 | $ (18,091 ) |
| Denominator: | | | | |
| Weighted-average common shares outstanding - basic | 36,046 | 34,790 | 35,670 | 34,578 |
| Dilutive effect of employee stock plans | 739 | - | 845 | - |
| Weighted-average common shares outstanding - diluted | 36,785 | 34,790 | 36,515 | 34,578 |
| Net income (loss) per share - basic | $0.18 | $ (0.02 ) | $0.18 | $ (0.52 ) |
| Net income (loss) per share - diluted | $0.17 | $ (0.02 ) | $0.17 | $ (0.52 ) |

The weighted-average number of shares outstanding used in the computation of basic and diluted net income (loss) per share does not include the effect of the following potential outstanding shares of common stock. The effects of these potentially outstanding shares were not included in the calculation of basic and diluted net income (loss) per share because the effect would have been anti-dilutive (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | October 31, 2015 | November 1, 2014 | October 31, 2015 | November 1, 2014 |
| Stock options | 2,380 | 3,933 | 2,415 | 3,947 |
| Restricted stock units and awards | 412 | 738 | 151 | 463 |

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**SIGMA DESIGNS, INC.**

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

**11. Shareholders' equity and employee benefits**

Condensed consolidated statement of shareholders' equity (amounts in thousands, except shares)

| | **Common Stock** | | **Treasury Stock** | | **Accumulated Other Comprehensive Loss** | | | |
|---|---|---|---|---|---|---|---|---|
| | **Shares** | **Amount** | **Shares** | **Amount** | **Unrealized Loss** | **Accumulated Translation Adjustment** | **Accumulated Deficit** | **Total Shareholders' Equity** |
| **Balance, January 31, 2015** | 39,973,689 | $493,550 | (4,659,143) | $(88,198) | $(27) | $ (1,084) | $ (260,951) | $ 143,290 |
| Unrealized loss on marketable securities | - | - | - | - | (103) | - | - | (103) |
| Currency translation adjustments | - | - | - | - | - | (388) | - | (388) |
| Stock-based compensation expense | - | 4,880 | - | - | - | - | - | 4,880 |
| Tax effect related to share awards | - | (81) | - | - | - | - | - | (81) |
| Net proceeds from common stock issued under share plans | 1,043,021 | 2,752 | - | - | - | - | - | 2,752 |
| Net income | - | - | - | - | - | - | 6,349 | 6,349 |
| **Balance, October 31, 2015** | 41,016,710 | $501,101 | (4,659,143) | $(88,198) | $(130) | $ (1,472) | $ (254,602) | $ 156,699 |

*Endowment insurance pension plan*

Related to our acquisition of our DTV business in May 2012, we added operations in Shanghai, China.  It is required by the "Procedures of Shanghai Municipality on Endowment Insurance for Town Employees" to provide pension insurance for Shanghai employees.  The mandatory plan is managed by the local authority.  Under the current plan, the employee will contribute 8.0% of the annual base to the plan and the employer will match 21% of the annual base.  For calendar year 2015, the annual base is capped at RMB 16,353 per employee. For the three and nine months ended October 31, 2015, we made matching contributions of $0.6 million and $1.7 million, respectively, and $0.5 million and $1.5 million for the three and nine months ended November 1, 2014, respectively.

*Retirement pension plans*

We maintain retirement pension plans for the benefit of qualified employees in Denmark, Taiwan, the Netherlands, and Germany. We made matching contributions of $0.2 million and $0.5 million for each of the three and nine months ended October 31, 2015 and November 1, 2014, respectively.

*Severance plan*

We maintain a severance plan for several Israeli employees pursuant to Israel's Severance Pay Law based on the most recent salary of the employees multiplied by the number of years of employment.  Upon termination of employment, employees are entitled to one month salary for each year of employment or a portion thereof.  As of October 31, 2015, we have an accrued severance liability of $0.8 million primarily offset by $0.7 million of severance employee funds.

**SIGMA DESIGNS, INC.**

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

*Equity Incentive Plan*

On July 10, 2015, the Board of Directors of the Company approved, subject to shareholder approval, the Company's 2015 Stock Incentive Plan (the "2015 Plan"), which was approved by the Company's shareholders at the 2015 annual meeting of shareholders held on August 20, 2015. The 2015 Plan is the successor to and continuation of the Company's 2001 Stock Plan (the "2001 Plan"), and the Amended and Restated 2009 Stock Incentive Plan (the "2009 Plan" and together with the 2001 Plan, the "Prior Plans"). Our 2015 Plan provides for the grant of stock options, restricted stock, restricted stock units, and other stock-related and performance awards that may be settled in cash, stock or other property. The total number of shares of the Company's common stock reserved for issuance under the 2015 Plan consists of 3,000,000 shares plus the number of shares subject to stock awards outstanding under the Prior Plans that terminate prior to exercise and would otherwise be returned to the share reserves under the Prior Plans up to a maximum of 5,000,000 shares.

*Employee Stock Purchase Plan*

On July 10, 2015, the Board of Directors of the Company approved, subject to shareholder approval, the Company's 2015 Employee Stock Purchase Plan (the "2015 ESPP"), which was approved by the Company's shareholders at the 2015 annual meeting of shareholders held on August 20, 2015. The 2015 ESPP has replaced the Company's 2010 Employee Stock Purchase Plan, which was terminated. There are 3,500,000 shares of common stock reserved for issuance under the 2015 ESPP. The 2015 ESPP is implemented by offerings of rights to eligible employees. Each offering will be in such form and will contain such terms and conditions as our Board or a committee thereof will deem appropriate, subject to compliance with applicable regulations. The provisions of separate offerings need not be identical. Under the terms of the offerings that have commenced to date under the 2015 ESPP, eligible employees may authorize payroll deductions of up to 15% of their regular base salaries to purchase common stock at 85% of the fair market value of our common stock at the beginning or end of the six-month offering period, whichever is lower. The maximum number of shares that can be purchased in any single offering period is limited under the terms of the offering. These terms will automatically apply to future offerings under the 2015 ESPP unless modified by the Board or a committee thereof.

During the first quarter of fiscal 2016, we discovered that we inadvertently sold shares of our common stock to our employees during fiscal 2015 in excess of the shares of common stock authorized to be issued under our 2010 Purchase Plan. As a result, we may have failed to comply with the registration or qualification requirements of federal securities laws. Certain purchasers of the shares that were issued in excess of the shares authorized under our 2010 Purchase Plan may have the right to rescind their purchases from us for an amount equal to the purchase price paid for shares, plus interest from the date of purchase. These shares were treated as issued and outstanding for financial reporting purposes as of the original date of issuance. We intend to make a registered rescission offer during fiscal 2017 to eligible participants who purchased shares in the last twelve months.

As of October 31, 2015, there were approximately 92,072 shares issued to participants in the 2010 Purchase Plan in the past twelve months that continued to be held by the original purchasers of such shares which may be subject to the rescission rights referenced above. All of these shares were originally purchased for $3.89 per share. If holders of all these shares seek to rescind their purchases, we could be required to make aggregate payments of up to approximately $0.4 million, which does not include statutory interest. However, the actual impact to our cash position may be lower depending on the number of holders who accept the rescission offer and tender their shares. Pursuant to the authoritative accounting guidance, the shares are considered mandatorily redeemable as the redemption may be outside of our control. The aforementioned amount is included in accrued compensation and related benefits in the accompanying condensed consolidated balance sheets. The shares subject to repurchase are included in permanent equity as of January 31, 2015 as these shares are legally outstanding with all rights and privileges therein. We also may be subject to civil and other penalties by regulatory authorities as a result of the failure to register these shares with the Securities and Exchange Commission. We do not believe that the failure to register the shares or the planned rescission offer will have a material impact on our condensed consolidated financial statements.

We are also evaluating the potential impact to our employees, including potential tax consequences, for issuing shares in excess of the number of shares reserved under our 2010 Purchase Plan. We may incur additional costs associated with any potential tax consequences and during the fourth quarter of fiscal 2015, we accrued $0.4 million of expense associated with these additional costs which were recorded in accrued compensation and related benefits in the accompanying condensed consolidated balance sheets.

**SIGMA DESIGNS, INC.**

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

## 12. Income taxes

We recorded a provision for and benefit from income taxes of $2.6 million and $0.6 million for the three months ended October 31, 2015 and November 1, 2014, respectively. The provision for income taxes was $6.1 million and $3.1 million for the nine months ended October 31, 2015 and November 1, 2014, respectively. The increase in tax expense is primarily attributable to the increase in profitability in taxable jurisdictions in the third quarter of fiscal year 2016 as compared to the same period in fiscal year 2015 and changes in tax reserves. During the three and nine months ended October 31, 2015 and November 1, 2014, we were unable to reasonably project our annual effective tax rate, and therefore computed our provision for income taxes based on year-to-date actual financial results. Included in our provision for income taxes are foreign exchange gains or losses on unsettled income tax liabilities.

