

PIXELWORKS, INC
Form 10-Q
November 04, 2011
Table of Contents

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 September 30, 2011

or

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

For the transition period from _____ to _____
Commission File Number: 000-30269

PIXELWORKS, INC.
(Exact name of registrant as specified in its charter)

OREGON 91-1761992
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

224 Airport Parkway, Suite 400 95110
San Jose, California
(Address of principal executive offices) (Zip Code)
(408) 200-9200
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

Number of shares of Common Stock outstanding as of October 31: 17,950,420

Table of Contents

PIXELWORKS, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2011
TABLE OF CONTENTS

	<u>PART I – FINANCIAL INFORMATION</u>	
Item 1.	<u>Financial Statements</u>	<u>3</u>
	<u>Condensed Consolidated Balance Sheets</u>	<u>3</u>
	<u>Condensed Consolidated Statements of Operations</u>	<u>4</u>
	<u>Condensed Consolidated Statements of Cash Flows</u>	<u>5</u>
	<u>Notes to Condensed Consolidated Financial Statements</u>	<u>6</u>
Item 2.	<u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>15</u>
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>21</u>
Item 4.	<u>Controls and Procedures</u>	<u>21</u>
	<u>PART II – OTHER INFORMATION</u>	
Item 1.	<u>Legal Proceedings</u>	<u>22</u>
Item 1A.	<u>Risk Factors</u>	<u>22</u>
Item 6.	<u>Exhibits</u>	<u>33</u>
	<u>SIGNATURE</u>	<u>34</u>

Table of Contents

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

PIXELWORKS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

(Unaudited)

	September 30, 2011	December 31, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	\$17,017	\$16,872
Short-term marketable securities	—	12,366
Accounts receivable, net	4,357	4,487
Inventories, net	4,683	4,858
Prepaid expenses and other current assets	2,149	2,337
Total current assets	28,206	40,920
Long-term marketable securities	—	603
Property and equipment, net	7,585	5,830
Other assets, net	3,265	5,061
Total assets	\$39,056	\$52,414
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$5,629	\$4,804
Accrued liabilities and current portion of long-term liabilities	8,545	8,983
Current portion of income taxes payable	97	282
Short-term line of credit	—	3,000
Debentures currently payable	—	15,779
Total current liabilities	14,271	32,848
Long-term liabilities, net of current portion	2,580	2,061
Income taxes payable, net of current portion	2,987	3,574
Total liabilities	19,838	38,483
Commitments and contingencies (Note 13)		
Shareholders' equity:		
Preferred stock	—	—
Common stock	346,381	336,254
Accumulated other comprehensive income (loss)	(64	) 167
Accumulated deficit	(327,099	) (322,490
Total shareholders' equity	19,218	13,931
Total liabilities and shareholders' equity	\$39,056	\$52,414
See accompanying notes to condensed consolidated financial statements.		

Table of Contents

PIXELWORKS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended September		Nine Months Ended September	
	30,		30,	
	2011	2010	2011	2010
Revenue, net	\$17,391	\$18,027	\$47,781	\$55,384
Cost of revenue (1)	8,935	9,733	25,334	29,787
Gross profit	8,456	8,294	22,447	25,597
Operating expenses:				
Research and development (2)	5,982	5,612	17,531	16,505
Selling, general and administrative (3)	3,641	3,685	11,132	11,435
Restructuring	—	—	—	94
Total operating expenses	9,623	9,297	28,663	28,034
Loss from operations	(1,167)	(1,003)	(6,216)	(2,437)
Interest expense and other, net	(89)	(127)	(395)	(378)
Gain on sale of marketable securities	—	316	264	660
Gain on sale of patents	—	—	1,600	—
Total other income (expense), net	(89)	189	1,469	282
Loss before income taxes	(1,256)	(814)	(4,747)	(2,155)
Benefit for income taxes	(173)	(821)	(138)	(5,749)
Net income (loss)	\$(1,083)	\$7	\$(4,609)	\$3,594
Net income (loss) per share:				
Basic	\$(0.06)	\$0.00	\$(0.29)	\$0.27
Diluted	\$(0.06)	\$0.00	\$(0.29)	\$0.25
Weighted average shares outstanding:				
Basic	17,905	13,465	15,787	13,417
Diluted	17,905	14,335	15,787	14,370

(1) Includes:

Additional amortization of non-cancelable prepaid royalty	\$103	\$—	\$321	\$5
Stock-based compensation	34	17	93	41
Amortization of acquired developed technology	—	—	—	1,050
(2) Includes stock-based compensation	214	120	624	309
(3) Includes stock-based compensation	260	225	771	500

See accompanying notes to condensed consolidated financial statements.

