

DSP GROUP INC /DE/
Form 10-K
March 16, 2015

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the Fiscal Year Ended December 31, 2014

Commission File Number 001-35256

DSP GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware

94-2683643

(State or other jurisdiction of
incorporation and organization) (I.R.S. Employer Identification No.)

161 S. San Antonio Road, Suite 10, Los Altos, CA 94022

(Address of principal executive offices, including zip code)

(408) 986-4300

(Registrant's telephone number)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, \$.001 per share

(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a 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 June 30, 2014, the aggregate market value of voting stock held by non-affiliates of the Registrant, based on the closing price of the Common Stock on June 30, 2014 as reported on the NASDAQ Global Select Market, was approximately \$110,662,000. Shares of Common Stock held by each officer and director and by each person who owns 5% or more of the outstanding Common Stock have been excluded from this computation in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of March 6, 2015, the Registrant had outstanding 22,292,670 shares of Common Stock.

Documents incorporated by reference: Portions of the Registrant's proxy statement to be filed pursuant to Regulation 14A within 120 days after Registrant's fiscal year end of December 31, 2014 are incorporated herein by reference into Item 5 of Part II and Items 10, 11, 12, 13 and 14 of Part III of this annual report.

INDEX**DSP GROUP, INC.**

	<u>Page No.</u>
PART I	
Item 1.	BUSINESS. 3
Item 1A.	RISK FACTORS. 12
Item 1B.	UNRESOLVED STAFF COMMENTS. 26
Item 2.	PROPERTIES. 26
Item 3.	LEGAL PROCEEDINGS. 27
Item 4.	MINE SAFETY DISCLOSURES. 27
PART II	
Item 5.	MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES. 28
Item 6.	SELECTED FINANCIAL DATA MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS. 31
Item 7.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK 32
Item 7A.	FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA. 48
Item 8.	CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE. 104
Item 9.	CONTROLS AND PROCEDURES. 104
Item 9A.	OTHER INFORMATION. 104
Item 9B.	
PART III	
Item 10.	DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE. 105
Item 11.	EXECUTIVE COMPENSATION. 105
Item 12.	SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS. 105
Item 13.	

Item 14.	CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE. PRINCIPAL ACCOUNTANT FEES AND SERVICES.	105
PART IV		
Item 15.	EXHIBITS AND FINANCIAL STATEMENT SCHEDULES. SIGNATURES	106 112

x

This report and certain information incorporated herein by reference contain forward-looking statements, which are provided under the “safe harbor” protection of the Private Securities Litigation Reform Act of 1995. All statements included or incorporated by reference in this report, other than statements that are purely historical in nature, are forward-looking statements. Forward-looking statements are generally written in the future tense and/or are preceded by words such as “will,” “may,” “should,” “could,” “expect,” “suggest,” “believe,” “anticipate,” “intend,” “plan,” or other similar words. Forward-looking statements include statements regarding:

Our belief that we are well positioned to achieve our 2015 key design and financial milestones, as well as a return to revenue growth for the full year 2015;

Our belief that sales of our DECT products will continue to represent a substantial percentage of our revenues for 2015;

Our belief that our past research and development investments in new technologies are beginning to materialize;

Our belief that the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity, the traditional cordless telephony market using fixed-line telephony is declining and will continue to decline, which will reduce our revenues derived from, and unit sales of, cordless telephony products;

Our belief that the market will remain price sensitive for 2015 for our traditional cordless telephony products and expect that price erosion and the decrease in the average selling prices of such products to continue;

Our anticipation that annual revenues generated from our new products to increase significantly in 2015 as compared to 2014, including generating revenues from products in our Mobile segment in 2015;

Our belief that commercial shipments of products incorporating our new products will continue during 2015; and

Our belief that our available cash and cash equivalents at December 31, 2014 should be sufficient to finance our operations for the foreseeable future.

This Annual Report on Form 10-K includes trademarks and registered trademarks of DSP Group. Products or service names of other companies mentioned in this Annual Report on Form 10-K may be trademarks or registered trademarks of their respective owners.

DSP Group, Inc. is referred to in this Annual Report as “DSP Group,” “we,” “us” “our” or “company.”

PART I

Item 1. BUSINESS.

Introduction

DSP Group, Inc. (NASDAQ: DSPG) is a leading global provider of wireless chipset solutions for converged communications. Delivering semiconductor system solutions with software and reference designs, DSP Group enables original equipment manufacturers (OEMs), original design manufacturers (ODMs), consumer electronics (CE) manufacturers and service providers to cost-effectively develop new revenue-generating products with fast time to market. At the forefront of semiconductor innovation and operational excellence for over two decades, DSP Group provides a broad portfolio of wireless chipsets integrating DECT (Digital Enhanced Cordless Telecommunications); CAT-iq (Cordless Advanced Technology - Internet Quality), ULE (Ultra Low Energy), Wi-Fi, video, VoIP (Voice over Internet Protocol), PSTN (Public Switched Telephone Network), HDClear™ (previously BoneTone™) noise suppression and voice quality enhancement technologies.

DSP Group enables converged voice, audio and data connectivity across diverse mobile, consumer and enterprise products - including connected multimedia terminals, mobile and wearable devices, home automation & security, cordless phones, VoIP systems and home gateways. Leveraging industry-leading experience and expertise, DSP Group partners with CE manufacturers and service providers to shape the future of converged communications at home, in the office and on the go.

We were incorporated in California in 1987 and reincorporated in Delaware in 1994. We completed our initial public offering in February 1994.

Industry Environment and Our Business

Our focus on the design of highly-integrated, mixed-signal devices that combine complex RF (radio frequency), analog and digital functions enables us to address the complex challenges of integrating various technologies, platforms and processes posed by these emerging trends in the communications industry. Our integrated circuit (IC) products are customizable, achieve high functionality and performance at reduced power consumption, especially for cordless telephony, IP telephony, as well as multimedia, mobile, wearable and home automation devices, that require very low power consumption, and can be manufactured in high volumes using cost-effective process technologies. Our systems architecture provides an open design environment for ODMs to design and market their own end products with maximum differentiation.

Our expertise and investment in software development, including Board Support Package (BSP) and drivers layer, telephony, communication stack and application layers in Real-time Operating System (RTOS) and Full Featured Operating System (FFOS) frameworks, enable our customers fast time to market with cost- and performance-optimized solutions.

In response to the growing trend towards wireless residential and business connectivity in the past few years, we developed and are offering leading wireless voice and data transmission solutions for various applications, including mobile handsets. Since 1999, we have developed and acquired various technologies, including Direct Sequence Spread Spectrum (DSSS), Frequency Hopping Spread Spectrum (FHSS), Orthogonal Frequency Digital Modulation (OFDM), Digital Narrow Band, Complementary Metal Oxide Semiconductor (CMOS), Gallium Arsenide (GaAs) technology, and Silicon Germanium (SiGe) RF chips for 900MHz, 2.4GHz and 5.8GHz Industry Scientific and Medical (ISM) bands, European DECT (1.9GHz), DECT 6.0 (1.8GHz), Korean DECT (1.7GHz), Bluetooth (2.4GHz), Wi-Fi (802.11, 2.4GHz/5GHz), BiCMOS (Bipolar CMOS) and deep sub-micron CMOS technologies.

Moreover, we have expanded our DECT solutions beyond cordless telephony to address the burgeoning Internet of Things (IoT) market via an ultra low energy version of DECT called DECT ULE, DECT ULE offers numerous technological benefits due to its licensed and interference-free, frequency bands, long range, RF robustness, propagation through multiple walls, voice and visual support, while using very low power consumption.

During the past few years, we expanded into chips and phones for office and business applications, and have quickly gained market share in this growing segment. Today, DSP Group offers comprehensive systems-on-a-chip (SoC) and solution for VoIP, home, SoHo and office IP phones. VoIP is a technology that enables users to make HD voice calls via a broadband Internet connection rather than an analog phone line.

Furthermore, with mobile devices playing an increasingly significant role in peoples' lives, in February 2013, we unveiled our revolutionary HDClear solution, a comprehensive noise suppression and voice quality enhancement product for mobile devices. There is a clear emerging market trend of mobile units incorporating technology to eliminate background noise, HDClear leverages this trend by incorporating proprietary noise cancellation algorithms, thereby dramatically improving user experience and delivering unparalleled voice quality and better voice call intelligibility. This technology will enable people to use their cell phones for conversations in virtually any environment, whether in a car, on a train or in any noisy surroundings. HDClear will also facilitate the use of speech recognition and voice commands by eliminating background noise. Our HDClear product family was developed through the acquisition of BoneTone Communications Ltd. ("BoneTone") and the addition of their innovative intelligent noise cancellation algorithms to our SoC.

Committed to advancing technology across the CE and telecommunications markets, DSP Group is actively involved in prominent industry associations, including the DECT Forum, the European Telecommunications Standards Institute and the Wi-Fi Alliance, DSP Group also participates in the 3GPP and MIPI alliance. DSP Group is also deeply involved in all stages of defining DECT CAT-iq as well as DECT ULE standards and ULE Alliance and is building full eco-systems to support these solutions. We are an active member of the Home Gateway Initiative (HGI), and support the specification activities of CableLabs, which is contributing to the evolution and implementation of CAT-iq in various markets and applications. Such involvement enables us to define standards and keep abreast of the latest innovations and requirements. We also maintain close relationships with many world-leading telecommunication service providers, thereby providing us with insight into future plans across the industry.

With our in-house innovations and acquired intellectual property, we are now able to bring additional value to our existing market verticals and address new market verticals, including markets for IoT, office phones, mobile and wearable devices and headsets, thus expanding our market opportunities.

Target Markets and DSP Group Products

In response to market trends, we are concentrating our development efforts on new products and opportunities to leverage our strong technology base and customer relationships to address evolving market opportunities and take advantage of the current market trends in our domain. In addition to our main product line that is targeted for cordless phones, new products include three main groups of products: (i) home segment products consisting of ULE ICs targeting the growing markets of IoT, smart home devices and home gateways; (ii) office segment products consisting of VoIP SoC products for Enterprise, SMB and SoHo; and (iii) mobile segment products consisting of products

targeted for mobile and wearable device markets that incorporate our HDClear technology, as well as other third party advanced voice processing, always on and sensor hub functionality.