## 13. Segment and geographical information

Operating segments are defined as components of an enterprise for which separate financial information is available and evaluated regularly by the chief operating decision-maker in deciding how to allocate resources and in assessing performance. We are organized as, and operate in, one reportable segment. Our operating segment consists of our geographically based entities in the United States, Israel and Singapore. Our chief operating decision-maker reviews consolidated financial information, accompanied by information about revenue by product group, target market and geographic region. We do not assess the performance of our geographic regions on other measures of income, expense or net income.

Our net revenue is derived principally from the sales of integrated semiconductor solutions, which we sell across all of our target markets. Smart TV products consist of a range of platforms that are based on highly integrated chips, embedded software, and hardware reference designs. Media Connectivity products consist of wired home networking controller chipsets that are designed to provide connectivity solutions between various home entertainment products and incoming video streams. Set-top Box products consist of connected media processors and players delivering IP streaming video, including hybrid versions of these products. IoT Devices consist of our wireless Z-Wave chipsets and modules.

Our License and other markets include revenue derived from the licensing of our technology to third parties and other sources. Revenue derived from other sources includes software development kits, engineering support services for hardware and software, and engineering development for customization of chipsets and other accessories. No revenue was derived from the licensing of our technology during the three and nine months ended October 31, 2015, and zero and 3.7% of our total net revenue for the three and nine months ended November 1, 2014, respectively, was derived from licensing arrangements.

Historically, we disclosed information encompassing product groupings by target markets with certain naming conventions, consisting of Digital Television ("DTV"), Set-top Box, Home Networking, Home Control, and License and other. Effective in the fourth quarter of fiscal 2015, we changed the naming conventions of some of our target markets, commensurate with changes taking effect in our industry as a whole. We renamed our "DTV" target market to "Smart TV," "Home Networking" to "Media Connectivity," and "Home Control" to "IoT Devices." These changes did not affe the products or related services categorization, or previously reported amounts related to the aforementioned historical target markets.

The following table sets forth net revenue attributable to each target market (in thousands):

| | **Three Months Ended** | | **Nine Months Ended** | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **October 31, 2015** | **November 1, 2014** |
| Smart TV | $32,244 | $ 16,570 | $78,378 | $ 32,667 |
| Media Connectivity | 14,003 | 23,022 | 43,149 | 56,968 |
| IoT Devices | 10,209 | 7,182 | 35,637 | 19,898 |
| Set-top Box | 4,744 | 6,759 | 17,582 | 17,976 |
| License and other | 381 | 251 | 1,054 | 5,958 |
| **Net revenue** | $61,581 | $ 53,784 | $175,800 | $ 133,467 |

**SIGMA DESIGNS, INC.**

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

The following table sets forth net revenue for each geographic region based on the ship-to location of customers (in thousands):

| | **Three Months Ended** | | **Nine Months Ended** | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **October 31, 2015** | **November 1, 2014** |
| Asia | $47,691 | $ 46,567 | $132,045 | $ 109,885 |
| North America | 11,464 | 3,986 | 33,698 | 13,532 |
| Europe | 2,426 | 3,023 | 8,207 | 7,385 |
| Other Regions | - | 208 | 1,850 | 2,665 |
| **Net revenue** | $61,581 | $ 53,784 | $175,800 | $ 133,467 |

The following table sets forth net revenue for each significant country based on the ship-to location of customers (in thousands):

| | **Three Months Ended** | | **Nine Months Ended** | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **October 31, 2015** | **November 1, 2014** |
| China, including Hong Kong | $26,556 | $ 20,341 | $69,861 | $ 51,159 |
| Taiwan | 15,355 | 7,615 | 39,520 | 18,605 |
| United States | 11,300 | 4,007 | 33,395 | 13,416 |
| Thailand | 1,428 | 14,191 | 11,021 | 28,472 |
| Rest of the world | 6,942 | 7,630 | 22,003 | 21,815 |
| **Net revenue** | $61,581 | $ 53,784 | $175,800 | $ 133,467 |

During the three and nine months ended October 31, 2015, Sunjet Components Corporation accounted for 18% and 16% of our net revenue, respectively. During the three months ended November 1, 2014, Cal-Comp Electronics, Benchmark Electronics and Nanning Fugui Precision accounted for 13%, 13% and 10% of our net revenue, respectively; during the nine months ended November 1, 2014, Benchmark Electronics accounted for 13% of our net revenue.

As of October 31, 2015, Sunjet Components Corporation and Nanning Fugui Precision accounted for approximately 17% and 10% of net accounts receivable, respectively. As of January 31, 2015, Benchmark Electronics, Nanning Fugui Precision and Arrow Electronics accounted for approximately 16%, 12%, and 10% of net accounts receivable.

**14. Subsequent events**

***Acquisition of Bretelon, Inc.—***On November 4, 2015, we completed the acquisition of Bretelon, Inc. ("Bretelon"), who is currently engaged in developing an advanced form of mobile IoT technology ("Acquisition"). In accordance with the related Agreement and Plan of Merger (the "Merger Agreement"), all of the outstanding equity interests of Bretelon were exchanged for aggregate consideration of approximately $22.7 million in cash, subject to certain adjustments (the "Merger Consideration"), which was funded with a combination of cash on hand and the incurrence of certain liabilities. We are retaining a portion of the consideration following the closing for the satisfaction of indemnification claims made within a specified period of time. The Acquisition was consummated on November 12, 2015. For a complete description of the aforementioned Acquisition and related Merger Agreement, refer to the Current Report on Form 8-K filed on November 10, 2015 and exhibit 2.1 therein.

For the three months ended October 31, 2015, we recorded transaction costs of approximately $0.3 million related to the Bretelon Acquisition in general and administrative expense in the accompanying condensed consolidated statements of operations.

Prior to the consummation of the Acquisition, we loaned approximately $2.7 million of cash to Bretelon in exchange for a number of interest-bearing promissory notes (the "Notes"). These Notes with principal amounts of $1.5 million, $1.0 million and $0.2 million were issued on August 28, 2015, September 14, 2015, and October 5, 2015, respectively; all of which bore interest at three percent per annum. Upon consummation of the Acquisition, the Notes along with accrued interest were deducted from the aggregate consideration. These Notes were outstanding as of October 31, 2015 and are included in prepaid expenses and other current assets in the accompanying condensed consolidated balance sheet as of the aforementioned date.

**SIGMA DESIGNS, INC.**

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

The Bretelon Acquisition was accounted for as a purchase and the operations of Bretelon will be included in our consolidated financial statements from the date of Acquisition.

Our acquisition of Bretelon during the fourth quarter was a major step forward in expanding our overall IoT footprint. This Acquisition expands our total addressable market to include outdoor applications, which are an ideal complement to our Z-Wave product line that covers indoor applications. Mobile IoT is a strong growth market with an expanding range of applications for both consumer and commercial consumption. Additionally, we intend to take advantage of the synergy between these two product lines to service smart city and commercial opportunities that make outdoor use of the Z-Wave mesh network and mobile IoT connectivity.

We will recognize the Bretelon assets acquired and liabilities assumed based upon the fair value of such assets and liabilities measured as of the date of Acquisition. The aggregate purchase price for Bretelon will be allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values at the date of Acquisition. The excess of the purchase price over the fair value of the acquired net assets represents cost and revenue synergies specific to the Company, as well as non-capitalizable intangible assets, such as the employee workforce acquired, and will be allocated to goodwill, none of which is expected to be tax deductible.

We expect to finalize the allocation of purchase price within 12 months of November 4, 2015. The preliminary allocation of purchase price as of December 6, 2015, is as follows (in thousands):

| | **Amount** | | |
|---|---|---|---|
| Cash consideration | $ | 21,072 | |
| Liabilities assumed | | 1,647 | |
| Total consideration | $ | 22,719 | |
| | | | |
| Assets acquired | $ | 32 | |
| Liabilities assumed | | (1,647 | ) |
| Net tangible liabilities assumed | | (1,615 | ) |

| | | **Estimated Useful Life**<br><br>**(in years)** |
|---|---|---|
| Identifiable intangible assets: | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Developed technology | | 14,190 | 8 | - | 10 |
| Customer relationships | | 4,700 | 3 | - | 5 |
| Goodwill | | 5,444 | | — | |
| Total consideration | $ | 22,719 | | | |

The purchase price allocation is preliminary and subject to completion including the areas of taxation where we are finalizing a study of the potential utilization of acquired net operating losses is not yet complete, and certain fair value measurements, particularly the finalization of the valuation assessment of the acquired tangible and intangible assets. The adjustments arising from the completion of the outstanding matters may materially affect the preliminary purchase accounting.

Disclosure of pro forma earnings attributable to Bretelon is excluded as it would be impracticable, due to our limited visibility into historical financial records as we are still in the preliminary stages of the Acquisition and related integration efforts.

Certain directors of ours owned shares and other securities of Bretelon prior to the Acquisition. Martin Manniche, a member of our Board of Directors, also served on the board of directors of Bretelon and held a fully vested option to purchase 700,000 shares of Bretelon common stock (the “Option”). At the consummation of the Acquisition, the Option was converted into a right to receive cash proceeds from the Merger Consideration equal to the difference between the price per share paid for Bretelon common stock in the Acquisition and the exercise price of the Option, or an aggregate of approximately $215,000.

