DSP GROUP INC /DE/
Form 10-Q
May 11, 2018

United States
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2018

or

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

For the transition period from ______ to

Commission File Number 1-35256

DSP GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-2683643**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number)
5 Shenkar Street, Herzelia 4672505 Israel	**94022**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: **(408) 986-4300**

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

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

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

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period of complying with any new or revised financial accounting standards provided pursuant to section 13(a) of the Exchange Act.

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 May 2, 2018, there were 22,676,065 shares of Common Stock ($.001 par value per share) outstanding.

INDEX

DSP GROUP, INC.

PART 1. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DSP GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(U.S. dollars in thousands, except share and per share data)

	March 31, 2018 Unaudited	**December 31, 2017 Audited**
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 15,635	$ 21,324
Restricted deposit	527	524
Marketable securities and short-term deposits	30,961	24,697
Trade receivables	15,910	13,416
Other accounts receivable and prepaid expenses	3,168	3,167
Inventories	8,414	9,422
TOTAL CURRENT ASSETS	74,615	72,550
PROPERTY AND EQUIPMENT, NET	2,991	3,184
NON-CURRENT ASSETS:		
Long-term marketable securities	76,446	82,669
Long-term prepaid expenses and lease deposits	1,574	1,541
Deferred income taxes	1,041	1,043
Severance pay fund	15,136	15,190
Intangible assets, net	2,354	2,779
Goodwill	6,243	6,243
TOTAL NON-CURRENT ASSETS	102,794	109,465

TOTAL ASSETS	$ 180,400	$ 185,199

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(U.S. dollars in thousands, except share and per share data)

	March 31, 2018 Unaudited	**December 31, 2017 Audited**
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Trade payables	$ 7,651	$ 8,660
Accrued compensation and benefits	6,720	8,699
Income tax accruals and payables	1,071	1,232
Accrued expenses and other accounts payable	2,190	2,888
TOTAL CURRENT LIABILITIES	17,632	21,479
NON-CURRENT LIABILITIES:		
Deferred income taxes	332	424
Accrued severance pay	15,274	15,463
Accrued pensions	912	883
TOTAL NON-CURRENT LIABILITIES	16,518	16,770
STOCKHOLDERS' EQUITY:		
Capital stock:		
Common stock, $ 0.001 par value - Authorized shares: 50,000,000 shares at March 31, 2018 and December 31, 2017; Issued and outstanding shares: 22,729,085 and 22,432,660 shares at March 31, 2018 and December 31, 2017, respectively	23	22
Additional paid-in capital	373,740	372,041
Treasury stock at cost	(115,731)	(118,397)
Accumulated other comprehensive loss	(2,517)	(1,874)
Accumulated deficit	(109,265)	(104,842)
TOTAL STOCKHOLDERS' EQUITY	146,250	146,950
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 180,400	$ 185,199

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(U.S. dollars in thousands, except per share amounts)

	Three months ended March 31,	
	2018	**2017**
Revenues	$28,111	$27,933
Cost of revenues (1)	14,397	15,686
Gross profit	13,714	12,247
Operating expenses:		
Research and development, net (2)	8,998	9,190
Sales and marketing (3)	4,068	3,575
General and administrative (4)	2,581	2,487
Intangible assets amortization	425	425
Total operating expenses	16,072	15,677
Operating loss	(2,358)	(3,430)
Financial income, net	396	416
Loss before taxes on income	(1,962)	(3,014)
Income tax benefit	209	148
Net loss	$(1,753)	$(2,866)
Net loss per share:		
Basic	$(0.08)	$(0.13)
Diluted	$(0.08)	$(0.13)
Weighted average number of shares used in per share computations of net earnings		
Basic	22,678	22,102
Diluted	22,678	22,102

(1) Includes equity-based compensation expense in the amount of $98 and $97 for the three months ended March 31, 2018 and 2017, respectively.

(2) Includes equity-based compensation expense in the amount of $652 and $616 for the three months ended March 31, 2018 and 2017, respectively.

(3)

Includes equity-based compensation expense in the amount of $406 and $300 for the three months ended March 31, 2018 and 2017, respectively.