Home Segment - Products Targeted for Cordless Telephony, Home Gateways and Home Automation (IoT) Market

Our DECT, 2.4 GHz and 5.8 GHz technologies are targeted at three broad categories of products: (a) digital cordless telephony, (b) gateways, both home gateways and fixed mobile convergence and (c) smart home & IoT applications.

As a market leader in DECT and next-generation CAT-iq cordless technology, we offer a wide range of cost-effective, highly integrated SoC solutions. Delivering high-quality audio with notably low power consumption, our field-proven chipset solutions are ideal for highly integrated digital cordless telephony, DECT-enabled gateways and home automation and security. Our chipsets provide a total integrated digital solution and include all required digital baseband, analog interface and RF functionality.

Our Home chipset solutions enable worldwide coverage, supporting all RF bands and cordless protocols, such as:

1.7GHz -1.9GHz DECT – used in Europe, U.S. (DECT6.0), Korea, Japan and Latin America;

2.4GHz – used in Japan, China, India and the U.S.; the dominant protocols for this RF band is our proprietary EDCT (Enhanced Digital Cordless Technology) and WDCT (Wireless Digital Cordless Technology) protocols; and

5.8GHz – used in the U.S., Australia and several other countries with our proprietary EDCT cordless protocol.

This chipset portfolio combines wireless communications technology with a range of telephony features, audio and voice-processing algorithms to provide the industry a low cost and small footprint solution. Enhanced with our hardware and software packages, these chipsets are highly versatile and enable the development of an array of cordless telephony solutions, DECT home gateways and smart-home applications and devices at a lower effort and faster time to market than alternative silicon offerings.

This portfolio supports cordless phones, cordless headsets, remote controls, home gateways, fixed-mobile convergence solutions and home security and automation devices.

Our home chipset solutions are available in three chipset families:

The DCE family is a highly integrated, low-power ROM-based chipset solution, delivering enhanced audio and extended range for entry-level applications. The chipset is used to develop fully integrated cordless telephone systems, digital voice recorders (DVRs), digital baby monitors, and other low-to-mid-range audio applications. Including the industry's most advanced digital cordless solutions, the DCE family maintains multi-line, multi-handset and digital answering machine capabilities, while supporting various RF protocols such as DECT (1.7GHz-1.9GHz), FHSS DECT 2.4GHz, EDCT 2.4GHz and 5.8GHz. Integration of the TeakLite™ RISC DSP core into the DE56,

DCE58 and DCE59 baseband chip enables software implementation of a variety of voice coders, and provides a flexible platform for developing a wide range of solutions. With its DSP-based architecture, the chipset enables cost-effective incorporation of the most advanced audio and telephony features.

The DCX family is a low-power, Flash and ROM-based chipset solution targeting mid-to-high-range cordless applications. Built on an open platform with powerful ARM9™ core processing capabilities, the cost-effective DCX family delivers unsurpassed telephony coverage and HD voice features. Combining state-of-the-art RF and ARM9 baseband functions in a single package with a rich set of telephony features and advanced audio-processing capabilities, the DCX provides the best cost-performance solution for mid-to-high-range DECT/DECT6.0/CAT-iq and WDCT cordless applications, home gateway applications, fixed mobile convergence applications and ULE gateways and devices. Supporting all RF bands and comprised of Flash-based chips and a full set of ROM-based products with various memory configurations, the DCX chipset family offers a total integrated solution that includes a digital baseband controller, analog interface, RF transceiver and power amplifier.

The DHX family is a low-power chipset solution for home automation and security. Equipped with audio capabilities and a powerful ARM926™ processor, it implements hibernation features to deliver advanced ULE. The ULE base utilizes existing and proven cordless SoCs, functioning as a standalone ULE over the top box (DVF99) and embedded module for home gateways (DCX81).

We achieved significant milestones in 2014 by incorporating DHX91, a DECT ULE SoC; in end customer products for home automation and security applications. Our customers' end products integrating DHX91 went through various field trials and officially launched in the market in 2014.

Office Segment - Products Targeted for the Office Market

As a leading silicon vendor for enterprise voice, we offer a comprehensive portfolio of solutions for VoIP terminals. Our DVF SoCs family is a comprehensive solution for developing affordable, scalable and green VoIP home and office products. DVF facilitates rapid introduction of embedded features into residential devices such as cordless IP and instant messaging (IM) phones. DVF enables development of low-power enterprise IP, analog terminal adapters (ATAs) and home VoIP phones that offer superb acoustic echo cancellation, high-quality HD voice, multi-line capabilities, and an enhanced user interface (UI). Built on an open platform with multi-ARM processors running on Linux OS, DVF includes IPfonePro™, an extensive SDK for IP phones and ATAs.

DVF99, the latest member of the DVF family, provides outstanding cost/performance value for mid-range to high-end IP phones. Designed specifically to meet Tier 1 requirements, DVF99 fully complements existing solutions, including DVFD818 VoIP processors for low- and mid-range applications, and the XpandR® media processor for video IP devices.

Since 2008, we have been selling products for the VoIP market while developing a new platform based on ARM9 and REAL DSP core, and the VegaFireBird and VegaOne SoC products, to the advanced IAD (Integrated Access Device) market.

During 2010, we launched a new VoIP chipset based on the VegaFireBird SoC and our RF products combining ARM9 and VoIP processing baseband functions in a single package with a rich set of telephony features targeting Corded IP phones for home and office, Analog Terminal Adaptors and Cordless IP Phones. These products support multi line and multi HD voice channels, superior audio processing capabilities including acoustic echo cancellation and superior full duplex speakerphone technologies.

In 2012, we taped-out a new VoIP SoC DVF99xx, which commercially launched in January 2013. Built with two ARM926EJ-S™ cores, this new VoIP SoC provides combined processing speed of 1.1 GHz, and is designed to support IP phone processing needs - from basic single-line IP phones to high-end multi-line gigabit Ethernet IP phones with large color display and advanced GUI. The DVF99 also integrates multiple hardware accelerators, including a hardware security engine which enables a new class of secure IP phones, an LCD controller, a 2D graphics engine, a high-speed USB 2.0 port, DDR3/DDR2 memory and minimal power consumption. This product was designed to meet the needs of the enterprise IP telephony market.

In 2013, we started commercial shipments of DVF99xx with two leading customers and continued to secure additional design wins with leading customers.

In 2014, we continued our design win momentum with DVF99xx SoC with confirmed wins from two additional tier-one VoIP OEMs. Prior design wins include products that went into production in 2014, which contributed to our VoIP revenue growth.

Products Targeted for Mobile Phones and Wearable Devices

As a result of the acquisition of BoneTone, we enhanced our product portfolio with technology of intelligent voice enhancement and noise elimination. This technology supports two solutions: HDClear and HDMobileSurround™ which are offered as part of the HDClear product line.

HDClear-based solutions offer mobile voice quality and intelligibility, while completely removing background noise. Delivering clearer voice calls made from noisy environments, HDClear also maximizes accuracy of Automatic Speech Recognition (ASR) applications in noisy environments by leveraging robust and powerful noise cancellation algorithms. HDClear more effectively isolates voice from ambient noise, thereby drastically lowering Word Error Rate (WER) and dramatically improves the user experience for speech-enabled applications like virtual assistants, voice search, speakerphone conference calls and speech-to-text on mobile and wearable devices, tablets and other consumer devices.

In 2012, we taped-out a new DBMD2, which we believe is one of the most efficient voice enhancement processors in the market. It is measured just 2.5 x 2.5mm. Offered with a 36-pin FCCSP and 0.4mm ball pitch, DBMD2 embeds a programmable 32-bit DSP, incorporates advanced connectivity options, including four TDM/I2S ports and SLIMbus, and equipped with a comprehensive software framework that enables rapid development and fast time-to-market, thereby overcoming the challenges of portable design, real estate and power consumption.

DBMD2's low power enables an always-on voice feature for mobile devices. Always-on is a low power decisive natural voice interface for mobile and wearable devices. An average user accesses his/her device tens or hundreds of times per day by physically pressing a screen or a button. A truly always-on technology enables the user to skip this step by using natural voice to access the device even while the device is in standby mode.

DBMD2 enables mobile OEMs to offload voice and audio tasks from mobile device CPUs, in addition to running HDClear to enhance ASR accuracy. OEMs can leverage DBMD2's open and flexible architecture to differentiate their products to run their own voice/audio enhancement software for pre- and post-processing.

The DBMD2 supports a rich set of voice processing features to significantly enhance voice call quality, intelligibility and speech recognition accuracy, including:

- ◆ Noise suppression for the far-end listener

- ◆ Noise reduction and speech conditioning for the near-end listener

- ◆ Acoustic Echo Cancellation (AEC)

- ◆ Flexispeech – variable speech playback for the hearing impaired

- ◆ Flexible Listening Experience (FLE) – automatic adjustment of incoming voice when the near-end listener is in a noisy environment

- ◆ Sensor hub and sensor fusion functionality

In 2014, we further enhanced our HDClear noise reduction capability, and we have added two microphone hands free AEC support. We also fully integrated DBMD2 with always-on latest android 5.0 lollipop.

Customers

We are a flexible customer-centric company that proactively partners with our broad base of CE manufacturer customers and service providers. As a reliable long-term industry supplier, We maintain a proven track record of operational excellence and successful delivery. With over 10 offices across Asia, Europe and North America, we deliver outstanding local service and support worldwide. We sell our products primarily through distributors and directly to OEMs and ODMs who incorporate our products into consumer products for the worldwide residential wireless communications market and enterprise products for the worldwide office communications market. In 2014, we continued expanding our customer base, and in some cases, increased our share of business with existing customers. Our blue-chip customer base features leading international CE manufacturers, including the world's top consumer brands, which have deployed our chipset solutions at prominent tier-one telecom operators across the globe, and include: Aprotech, ADB, AEG, Alcatel, AT&T, Arris, Atlink, Arcadyan, Askey, Audioline, Ayecom, Baycom, Belgacom, Binatone, British Telecom, Brother, CCT Tech, Cetus, China Telecom, Cisco, Comcast, Crow, Cybertan, Grandstream, Deutsche Telekom, Doro, Eclogic, Escene, France Telecom, Freebox, Giant, Gaoxinqi, Gemtek, Global China Technologies, Grandstream, Hagenuk, Huawei, Innomedia, Intelbras, Invoxia, JXE, Kaonmedia, Kocom, Korea Telecom, KPN, LG Electronics, Matsushita, Mitac, Mitrastar, Motorola, Moimstone, NEC, NTT, OnReal, Ooma, Panasonic, Philips, Pioneer, Plantronics, Sagemcom, Samsung, Sanyo, Sercomm, SGW, Skymotion, Sharp, Siemens (Gigaset), SK Telecom, Sony, Spracht, Sumitomo, Swissvoice, Swisscom, TCL, Tecom, Telecom Italia, Telefonica, Telstra, Technicolor, Telefield (RCA), Topcom, Uniden, Unihan, Urmet, Uwin, Turkcell, Turkish Telecom, Verizon, VTech, Vodafone, WNC, Xingtel, Yamaha, Yealink and ZTE.