**SIGMA DESIGNS, INC.**

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

Our President, Chief Executive Officer and a member of our Board, Thinh Tran, also beneficially owned 1,710,526 shares of Bretelon common stock, or 3.9% of the outstanding shares of Bretelon capital stock on a fully diluted basis. Pursuant to the terms of the Merger Agreement, Mr. Tran divested his shares of Bretelon common stock prior to the consummation of the Acquisition by transferring such shares at original cost to us at an aggregate price of $97,500. We have received the benefit of the proceeds that would have been otherwise allocated to these shares held by Mr. Tran in the Acquisition, which proceeds equaled approximately six times the original cost of such shares. This transfer from Mr. Tran to the Company was subject to, and occurred immediately prior to, the consummation of the Acquisition.

In light of the interests of certain members of our Board in this transaction, our Board established a special committee of the Board (the "Special Committee") consisting of independent directors who had no interest or prior dealings with Bretelon. The members of the Special Committee were Tor Braham, J. Michael Dodson and Pete Thompson. These directors also comprise our Audit Committee, which committee is also charged with reviewing related-party transactions. The primary duties of the Special Committee were to evaluate the strategic opportunity with Bretelon, to review the principal terms of any proposed transaction with Bretelon and to make a final recommendation to our Board on whether to approve any definitive agreement with Bretelon. The Special Committee unanimously approved the Acquisition and the Merger Agreement and recommended to the full Board that it approve the Acquisition and the Merger Agreement. Upon such recommendation, our Board approved the Acquisition and the Merger Agreement, with Mr. Tran abstaining from the vote and Mr. Manniche not in attendance at our Board meeting in which the Acquisition and the Merger Agreement were approved.

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

*You should read the following discussion in conjunction with our condensed consolidated financial statements and related notes in this Form 10-Q. Except for historical information, the following discussion contains forward-looking statements within the meaning of Section 27A of the Securities Exchange Act of 1933 and Section 21E of the Securities Exchange Act of 1934. In some cases, you can identify forward-looking statements by terms such as "may," "might," "will," "objective," "intend," "should," "could," "can," "would," "expect," "believe," "estimate," "predict," "potential," "plan," or the negative of these terms, and similar expressions intended to identify forward-looking statements. These forward-looking statements, include, but are not limited to, statements about our capital resources and needs, including the adequacy of our current cash reserves, the expectation that our revenue from the IoT Devices market will continue to increase in the foreseeable future, anticipated deployments and design wins in the Set-top Box market, anticipated seasonality associated with our Smart TV market, our expectations that our gross margin will vary from period to period and anticipated payments or expectations related to possible share rescissions. These forward-looking statements involve risks and uncertainties. Our actual results may differ significantly from those projected in the forward-looking statements. Factors that might cause future results to differ materially from those discussed in the forward-looking statements include, but are not limited to, those discussed under Part II, Item 1A "Risk Factors" in this Form 10-Q as well as other information found in the documents we file from time to time with the Securities and Exchange Commission. Also, these forward-looking statements represent our estimates and assumptions only as of the date of this Form 10-Q. Unless required by U.S. federal securities laws, we do not intend to update any of these forward-looking statements to reflect circumstances or events that occur after the statement is made.*

**Overview**

We are a global integrated semiconductor solutions provider offering intelligent media platforms for use in the home entertainment and home control markets. Our goal is to ensure that our chipsets serve as the foundation for some of the world's leading consumer products, including televisions, set-top boxes, media connectivity and home control products. Our business generates revenue primarily by delivery of relevant, cost-effective semiconductors that are targeted toward end-product manufacturers, Original Equipment Manufacturers, or OEMs, and Original Design Manufacturers, or ODMs. We also derive a portion of our revenue from other products and services, including technology licenses, software development kits, engineering support services for hardware and software, engineering development for customization of chipsets and other accessories.

**Our chipset products and target markets**

We consider all of our semiconductor products to be chipsets because each of our products is comprised of multiple semiconductors. We believe our chipsets enable our customers to efficiently bring consumer multimedia devices to market.  We design our highly integrated products to significantly improve performance, lower power consumption and reduce cost.

We sell our products into four primary or target markets: (i) Smart TV, (ii) Media Connectivity, (iii) Set-top Box and (iv) Internet of Things (“IoT”) Devices. Smart TV products consist of a range of platforms that are based on highly integrated chips, embedded software, and hardware reference designs. Media Connectivity products consist of wired home networking controller chipsets that are designed to provide connectivity solutions between various home entertainment products and incoming video streams. Set-top Box products consist of connected media processors and players delivering IP streaming video, including hybrid versions of these products. IoT Devices consist of our wireless Z-Wave chipsets and modules.

Historically, we disclosed information encompassing product groupings by target markets with certain naming conventions, consisting of Digital Television (“DTV”), Set-top Box, Home Networking, Home Control, and License and other. Effective in the fourth quarter of fiscal 2015, we changed the naming conventions of some of our target markets, commensurate with changes taking effect in our industry as a whole. We renamed our “DTV” target market to “Smart TV,” “Home Networking” to “Media Connectivity,” and “Home Control” to “IoT Devices.” These changes did not affe the products or related services categorization, or previously reported amounts related to the aforementioned historical target markets.

*Smart TV Market*

The Smart TV market (previously referred to as our DTV market) consists of all products that are sold into digital televisions as well as other adjacent markets using chipset products that are designed for video post-processing. We believe Smart TV products complement our existing Set-top Box products, which will provide substantial research and development leverage and improved operating scale to augment our ability to develop innovative solutions for the anticipated convergence of IP-video delivery across any device within the connected home. Furthermore, our early entry into the emerging ultra-high definition ("UHD," "Ultra-HD" or "4K") television market has provided a differential opportunity for us to penetrate key customers for high-end products, which will eventually become mainstream over time. We serve this market with our media processor chips and dedicated post-processing products.

*Set-top Box Market*

The Set-top Box target market consists of all Set-top Box products delivering IP streaming video, including hybrid versions of these products.  We serve this market primarily with our media processor products.

*Media Connectivity Market*

The Media Connectivity market consists of communication devices that use a standard protocol to connect equipment inside the home and stream IP-based video and audio, VoIP, or data through wired or wireless connectivity. We serve the Media Connectivity market with our wired home networking controllers that are designed to provide the most reliable connectivity solutions between various home entertainment products and incoming video streams.

*Internet of Things ("IoT") Devices Market*

The IoT Devices market consists of all interconnected Z-Wave enabled gateways, appliances and devices that provide monitoring and control capabilities for the management of any consumer ecosystem. Our IoT Devices product line consists of our wireless Z-Wave chips, modules and Z-Wave mesh networking protocol.

Our acquisition of Bretelon, Inc., an advanced form of mobile IoT Technology Company in the fourth quarter is intended to expand our overall IoT footprint. This acquisition expands our total addressable market to include products with outdoor applications, which are an ideal complement to our Z-Wave product line that covers indoor applications. We intend to take advantage of the synergy between these two product lines to service smart city and commercial opportunities that make outdoor use of the Z-Wave mesh network and mobile IoT connectivity.

*License and Other Markets*

The license and other markets includes other products and services, including technology licenses, software development kits, engineering support services for hardware and software, engineering development for customization of chipsets and other accessories.

**Restructuring program**

In fiscal 2013, as a result of significant expansion in our infrastructure and operational activities in connection with purchases and acquisitions that took place between fiscal years 2008 and 2013, and in response to certain redundancies, underperforming operations and delays in programs and product releases, we implemented a restructuring program to realign our global operating expenses with our new business conditions, and to improve efficiency, competitiveness and profitability. Costs relating to facilities closure or lease commitment are recognized when the facility has been exited. Termination costs are recognized when the costs are deemed both probable and estimable and after notification to impacted employees has occurred.

During the first quarter of fiscal 2016, we incurred restructuring charges of less than $0.1 million, substantially all of which was related to facility exit cost adjustments, which was reflected in operating expenses. During the second and third quarters of fiscal 2016, we incurred no restructuring charges.

In the first quarter of fiscal 2015, we incurred restructuring charges of $1.0 million, all of which was related to workforce reductions of 29 employees across several geographic regions, the majority of which were in our operations in Israel. Of the total restructuring charges recorded in the first fiscal quarter, approximately $0.1 million was reflected in cost of revenue and $0.9 million was reflected in operating expenses. During the second and third quarters of fiscal 2015, we incurred less than $0.1 million of restructuring charges.

Expenses recognized for restructuring activities impacting our operating expenses are included in “Restructuring costs” in the condensed consolidated statements of operations. Our restructuring measures could negatively impact our revenue and results of operations in the future as a result of less employees developing future products and working to sell our products.

**Critical accounting policies and estimates**

There have been no significant changes in our critical accounting policies during the nine months ended October 31, 2015, as compared to the critical accounting policies described in our Annual Report on Form 10-K for the year ended January 31, 2015. For a complete summary of our significant accounting policies, refer to Note 1, "Organization and Summary of Significant Accounting Policies”, in Part II, Item 8 of our fiscal 2015 Annual Report.