(4) Includes equity-based compensation expense in the amount of $543 and $518 for the three months ended March 31, 2018 and 2017, respectively.

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

DSP GROUP, INC.

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

(U.S. dollars in thousands)

	Three months ended March 31, 2018	2017
Net loss:	$(1,753)	$(2,866)
Other comprehensive income (loss):		
Available-for-sale securities:		
Changes in unrealized gains/losses	(662)	204
Reclassification adjustments for (gains) losses included in net loss	(2)	47
Net change	(664)	251
Cash flow hedges:		
Changes in unrealized gains/losses	-	143
Reclassification adjustments for (gains) losses included in net loss	-	(75)
Net change	-	68
Change in unrealized components of defined benefit plans:		
Amortization of actuarial loss and prior service benefit	5	5
Net change	5	5
Foreign currency translation adjustments, net	16	(9)
Other comprehensive income	(643)	315
Comprehensive loss	$(2,396)	$(2,551)

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(U.S. dollars in thousands)

	Three months ended March 31,	
	2018	**2017**
Net cash used in operating activities	$(3,372)	$(4,118)
Investing activities		
Purchases of marketable securities	(3,277)	(3,297)
Proceeds from maturity of marketable securities	1,855	4,779
Proceeds from sales of marketable securities	500	3,089
Purchases of property and equipment	(250)	(387)
Other investing activities	(104)	-
Net cash provided by investing activities	(1,276)	4,184
Financial activities		
Purchase of treasury stock	(1,211)	(1,313)
Issuance of common stock and treasury stock upon exercise of stock options	155	647
Net cash used in financing activities	(1,056)	(666)
Decrease in cash and cash equivalents	(5,704)	(600)
Erosion due to exchange rate differences	18	(1)
Cash and cash equivalents at the beginning of the period	21,848	17,822
Cash and cash equivalents at the end of the period	$16,162	$17,221

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(UNAUDITED)

(U.S. dollars in thousands)

Three months ended March 31, 2017	**Number of common stock**	**Common stock**	**Additional paid-In capital**	**Treasury stock**	**Accumulated deficit**	**Accumulated other comprehensive income (loss)**	**Total stockholders' equity**
Balance at December 31, 2016	21,931	$ 22	$ 366,121	$ (122,632)	$ (96,112)	$ (1,852)	$ 145,547
Net loss	-	-	-	-	(2,866)	-	(2,866)
Change in accumulated other comprehensive income	-	-	-	-	-	315	315
Purchase of treasury stock	(124)	*)-	-	(1,313)	-	-	(1,313)
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	113	*)-	-	1,110	(168)	-	942
Issuance of treasury stock upon exercise of stock options, stock appreciation rights and vesting of restricted stock units by employees and directors	249	*)-	-	2,431	(2,130)		301
Equity-based compensation	-	-	1,531	-	-	-	1,531
Balance at March 31, 2017	**22,169**	**$ 22**	**$ 367,652**	**$ (120,404)**	**$ (101,276)**	**$ (1,537)**	**$ 144,457**
Three Months Ended March 31, 2018							
Balance at December 31, 2017	22,433	$ 22	$ 372,041	$ (118,397)	$ (104,842)	$ (1,874)	$ 146,950
Net loss	-	-	-	-	(1,753)	-	(1,753)
Cumulative effect adjustment on retained earnings **)	-	-	-	-	94	-	94
Change in accumulated other comprehensive income	-	-	-	-	-	(643)	(643)
Purchase of treasury stock	(102)	*)-	-	(1,255)	-	-	(1,255)
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	119	*)-	-	1,169	(166)	-	1,003

Issuance of treasury stock upon exercise of stock options, stock appreciation rights and vesting of restricted stock units by employees and directors	279	1	-	2,752	(2,598)		155
Equity-based compensation	-	-	1,699	-	-	-	1,699
Balance at March 31, 2018	**22,729**	**$ 23**	**$ 373,740**	**$ (115,731)**	**$ (109,265)**	**$ (2,517)**	**$ 146,250**

(*) Represents an amount lower than $1.

(**) Resulting from adoption of ASC 606.

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

DSP GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2017

(UNAUDITED)

(U.S. dollars in thousands, except share and per share data)

NOTE A—BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. For further information, reference is made to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K of DSP Group, Inc. (the "Company") for the year ended December 31, 2017.