International Sales and Operations

Export sales accounted for 97% of our total revenues for both 2014 and 2013 and 99% of our total revenues for 2012. Although most of our sales to foreign entities are denominated in United States dollars, we are subject to risks of conducting business internationally. See Note 18 of the attached Notes to Consolidated Financial Statements for the year ended December 31, 2014, for a summary of the geographic breakdown of our revenues and location of our long-lived assets.

Moreover, a portion of our expenses in Israel is paid in the Israeli currency (New Israeli Shekel (NIS)). Our primary expenses paid in NIS are employee salaries and lease payments on our Israeli facilities. As a result, an increase in the value of Israeli currency in comparison to the U.S. dollar could increase the cost of our technology development, research and development expenses and general and administrative expenses. From time to time, we use derivative instruments to minimize the effects of currency fluctuations, but our hedging positions may be partial, may not exist at all in the future or may not succeed in minimizing our foreign currency fluctuation risks.

In addition, a portion of our expenses in Europe is paid in Euro. Our primary expenses paid in Euro are employee salaries and lease and operational payments on our European facilities. As a result, an increase in the value of the Euro in comparison to the U.S. dollar also could increase the cost of our technology development, research and development expenses and general and administrative expenses.

Sales, Marketing and Distribution

We market and distribute our products through our direct sales and marketing offices, as well as through a network of distributors. Our sales and marketing team, working out of our sales offices in Hong Kong, China; Nierenberg, Germany; Los Altos, California; Tokyo, Japan; Herzlia Pituach, Israel, Edinburgh, Scotland; and Shenzhen, China; pursues business with our customers in North and South America, Europe and Asia. In territories where we do not have sales offices, we operate solely through a network of distributors and representatives. Revenues derived from sales through our Japanese distributor, Tomen Electronics, represented 20% of our total revenues for 2014, 19% for 2013 and 21% for 2012. We also derive a significant amount of revenues from a limited number of customers. Sales to VTech represented 35% of our total revenues for 2014, 36% for 2013 and 35% for 2012. Sales to Panasonic through Tomen Electronics represented 15%, 14% and 15% of our total revenues for 2014, 2013 and 2012, respectively. Sales to Uniden represented 2%, 4% and 11% of our total revenues for 2014, 2013 and 2012, respectively.

As our products are generally incorporated into consumer products sold by our OEM customers, our revenues may be affected by seasonal buying patterns of consumer products sold by our OEM customers.

Manufacturing and Design Methodology

We contract product wafer fabrication services mostly from TSMC. A majority of our integrated circuit products at this time are manufactured by TSMC. We intend to continue to use independent foundries to manufacture our products. Our reliance on independent foundries involves a number of risks, including the foundries' ability to achieve acceptable manufacturing yields at competitive costs and their allocation of sufficient capacity to us to meet our needs. While we currently believe we have adequate capacity to support our current sales levels, we may encounter capacity issues in the future. In the event of a worldwide shortage in foundry capacity, we may not be able to obtain a sufficient allocation of foundry capacity to meet our product needs. Shortage or lack of capacity at the foundries we use to manufacture our products may lead to increased operating costs and lower gross margins. In addition, such a shortage could lengthen our products' manufacturing cycle and cause a delay in the shipment of our products to our customers. Unforeseen difficulties with our independent foundries could harm our business, financial condition and results of operations.

We use independent subcontractors located in Asia, to assemble and test certain of our products. We develop detailed testing procedures and specifications for each product and require each subcontractor to use these procedures and specifications before shipping us the finished products. We test and/or assemble our products at ASE, KYEC, SPIL and Giga Solutions.

Furthermore, our digital cordless products require an external component in the finished product, which is supplied by a third party, to provide flash memory.

Competition

The principal competitive factors in the cordless telephony market include price, performance, system integration level, range, voice quality, customer support and the timing of product introductions by us and our competitors. We believe that we are competitive with respect to most of these factors. Our principal competitors in the cordless market include Lantiq (Lantiq recently signed an agreement to be acquired by Intel) and Dialog Semiconductors. Similar principal competitive factors affect the VoIP market. We also believe that we are competitive with respect to most of these factors. Our principal competitors in the VoIP market include Broadcom, Dialog Semiconductors, Lantiq, Texas Instruments and new Taiwanese IC vendors.

Similar principal competitive factors affect the Home Automation (DECT ULE) market. We also believe that we are competitive with respect to most of these factors. Our principal competitors are developers of different wireless home automation technologies, including Analog, Z-wave and Zigbee. Among those, the major competitors for digital home connectivity are Atmel, Freescale, NXP, Texas Instruments, Sigma Design and Silicon Lab.

Similar principal competitive factors affect the mobile audio noise reduction market. An additional competitive factor relating to this market is that we are a newcomer to this market and this market already has a number of dominant, well-established companies with significant existing market shares. Nonetheless, we believe that we are competitive in this market with HDClear's outstanding performance. Competitors in this market include Audience, Cirrus Logic and developers of noise cancellation software running on mobile phones such as NXP and ForteMedia.

In future periods, due to various new developments in the residential telephony, enterprise telephony, home automation and mobile markets, we intend to enter into new markets with competitors that have more established presence, and significantly greater financial, technical, manufacturing, marketing, sales and distribution resources than we do.

Furthermore, there is a growing threat from alternative technologies accelerating the decline of the fixed-line telephony market. This competition comes from mobile telephony, including emerging dual-mode mobile Wi-Fi phones, and other innovative applications, such as Skype and iChat. Given that we derive a significant amount of revenues from chipsets incorporated into fixed-line telephony products, if we are unable to develop new technologies in the face of the decline of this market, our business could be materially adversely affected.

Research and Development

We believe that timely development and introduction of new products are essential to maintain our competitive position. We currently conduct most of our product development at our facilities. At December 31, 2014, we had a staff of 195 research and development personnel, of which 138 were located in Israel. We also employ independent contractors to assist with certain product development and testing activities. We spent \$33.5 million in 2014, \$35.0 million in 2013 and \$42.5 million in 2012 on research and development activities.

Due to various new developments in the home residential market, including the rapid deployment of new communication access methods and the rise of alternative technologies in lieu of fixed-line telephony, we are expanding our current product lines and develop products and services targeted at wider markets, including office enterprise market and the intensively competitive mobile device market. We will need to continue to invest in research and development, and our research and development expenses may increase in the future, including the addition of new research and development personnel, to keep pace with new and rapidly changing trends in our industry.

Licenses, Patents and Trademarks

As of December 31, 2014, we have been granted a total of 150 patents and 94 patents are pending.

We actively pursue foreign patent protection in countries of interest to us. Our policy is to apply for patents or for other appropriate statutory protection when we develop valuable new or improved technology. The status of any patent involves complex legal and factual questions, and the breadth of claims allowed is uncertain. Accordingly, we cannot assure that any patent application filed by us will result in a patent being issued, or that our patents, and any

patents that may be issued in the future, will afford adequate protection against competitors with similar technology; nor can we provide assurance that patents issued to us will not be infringed or designed around by others. In addition, the laws of certain countries in which our products are or may be developed, manufactured or sold, including China, Hong Kong, Japan, Korea and Taiwan, may not protect our products and intellectual property rights to the same extent as the laws of the United States.

We attempt to protect our trade secrets and other proprietary information through agreements with our customers, suppliers, employees and consultants, and through other security measures. Although we intend to protect our rights vigorously, we cannot assure that these measures will be successful.

While no material claims involving patent or other intellectual property rights have been brought against us to date, we cannot provide assurance that third parties will not assert claims against us or our customers with respect to existing or future products, or that we will not need to assert claims against third parties to protect our proprietary technology. In addition, patent infringement claims are increasingly being asserted by patent holding companies (so-called patent “trolls”), which do not use technology and whose sole business is to enforce patents against companies, such as us, for monetary gain. Because such patent holding companies do not provide services or use technology, the assertion of our own patents by way of counter-claim may be ineffective. We have received claims that our products infringe upon the proprietary rights of such patent holding companies. In addition, third parties have asserted and may in the future assert intellectual property infringement claims against our customers, which we have agreed in certain circumstances to indemnify and defend against such claims. If litigation becomes necessary to determine the validity of any third party claims or to protect our proprietary technology, it could result in significant expense to us and could divert the efforts of our technical and management personnel, whether or not the claim has any merit and notwithstanding that the litigation is determined in our favor. In the event of an adverse result in any litigation, we could be required to expend significant resources to develop non-infringing technology or to obtain licenses to the technology that is the subject of the litigation. We cannot provide assurance that we would be successful in developing non-infringing technology or that any licenses would be available on commercially reasonable terms.

While our ability to compete may be affected by our ability to protect our intellectual property, we believe that because of the rapid pace of technological change in our industry, our technical expertise and ability to innovate on a timely basis and in a cost-effective manner will be more important in maintaining our competitive position than the protection of our intellectual property. In addition, we believe that due to rapid technological changes in residential telephony, computer telephony and personal computer markets, patents and trade secret protection are important but must be supported by other factors, including expanding the knowledge, ability and experience of our personnel, new product introductions and frequent product enhancements. Although we continue to implement protective measures and intend to defend our intellectual property rights vigorously, we cannot assure that these measures will be successful.

Backlog

At December 31, 2014, our backlog was approximately \$34.1 million, compared to approximately \$25.1 million and \$32.7 million at December 31, 2013 and 2012, respectively. We include in our backlog all accepted product purchase orders with respect to which a delivery schedule has been specified for product shipment within one year. Our business is characterized by short-term order and shipment schedules. Product orders in our current backlog are subject to change, sometimes on short notice, due to changes in delivery schedules or cancellation by a purchaser. Accordingly, although useful for scheduling production, backlog as of any particular date may not be a reliable measure of our sales for any future period.