**Results of operations**

The following table is derived from our unaudited condensed consolidated financial statements and sets forth our historical operating results as a percentage of net revenue for each of the periods indicated (in thousands, except percentages):

| | Three Months Ended | | | | Nine Months Ended | | | |
|---|---|---|---|---|---|---|---|---|
| | October 31, 2015 | % of Net Revenue | November 1, 2014 | % of Net Revenue | October 31, 2015 | % of Net Revenue | November 1, 2014 | % of Net Revenue |
| **Net revenue** | $61,581 | 100 % | $53,784 | 100 % | $175,800 | 100 % | $133,467 | 100 % |
| Cost of revenue | 30,794 | 50 % | 27,272 | 51 % | 87,141 | 50 % | 64,841 | 49 % |
| **Gross profit** | 30,787 | 50 % | 26,512 | 49 % | 88,659 | 50 % | 68,626 | 51 % |
| **Operating expenses** | | | | | | | | |
| Research and development | 17,339 | 28 % | 16,603 | 31 % | 49,754 | 28 % | 50,158 | 37 % |
| Sales and marketing | 5,875 | 10 % | 5,559 | 10 % | 16,940 | 10 % | 16,484 | 12 % |
| General and administrative | 5,314 | 9 % | 4,808 | 9 % | 16,091 | 9 % | 14,394 | 11 % |
| Restructuring costs | - | - % | (18) | 0 % | 9 | 0 % | 1,002 | 1 % |

| | | | | | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Impairment of IP, mask sets and design tools | | 795 | 1 | % | | 856 | | 2 | % | | 1,783 | 1 | % | | 2,122 | | 2 | % |
| Total operating expenses | | 29,323 | 48 | % | | 27,808 | | 52 | % | | 84,577 | 48 | % | | 84,160 | | 63 | % |
| **Income (loss) from operations** | | 1,464 | 2 | % | | (1,296 | ) | (3 | %) | | 4,082 | 2 | % | | (15,534 | ) | (12 | %) |
| Gain on sale of development project | | 7,551 | 12 | % | | - | | - | | | 7,551 | 4 | % | | - | | - | |
| Interest and other income, net | | 37 | 0 | % | | 188 | | 0 | % | | 821 | 1 | % | | 508 | | 0 | % |
| **Income (loss) before income taxes** | | 9,052 | 14 | % | | (1,108 | ) | (3 | %) | | 12,454 | 7 | % | | (15,026 | ) | (12 | %) |
| Provision for (benefit from) income taxes | | 2,617 | 4 | % | | (551 | ) | (1 | %) | | 6,105 | 3 | % | | 3,065 | | 2 | % |
| **Net income (loss)** | $ | 6,435 | 10 | % | $ | (557 | ) | (2 | %) | $ | 6,349 | 4 | % | $ | (18,091 | ) | (14 | %) |

**Net revenue**

Our net revenue for the three months ended October 31, 2015 increased $7.8 million, or 14%, compared to the corresponding period in the prior fiscal year. Net revenue increased primarily due to a $15.7 million increase within the Smart TV market and an increase in the IoT Devices market of $3.0 million, partially offset by a decrease in sales into the Media Connectivity market of $9.0 million and a decrease in revenue from the Set-top Box market of $2.0 million.

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For the nine months ended October 31, 2015, our net revenue increased $42.3 million, or 32%, compared to the corresponding period in the prior fiscal year. Net revenue increased primarily due to a $45.7 million increase within the Smart TV market and an increase in the IoT Devices market of $15.7 million, partially offset by a decrease in sales into the Media Connectivity market of $13.8 million, a decrease of $0.4 million in the Set-top Box market and decreases from revenue related to the licensing of our technology to third parties of $4.9 million.

**Net revenue by target market**

We sell our products into four primary target markets, which are the Smart TV market, Media Connectivity market, Set-top Box market, and the Internet of Things, or "IoT," Devices market. We also have license revenue, included in license and other markets, which we receive from the license of our technology to third parties. Historically, we disclosed information encompassing product groupings by target markets with certain naming conventions, consisting of Digital Television ("DTV"), Set-top Box, Home Networking, Home Control, and License and other. Effective in the fourth quarter of fiscal 2015, we changed the naming conventions of some of our target markets, commensurate with changes taking effect in our industry as a whole. We renamed our "DTV" target market to "Smart TV," "Home Networking" to "Media Connectivity," and "Home Control" to "IoT Devices." These changes did not affect the products or related services categorization, or previously reported amounts related to the aforementioned historical target markets.

The following table sets forth our net revenue by target market and the percentage of net revenue represented by our product sales to each of those markets (in thousands, except percentages):

| | **Three Months Ended** | | | | **Nine Months Ended** | | | |
|---|---|---|---|---|---|---|---|---|
| | **October 31, 2015** | **% of Net Revenue** | **November 1, 2014** | **% of Net Revenue** | **October 31, 2015** | **% of Net Revenue** | **November 1, 2014** | **% of Net Revenue** |
| Smart TV | $32,244 | 52 % | $ 16,570 | 31 % | $78,378 | 45 % | $ 32,667 | 24 % |
| Media Connectivity | 14,003 | 23 % | 23,022 | 43 % | 43,149 | 25 % | 56,968 | 43 % |
| IoT Devices | 10,209 | 17 % | 7,182 | 13 % | 35,637 | 20 % | 19,898 | 15 % |
| Set-top box | 4,744 | 8 % | 6,759 | 13 % | 17,582 | 10 % | 17,976 | 13 % |
| License and other | 381 | 0 % | 251 | 0 % | 1,054 | 0 % | 5,958 | 5 % |
| Net revenue | $61,581 | 100 % | $ 53,784 | 100 % | $175,800 | 100 % | $ 133,467 | 100 % |

***Smart TV:*** For the three months ended October 31, 2015, net revenue from sales of our products into the Smart TV market increased by $15.7 million, or 95%, compared to the corresponding period in the prior fiscal year. For the nine months ended October 31, 2015, net revenue increased by $45.7 million, or 140%, compared to the corresponding period in the prior fiscal year. We experienced an increase of 114% in average selling price, or ASP, partially offset by a decrease of 9% in units shipped during the three months ended October 31, 2015. Similarly, we experienced an increase of 194% in ASP partially offset by a decline of 18% in units shipped in the Smart TV market during the nine months ended October 31, 2015.

In both cases, the increase in ASP is primarily the result of continued penetration of our new product offerings in the market having higher ASP for use in ultra-high definition, also known as Ultra-HD televisions. The Smart TV market transition, and consequently, anticipated demand of Ultra-HD is bolstering the demand for our new generation products. The volume decline in our Smart TV market resulted primarily from the continued decline of demand for our older legacy products, many of which are now approaching end-of-life. Our Smart TV revenue was derived mainly from our Asian and North American regions. We typically expect our strongest Smart TV sales in the third calendar quarter and declining Smart TV sales in the first and fourth quarter of each calendar year. We expect our net revenue from the Smart TV market to continue to be a significant percentage of net revenue but will fluctuate in future periods as we continue to develop and introduce new products for this market and as a result of seasonality typically experienced in the consumer electronics market.

***Media Connectivity:*** For the three months ended October 31, 2015, net revenue from sales of our products into the Media Connectivity market decreased $9.0 million, or 39%, compared to the corresponding period in the prior fiscal year primarily due to a decrease of 30% in ASP, compounded by a decrease of 13% in units shipped. For the nine months ended October 31, 2015, net revenue decreased $13.8 million, or 24%, compared to the corresponding period in the prior fiscal year due to a decrease of 14% in ASP, compounded by a decline of 12% in units shipped. In both cases, the decrease in units shipped and ASP was primarily the result of reduced demand due to the continued expansion of wireless technologies in the market impacting our existing product offerings.

We expect our revenue from the Media Connectivity market to fluctuate in future periods with varying levels of sustainability primarily as a result of telecommunications provider's pending transitions to next generation technologies. Our success in this market will depend primarily on how quickly the market transitions from our current HPNA solutions, which enjoy a significant share of the market, to next generation technologies. We have developed wired connectivity solutions based on G.hn technology. To date, we have not derived meaningful revenue from our G.hn solutions, which compete against other wired solutions as well as emerging wireless solutions. If our revenue from our HPNA solutions declines and we are not able to gain market acceptance of our G.hn solutions, the revenue in our Media Connectivity market will likely decline. Fluctuations in revenue are primarily based on changes in inventory levels at contract manufacturers who manufacture equipment incorporating our products for deployment by telecommunication providers.

***IoT Devices:*** For the three months ended October 31, 2015, net revenue from sales of our products into the IoT Devices market increased $3.0 million, or 42%, compared to the corresponding period in the prior fiscal year. For the nine months ended October 31, 2015, net revenue increased $15.7 million, or 79%, compared to the corresponding period in the prior fiscal year. In both cases, the increase was primarily the result of increased demand in the IoT Devices market, evidenced by increases of 62% and 100% in unit shipments primarily to the Asian and North American regions for the three and nine months ended October 31, 2015, respectively. These increases were partially offset by a decline in ASP of 12% and 10% for the three and nine months ended October 31, 2015, respectively, due to higher volume pricing of service providers. We have compelling products for our IoT Devices market and we continue to target large operators who are introducing home control products primarily in the aforementioned regions. We expect our revenue from the IoT Devices market to continue to increase in the foreseeable future, subject to fluctuations due to seasonality and changes in inventory levels at contract manufacturers who manufacture equipment incorporating our products for deployment by operators.