The significant accounting policies applied in the annual consolidated financial statements of the Company as of December 31, 2017, contained in the Company’s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 16, 2018, have been applied consistently in these unaudited interim condensed consolidated financial statements, except as noted below:

Recently Adopted Accounting Pronouncements.

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) 2014-09, “Revenue from Contracts with Customers (Topic 606)” (“ASU 2014-09”), which amends the existing accounting standards for revenue recognition. On January 1, 2018, the Company adopted Accounting Standards Codification (“ASC”) 606, “Revenue from Contracts with Customers” and all the related amendments (collectively “ASC 606”) using the modified retrospective method. The Company recognized the cumulative effect of initially applying ASC 606 as an adjustment to the opening balance of retained earnings. The comparative information has not been restated and continues to be reported under the revenue recognition standards in effect for those periods. The Company’s reported results for 2018 reflect the application of ASC 606 guidance while the reported results for 2017 were prepared under the guidance of ASC 605, "Revenue Recognition (ASC 605)". The impact of the Company’s adoption of Topic 606 on its balance sheet was an increase in accumulated deficit as of March 31, 2018 of $94.

Under ASC 606, certain product sales through the Company’s distributors where revenue was previously deferred until the distributors resell the Company’s products to the end customers are now recognized when products are delivered to the distributor. Revenues are recognized when control of the promised goods or services are transferred to the Company’s customers, in an amount that reflects the consideration that the Company expects to receive in exchange for those goods or services.

The Company determines revenue recognition through the following steps:

identification of the contract with a customer;

identification of the performance obligations in the contract;

determination of the transaction price;

allocation of the transaction price to the performance obligations in the contract; and recognition of revenue when, or as, the Company satisfies a performance obligation.

The Company's contracts with customers for the sale of products generally include one performance obligation. The Company has concluded that revenue from sale of products should be recognized at the point in time when control of the product is transferred to the customer, generally on delivery of the products.

In accordance with the ASC 606 requirements, the disclosure of the impact of adoption of ASC 606 on the Company's consolidated income statement and balance sheet was as follows (in thousands):

	For the three months ended March 31, 2018		
	As Reported	Prior to Adoption of ASC 606	Effect of Change Higher/(Lower)
Income statement			
Revenues	$28,111	$ 27,157	$ 954
Cost of revenues	14,397	14,017	380
Gross margin:	13,714	13,140	574
Operating expenses:			
Research and development, net	8,998	8,998	-
Sales and marketing	4,068	4,015	53
General and administrative	2,581	2,581	-
Intangible assets amortization	425	425	-
Total operating expenses:	16,072	16,019	53
Operating loss:	(2,358)	(2,879)	521
Financial income	396	396	-
Income (loss) before taxes on income	(1,962)	(2,483)	521
Taxes on income	209	209	-
Net income	(1,753)	(2,274)	521

	March 31, 2018		
	As Reported	Prior to Adoption of ASC 606	Effect of Change Higher/(Lower)
Balance Sheet			

Assets			
Trade receivables	$15,910	$14,884	$ 1,026
Inventories	8,414	8,812	(398)
Other accounts receivable and prepaid expenses	3,168	3,226	(58)
Liabilities			
Accrued expenses and other accounts payable	(2,190)	(2,235)	(45)
Equity			
Accumulated deficit	(109,265)	(109,880)	615

In August 2016, FASB issued "ASU 2016-15, Statement of Cash Flows (Topic 230) Classification of Certain Cash Receipts and Cash Payments," ("ASU 2016-15"). ASU 2016-15 eliminates the diversity in practice related to the classification of certain cash receipts and payments for debt prepayment or extinguishment costs, the maturing of a zero coupon bond, the settlement of contingent liabilities arising from a business combination, proceeds from insurance settlements, distributions from certain equity method investees and beneficial interests obtained in a financial asset securitization. ASU 2016-15 designates the appropriate cash flow classification, including requirements to allocate certain components of these cash receipts and payments among operating, investing and financing activities. The retrospective transition method, requiring adjustment to all comparative periods presented, is required unless it is impracticable for some of the amendments, in which case those amendments would be prospectively as of the earliest date practicable. The Company adopted the standard effective as of January 1, 2018, and the adoption of this standard did not have an impact on the Company's consolidated financial statements.