Employees

At December 31, 2014, we had 312 employees, including 195 in research and development, 53 in marketing and sales and 64 in corporate, administration and manufacturing coordination. Competition for personnel in the semiconductor industry in general is intense. We believe that our future prospects will depend, in part, on our ability to continue to attract and retain highly-skilled technical, marketing and management personnel, who are in demand. In particular, there is a limited supply of RF chip designers and highly-qualified engineers with digital signal processing experience. We believe that our relations with our employees are good.

Web Site Access to Company's Reports

Our Internet Web Site address is *www.dspg.com*. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are available free of charge through our Web site as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission. We will also provide the reports in electronic or paper form free of charge upon request.

Our website and the information contained therein or connected thereto are not intended to be incorporated into this Annual Report on Form 10-K.

Item 1A. RISK FACTORS.

The following risk factors, among others, could in the future affect our actual results of operations and could cause our actual results to differ materially from those expressed in forward-looking statements made by us. These forward-looking statements are based on current expectations and we assume no obligation to update this information. Before you decide to buy, hold, or sell our common stock, you should carefully consider the risks described below, in addition to the other information contained elsewhere in this report. The following risk factors are not the only risk factors facing our company. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business. Our business, financial condition, and results of operation could be seriously harmed if any of the events underlying any of these risks or uncertainties actually occurs. In that event, the market price for our common stock could decline, and you may lose all or part of your investment.

We generate a significant amount of our total revenues from the sale of digital cordless telephony products and our business and operating results may be materially adversely affected if we do not continue to succeed in this competitive market or if sales within the overall cordless digital market continue to decrease.

Sales of our digital cordless telephony products comprised 79% of our total revenues for 2014, 85% for 2013 and 88% for 2012. Any adverse change in the digital cordless market or in our ability to compete and maintain our competitive position in that market would harm our business, financial condition and results of operations.

The digital cordless telephony market is undergoing a challenging period. With the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity, the traditional cordless telephony market using fixed-line telephony is declining and will continue to decline, which reduces our revenues derived from, and unit sales of, cordless telephony products. Moreover, macro-economic trends in the consumer electronics industry may adversely impact our future revenues.

Furthermore, the decline in fixed line telephony together with the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity will decrease sales of products using fixed-line telephony. Our business also may be affected by the outcome of the competition between cellular phone operators and fixed-line operators for the provision of residential communication. A significant majority of our revenues are currently generated from sales of chipsets used in cordless phones that are based on fixed-line telephony, and the continued decline in fixed-line telephony would reduce our revenues derived from, and unit sales of, our digital cordless telephony products.

In addition, the digital cordless telephony market is competitive and is facing pricing pressures, and we expect that competition and pricing pressures will continue. It is possible that we may one day be unable to respond to increased pricing competition for digital cordless telephony processors or other products through the introduction of new

products or reduction of manufacturing costs. This inability to compete would have a material adverse effect on our business, financial condition and results of operations. Likewise, any significant delays by us in developing, manufacturing or shipping new or enhanced products in this market also would have a material adverse effect on our business, financial condition and results of operations.

We rely significantly on revenue derived from a limited number of customers.

We expect that a limited number of customers, varying in identity from period-to-period, will account for a substantial portion of our revenues in any period. Our four largest customers – VTech, Panasonic (through Tomen), CCT Telecom and Shenzhen Guo Wei Electronics Ltd. accounted for approximately 66%, 66% and 62% of our total revenues for each of 2014, 2013 and 2012, respectively. Sales to VTech represented 35% of our total revenues for 2014, 36% for 2013 and 35% for 2012. Sales to Panasonic through our distributor represented 15% of our total revenues for 2014, 14% for 2013, and 15% for 2012. Typically, our sales are made on a purchase order basis, and most of our customers have not entered into a long-term agreement requiring it to purchase our products. Moreover, we do not typically require our customers to purchase a minimum quantity of our products, and our customers can generally reschedule the delivery date of their orders on short notice without significant penalties. A significant amount of our revenues will continue to be derived from a limited number of large customers. Furthermore, the primary customers for our products are original equipment manufacturers (OEMs) and original design manufacturers (ODMs) in the cordless digital market. This industry is highly cyclical and has been subject to significant economic downturns at various times, particularly in recent periods. These downturns are characterized by production overcapacity and reduced revenues, which at times may affect the financial stability of our customers. Therefore, the loss of one of our major customers, or reduced demand for products from, or the reduction in purchasing capability of, one of our major customers, could have a material adverse effect on our business, financial condition and results of operations.

Our future success is dependent on market acceptance of our HDClear product family targeted for the mobile device market and on market acceptance of our VoIP products, which are intensively competitive markets with dominant and established players.

Our ability to increase our revenues and offset declining revenues from our cordless product family are substantially dependent on our ability to gain market share for our HDClear and VoIP product families. Although a number of potential customers have expressed interest in our HDClear products, we have not yet started mass production and we cannot assure you that we will be successful in doing so. Moreover, we are targeting a new market with our HDClear product family, a market with dominant and established players selling to OEM customers with whom they have established relationships. We will need to win over such customers, with whom we do not have established relationships, to gain market share. If we are unable to generate revenues from our HDClear product family and gain significant market share in the mobile device market, our operating results would be adversely affected. Furthermore, our future growth is also dependent on the market acceptance of our VoIP products, a market where we also compete with existing and potential competitors, many of whom have significantly greater financial, technical, manufacturing, marketing, sales and distribution resources and management expertise than we do.

The market for mobile device components is highly competitive and we expect competition to intensify in the future.

The market for mobile device components is highly competitive and characterized by the presence of large companies with significantly greater resources than we have. Our HDClear product family relates only to the voice and audio subsystem of a mobile device and there are only a limited number of OEMs targeted for this market. Our main competitors include Audience and Cirrus Logic. We also face competition from other companies and could face competition from new market entrants. We also compete against solutions internally developed by OEMs, as well as combined third-party software and hardware systems. If we are unable to compete effectively, we may not succeed in achieving any design wins and may have to lower our pricing to gain design wins, both of which would adversely impact our operating results.

Because our products are components of end products, if OEMs do not incorporate our products into their end products or if the end products of our OEM customers do not achieve market acceptance, we may not be able to generate adequate sales of our products.

Our products are not sold directly to the end-user; rather, they are components of end products. As a result, we rely upon OEMs to incorporate our products into their end products at the design stage. Once an OEM designs a competitor's product into its end product, it becomes significantly more difficult for us to sell our products to that customer because changing suppliers involves significant cost, time, effort and risk for the customer. As a result, we may incur significant expenditures on the development of a new product without any assurance that an OEM will select our product for design into its own product and without this "design win" it becomes significantly difficult to sell our products. This is especially the case for our HDClear product family. Moreover, even after an OEM agrees to design our products into its end products, the design cycle is long and may be delayed due to factors beyond our control which may result in the end product incorporating our products not to reach the market until long after the initial "design win" with the OEM. From initial product design-in to volume production, many factors could impact the timing and/or amount of sales actually realized from the design-in. These factors include, but are not limited to, changes in the competitive position of our technology, our customers' financial stability, and our ability to ship products according to our customers' schedule. Moreover, the continued uncertainty about the sustainability of the global economic recovery and outlook may further prolong an OEM customer's decision-making process and design cycle.

Furthermore, we rely on the end products of our OEM customers that incorporate our products to achieve market acceptance. Many of our OEM customers face intense competition in their markets. If end products that incorporate our products are not accepted in the marketplace, we may not achieve adequate sales volume of our products, which would have a negative effect on our results of operations.

We rely on a primary distributor for a significant portion of our total revenues and the failure of this distributor to perform as expected would materially reduce our future sales and revenues.

In addition to direct sales, we use a network of distributors to sell our products. Particularly, revenues derived from sales through our Japanese distributor, Tomen Electronics, accounted for 20% of our total revenues for 2014, 19% for 2013 and 21% for 2012. Our future performance will depend, in part, on this distributor to continue to successfully market and sell our products. Furthermore, Tomen Electronics sells our products to a limited number of customers. One customer, Panasonic, has continually accounted for a majority of the sales through Tomen Electronics. Sales to Panasonic through Tomen Electronics generated approximately 15% of our total revenues for 2014, 14% for 2013 and 15% for 2012. The loss of Tomen Electronics as our distributor and our inability to obtain a satisfactory replacement in a timely manner would materially harm our sales and results of operations. Additionally, the loss of Panasonic and Tomen Electronics' inability to thereafter effectively market our products would also materially harm our sales.

Because our quarterly operating results may fluctuate significantly, the price of our common stock may decline.

Our quarterly results of operations may vary significantly in the future for a variety of reasons, many of which are outside our control, including the following:

fluctuations in volume and timing of product orders;

timing, rescheduling or cancellation of significant customer orders and our ability, as well as the ability of our customers, to manage inventory;

changes in demand for our products due to seasonal consumer buying patterns and other factors;

timing of new product introductions by us and by our customers or competitors;

changes in the mix of products sold by us or our competitors;

fluctuations in the level of sales by our OEM customers and other vendors of end products incorporating our products;

timing and size of expenses, including expenses to develop new products and product improvements, and expenses resulting from restructuring activities;

entry into new markets, including China, Korea and South America;

our ability to scale our operations in response to changes in demand for our existing products and services or demand for new products requested by our customers;

mergers and acquisitions by us, our competitors and our existing and potential customers; and

general economic conditions, including current economic conditions in the United States and worldwide, and the adverse effects on the semiconductor and consumer electronics industries.

Each of the above factors is difficult to forecast and could harm our business, financial condition and results of operations. Also, we sell our products to OEM customers that operate in consumer markets. As a result, our revenues are affected by seasonal buying patterns of consumer products sold by our OEM customers that incorporate our products and the market acceptance of such products supplied by our OEM customers.

Our revenues, gross margins and profitability may be materially adversely affected by the continued decline in average selling prices of our products and other factors, including increases in assembly and testing expenses, and raw material and commodity costs.