***Set-top Box:*** For the three months ended October 31, 2015, net revenue from sales of our products into the Set-top Box market decreased $2.0 million, or 30%, compared to the corresponding period in the prior fiscal year. For the nine months ended October 31, 2015, net revenue decreased $0.4 million, or 2%, compared to the corresponding period in the prior fiscal year. In both cases, the decrease was primarily the result of decreased demand in the Set-top Box market, evidenced by decreases of 32% and 10% in unit shipments primarily to the Asian region for the three and nine months ended October 31, 2015, respectively, due to IPTV service providers' pending transition to new generations of set-top box products. ASP increased 3% and 9% for the three and nine months ended October 31, 2015, respectively, in comparison to the corresponding periods in the prior fiscal year primarily due to some of our maturing product lines constricted availability in the market thereby bolstering their prices. IPTV service providers deploy set-top boxes for many years and take a long time to evaluate potential new platforms, which results in long cycles between design wins and actual revenue. We expect our revenue from the Set-top Box market to fluctuate and perhaps decline in future periods as this revenue is dependent on IPTV service deployments by telecommunication service providers, adoption of new and future generations of our ARM-based products, changes in inventory levels at the contract manufacturers that supply them and competitive market pressures.

***License and other markets*****:** Our license and other markets consist primarily of technology license revenue and revenue from other ancillary markets. For the three months ended October 31, 2015, net revenue increased $0.1 million, or 52%, compared to the corresponding period in the prior fiscal year. For the nine months ended October 31, 2015, net revenue decreased $4.9 million, or 82%, compared to the corresponding period in the prior fiscal year. The license revenue in the prior fiscal year was attributable to two license agreements pursuant to which we licensed our technology to third parties for which we were able to recognize revenue. Our obligations under the aforementioned license arrangements were completed during the second quarter of fiscal 2015. We expect license revenue to fluctuate in future periods.

**Net revenue by geographic region**

The following table sets forth net revenue for each geographic region based on the ship-to location of customers (in thousands, except percentages):

| | Three Months Ended | | | | | | Nine Months Ended | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | October 31, 2015 | % of Net Revenue | | November 1, 2014 | % of Net Revenue | | October 31, 2015 | % of Net Revenue | | November 1, 2014 | % of Net Revenue | |
| Asia | $47,691 | 77 | % | $ 46,567 | 87 | % | $132,045 | 75 | % | $ 109,885 | 82 | % |
| North America | 11,464 | 19 | % | 3,986 | 7 | % | 33,698 | 19 | % | 13,532 | 10 | % |
| Europe | 2,426 | 4 | % | 3,023 | 6 | % | 8,207 | 5 | % | 7,385 | 6 | % |
| Other regions | - | - | % | 208 | 0 | % | 1,850 | 1 | % | 2,665 | 2 | % |
| Net revenue | $61,581 | 100 | % | $ 53,784 | 100 | % | $175,800 | 100 | % | $ 133,467 | 100 | % |

***Asia:*** Our net revenue from Asia increased $1.1 million, or 2%, for the three months ended October 31, 2015, compared to the corresponding period in the prior fiscal year. Our net revenue for the nine months ended October 31, 2015 increased $22.2 million, or 20%, compared to the corresponding period in the prior fiscal year. In both cases, the increases were largely attributable to the increasing deployments of new generation products by our customers within the Smart TV market. In Asia, we also experienced increases in the IoT Devices market due to increasing demand of home control products by an increasing number of operators leveraging these technologies in their service offerings to end users. These increases were partially offset by a decrease in the Media Connectivity market resulting from decreased demand from telecommunication providers. Net revenue from customers in Asia as a percentage of our total net revenue for the three and nine months ended October 31, 2015 decreased ten and seven percentage points, respectively, compared to the corresponding periods in the prior fiscal year. These decreases are primarily due to the significant increase in revenue in North America.

***North America:*** Our net revenue from North America increased $7.5 million, or 188%, for the three months ended October 31, 2015, compared to the corresponding period in the prior fiscal year. Our net revenue for the nine months ended October 31, 2015 increased $20.2 million, or 149%, compared to the corresponding period in the prior fiscal year. In both cases, the increases were primarily attributable to the increasing deployments of newer generation products by our operators' customers within the Smart TV market and increases in the IoT Devices market due to increasing demand of home control products by an increasing number of operators leveraging these technologies in their service offerings to end users. These increases were partially offset by lower revenue recorded in the license and other revenue market. The obligations under license agreements with two main customers in the North American region were completed during the second quarter of fiscal 2015. Net revenue from North American customers as a percentage of our total net revenue for the three and nine months ended October 31, 2015 increased twelve and nine percentage points, respectively, compared to the corresponding periods in the prior fiscal year primarily due to an increasing IoT Devices market base and increased deployments of products within the Smart TV market.

***Europe:*** Our net revenue from Europe decreased $0.6 million, or 20%, for the three months ended October 31, 2015, compared to the corresponding period in the prior fiscal year. Our net revenue for the nine months ended October 31, 2015 increased $0.8 million, or 11%, compared to the corresponding period in the prior fiscal year. We are experiencing increases in the IoT Devices market due to increasing demand of home control products by an increasing number of operators leveraging these technologies in their service offerings to end users, contributing to the increase experienced during the nine months ended October 31, 2015. These increases were partially offset by a decrease in demand for our Smart TV products in Germany during the three months ended October 31, 2015. Net revenue from Europe as a percentage of our total net revenue for the three and nine months ended October 31, 2015 remained relatively flat compared to the corresponding periods in the prior fiscal year.

***Other regions:*** Our net revenue from other regions decreased $0.2 million, or 100%, for the three months ended October 31, 2015, compared to the corresponding period in the prior fiscal year. Our net revenue for the nine months ended October 31, 2015 decreased $0.8 million, or 31%, compared to the corresponding period in the prior fiscal year. The decreases were primarily the result of a decrease in demand for our products in the Media Connectivity market in Brazil.

**Major customers**

During the three and nine months ended October 31, 2015, Sunjet Components Corporation accounted for 18% and 16% of our net revenue, respectively. During the three months ended November 1, 2014, Cal-Comp Electronics, Benchmark Electronics and Nanning Fugui Precision accounted for 13%, 13% and 10% of our net revenue, respectively; during the nine months ended November 1, 2014, Benchmark Electronics accounted for 13% of our net revenue.

As of October 31, 2015, Sunjet Components Corporation and Nanning Fugui Precision accounted for approximately 17% and 10% of net accounts receivable, respectively. As of January 31, 2015, Benchmark Electronics, Nanning Fugui Precision and Arrow Electronics accounted for approximately 16%, 12%, and 10% of net accounts receivable.

**Gross profit and gross margin**

The following table sets forth our gross profit and gross margin (in thousands, except percentages):

| | Three Months Ended | | | Nine Months Ended | | |
|---|---|---|---|---|---|---|
| | October 31, 2015 | % Change | November 1, 2014 | October 31, 2015 | % Change | November 1, 2014 |
| Gross profit | $30,787 | 16 % | $ 26,512 | $88,659 | 29 % | $ 68,626 |
| Gross margin % | 50.0 % | 1 % | 49.3 % | 50.4 % | (1% ) | 51.4 % |

Gross profit increased $4.3 million, or 16%, for the three months ended October 31, 2015, compared to the corresponding period in the prior fiscal year. The increase was primarily due to higher gross profit per unit within the Smart TV market resulting from continued penetration of our new product offerings with a related impact of $9.9 million and increases in sales volumes within the IoT Devices market with a related impact of $2.4 million. Gross profit was negatively impacted by ASP declines and a decrease in sales volumes within the Media Connectivity market with related impacts of $5.9 million and $1.8 million, respectively. Our gross margin increased approximately one percentage point for the three months ended October 31, 2015, compared to the corresponding period in the prior fiscal year primarily due to product mix within the Smart TV market driven by increased sales volumes of certain legacy products, which are now approaching end-of-life, and yield higher product margins when compared to newer product offerings.

Gross profit increased $20.0 million, or 29%, for the nine months ended October 31, 2015, compared to the corresponding period in the prior fiscal year. The increase was primarily due to higher gross profit per unit within the Smart TV market resulting from continued penetration of our new product offerings with a related impact of $28.5 million and increases in sales volumes within the IoT Devices market with a related impact of $10.8 million. Gross profit was negatively impacted by ASP declines and a decrease in sales volumes within the Media Connectivity market with related impacts of $7.3 million and $3.7 million, respectively. We also experienced $4.9 million of lower sales in license technology, which has very little cost of revenue. Our gross margin declined one percentage point for the nine months ended October 31, 2015, compared to the corresponding period in the prior fiscal year primarily due to the aforementioned decline in license revenue.

Although ASP declined across some of our target markets, we continued our significant efforts to reduce the average cost per unit, or ACU, across our markets. The decrease in ACU was primarily due to cost reduction efforts through activities targeting fixed costs. Our fixed costs include items such as depreciation and amortization and compensation costs for operations.