In November 2016, FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash." This standard requires the presentation of the statement of cash flows to show the changes in the total cash, cash equivalents, restricted cash and restricted cash equivalents. The standard is effective for fiscal years and the interim periods within those fiscal years beginning after December 15, 2017. The Company adopted the standard retrospectively for all periods presented effective as of January 1, 2018.

Recent Accounting Pronouncements.

In February 2016, FASB issued ASU 2016-02-Leases (ASC 842), which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e. lessees and lessors). The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight line basis over the term of the lease, respectively. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than twelve months regardless of their classification. Leases with a term of twelve months or less will be accounted for similar to existing guidance for operating leases. The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. ASC 842 supersedes the previous leases standard, ASC 840. The standard is effective on January 1, 2019, with early adoption permitted. The Company currently anticipates adopting the new standard effective January 1, 2019 and is evaluating the impact of the adoption of this standard on its consolidated financial statements.

Use of Estimates

The preparation of the interim condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates, judgments and assumptions. The Company's management believes that the estimates, judgments and assumptions used are reasonable based upon information available at the time they are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the dates of the interim condensed consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

NOTE B—INVENTORIES

Inventories are stated at the lower of cost or market value. The Company periodically evaluates the quantities on hand relative to current and historical selling prices, and historical and projected sales volume. Based on these evaluations, provisions are made in each period to write inventory down to its net realizable value. Inventories are composed of the following:

	March 31, 2018 (Unaudited)	**December 31, 2017 (Audited)**
Work-in-process	$ 4,370	$ 3,577
Finished goods	4,044	5,845
	$ 8,414	$ 9,422

Inventory write-off amounted to $49 and $59 for the three months ended March 31, 2018 and 2017, respectively.

NOTE C—NET EARNINGS (LOSS) PER SHARE

Basic net earnings (loss) per share are computed based on the weighted average number of shares of common stock outstanding during the period. For the same periods, diluted net earnings (loss) per share further include the effect of dilutive stock options, stock appreciation rights and restricted share units outstanding during the period, all in accordance with FASB ASC No. 260 "Earnings per Share." The following table sets forth the computation of basic and diluted net earnings (loss) per share:

	Three months ended March 31,	
	2018	**2017**
	(Unaudited)	
Net loss	$(1,753)	$(2,866)
Loss per share:		
Basic	$(0.08)	$(0.13)
Diluted	$(0.08)	$(0.13)
Weighted average number of shares of common stock outstanding during the period used to compute basic net loss per share (in thousands)	22,678	22,102
Incremental shares attributable to exercise of outstanding options, stock appreciation rights and restricted stock units (assuming proceeds would be used to purchase treasury stock) (in thousands)	-	-
Weighted average number of shares of common stock used to compute diluted net loss per share (in thousands)	22,678	22,102

NOTE D — MARKETABLE SECURITIES and time deposits

The Company accounts for investments in marketable securities in accordance with FASB ASC No.320-10 "Investments in Debt and Equity Securities". Management determines the appropriate classification of its investments in government and corporate marketable debt securities at the time of purchase and reevaluates such determinations at each balance sheet date.

The Company classifies marketable securities as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses, net of taxes, reported in other comprehensive income. The amortized cost of marketable securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and interest are included in financial income, net. Interest and dividends on securities are included in financial income, net. The following is a summary of available-for-sale securities at March 31, 2018 and December 31, 2017:

	Amortized cost		**Unrealized losses, net**		**Fair value**	
	March 31, 2018 (Unaudited)	**December 31, 2017 (Audited)**	**March 31, 2018 (Unaudited)**	**December 31, 2017 (Audited)**	**March 31, 2018 (Unaudited)**	**December 31, 2017 (Audited)**
Short-term deposits	5,465	$ 5,481	$ -	$ -	$ 5,465	$ 5,481
Long-term deposits	5,041	5,013	-	-	5,041	5,013
U.S. GSE securities	23,059	22,359	(434)	(315)	22,625	22,044
Corporate obligations	75,715	75,722	(1,439)	(894)	74,276	74,828
	$ 109,280	$ 108,575	$ (1,873)	$ (1,209)	$ 107,407	$ 107,366