We have experienced and will continue to experience a decrease in the average selling prices of our products. Decreasing average selling prices could result in decreased revenues even if the volume of products sold increases. Decreasing average selling prices may also require us to sell our products at much lower gross margin than in the past and reduce profitability. Although we have to date been able to partially offset on an annual basis the declining average selling prices of our products through general operational efficiencies and manufacturing cost reductions by achieving a higher level of product integration and improving our yield percentages, there is no guarantee that our ongoing efforts will be successful or that they will keep pace with the anticipated, continued decline in average selling prices of our products.

Moreover, we believe there are significant pressures in the supply chain as a result principally of the uncertainty relating to the sustainability of the global economic recovery, which has negatively affected the consumer electronics industry. The pressures in the supply chain make it very difficult for us to increase or even maintain our product pricing, which further adversely affects our gross margins.

In addition to the continued decline in the average selling prices of our products, our gross profit may decrease in the future due to other factors, including the roll-out of new products in any given period and the penetration of new markets which may require us to sell products at a lower margin, our failure to introduce new engineering processes and mix of products sold.

Our gross margins also are affected by the product mix. For example, mature products have lower average gross margins than other products. Therefore, increased sales of certain products would lower our gross margins.

Furthermore, increases in the price of silicon wafers, testing costs and commodities such as gold and oil, which may result in increased production costs, mainly assembly and packaging costs, may result in a decrease in our gross margins. Moreover, our suppliers may pass the increase in raw materials and commodity costs onto us which would further reduce the gross margin of our products. In addition, as we are a fabless company, global market trends such as “over-capacity” problems so that there is a shortage of capacity to fulfill our fabrication needs also may increase our raw material costs and thus decrease our gross margin.

There are several emerging market trends that may challenge our ability to continue to grow our business.

New technological developments in the home connectivity market may adversely affect our operating results. For example, the rapid deployment of new communication access methods, including mobile, wireless broadband, cable and other connectivity, as well as the lack of growth in products using fixed-line telephony would reduce our total revenues derived from, and unit sales of, cordless fixed-line telephony products. Our ability to maintain our growth will depend on the expansion of our product lines to capitalize on the emerging access methods and on our success in developing and selling a portfolio of “system-on-a-chip” solutions targeted at wider markets, including the intensively competitive mobile devices market. We cannot assure you that we will succeed in expanding our product lines or portfolio of “system-on-a-chip” solutions, or that they would receive market acceptance.

Furthermore, there is a growing threat from alternative technologies accelerating the decline of the fixed-line telephony market. This competition comes from mobile telephony, including emerging dual-mode mobile Wi Fi phones and other innovative applications, such as Skype and iChat. Given that we derive a significant amount of revenues from chipsets incorporated into fixed-line telephony products, if we are unable to develop new technologies in the face of the decline of this market, our business could be materially adversely affected.

Our future business growth depends on the growth in demand for mobile devices with improved sound quality.

Our HDClear product family is designed to enhance the sound quality and eliminate background voices for mobile device users. OEMs and ODMs may decide that the costs of improving sound quality outweigh the benefits which could limit demand for our HDClear product family. Moreover, users may also be satisfied with existing sound quality or blame poor quality on their phone carriers. The market that we are targeting is evolving rapidly and is technologically challenging. New mobile devices with different components or software may be introduced that provide the same functionality as HDClear product family. Alternatively, wireless network technology may be improved to serve the same functionality. Our future business growth will depend on the growth of this market and our ability to adapt to technological changes, user preferences and OEM demands. Our business could be materially adversely affected if we fail to do so.

Because we have significant international operations, we may be subject to political, economic and other conditions relating to our international operations that could increase our operating expenses and disrupt our business.

Although the majority of end users of the consumer products that incorporate our products are located in the U.S., we are dependent on sales to OEM customers, located outside of the U.S., that manufacture these consumer products. Also, we depend on a network of distributors to sell our products that also are primarily located outside of the U.S. Export sales, primarily consisting of digital cordless telephony products shipped to manufacturers in Europe and Asia, including Japan and Asia Pacific, represented 97% of our total revenues for both 2014 and 2013 and 99% for 2012. Furthermore, we have material operations in Germany, Hong Kong and India and employ a number of individuals within those foreign operations. As a result, the occurrence of any negative international political, economic or geographic events, as well as our failure to mitigate the challenges in managing an organization operating in various countries, could result in significant revenue shortfalls and disrupt our workforce within our foreign operations. These shortfalls and disruptions could cause our business, financial condition and results of operations to be harmed. Some of the risks of doing business internationally include:

unexpected changes in foreign government regulatory requirements;

fluctuations in the exchange rate for the United States dollar;

import and export license requirements;

imposition of tariffs and other barriers and restrictions;

burdens of complying with a variety of foreign laws, treaties and technical standards;

uncertainty of laws and enforcement in certain countries relating to the protection of intellectual property;

difficulty in collecting accounts receivable and longer payment cycles for international customers than existing customers;

difficulty in staffing and managing foreign operations and maintaining the morale and productivity of employees within foreign operations;

multiple and possibly overlapping tax structures and potentially adverse tax consequences;

political and economic instability; and

changes in diplomatic and trade relationships.

One or more of these factors may have a material adverse effect on our future operations and consequently, on our business, financial conditions and operating results.

In order to sustain the future growth of our business, we must penetrate new markets and our new products must achieve widespread market acceptance.

In order to increase our sales volume and expand our business, we must penetrate new markets and introduce new products, especially our HDClear product family. We are exploring opportunities to expand sales of our products in China, Japan, Korea and South America. However, there are no assurances that we will gain significant market share in those competitive markets. In addition, due to the cyclical nature of manufacturing capacity issues, the increasing cost of silicon integrated circuits, the continued decline of average selling prices of chipsets and other industry-wide factors, many North American, European and Japanese OEMs are moving their manufacturing sites to Asia. This trend may cause the mix of our OEM customers to change in the future, thereby further necessitating our need to penetrate new markets. Furthermore, to sustain the future growth of our business, we need to introduce new products as sales of our older products taper off. Moreover, the penetration of new competitive markets and introduction of new products could require us to reduce the sale prices of our products or increase the cost per product and thus reducing our total gross profit in future periods. Our future growth is dependent on market acceptance and penetration of our new products, especially our HDClear product family, for which we can provide no assurances. Our revenue growth is also dependent on the successful deployment of our new VoIP and HDClear products. Our inability to penetrate the market or lack of customer acceptance of these products may harm our business and potential growth.

Because the markets in which we compete are subject to rapid changes, our products may become obsolete or unmarketable.

The markets for our products and services are characterized by rapidly changing technology, short product life cycles, evolving industry standards, changes in customer needs, demand for higher levels of integration, growing competition and new product introductions. This is especially the case for the mobile device market. Our future growth is dependent not only on the continued success of our existing products but also successful introduction of new products. Our ability to adapt to changing technology and anticipate future standards, and the rate of adoption and acceptance of those standards, will be a significant factor in maintaining or improving our competitive position and prospects for growth. If new industry standards emerge, our products or our customers' products could become unmarketable or

obsolete, and we could lose market share. We may also have to incur substantial unanticipated costs to comply with these new standards. If our product development and improvements take longer than planned, the availability of our products would be delayed. Any such delay may render our products obsolete or unmarketable, which would have a negative impact on our ability to sell our products and our results of operations.

Because of changing customer requirements and emerging industry standards, we may not be able to achieve broad market acceptance of our products. Our success is dependent, in part, on our ability to:

successfully develop, introduce and market new and enhanced products at competitive prices and in a timely manner in order to meet changing customer needs;

convince leading OEMs to select our new and enhanced products for design into their own new products;

respond effectively to new technological changes or new product announcements by others;

effectively use and offer leading technologies; and

maintain close working relationships with our key customers.

There are no assurances that we will be successful in these pursuits, that the demand for our products will continue or that our products will achieve market acceptance. Our failure to develop and introduce new products that are compatible with industry standards and that satisfy customer requirements, and the failure of our products to achieve broad market acceptance, could have a negative impact on our ability to sell our products and our results of operations.

Because we depend on independent foundries and other third party suppliers to manufacture and test all of our integrated circuit products, we are subject to additional risks that may materially disrupt our business.

All of our integrated circuit products are manufactured and tested by independent foundries and other third party suppliers. While these foundries and other third party suppliers have been able to adequately meet the demands of our increasing business, we are and will continue to be dependent upon these foundries and third party suppliers to achieve acceptable manufacturing yields, quality levels and costs, and to allocate to us a sufficient portion of their foundry, assembly and test capacity to meet our needs in a timely manner.

While we currently believe we have adequate capacity to support our current sales levels pursuant to our arrangement with our foundries and other third party suppliers, we may encounter capacity shortage issues in the future. In the event of a worldwide shortage in foundry, assembly and/or test capacity, we may not be able to obtain a sufficient allocation of such capacity to meet our product needs or we may incur additional costs to ensure specified quantities of products and services. Over-capacity at the current foundries and other third party suppliers we use, or future foundries or other third party suppliers we may use, to manufacture and test our integrated circuit products may lead to increased operating costs and lower gross margins. In addition, such a shortage could lengthen our products' manufacturing and testing cycle and cause a delay in the shipment of our products to our customers. This could ultimately lead to a loss of sales of our products, harm our reputation and competitive position, and our revenues could be materially reduced. Our business could also be harmed if our current foundries or other third party suppliers terminate their relationship with us and we are unable to obtain satisfactory replacements to fulfill customer orders on a timely basis and in a cost-effective manner. Moreover, we do not have long term capacity guarantee agreements with our foundries and with other third party suppliers.

In addition, as TSMC produces a significant portion of our integrated circuit products and ASE tests and assembles a significant portion of them, earthquakes, aftershocks or other natural disasters in Asia, or adverse changes in the political situation in Taiwan, could preclude us from obtaining an adequate supply of wafers to fill customer orders. Such events could harm our reputation, business, financial condition, and results of operations.

Our operating results are affected by general economic conditions and the highly cyclical nature of the semiconductor industry.

Notwithstanding improvements in business conditions since the global downturn in 2008 and 2009, recovery is slow and general worldwide economic conditions remain uncertain which continues to make it difficult for our customers, the end-product customers, our vendors and us to accurately forecast and plan future business activities and make reliable projections. Moreover, we operate within the semiconductor industry which experiences significant fluctuations in sales and profitability. Downturns in the semiconductor industry are characterized by diminished product demand, excess customer inventories, accelerated erosion of prices and excess production capacity. These factors could cause substantial fluctuations in our revenues and in our results of operations. If global economic and market conditions remain uncertain or deteriorate, we could experience a material adverse impact on our business and results of operations.

Because the manufacture of our products is complex, the foundries on which we depend may not achieve the necessary yields or product reliability that our business requires.

The manufacture of our products is a highly complex and precise process, requiring production in a highly controlled environment. Changes in manufacturing processes or the inadvertent use of defective or contaminated materials by a foundry could adversely affect the foundry's ability to achieve acceptable manufacturing yields and product reliability. If the foundries we currently use do not achieve the necessary yields or product reliability, our ability to fulfill our customers' needs could suffer. This could ultimately lead to a loss of sales of our products and have a negative effect on our gross margins and results of operations.

Furthermore, there are other significant risks associated with relying on these third-party foundries, including:

risks due to the fact that we have reduced control over production cost, delivery schedules and product quality;

less recourse if problems occur as the warranties on wafers or products supplied to us are limited; and

increased exposure to potential misappropriation of our intellectual property.

As we depend on independent subcontractors, located in Asia, to assemble and test our semiconductor products, we are subject to additional risks that may materially disrupt our business.

Independent subcontractors, located in Asia, assemble and test our semiconductor products. Because we rely on independent subcontractors to perform these services, we cannot directly control our product delivery schedules or quality levels. We are dependent on these subcontractors to allocate to us a sufficient portion of their capacity to meet our needs in a timely manner. Our future success also depends on the financial viability of our independent subcontractors. If the capital structures of our independent subcontractors weaken, we may experience product shortages, production delays, quality assurance problems, increased manufacturing costs, and/or supply chain disruption. All of this could ultimately lead to a loss of sales of our products, harm our reputation and competitive position, and our revenues could be materially harmed.

Moreover, the economic, market, social, and political situations in countries where some of our independent subcontractors are located are unpredictable, can be volatile, and can have a significant impact on our business because we may not be able to obtain product in a timely manner. Market and political conditions, including currency fluctuation, terrorism, political strife, war, labor disruption, and other factors, including natural or man-made disasters, adverse changes in tax laws, tariff, import or export quotas, power and water shortages, or interruption in air

transportation, in areas where our independent subcontractors are located also could have a severe negative impact on our operating capabilities.

We are subject to order and shipment uncertainties and if we are unable to accurately predict customer demand, our business may be harmed.

We typically sell products pursuant to purchase orders rather than long-term purchase commitments. Customers can generally change or defer purchase orders on short notice without incurring a significant penalty. Given current market conditions, we have less ability to accurately predict what or how many products our customers will need in the future. In addition, we have little visibility into and no control of the demand by our customer's customers – generally consumer electronics retailers. Furthermore, based on discussions with our customers, we understand that our customers also have less visibility into their product demands. A decrease in the consumer electronics retailers' demand or a build-up of their inventory, both of which are out of the control of our customers and us, may cause a cancellation, change or deferral of purchase orders on short notice by our customers. Anticipating demand is difficult because our customers and their customers face volatile pricing and unpredictable demand for their own products, and are increasingly focused on cash preservation and tighter inventory management. Based on these trends, our customers are reluctant to place orders with normal lead times, and we are seeing a shift to shorter lead-times and rush orders. However, we place orders with our suppliers based on forecasts of our customers' demand and, in some instances, may establish buffer inventories to accommodate anticipated demand. Our forecasts are based on multiple assumptions, each of which may introduce error into our estimates. If we overestimate our customers' demand or our customers overestimate their demand, we may allocate resources to manufacturing products that we may not be able to sell when we expect to, if at all. As a result, we could hold excess or obsolete inventory, which would reduce our profit margins and adversely affect our financial results. Conversely, if we underestimate our customers' demand or our customers underestimate their demand and insufficient manufacturing capacity is available, we could forego revenue opportunities and potentially lose market share and damage our customer relationships.

Furthermore, we maintain inventory, or hubbing, arrangements with certain of our customers. Pursuant to these arrangements, we deliver products to a customer or a designated third party warehouse based upon the customer's projected needs, but do not recognize product revenue unless and until the customer reports that it has removed our product from the warehouse to incorporate into its end products. Since we own inventory that is physically located in a third party's warehouse, our ability to effectively manage inventory levels may be impaired, causing our total inventory turns to decrease, which could increase expenses associated with excess and obsolete product and negatively impact our cash flow.

We are dependent on a small number of OEM customers, and our business could be harmed by the loss of any of these customers or reductions in their purchasing volumes.

We sell our products to a limited number of OEM customers directly or through a network of distributors. Moreover, many North American, European and Japanese OEMs are moving their manufacturing sites to Southeast Asia, as a result of the cyclical nature of manufacturing capacity issues and cost of silicon integrated circuits, the continued decline of average selling prices of chipsets and other industry-wide factors. In addition, OEMs located in Southeast Asia are growing and gaining competitive strength. As a result, the mix of our OEM customers may change in the future. However, we may not succeed in attracting new customers as these potential customers may have pre-existing relationships with our current or potential competitors. This trend also may promote the consolidation of OEMs located in North America, Europe and Japan with OEMs located in Southeast Asia, which may reduce the number of our potential customers and reduce the volume of chipsets the combined OEM customer may purchase from us. However, as is common in our industry, we typically do not enter into long term contracts with our customers in which they commit to purchase products from us. The loss of any of our OEM customers may have a material adverse effect on our results of operations. To attract new customers, we may be faced with intense price competition, which may affect our revenues and gross margins.

The possible emerging trend of our OEM customers outsourcing their production may cause our revenue to decline.

We believe there may be an emerging trend of our OEM customers outsourcing their production to third parties. We have invested substantial resources to build relationships with our OEM customers. However the outsourcing companies whom our OEM customers may choose to outsource production may not have prior business relationship with us or may instead have prior or ongoing relationships with our competitors. The emergence of this trend may require us to expend substantial additional resources to build relationships with these outsourcing companies, which would increase our operating expenses. Even if we do expend such resources, there are no assurances that these outsourcing companies will choose to incorporate our chipsets rather than chipsets of our competitors. Our inability to retain an OEM customer once such customer chooses to outsource production would have a material adverse effect on our future revenue.

Third party claims of infringement or other claims against us could adversely affect our ability to market our products, require us to redesign our products or seek licenses from third parties, and seriously harm our operating results and disrupt our business.

As is typical in the semiconductor industry, we and our customers have been and may from time to time be notified of claims that we may be infringing patents or intellectual property rights owned by third parties. In addition, patent infringement claims are increasingly being asserted by patent holding companies (so-called patent “trolls”), which do not use technology and whose sole business is to enforce patents against companies, such as us, for monetary gain. Because such patent holding companies do not provide services or use technology, the assertion of our own patents by way of counter-claim may be ineffective. We have received claims that our products infringe upon the proprietary rights of such patent holding companies. In addition, third parties have asserted and may in the future assert intellectual property infringement claims against our customers, which we have agreed in certain circumstances to indemnify and defend against such claims. If litigation becomes necessary to determine the validity of any third party claims, it could result in significant expense to us and could divert the efforts of our technical and management personnel, whether or not the claim has merit and notwithstanding that the litigation is determined in our favor.

If it appears necessary or desirable, we may try to obtain licenses for those patents or intellectual property rights that we are allegedly infringing. Although holders of these types of intellectual property rights commonly offer these licenses, we cannot assure you that licenses will be offered or that the terms of any offered licenses will be acceptable to us. Our failure to obtain a license for key intellectual property rights from a third party for technology used by us could cause us to incur substantial liabilities, suspend the manufacturing of products utilizing the technology or damage the relationship with our customers. Alternatively, we could be required to expend significant resources to develop non-infringing technology. We cannot assure you that we would be successful in developing non-infringing technology. The occurrence of any of these events could harm our business, financial condition or results of operations.

Because we have significant operations in Israel, we may be subject to political, economic and other conditions affecting Israel that could increase our operating expenses and disrupt our business.

Our principal research and development facilities are located in the State of Israel and, as a result, at December 31, 2014, 204 of our 312 employees were located in Israel, including 138 out of 195 of our research and development personnel. In addition, although we are incorporated in Delaware, a majority of our directors and executive officers are residents of Israel. Although substantially all of our sales currently are being made to customers outside of Israel, we are nonetheless directly influenced by the political, economic and military conditions affecting Israel. Any major hostilities involving Israel, or the interruption or curtailment of trade between Israel and its present trading partners, could significantly harm our business, operating results and financial condition.

Israel's economy has been subject to numerous destabilizing factors, including a period of rampant inflation in the early to mid-1980s, low foreign exchange reserves, fluctuations in world commodity prices, military conflicts and civil unrest. In addition, Israel and companies doing business with Israel have been the subject of an economic boycott by the Arab countries since Israel's establishment. Although they have not done so to date, these restrictive laws and policies may have an adverse impact on our operating results, financial condition or expansion of our business.

Since the establishment of the State of Israel in 1948, a state of hostility has existed, varying in degree and intensity, between Israel and the Arab countries. Although Israel has entered into various agreements with certain Arab countries and the Palestinian Authority, and various declarations have been signed in connection with efforts to resolve some of the economic and political problems in the Middle East, hostilities between Israel and some of its Arab neighbors have recently escalated and intensified. We cannot predict whether or in what manner these conflicts will be resolved. Our results of operations may be negatively affected by the obligation of key personnel to perform military service. In addition, certain of our officers and employees are currently obligated to perform annual reserve duty in the Israel Defense Forces and are subject to being called for active military duty at any time. Although we have operated effectively under these requirements since our inception, we cannot predict the effect of these obligations on the company in the future. Our operations could be disrupted by the absence, for a significant period, of one or more of our officers or key employees due to military service.

The tax benefits available to us under Israeli law require us to meet several conditions, and may be terminated or reduced in the future, which would increase our taxes.