Our future gross margin could be impacted by our product mix and could be adversely affected by further growth in sales of products that have lower gross margins. Our gross margin may also be impacted by the geographic mix of our revenue and may be adversely affected by increased sales discounts, rebates, royalties, and product pricing attributable to competitive factors. Additionally, our manufacturing-related costs may be negatively impacted by constraints in our supply chain, which in turn could negatively affect gross margin. If any of the preceding factors that in the past have negatively impacted our gross margin arises in the future, our gross margin could decline.

**Research and development expense**

Research and development expense consists of compensation and benefits costs including variable compensation expense, development and design costs such as mask, prototyping, testing and subcontracting costs, depreciation and amortization of our engineering design tools and equipment costs, stock-based compensation expense, and other expenses such as costs for facilities and travel. During certain periods, research and development expense may fluctuate relative to product development phases and project timing. The following table sets forth our research and development expense and the related change (in thousands, except percentages):

| | **Three Months Ended** | | | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **$ Change** | **% Change** |
| Research and development expense | $17,339 | $ 16,603 | $ 736 | 4 % |
| Percent of net revenue | 28.2 % | 30.9 % | | |

| | **Nine Months Ended** | | | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **$ Change** | **% Change** |
| Research and development expense | $49,754 | $ 50,158 | $ (404 ) | (1 %) |
| Percent of net revenue | 28.3 % | 37.6 % | | |

The increase in research and development expense for the three months ended October 31, 2015 compared to the corresponding period in the prior fiscal year is primarily due to an increase in research and development personnel of approximately 6% from November 1, 2014 to October 31, 2015, primarily in Shanghai, China and the United States, due to our continuing efforts to develop emerging technologies and expand our product offerings within our target markets, specifically within the Smart TV and IoT Devices markets.

The decrease in research and development expense for the nine months ended October 31, 2015 compared to the corresponding period in the prior fiscal year is primarily due to decreases of $0.5 million in equipment and engineering support costs and decreases of $0.4 million of allocable overhead and facility related costs. These decreases were partially offset by the aforementioned hiring activities of additional employees in Shanghai, China and the United States.

**Sales and marketing expense**

Sales and marketing expense consists primarily of compensation and benefits costs, including commissions to our direct sales force, stock-based compensation expense, trade shows, travel and entertainment expenses and external commissions. Our sales and marketing expense is summarized as follows (in thousands, except percentages):

| | **Three Months Ended** | | | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **$ Change** | **% Change** |
| Sales and marketing expense | $5,875 | $ 5,559 | $ 316 | 6 % |
| Percent of net revenue | 9.5 % | 10.3 % | | |

| | **Nine Months Ended** | | | |
|---|---|---|---|---|
| | **October 31, 2015** | **November 1, 2014** | **$ Change** | **% Change** |
| Sales and marketing expense | $16,940 | $ 16,484 | $ 456 | 3 % |
| Percent of net revenue | 9.6 % | 12.4 % | | |

The increase in sales and marketing expense for the three and nine months ended October 31, 2015 compared to the corresponding periods in the prior fiscal year is primarily due to increases in tradeshow costs of $0.3 million and $0.9 million, respectively, partially offset by decreased personnel related compensation costs.

**General and administrative expense**

General and administrative expense consists primarily of compensation and benefits costs, stock-based compensation expense, legal, accounting and other professional fees and facilities expenses. Our general and administrative expense is summarized as follows (in thousands, except percentages):

| | **Three Months Ended October 31, 2015** | **November 1, 2014** | **$ Change** | **% Change** |
|---|---|---|---|---|
| General and administrative expense | $5,314 | $ 4,808 | $ 506 | 11 % |
| Percent of net revenue | 8.6 % | 8.9 % | | |

| | **Nine Months Ended October 31, 2015** | **November 1, 2014** | **$ Change** | **% Change** |
|---|---|---|---|---|
| General and administrative expense | $16,091 | $ 14,394 | $ 1,697 | 12 % |
| Percent of net revenue | 9.2 % | 10.8 % | | |

The increase in general and administrative expense for the three and nine months ended October 31, 2015 compared to the corresponding periods in the prior fiscal year is primarily due to higher professional fees of $0.1 million and $1.1 million, respectively, associated with legal, audit and tax activities and other outside services. We also experienced an increase in personnel related costs of $0.3 million for each of the three and nine months ended October 31, 2015 despite a 3% decrease in personnel from November 1, 2014 to October 31, 2015. These increases were primarily the result of one-time incentive compensation activities and increased stock compensation expense resulting from the appreciation of our stock price.

**Impairment of IP, mask sets and design tools**

We test long-lived assets, including our purchased intangible assets, for impairment whenever events or changes in circumstances, such as a change in technology, indicate that the carrying value of these assets may not be recoverable. If indicators of impairment exist, we determine whether the carrying value of an asset or asset group is recoverable, based on comparisons to undiscounted expected future cash flows that the assets are expected to generate. If an asset is not recoverable, we record an impairment loss equal to the amount by which the carrying value of the asset exceeds its fair value. We primarily use the income valuation approach to determine the fair value of our long-lived assets and purchased intangible assets. We also periodically review our current assets for other-than-temporary declines in fair-value based on the specific identification method and write-down the carrying value when an other-than temporary decline has occurred.

Our business requires investment in purchased intellectual properties, mask sets and design tools that are technologically advanced but can quickly become significantly underutilized or rendered obsolete by rapid changes in demand in the semiconductor industry. We periodically review our purchased intellectual properties, mask sets and design tools for possible impairment or whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. As a result of this review, we recorded $0.4 million of impairment charges during the three and nine months ended October 31, 2015 related to IP within the Media Connectivity market for which the related products had little to no market. We also recorded $0.4 million and $1.4 million of impairment charges during the three and nine months ended October 31, 2015 related to mask sets within the Media Connectivity and other ancillary markets for the aforementioned reasons.

During the three and nine months ended November 1, 2014, we recorded impairment charges related to our IP, mask sets and design tools of $0.9 million and $2.1 million, respectively, primarily related to a mask set and related IP within the set-top box market and IP within the DTV market for which the related products had minimal-to-no market.

**Restructuring costs**

In fiscal 2013, as a result of significant expansion in our infrastructure and operational activities in connection with purchases and acquisitions that took place between fiscal years 2008 and 2013, and in response to certain redundancies, underperforming operations and delays in programs and product releases, we implemented a restructuring program to realign our global operating expenses with our new business conditions, and to improve efficiency, competitiveness and profitability. Costs relating to facilities closure or lease commitment are recognized when the facility has been exited. Termination costs are recognized when the costs are deemed both probable and estimable and after notification to impacted employees has occurred.

During the first quarter of fiscal 2016, we incurred restructuring charges of less than $0.1 million, substantially all of which was related to facility exit cost adjustments, which was reflected in operating expenses. During the second and third quarters of fiscal 2016, we incurred no restructuring charges.

In the first quarter of fiscal 2015, we incurred restructuring charges of $1.0 million, all of which was related to workforce reductions of 29 employees across several geographic regions, the majority of which were in our operations in Israel. Of the total restructuring charges recorded in the first fiscal quarter, approximately $0.1 million was reflected in cost of revenue and $0.9 million was reflected in operating expenses. During the second and third quarters of fiscal 2015, we incurred less than $0.1 million of restructuring charges.

Expenses recognized for restructuring activities impacting our operating expenses are included in “Restructuring costs” in the condensed consolidated statements of operations. Our restructuring measures could negatively impact our revenue and results of operations in the future as a result of less employees developing future products and working to sell our products.

A combined summary of the recent activity of the restructuring plans initiated by us is as follows (in thousands):

| | Workforce Reduction | Asset Impairment | Facility Exit Costs | Total | Cumulative Restructuring Costs |
|---|---|---|---|---|---|
| Liability, February 1, 2014 | $ 363 | $ - | $ 2 | $ 365 | $ 5,570 |
| Charges in fiscal 2015 | 1,083 | - | (20) | 1,063 | 1,063 |
| Cash payments | (1,382) | - | 8 | (1,374) | - |
| Non-cash items | 38 | - | 10 | 48 | - |
| Liability, January 31, 2015 | 102 | - | - | 102 | 6,633 |
| Charges for the nine months ended October 31, 2015 | 3 | - | 6 | 9 | 9 |
| Cash payments | (3) | - | (7) | (10) | - |
| Non-cash items | - | | 1 | 1 | - |
| Liability, October 31, 2015 | $ 102 | $ - | $ - | $ 102 | $ 6,642 |

**Sale of development project**

On March 8, 2013, we entered into an Asset Purchase Agreement with a third party (the “Buyer”) to sell certain development projects (intellectual property) and long-lived assets (the “Connectivity Assets”) related to the connectivity technology over coaxial cable market, including the transfer of 21 employees (the “Connectivity Employees”) to the Buyer. The aggregate carrying amount of the Connectivity Assets ultimately transferred was approximately $0.6 million and were classified as assets held for sale in prepaid expenses and other current assets in the consolidated balance sheet at February 2, 2013. We received an initial payment of $2.0 million in cash at the closing of the transaction and a payroll expense reimbursement payment of $0.6 million (as described more fully below). Under the terms of the Asset Purchase Agreement, if certain technical milestones were met by September 30, 2013 as a result of further development of the transferred technology by the Buyer, we were to be paid an additional $5.0 million in cash.