The amortized cost of marketable debt securities and term deposits at March 31, 2018, by contractual maturities, is shown below:

	Amortized cost	Unrealized gains (losses) Gains	Losses	Fair value
Due in one year or less	$ 31,048	$ 1	$ (88)	$ 30,961
Due after one year to five years	78,232	1	(1,787)	76,446
	$ 109,280	$ 2	$ (1,875)	$ 107,407

The actual maturity dates may differ from the contractual maturities because debtors may have the right to call or prepay obligations without penalties.

Management believes that as of March 31, 2018, the unrealized losses in the Company's investments in all types of marketable securities were temporary and no impairment loss was realized in the Company's condensed consolidated statement of income.

The unrealized losses related to corporate obligations were primarily due to changes in interest rates. Because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at March 31, 2018.

The total fair value of marketable securities with outstanding unrealized losses as of March 31, 2018 amounted to $93,813, while the unrealized losses for these marketable securities amounted to $1,875. Of the $1,875 unrealized losses outstanding as of March 31, 2018, a portion of which in the amount of $1,319 related to marketable securities that were in a loss position for more than 12 months and the remaining portion in the amount of $556 was related to marketable securities that were in a loss position for less than 12 months.

Proceeds from maturity of available-for-sale marketable securities during the three months ended March 31, 2018 and 2017 were $1,855 and $4,779, respectively. Proceeds from sales of available-for-sale marketable securities during the three months ended March 31, 2018 and 2017 were $500 and $3,089, respectively. Net realized gains from the sale of available-for-sale securities for the three months ended March 31, 2018 were $2 compared to net realized losses for the three months ended March 31, 2017 of $47. The Company determines realized gains or losses on the sale of marketable securities based on a specific identification method.

Marketable securities are periodically reviewed for impairment. If management concludes that any marketable security is impaired, management determines whether such impairment is other-than-temporary. Factors considered in making such a determination include the duration and severity of the impairment, the reason for the decline in value and the potential recovery period, and the Company’s intent to sell, or whether it is more likely than not that the Company will be required to sell the marketable security before recovery of cost basis. If any impairment is considered other-than-temporary, the marketable security is written down to its fair value through a corresponding charge to financial income, net.

NOTE e—TAXES ON Income

The effective tax rate used in computing the provision for income taxes is based on projected fiscal year income before taxes, including estimated income by tax jurisdiction.

The total amount of net unrecognized tax benefits was $1,132 and $1,273 at March 31, 2018 and December 31, 2017, respectively. The Company accrues interest and penalties, relating to unrecognized tax benefits, in its provision for income taxes. At March 31, 2018 and December 31, 2017, the Company had accrued interest and penalties relating to unrecognized tax benefits of $80 and $68, respectively.

The Company intends to permanently reinvest earnings of its foreign operations and its current operating plans do not demonstrate a need to repatriate foreign earnings to fund the Company’s U.S. operations. However, if these funds were needed for the Company’s operations in the United States, the Company would be required to accrue and pay taxes in several countries to repatriate these funds. The determination of the amount of additional taxes related to the repatriation of these earnings is not practicable, as it may vary based on various factors such as the location of the cash and the effect of regulation in the various jurisdictions from which the cash would be repatriated.

NOTE f—SIGNIFICANT CUSTOMERS

The Company sells its products primarily through distributors and directly to original equipment manufacturers (OEMs) and original design manufacturers (ODMs) who incorporate the Company’s products into consumer products. The Company’s future performance will depend, in part, on the continued success of its distributors in marketing and selling its products. The loss of the Company’s distributors and the Company’s inability to obtain satisfactory replacements in a timely manner may harm the Company’s sales and results of operations. In addition, the Company expects that a limited number of customers, varying in identity from period-to-period, will account for a substantial portion of its revenues in any period. The loss of, or reduced demand for products from, any of the Company’s major customers could have a material adverse effect on the Company’s business, financial condition and results of operations.