Our facilities in Israel have been granted Approved Enterprise and Beneficiary Enterprise status under the Law for the Encouragement of Capital Investments, 1959, commonly referred to as the “Investment Law,” as amended. The Investment Law provides that capital investments in a production facility (or other eligible assets) designated as an Approved Enterprise or Beneficiary Enterprise receive certain tax benefits in Israel. Our investment programs that generate taxable income are currently subject to an average tax rate of up to approximately 10% based on a variety of factors, including percentage of foreign ownership and approvals for the erosion of the tax basis of our investment programs. To be eligible for tax benefits, we must meet certain conditions, relating principally to adherence to the investment program filed with the Investment Center of the Israeli Ministry of Economy and periodic reporting obligations. Although we believe we have met such conditions in the past, should we fail to meet such conditions in the future, we would be subject to corporate tax in Israel at the standard corporate tax rate (26.5% for 2015) and could be required to refund tax benefits (including with interest and adjustments for inflation based on the Israeli consumer price index) already received. Our average tax rate for our investment programs also may change in the future due to circumstances outside of our control, including changes to legislation. For example, in July 2013, the Investment Law was amended whereby the reduction of corporate tax rate for preferred enterprises was eliminated such that such enterprises, which are subject to the new law, would be subject to a 16% tax rate. Therefore, we cannot provide any assurances that our average tax rate for our investment programs will continue in the future at their current levels, if at all. The termination or reduction of certain programs and tax benefits or a requirement to refund tax benefits (including with interest and adjustments for inflation based on the Israeli consumer price index) already received may have a material adverse effect on our business, operating results and financial condition.

We may engage in future acquisitions that could dilute our stockholders’ equity and harm our business, results of operations and financial condition.

We have pursued, and will continue to pursue, growth opportunities through internal development and acquisition of complementary businesses, products and technologies. We are unable to predict whether or when any other prospective acquisition will be completed. The process of integrating an acquired business may be prolonged due to unforeseen difficulties and may require a disproportionate amount of our resources and management’s attention. We cannot assure you that we will be able to successfully identify suitable acquisition candidates, complete acquisitions, integrate acquired businesses into our operations, or expand into new markets. Further, once integrated, acquisitions may not achieve comparable levels of revenues, profitability or productivity as our existing business or otherwise perform as expected. The occurrence of any of these events could harm our business, financial condition or results of operations. Future acquisitions may require substantial capital resources, which may require us to seek additional debt or equity financing.

Future acquisitions by us could result in the following, any of which could seriously harm our results of operations or the price of our stock:

issuance of equity securities that would dilute our current stockholders' percentages of ownership;

large one-time write-offs;

the incurrence of debt and contingent liabilities;

difficulties in the assimilation and integration of operations, personnel, technologies, products and information systems of the acquired companies;

diversion of management's attention from other business concerns;

contractual disputes;

risks of entering geographic and business markets in which we have no or only limited prior experience; and

potential loss of key employees of acquired organizations.

We may not be able to adequately protect or enforce our intellectual property rights, which could harm our competitive position.

Our success and ability to compete is in part dependent upon our internally-developed technology and other proprietary rights, which we protect through a combination of copyright, trademark and trade secret laws, as well as through confidentiality agreements and licensing arrangements with our customers, suppliers, employees and consultants. In addition, we have filed a number of patents in the United States and in other foreign countries with respect to new or improved technology that we have developed. However, the status of any patent involves complex legal and factual questions, and the breadth of claims allowed is uncertain. Accordingly, we cannot assure you that any patent application filed by us will result in a patent being issued, or that the patents issued to us will not be infringed by others. Also, our competitors and potential competitors may develop products with similar technology or functionality as our products, or they may attempt to copy or reverse engineer aspects of our product line or to obtain and use information that we regard as proprietary. Moreover, the laws of certain countries in which our products are or may be developed, manufactured or sold, including Hong Kong, Japan, Korea and Taiwan, may not protect our products and intellectual property rights to the same extent as the laws of the United States. Policing the unauthorized use of our products is difficult and may result in significant expense to us and could divert the efforts of our technical and management personnel. Even if we spend significant resources and efforts to protect our intellectual property, we cannot assure you that we will be able to prevent misappropriation of our technology. Use by others of our proprietary rights could materially harm our business and expensive litigation may be necessary in the future to enforce our intellectual property rights.

Because our products are complex, the detection of errors in our products may be delayed, and if we deliver products with material defects, our credibility will be harmed, the sales and market acceptance of our products may decrease and product liability claims may be made against us.

Our products are complex and may contain errors, defects and bugs when introduced. If we deliver products with material errors, defects or bugs, our credibility and the market acceptance and sales of our products could be significantly harmed. Furthermore, the nature of our products may also delay the detection of any such error or defect. If our products contain material errors, defects and bugs, then we may be required to expend significant capital and resources to alleviate these problems. This could result in the diversion of technical and other resources from our other development efforts. Any actual or perceived problems or delays may also adversely affect our ability to attract or retain customers. Furthermore, the existence of any defects, errors or failures in our products could lead to product liability claims or lawsuits against us or against our customers. We generally provide our customers with a standard warranty for our products, generally lasting one year from the date of purchase. Although we attempt to limit our liability for product defects to product replacements, we may not be successful, and customers may sue us or claim liability for the defective products. A successful product liability claim could result in substantial cost and divert management's attention and resources, which would have a negative impact on our financial condition and results of operations.

We are exposed to the credit risk of our customers and to credit exposures in weakened markets, which could result in material losses.

Most of our sales are on an open credit basis. Because of current conditions in the global economy, our exposure to credit risks relating to sales on an open credit basis has increased. We expect demand for enhanced open credit terms, for example, longer payment terms, to continue and believe that such arrangements are a competitive factor in obtaining business. Although we monitor and attempt to mitigate credit risks, including through insurance coverage from time to time, there can be no assurance that our efforts will be effective. Moreover, even if we attempt to mitigate credit risks through insurance coverage, such coverage may not be sufficient to cover all of our losses and we would be subject to a deductible under any insurance coverage. As a result, our future credit risk exposure may increase. Although any losses to date relating to credit exposure of our customers have not been material, future losses, if incurred, could harm our business and have a material adverse effect on our operating results and financial condition. Moreover, the loss of a customer due to its financial default also could harm our future business and potential growth.

Our executive officers and key personnel are critical to our business, and because there is significant competition for personnel in our industry, we may not be able to attract and retain such qualified personnel.

Our success depends to a significant degree upon the continued contributions of our executive management team, and our technical, marketing, sales customer support and product development personnel. The loss of significant numbers of such personnel could significantly harm our business, financial condition and results of operations. We do not have any life insurance or other insurance covering the loss of any of our key employees. Because our products are specialized and complex, our success depends upon our ability to attract, train and retain qualified personnel, including qualified technical, marketing and sales personnel. However, the competition for personnel is intense and we may have difficulty attracting and retaining such personnel.

We may have exposure to additional tax liabilities as a result of our foreign operations.

We are subject to income taxes in the United States and various foreign jurisdictions. In addition to our significant operations in Israel and have operations in Germany, Hong Kong and India. Significant judgment is required in determining our worldwide provision for income taxes and other tax liabilities. In the ordinary course of a global business, there are many intercompany transactions and calculations where the ultimate tax determination is uncertain. We are regularly under audit by tax authorities and as an example, we are now under audit for one of our subsidiaries, the outcome of which could have material adverse impact on our financial condition. Our intercompany transfer pricing may be reviewed by the U.S. Internal Revenue Service and by foreign tax jurisdictions. Although we believe that our tax estimates are reasonable, due to the complexity of our corporate structure, the multiple intercompany transactions and the various tax regimes, we cannot assure you that a tax audit or tax dispute to which we may be subject will result in a favorable outcome for us. If taxing authorities do not accept our tax positions and impose higher tax rates on our foreign operations, our overall tax expenses could increase.

We are exposed to fluctuations in currency exchange rates.

A significant portion of our business is conducted outside the United States. Export sales to manufacturers in Europe and Asia, including Japan and Asia Pacific, represented 97% of our total revenues for 2014 and 2013 and 99% for 2012. Although most of our revenue and expenses are transacted in U.S. dollars, we may be exposed to currency exchange fluctuations in the future as business practices evolve and we are forced to transact business in local currencies. Moreover, part of our expenses in Israel are paid in Israeli currency, which subjects us to the risks of foreign currency fluctuations between the U.S. dollar and the New Israeli Shekel (NIS) and to economic pressures resulting from Israel's general rate of inflation. Our primary expenses paid in NIS are employee salaries and lease payments on our Israeli facilities. Furthermore, a portion of our expenses for our European operations are paid in the Euro, which subjects us to the risks of foreign currency fluctuations between the U.S. dollar and the Euro. Our primary expenses paid in the Euro are employee salaries, lease and operational payments on our European facilities. As a result, an increase in the value of the NIS and Euro in comparison to the U.S. dollar could increase the cost of our

technology development, research and development expenses and general and administrative expenses, all of which could harm our operating profit. From time to time, we use derivative instruments in order to minimize the effects of currency fluctuations, but our hedging positions may be partial, may not exist at all in the future or may not succeed in minimizing our foreign currency fluctuation risks. Our financial results may be harmed if the trend relating to the devaluation of the U.S. dollars continues for an extended period.

Because the markets in which we compete are highly competitive, and many of our competitors have greater resources than we do, we cannot be certain that our products will be accepted in the marketplace or capture market share.

The markets in which we operate are extremely competitive and characterized by rapid technological change, evolving standards, short product life cycles and price erosion. We expect competition to intensify as current competitors expand their product offerings and new competitors enter the market. Given the highly competitive environment in which we operate, we cannot be sure that any competitive advantages enjoyed by our current products would be sufficient to establish and sustain our new products in the market. Any increase in price or competition could result in the erosion of our market share, to the extent we have obtained market share, and would have a negative impact on our financial condition and results of operations.

In each of our business activities, we face current and potential competition from competitors that have significantly greater financial, technical, manufacturing, marketing, sales and distribution resources and management expertise than we do. These competitors may also have pre-existing relationships with our customers or potential customers. Further, in the event of a manufacturing capacity shortage, these competitors may be able to manufacture products when we are unable to do so. Our principal competitors in the cordless market include Lantiq and Dialog Semiconductors. Our principal competitors in the VoIP market include Broadcom, Dialog Semiconductors, Infineon, Texas Instruments and new Taiwanese IC vendors.

As discussed above, various new developments in the home residential market may require us to enter into new markets with competitors that have more established presence, and significantly greater financial, technical, manufacturing, marketing, sales and distribution resources and management expertise than we do. The expenditure of greater resources to expand our current product lines and develop a portfolio of “system-on-a-chip” solutions that integrate video, voice, data and communication technologies in a wider multimedia market may increase our operating expenses and reduce our gross profit. We cannot assure you that we will succeed in developing and introducing new products that are responsive to market demands.