In April 2013, upon receiving the closing consideration of $2.0 million, we recorded a gain of $1.1 million, net of the carrying value of the Connectivity Assets and fees for legal and bank services of approximately $0.4 million. The gain is included in “Gain on sale of development project” in the consolidated statements of operations for fiscal 2014. Additionally, in April 2013, in connection with the Asset Purchase Agreement, the Buyer reimbursed us for payroll expenses related to the employees transferred to the Buyer for the period from February 1, 2013 through the actual payroll transfer, totaling $0.6 million. As the contingent consideration was uncertain at the time of the initial sale, we did not recognize the contingent payment.

The Buyer advised us that it did not believe the milestones had been met by the deadline of September 30, 2013. On May 19, 2014, the parties amended the Asset Purchase Agreement to require the use of Judicial Arbitration and

Mediations Services ("JAMS") for arbitration to settle the dispute between the parties. We pursued our rights to the milestone consideration payment through the alternative dispute resolution provisions set forth in the amendment. On September 5, 2014, the Buyer filed counterclaims in response to our claims arising from the Asset Purchase Agreement. Arbitration regarding this dispute took place on June 1, 2015. In August 2015, we prevailed on all of the claims we asserted against the Buyer, and all of the Buyer's counterclaims against us were denied. We were awarded $5.0 million plus reimbursement of reasonable legal and other associated costs and interest. We have recovered $2.6 million in legal costs, interest and other associated expenses to date from the Buyer, for a total recovery of $7.6 million, which was recorded as other income in our condensed consolidated statements of operations in its entirety.

**Interest and other income, net**

The following table sets forth net interest and other income and the related change (in thousands, except percentages):

| | **Three Months Ended** | | | **Nine Months Ended** | | |
|---|---|---|---|---|---|---|
| | **October 31, 2015** | **% change** | **November 1, 2014** | **October 31, 2015** | **% change** | **November 1, 2014** |
| Interest and other income, net | $37 | (80 %) | $ 188 | $821 | 62 % | $ 508 |

Interest and other income primarily consists of interest income from marketable securities, income from refundable research and development credits, gains or losses on foreign exchange transactions, gains or losses on sales of marketable securities and gains or losses on disposals of software, equipment and leasehold improvements. The decrease of $0.2 million for the three months ended October 31, 2015 compared to the corresponding period in the prior fiscal year was primarily a result of a $0.4 million decrease in foreign currency gains due to the weakening of the US Dollar over other currencies in countries in which we operate and $0.1 million lower interest income from a lower average marketable security balance, partially offset by $0.2 million of charges in connection with investments we have made in support of our Z-Wave brand during the three months ended November 1, 2014 with no corresponding charges during the three months ended October 31, 2015.

The increase of $0.3 million for the nine months ended October 31, 2015 compared to the corresponding period in the prior fiscal year was primarily due to cash received of $0.5 million, which had been held in an escrow account from the liquidation of an investment that occurred in fiscal 2014, partially offset by a $0.2 million decrease in foreign currency gains due to the weakening of the US Dollar over other currencies in countries in which we operate and $0.1 million lower interest income from a lower average marketable security balance.

**Provision for income taxes**

We recorded a provision for and benefit from income taxes of $2.6 million and $0.6 million for the three months ended October 31, 2015 and November 1, 2014, respectively. The provision for income taxes was $6.1 million and $3.1 million for the nine months ended October 31, 2015 and November 1, 2014, respectively. The increase in tax expense is primarily attributable to the increase in profitability in taxable jurisdictions in the third quarter of fiscal year 2016 as compared to the same period in fiscal year 2015 and changes in tax reserves. During the three and nine months ended October 31, 2015 and November 1, 2014, we were unable to reasonably project our annual effective tax rate, and therefore computed our provision for income taxes based on year-to-date actual financial results. Included in our provision for income taxes are foreign exchange gains or losses on unsettled income tax liabilities.

**Liquidity and Capital Resources**

The following table sets forth the balances of cash and cash equivalents and short-term marketable securities (in thousands):

| | October 31, 2015 | January 31, 2015 |
| --- | --- | --- |

| | | |
|---|---|---|
| Cash and cash equivalents | $67,164 | $83,502 |
| Short-term marketable securities | 24,528 | 6,347 |
| | $91,692 | $89,849 |

We believe our existing balances of cash, cash equivalents and marketable securities will be sufficient to satisfy our working capital needs, capital asset purchases, outstanding commitments and other liquidity requirements associated with existing operations over the next 12 months.

As of October 31, 2015, our principal sources of liquidity consisted of cash and cash equivalents and short-term marketable securities of $91.7 million, which represents approximately $2.52 per share of outstanding common stock as compared to $2.54 as of January 31, 2015. Working capital as of October 31, 2015 was $118.2 million. Total cash and cash equivalents decreased by $16.3 million compared to January 31, 2015, primarily due to changes in operating assets and liabilities of $21.6 million, net purchases of marketable securities of $17.6 million, purchases of intangible and tangible assets of $8.3 million, issuances of short-term promissory notes of $2.7 million, $31.3 million of net income generated after adjusting for non-cash items and net proceeds of $2.8 million from exercises of employee stock options and stock purchase rights.

As of October 31, 2015, we held $3.5 million of long-term marketable securities. Although these marketable securities have maturities of greater than one year, we hold them as available-for-sale and may access these funds prior to their contractual maturities.

The following table sets forth the primary net cash inflows and outflows (in thousands):

| | Nine Months Ended | |
|---|---|---|
| | October 31, 2015 | November 1, 2014 |
| Net cash provided by (used in): | | |
| Operating activities | $9,757 | $ 12,760 |
| Investing activities | (28,583) | 3,055 |
| Financing activities | 2,671 | 1,306 |
| Effect of foreign exchange rate changes on cash and cash equivalents | (183) | (151) |
| **Net (decrease) increase in cash and cash equivalents** | $(16,338) | $ 16,970 |

**Cash flows from operating activities**

Net cash provided by operating activities of $9.8 million for the nine months ended October 31, 2015 was primarily due to a net change of $31.3 million of net income after non-cash adjustments of $25.0 million, partially offset by $21.6 million in operating assets and liabilities. Cash used in accounts receivable of $5.3 million during the nine months ended October 31, 2015 was primarily related to increased revenue and timing of collections. Cash provided by accounts payable of $4.3 million during the nine months ended October 31, 2015 was primarily a result of timing of payments. Cash used in income taxes payable of $1.4 million was primarily the result of large income tax payments in Singapore and Israel. Cash used in inventory of $9.8 million was primarily the result of increased purchases in anticipation of expected demand primarily within the Smart TV and IoT Devices markets. Cash used in accrued liabilities, compensation and related benefits of $4.5 million was primarily the result of timing of payments and payments on previously reserved rebates. Cash used in other non-current assets of $6.0 million was primarily the result of commitments for purchases of IP for use in future product offerings.

Net cash provided by operating activities of $9.8 million for the nine months ended October 31, 2015 represents a $3.0 million decrease from the cash provided by operating activities during the corresponding period in fiscal 2015. The change was partially attributable to the increase in cash used for inventory and accounts receivable of $7.7 million and $6.6 million, respectively. Cash used for other non-current assets and accrued liabilities, compensation and related benefits increased $6.1 million and $9.8 million, respectively. The increase in net income of $26.3 million after adjusting for non-cash items partially offset the overall decrease from the nine months ended November 1, 2014.

During the nine months ended October 31, 2015, we experienced higher media processor wafer purchases resulting in an increase in inventory in anticipation of seasonal customer demand and expanding opportunities in our target markets. The change in accounts receivable from the corresponding period in fiscal 2015 was primarily the result of increased revenue as well as the timing of product shipments and collections. Cash used in accrued liabilities, compensation and related benefits was primarily the result of timing of payments and higher rebates payments. Cash used in other non-current assets was primarily the result of larger commitments for purchases of IP for use in future product offerings.

Cash flows from our operating activities will continue to fluctuate based upon our ability to grow net revenues while reducing our costs and managing the timing of payments to us from customers and to vendors from us, the timing of inventory purchases and subsequent manufacture and sale of our products.

**Cash flows from investing activities**

Net cash used in investing activities was $28.6 million for the nine months ended October 31, 2015, which was due to net purchases of marketable securities, purchases of IP, and purchases of software, equipment and leasehold improvements of $17.6 million, $2.8 million and $5.6 million, respectively. Purchases of intangible and tangible property were primarily to support the development and advancement of emerging technologies within our target markets. We also loaned approximately $2.7 million of cash to an entity in exchange for a number of short-term interest-bearing promissory notes in connection with an acquisition that was consummated in our fourth fiscal quarter. Refer to Note 14 for details on the aforementioned event.

Net cash used in investing activities of $28.6 million for the nine months ended October 31, 2015 represents a $31.6 million decrease from the amount of cash provided by investing activities during the corresponding period in fiscal 2015. The decrease was primarily due to the purchases of marketable securities of $22.6 million during the nine months ended October 31, 2015 as compared to $3.1 million of purchases in the corresponding period in the prior fiscal year. Additionally, we received proceeds from the sale and maturities of marketable securities of $13.2 million during the nine months ended November 1, 2014 as compared to $5.0 million of sales or maturities during the nine months ended October 31, 2015. Increased purchases of tangible and intangible property and equipment were made in comparison to the corresponding period in fiscal 2015 resulting in a net decrease of $0.7 million. We also issued short-term interest-bearing promissory notes of $2.7 million to an entity in exchange for cash in connection with an acquisition that occurred in our fourth fiscal quarter with no similar issuances in the corresponding period in the prior fiscal year. Refer to Note 14 for details on the aforementioned event.

Our marketable securities primarily include corporate bonds, money market funds and fixed income mutual funds. We monitor all of our marketable securities for impairment and if these securities are reported to have had a decline in fair value, we may need to use significant judgment to identify events or circumstances that would likely have a significant adverse effect on the future value of each investment including: (i) the nature of the investment; (ii) the cause and duration of any impairment; (iii) the financial condition and near term prospects of the issuer; (iv) for securities with a reported decline in fair value, our ability to hold the security for a period of time sufficient to allow for any anticipated recovery of fair value; (v) the extent to which fair value may differ from cost; and (vi) a comparison of the income generated by the securities compared to alternative investments. We would recognize an impairment charge if a decline in the fair value of our marketable securities is judged to be other-than-temporary.

**Cash flows from financing activities**

Net cash provided by financing activities was $2.7 million for the nine months ended October 31, 2015, which was due to the net proceeds from the exercise of employee stock options and stock purchase rights. The increase of $1.4 million from the corresponding period in fiscal 2015 was primarily the result of higher exercise activity related to stock options in the current period.

**Off-Balance Sheet Arrangements**

As of October 31, 2015, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

**Contractual obligations and commitments**

We generally do not have guaranteed price or quantity commitments from any of our suppliers. Additionally, we generally acquire products for sale to our customers based on purchase orders received as well as forecasts from such customers. Purchase orders with delivery dates greater than twelve weeks are typically cancelable without penalty to our customers. We currently place non-cancelable orders to purchase semiconductor wafers, other materials and finished goods from our suppliers on an eight to twelve week lead-time basis.

The following table sets forth the amounts of payments due under specified contractual obligations as of October 31, 2015 (in thousands):

| | **Payments due by Period** | | | | |
|---|---|---|---|---|---|
| | **Fiscal 2016 (Remaining 3 months)** | **Fiscal 2017 - 2018** | **Fiscal 2019 - 2020** | **Thereafter** | **Total** |
| Operating leases | $1,085 | $7,296 | $1,688 | $ 1,149 | $11,218 |
| Design tools | 3,032 | 2,819 | - | - | 5,851 |
| Non-cancelable purchase obligations | 28,171 | - | - | - | 28,171 |
| **Total contractual obligations** | $32,288 | $10,115 | $1,688 | $ 1,149 | $45,240 |

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

There has been no significant change in our exposure to market risk since January 31, 2015.

The following discussion about our market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We face exposure to market risk from adverse movements in interest rates and foreign currency exchange rates, which could impact our operations and financial condition. In the past, to mitigate some of the foreign currency exchange rate risk, we utilized derivative financial instruments to hedge certain foreign currency exposures. However, we discontinued this practice in fiscal 2015 as we determined the balance sheet exposure to be relatively low based on the factors described below.

***Interest rate sensitivity:*** As of October 31, 2015 and January 31, 2015, we held approximately $95.2 million and $94.1 million, respectively, of cash, cash equivalents and short-term and long-term marketable securities. If short-term interest rates were to decrease 10%, the decreased interest income associated with these cash, cash equivalents and marketable securities would not have a significant impact on our net income (loss) and cash flows.

***Foreign currency exchange rate sensitivity:*** We transact our revenue in U.S. dollars. The U.S. dollar is our reporting currency. The U.S. dollar is our functional currency except for our subsidiaries in China, Denmark, France, Japan, Taiwan, Korea and Vietnam where the Chinese Yuan, Danish Krone, Euro, Japanese Yen, Taiwanese Dollar, Korean Won and Vietnamese Dong are the functional currencies, respectively. Additionally, significant portions of our Israel subsidiary's expenses are payroll related and are denominated in Israeli Shekels. This foreign currency exposure gives rise to market risk associated with exchange rate movements of the U.S. Dollar against the Israeli Shekel. To the extent the U.S. dollar weakens against the Israeli Shekel, our Israeli subsidiary will experience a negative impact on its results of operations.

As of October 31, 2015, we did not have any foreign exchange forward contracts to hedge certain balance sheet exposures and inter-company balances against future movements in foreign exchange rates.

We maintain certain cash balances denominated in the Chinese Yuan, Danish Krone, Euro, Japanese Yen, Hong Kong Dollar, Israeli Shekel, Singapore Dollar, Taiwanese Dollar, Korean Won and Vietnamese Dong. If foreign exchange rates were to weaken against the U.S. Dollar immediately and uniformly by 10% from the exchange rates at October 31, 2015 and January 31, 2015, the fair value of these foreign currency amounts would decline and we would record a charge of approximately $0.5 million and $0.8 million, respectively.

## ITEM 4. CONTROLS AND PROCEDURES

### Evaluation of Disclosure Controls and Procedures

We are committed to maintaining disclosure controls and procedures designed to ensure that information required to be disclosed in our periodic reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and we necessarily are required to apply our judgment in evaluating the cost-benefit relationship of possible controls and procedures and implementing controls and procedures.

As of October 31, 2015, the end of the period covered by this Annual Report on Form 10-Q, we have, with the participation of our Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and effectiveness of our disclosure controls and procedures, as such terms are defined in Rule 13a-15(e) and Rule 15d-15(e) under the Securities and Exchange Act of 1934 as amended (the "Exchange Act"). Based on this evaluation, we have concluded that our disclosure controls and procedures were effective as of October 31, 2015.

### Changes in Internal Control Over Financial Reporting

There has been no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during the three months ended October 31, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

For a discussion of legal proceedings, see Note 9, “Commitments and contingencies,” in the Notes to condensed consolidated financial statements, included in Part I, Item 1, of this Form 10-Q.

### ITEM 1A. RISK FACTORS

There has been no material changes in the risk factors previously disclosed in “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended January 31, 2015.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

### ITEM 4. MINE SAFETY DISCLOSURES

None.

### ITEM 5. OTHER INFORMATION

None.

**ITEM 6. EXHIBITS**

(a) Exhibits

The following exhibits are filed herewith:

| | |
|---|---|
| 2.1** | Agreement and Plan of Merger dated November 4, 2015 by and between Sigma Designs, Inc., a California corporation, Torrey Acquisition Corp., a Delaware corporation and wholly owned subsidiary of Sigma Designs, Inc., Bretelon, Inc., a Delaware corporation, and Fortis Advisory, LLC, a Delaware limited liability corporation, as Stockholder Representative. Incorporated by reference to exhibit 2.1 filed with the Current Report on Form 8-K on November10, 2015. |
| 10.1* | Sigma Designs 2015 Employee Stock Purchase Plan. Incorporated by reference to exhibit 10.1 filed with the Current Report on Form 8-K on August 24, 2015. |
| 10.2* | Sigma Designs 2015 Stock Incentive Plan. Incorporated by reference to exhibit 10.2 filed with the Current Report on Form 8-K on August 24, 2015. |
| 10.3* | Forms of Awards under Sigma Designs 2015 Stock Incentive Plan. Incorporated by reference to exhibit 10.2 filed with the Current Report on Form 8-K on August 24, 2015. |
| 31.1 | Certification of the President and Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of the Chief Financial Officer and Secretary pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certificate of President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1) |
| 32.2 | Certificate of Chief Financial Officer and Secretary pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1) |
| 101.INS | XBRL Instance Document. |
| 101.SCH | XBRL Taxonomy Extension Schema Document. |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document. |

101.DEF XBRL Taxonomy Extension Definition Linkbase Document.

101.LAB XBRL Taxonomy Extension Label Linkbase Document.

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.

* Indicates management contract or compensatory plan or arrangement.

** Sigma Designs, Inc. hereby undertakes to furnish supplementally a copy of any omitted schedule or exhibit to such agreement to the U.S. Securities and Exchange Commission upon request.

(1) The certificates contained in Exhibits 32.1 and 32.2 are not deemed “filed” for purposes of Section 18 of the Securities and Exchange Act of 1934 and are not to be incorporated by reference into any filing of the registrant under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof irrespective of any general incorporation by reference language contained in any such filing, except to the extent that the registration specifically incorporates it by reference.

**SIGNATURES**

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

| | |
|---|---|
| | SIGMA DESIGNS, INC. |
| Date: December 9, 2015 | |
| | By: /s/ Thinh Q. Tran |
| | Thinh Q. Tran |
| | *President and Chief Executive Officer* |
| | *(Principal Executive Officer)* |
| | By: /s/ Elias N. Nader |
| | Elias N. Nader |
| | *Chief Financial Officer and Secretary* |
| | *(Principal Financial and Accounting Officer)* |

**EXHIBIT INDEX**

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