The following table represents the Company’s sales, as a percentage of the Company’s total revenues, for the three months ended March 31, 2018 and 2017, of the Company’s significant customers:

Major customers/ distributors	Three months ended March 31, 2018	2017
Ascend Technology Inc. [1] [3]	26%	21 %
VTech Holdings Ltd.	25%	30 %
Nexty Electronics Corporation (previously named Tomen Electronics Corporation)[1] [2]	11%	12 %

[1] Distributor.

[2] Nexty Electronics sells the Company's products to a limited number of customers; however none of those customers accounted for more than 10% of the Company's total revenues for the three months periods ended March 31, 2018 and 2017.

[3] Ascend Technology sells the Company's products to a limited number of customers; however none of those customers accounted for more than 10% of the Company's total revenues for the three months periods ended March 31, 2018 and 2017 .

NOTE G—DERIVATIVE INSTRUMENTS

The Company accounts for derivative instruments in accordance with FASB. ASC No. 815 "Derivatives and Hedging" ("ASC 815"). Due to the Company's global operations, it is exposed to foreign currency exchange rate fluctuations in the normal course of its business. The Company's treasury policy allows it to offset the risks associated with the effects of certain foreign currency exposures through the purchase of foreign exchange forward contracts and put options (collectively, "hedging contracts"). The policy, however, prohibits the Company from speculating on hedging contracts for profit.

To protect against the increase in value of forecasted foreign currency cash flows resulting from salary and lease payments of its Israeli facilities denominated in the Israeli currency, the New Israeli Shekels ("NIS"), during the year, the Company instituted a foreign currency cash flow hedging program. The Company hedges portions of the anticipated payroll and lease payments denominated in NIS for a period of one to twelve months with hedging contracts. Accordingly, when the dollar strengthens against the foreign currencies, the decline in present value of future foreign currency expenses is offset by losses in the fair value of the hedging contracts. Conversely, when the dollar weakens, the increase in the present value of future foreign currency cash flows is offset by gains in the fair value of the hedging contracts. These hedging contracts are designated as cash flow hedges, as defined by ASC 815 and are all effective hedges of these expenses.

In accordance with ASC 815, for derivative instruments that are designated and qualify as a cash flow hedge (i.e. hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Any gain or loss on a derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item is recognized in current earnings during the period of change. As of March 31, 2018, the Company had no outstanding option contracts or foreign exchange forward contracts. See Note K for information on the fair value of hedging contracts.

The effect of derivative instruments in cash flow hedging transactions on income and other comprehensive income ("OCI") for the three months ended March 31, 2018 and 2017 is summarized below:

Gains on Derivatives

	Recognized in OCI for the three months ended March 31, Unaudited	
	2018	2017
Foreign exchange forward and option contracts	$ -	$ 143

	Gains (losses) reclassified from OCI into income	for the three months ended March 31, Unaudited	
	Location	2018	2017
Foreign exchange forward and option contracts	Operating expenses	$ -	$ 75

14

NOTE h—CONTINGENCIES

From time to time, the Company may become involved in litigation relating to claims arising from its ordinary course of business. In addition, as is typical in the semiconductor industry, the Company has been and may from time to time be notified of claims that the Company may be infringing patents or intellectual property rights owned by third parties. The Company currently believes that there are no claims or actions pending or threatened against it, the ultimate disposition of which would have a material adverse effect on the Company.

NOTE i—EQUITY-BASED COMPENSATION

Grants for the three months ended March 31, 2018 and March 31, 2017:

The weighted average estimated fair value of employee restricted stock units (“RSUs”) granted during the three months ended March 31, 2018 and 2017 was $11.27 and $9.51 per share, respectively (using the weighted average pre vest cancellation rate of 3.70% and 3.59% for the three months ended March 31, 2018 and 2017, respectively, on an annual basis).