An unfavorable government review of our federal income tax returns or changes in our effective tax rates could adversely affect our operating results.

Our future effective tax rates could be adversely affected by earnings being lower than anticipated in countries where we have lower statutory rates and higher than anticipated in countries where we have higher statutory rates, by changes in the valuation of our deferred tax assets and liabilities, or by changes in tax laws, regulations, accounting principles or interpretations thereof. In addition, we are subject to the periodic examination of our income tax returns by the IRS and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes, as an example, we are now under audit for one of our subsidiaries. The outcome from this examination may have an adverse effect on our operating results and financial condition.

Our business operations would be disrupted if the information technology systems we rely on fail to function properly.

We rely on complex information technology systems to manage our business which operates in many geographical locations. For example, to achieve short delivery lead times and superior levels of customer service while maintaining low levels of inventory, we constantly adjust our production schedules with manufacturers and subcontractors. We develop and adjust these schedules based on end customer demand as communicated by our customers and distributors and based on our inventory levels, manufacturing cycle times, component lead times, and projected production yields. We combine and distribute all of this information electronically over a complex global communications network. Our ability to estimate demand and to adjust our production schedules is highly dependent

on this network. Any delay in the implementation of, or disruption in the transition to, new or enhanced processes, systems or controls, could adversely affect our ability to manage customer orders and manufacturing schedules, as well as generate accurate financial and management information in a timely manner. These systems are also susceptible to power and telecommunication disruptions and other system failures. Failure of our IT systems or difficulties in managing them could result in business disruption. Our business could be significantly disrupted and we could be subject to third party claims associated with such disruptions.

We may experience difficulties in transitioning to smaller geometry process technologies or in achieving higher levels of design integration, which may result in reduced manufacturing yields, delays in product deliveries and increased expenses.

A growing trend in our industry is the integration of greater semiconductor content into a single chip to achieve higher levels of functionality. In order to remain competitive, we must achieve higher levels of design integration and deliver new integrated products on a timely basis. This will require us to expend greater research and development resources, and may require us to modify the manufacturing processes for some of our products, to achieve greater integration. We periodically evaluate the benefits, on a product-by-product basis, of migrating to smaller geometry process technologies to reduce our costs. Although this migration to smaller geometry process technologies has helped us to offset the declining average selling prices of our products, this effort may not continue to be successful. Also, because we are a fabless semiconductor company, we depend on our foundries to transition to smaller geometry processes successfully. We cannot assure you that our foundries will be able to effectively manage the transition. In case our foundries or we experience significant delays in this transition or fail to efficiently implement this transition, our business, financial condition and results of operations could be materially and adversely affected.

The anti-takeover provisions in our certificate of incorporation and bylaws could prevent or discourage a third party from acquiring us.

Our certificate of incorporation and bylaws contain provisions that may prevent or discourage a third party from acquiring us, even if the acquisition would be beneficial to our stockholders. Our board of directors also has the authority to fix the rights and preferences of shares of our preferred stock and to issue such shares without a stockholder vote. Our bylaws also place limitations on the authority to call a special meeting of stockholders. Our stockholders may take action only at a meeting of stockholders and not by written consent. We have advance notice procedures for stockholders desiring to nominate candidates for election as directors or to bring matters before an annual meeting of stockholders. In addition, these factors may also adversely affect the market price of our common stock, and the voting and other rights of the holders of our common stock.

Our stock price may be volatile so you may not be able to resell your shares of our common stock at or above the price you paid for them.

Announcements of developments related to our business, announcements by competitors, quarterly fluctuations in our financial results, changes in the general conditions of the highly dynamic industry in which we compete or the national economies in which we do business, and other factors could cause the price of our common stock to fluctuate, perhaps substantially. In addition, in recent years, the stock market has experienced extreme price fluctuations, which have often been unrelated to the operating performance of affected companies. These factors and fluctuations could have a material adverse effect on the market price of our common stock.

Item 1B. UNRESOLVED STAFF COMMENTS.

None.

Item 2. PROPERTIES.

Our principal offices in the United States are located in Los Altos, California, where we lease approximately 700 square feet under a lease that expires in January 2016. Portions of our U.S. operations are located in leased facilities in El Dorado Hills, California under a lease that expires in March 2015 and we do not currently intend to extend this lease. Our operations in Israel are located in leased facilities, with the primary leased facility of approximately 45,359 square feet located in Herzeliya Pituach, Israel. These facilities are leased through November 2018. Our subsidiary in Tokyo, Japan has a lease that terminates in December 2017. Our subsidiary in Nuremberg, Germany has a lease that terminates in December 2016. Our subsidiary in Scotland has 2 lease agreements for its facilities, one with automatic renewals on a month-to-month basis and another that terminates in December 2019. Our subsidiary in India has

sublease agreements with NXP for its facilities that terminate in March 2017. Our subsidiary in Shenzhen, China has a lease that terminates in September 2016. Our subsidiary in Hong Kong entered into a lease agreement that is effective until November 2016. We believe that our existing facilities are adequate to meet our needs for the immediate future.

Item 3. LEGAL PROCEEDINGS.

From time to time, we may become involved in litigation relating to claims arising from our ordinary course of business activities. Also, as is typical in the semiconductor industry, we have been and may from time to time be notified of claims that we may be infringing patents or intellectual property rights owned by third parties. We currently believe that there are no claims or actions pending or threatened against us, the ultimate disposition of which would have a material adverse effect on us.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II**Item MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND
5. ISSUER PURCHASES OF EQUITY SECURITIES.**

Our common stock, par value \$0.001, trades on the NASDAQ Global Select Market (NASDAQ symbol "DSPG"). The following table presents for the periods indicated the high and low sales prices for our common stock as reported by the NASDAQ Global Select Market:

Year Ended	High	Low
December 31, 2013		
First Quarter	8.33	5.63
Second Quarter	8.76	6.95
Third Quarter	8.75	6.3
Fourth Quarter	10.14	6.78

Year Ended	High	Low
December 31, 2014		
First Quarter	10.32	8.31
Second Quarter	9.21	7.90
Third Quarter	9.48	8.30
Fourth Quarter	11.48	8.83

As of March 6, 2015, there were 22,292,670 shares of common stock outstanding. As of March 10, 2015, the company had approximately 30 holders of record and we believe greater than 2,100 beneficial holders. We have never paid cash dividends on our common stock and presently intend to continue a policy of retaining any earnings for reinvestment in our business.

Equity Compensation Plan Information

Information relating to our equity compensation plans will be presented under the caption “Equity Compensation Plan Information” of our definitive proxy statement pursuant to Regulation 14A in connection with the annual meeting of stockholders to be held on June 8, 2015. The definitive proxy statement will be filed with the Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this report. Such information is incorporated herein by reference.

Issuer Purchases of Equity Securities

There were no repurchases of our common stock pursuant to our board authorized share repurchase program during the fourth quarter of 2014.

In November 2013, our board of directors authorized the company's entry into a share repurchase plan, in accordance with Rule 10b5-1 of the Securities Exchange Act of 1934, for the repurchase of up to 2,700,000 shares of our common stock. This authorization is in addition to the approximately 308,000 shares that were available for repurchase under the Board's prior authorizations.

At December 31, 2014, 1,203,601 shares of our common stock remained available for repurchase under our board authorized share repurchase program. The repurchase program is being affected from time to time, depending on market conditions and other factors, through open market purchases and privately negotiated transactions.

Information relating to our equity compensation plans will be presented under the caption "Equity Compensation Plan Information" of our definitive proxy statement pursuant to Regulation 14A in connection with the annual meeting of stockholders to be held on June 8, 2015. The definitive proxy statement will be filed with the Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this report. Such information is incorporated herein by reference.

Stock Performance Graph

Notwithstanding anything to the contrary set forth in any of the Company's previous or future filings under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, that might incorporate this proxy statement or future filings made by the Company under those statutes, the Stock Performance Graph shall not be deemed filed with the United States Securities and Exchange Commission and shall not be deemed incorporated by reference into any of those prior filings or into any future filings made by the Company under those statutes.

The graph below compares the cumulative total stockholder return on our common stock with the cumulative total return on the Standard & Poor's 500 Index and Standard & Poor's Information Technology Index. The period shown commences on December 31, 2009 and ends on December 31, 2014, the end of our last fiscal year. The graph assumes an investment of \$100 on December 31, 2009, and the reinvestment of any dividends.

Comparisons in the graph above are based upon historical data and are not indicative of, nor intended to forecast, future performance of our common stock.

Item 6. SELECTED FINANCIAL DATA.

The selected historical consolidated financial data presented below is derived from our consolidated financial statements. The selected consolidated financial data set forth below is qualified in its entirety by, and should be read in conjunction with, our consolidated financial statements for the year ended December 31, 2014, and the discussion of our business, operations and financial results in the section captioned, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Year Ended December 31,

	2014	2013	2012	2011	2010
	(U.S. dollars in thousands)				
Statements of Operations Data:					
Revenues	\$ 143,036	\$ 151,063	\$ 162,790	\$ 193,861	\$ 225,482
Cost of revenues	85,992	91,237	101,660	123,734	137,571
Gross profit	57,044	59,826	61,130	70,127	87,911
Operating expenses					
Research and development, net	33,468	35,000	42,539	53,244	55,588
General, administrative, sales and marketing	22,446	23,085	24,875	29,417	31,561
Amortization of intangible assets	1,573	1,672	2,310	7,972	9,975
Restructuring cost (income)	-	-	2,008	(170)	463
Total operating expenses	57,487	59,757	71,732	90,463	97,587
Operating income (loss)	(443)	69	(10,602)	(20,336)	(9,676)
Financial and other income					
Financial income, net	1,204	2,457	2,388	1,885	1,468
Other income from remeasurement of investment in a business Combination	-	-	-	1,343	-
Income (loss) before taxes	761	2,526	(8,214)	(17,108)	(8,208)
Income tax benefit	(2,841)	(150)	(172)	(866)	(783)
Net income (loss)	\$ 3,602	\$ 2,676	\$ (8,042)	\$ (16,242)	\$ (7,425)
Weighted average number of Common Stock outstanding during the period used to compute basic net earnings (loss) per share	21,968				