Table of Contents

PIXELWORKS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (In thousands)
 (Unaudited)

	Nine Months Ended September 30,	
	2011	2010
Cash flows from operating activities:		
Net income (loss)	\$(4,609	) \$3,594
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,800	3,328
Gain on sale of patents	(1,600) —
Stock-based compensation	1,488	850
Reversal of uncertain tax positions	(967	) (5,957
Gain on sale of marketable securities	(264	) (660
Deferred income tax expense	69	—
Other non-cash tax expense (benefit)	26	(27
Amortization of acquired developed technology	—	1,050
Other	89	162
Changes in operating assets and liabilities:		
Accounts receivable, net	130	300
Inventories, net	175	692
Prepaid expenses and other current and long-term assets, net	808	1,024
Accounts payable	787	(1,797
Accrued current and long-term liabilities	(167	) 373
Income taxes payable	195	123
Net cash provided by (used in) operating activities	(40	) 3,055
Cash flows from investing activities:		
Proceeds from sales and maturities of marketable securities	12,961	12,150
Purchases of property and equipment	(2,017	) (1,171
Proceeds from sale of patents	1,600	—
Purchases of marketable securities	—	(13,567
Purchases of other assets	—	(290
Proceeds from sales of property and equipment	—	5
Net cash provided by (used in) investing activities	12,544	(2,873
Cash flows from financing activities:		
Repurchase of debentures currently payable	(15,779) —
Net proceeds from equity offering	8,327	—
Payments on line of credit	(3,000) —
Payments on asset financings	(2,219	) (1,794
Proceeds from issuances of common stock	312	193
Net cash used in financing activities	(12,359	) (1,601
Net change in cash and cash equivalents	145	(1,419
Cash and cash equivalents, beginning of period	16,872	17,797
Cash and cash equivalents, end of period	\$17,017	\$16,378
See accompanying notes to condensed consolidated financial statements.		

Table of Contents

PIXELWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except share and per share data)

(Unaudited)

NOTE 1: BASIS OF PRESENTATION

Nature of Business

We are an innovative designer, developer and marketer of video and pixel processing semiconductors and software for high-end digital video applications and hold 114 patents related to the visual display of digital image data. Our solutions enable manufacturers of digital display and projection devices, such as large-screen flat panel televisions and digital front projectors, to manufacture their products with a consistently high level of video quality, regardless of the content's source or format. Our core technology leverages unique proprietary techniques for intelligently processing video signals from a variety of sources to ensure that all resulting images are optimized. Additionally, our products help our customers reduce costs and differentiate their display and projection devices, an important factor in industries that experience rapid innovation. Pixelworks was founded in 1997 and is incorporated under the laws of the state of Oregon.

Condensed Consolidated Financial Statements

These condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to such regulations, although we believe that the disclosures provided are adequate to prevent the information presented from being misleading.

The financial information included herein for the three and nine month periods ended September 30, 2011 and 2010 is unaudited; however, such information reflects all adjustments, consisting of normal recurring adjustments, that are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows of the Company for these interim periods. The financial information as of December 31, 2010 is derived from our audited consolidated financial statements and notes thereto for the fiscal year ended December 31, 2010, included in Item 8 of our Annual Report on Form 10-K, filed with the SEC on March 9, 2011, and should be read in conjunction with such consolidated financial statements.

The results of operations for the three and nine month periods ended September 30, 2011 are not necessarily indicative of the results expected for the entire fiscal year ending December 31, 2011.

Recent Accounting Pronouncements

In May 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (Topic 820)-Fair Value Measurement ("ASU 2011-04"), to provide a consistent definition of fair value and ensure that the fair value measurement and disclosure requirements are similar between U.S. GAAP and International Financial Reporting Standards. ASU 2011-04 changes certain fair value measurement principles and enhances the disclosure requirements. The provisions of this new guidance are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The guidance is not expected to have a material impact on our consolidated financial statements.

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, Comprehensive Income (Topic 220)-Presentation of Comprehensive Income ("ASU 2011-05"), to require an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of equity. The provisions of this new guidance require retrospective application and are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The guidance will change the presentation of our consolidated financial statements but will not impact our financial position or results of operations.

Reclassifications

Certain reclassifications have been made to the 2010 condensed consolidated financial statements and notes to conform to the 2011 presentation.

Table of Contents

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires us to make estimates and judgments that affect amounts reported in the financial statements and accompanying notes. Our significant estimates and judgments include those related to product returns, warranty obligations, bad debts, inventories, property and equipment, impairment of long-lived assets, amortization of prepaid royalties, valuation of share-based payments, income taxes, litigation and other contingencies. The actual results experienced could differ materially from our estimates.

NOTE 2: BALANCE SHEET COMPONENTS

Accounts Receivable, Net

Accounts receivable are recorded at invoiced amount and do not bear interest when recorded or accrue interest when past due. Accounts receivable are stated net of an allowance for doubtful accounts, which is maintained for estimated losses that may result from the inability of our customers to make required payments. Accounts receivable consists of the following:

	September 30, 2011	December 31, 2010
Accounts receivable, gross	\$4,750	\$4,886
Less: allowance for doubtful accounts	(393	) (399
Accounts receivable, net	\$4,357	\$4,487

The following is the change in our allowance for doubtful accounts:

	Nine Months Ended September 30,	
	2011	2010
Balance at beginning of period	\$399	\$428
Additions charged (reductions credited)	(6	) 8
Balance at end of period	\$393	\$436

Inventories, Net

Inventories consist of finished goods and work-in-process, and are stated at the lower of standard cost (which approximates actual cost on a first-in, first-out basis) or market (net realizable value), net of a reserve for slow-moving and obsolete items.

Inventories consist of the following:

	September 30, 2011	December 31, 2010
Finished goods	\$2,475	\$2,961
Work-in-process	3,078	3,232
Total	5,553	6,193
Less: reserve for slow-moving and obsolete items	(870	) (1,335
Inventories, net	\$4,683	\$4,858