The weighted-average estimated fair value of employee stock options and stock appreciation rights ("SARs") granted during the three months ended March 31, 2018 and 2017 was $4.75 and $2.97 per stock option and SARs, respectively, using the binomial model with the following weighted-average assumptions (annualized percentages):

	Three months ended March 31,	
	2018	**2017**
Volatility	46.24%	37.69%
Risk-free interest rate	2.40%	2.24%
Dividend yield	0%	0%
Pre-vest cancellation rate	2.29%	4.03%
Post-vest cancellation rate	3.40%	3.45%
Suboptimal exercise factor	1.61	1.33

The expected life of employee stock options and SARs is impacted by all of the underlying assumptions used in the Company's model. The binomial model assumes that employees' exercise behavior is a function of the remaining contractual life of the stock option or SAR and the extent to which the stock option or SAR is in-the-money (*i.e.*, the average stock price during the period is above the exercise price of the stock option or SAR). The binomial model estimates the probability of exercise as a function of these two variables based on the history of exercises and cancellations on past award grants made by the Company. The expected life for stock options and SARs granted during the three months ended March 31, 2018 and 2017 derived from the binomial model was 6.27 and 4.24 years, respectively.

Employee stock benefit plans

As of March 31, 2018, the Company had two equity incentive plans from which the Company may grant future equity awards and three expired equity incentive plans from which no future equity awards may be granted but had outstanding equity awards granted prior to expiration. The Company also had one employee stock purchase plan. As of March 31, 2018, approximately 591,000 shares of common stock remain available for grant under the Company's employee stock purchase plan and 142,000 shares of common stock remain available for grant under the Company's equity incentive plans.

The table below presents a summary of information relating to the Company's stock option, RSU and SAR grants pursuant to its equity incentive plans:

	Number of Options/SARs/ RSUs in thousands	**Weighted average exercise price**	**Weighted average remaining contractual term (years) (3)**	**Aggregate value (*) in thousands**
Outstanding at December 31, 2017	1,992	$ 5.02		
Options granted	48	12.50		
RSUs granted	513	-		
Options / SARs / RSUs cancelled/forfeited/expired	(12)	8.91		
Options / SARs exercised and RSUs vested	(329)	$ 2.39		
Outstanding at March 31, 2018 (1)	2,212	$ 4.38	4.87	$ 16,502
Exercisable at March 31, 2018 (2)	814	$ 8.70	4.41	$ 2,585

(*) Calculation of aggregate intrinsic value is based on the share price of the Company's common stock on March 31, 2018 ($11.80 per share).

(1) Due to the ceiling imposed on the SAR grants, the outstanding amount above can be exercised for a maximum of 2,120,000 shares of the Company's common stock as of March 31, 2018. SAR grants made on or after January 1, 2012 are convertible for a maximum number of shares of the Company's common stock equal to 50% of the SARs subject to the grant.

(2) Due to the ceiling imposed on the SAR grants, the exercisable amount above can be exercised for a maximum of 793,000 shares of the Company's common stock as of March 31, 2018.

(3) Calculation of weighted average remaining contractual term does not include RSUs that were granted, which have indefinite contractual term.

Additional information about stock options, SARs and RSUs outstanding and exercisable at March 31, 2018 with exercise prices above $11.80 per share (the closing price of the Company's common stock on March 31, 2018) is as follows:

	Exercisable		Unexercisable		Total	
Exercise prices	**Number of Options/ SARs / RSUs (in thousands)**	**Weighted average exercise price**	**Number of Options/ SARs / RSUs (in thousands)**	**Weighted average exercise price**	**Number of Options/ SARs / RSUs (in thousands)**	**Weighted average exercise price**
Less than $11.80	766	$ 8.42	1,333	$ 1.35	2,098	$ 3.93
Above $11.80	48	$ 13.05	66	$ 12.45	114	$ 12.70
Total	814	$ 8.70	1,399	$ 1.88	2,212	$ 4.38

The Company's aggregate equity-based compensation expense for the three months ended March 31, 2018 and 2017 totaled $1,699 and $1,531, respectively.

As of March 31, 2018, there was $8,389 of total unrecognized equity-based compensation expense related to unvested equity-based compensation awards granted under the Company's equity incentive plans. This amount is expected to be recognized during the period from 2018 through 2022.

NOTE j—Pension Liability

The information in this note represents the net periodic pension and post-retirement benefit costs and related components in accordance with FASB ASC No. 715 "Employers' Disclosures about Pensions and Other Post-Retirement Benefits." The components of net pension and post-retirement periodic benefit cost (income) for the three months ended March 31, 2017 and 2016 are as follows: