DSP GROUP INC /DE/
Form 10-Q
November 10, 2014

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, 2014

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 (State or other jurisdiction of incorporation or organization)	**94-2683643** (I.R.S. employer identification number)
2161 S. San Antonio Road, Suite 10 **San Jose, California** (Address of Principal Executive Offices)	**95131** (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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer 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 November 5, 2014, there were 21,612,193 shares of Common Stock ($.001 par value per share) outstanding.

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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)

	September 30, 2014 Unaudited	**December 31, 2013 Audited**
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 14,509	$ 23,578
Restricted deposits	394	77
Marketable securities and short-term deposits	9,275	13,895
Trade receivables, net	25,091	21,195
Deferred income taxes	97	92
Other accounts receivable and prepaid expenses	1,640	2,641
Inventories	13,908	12,334
TOTAL CURRENT ASSETS	64,914	73,812
PROPERTY AND EQUIPMENT, NET	2,865	2,837
LONG-TERM ASSETS:		
Long-term marketable securities and deposits	93,214	90,162
Long-term prepaid expenses and lease deposits	87	100
Severance pay fund	11,456	11,168
Investment in other companies	2,200	2,200
Intangible assets, net	5,517	6,710
Goodwill	5,276	5,276
	117,750	115,616
TOTAL ASSETS	$ 185,529	$ 192,265

Note: The balance sheet at December 31, 2013 has been derived from the audited financial statements on that date.

See notes to condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

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

	September 30, 2014 Unaudited	**December 31, 2013 Audited**
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Trade payables	$ 15,468	$ 14,149
Accrued compensation and benefits	7,579	9,845
Income tax accruals and payables	1,946	1,985
Accrued expenses and other accounts payable	5,565	5,532
Total current liabilities	30,558	31,511
LONG-TERM LIABILITIES:		
Deferred income taxes	894	1,183
Accrued severance pay	11,525	11,179
Accrued pensions	927	981
Total long-term liabilities	13,346	13,343
COMMITMENTS AND CONTINGENCIES STOCKHOLDERS' EQUITY:		
Capital stock:		
Preferred stock, $ 0.001 par value - Authorized shares: 5,000,000 at September 30, 2014 and December 31, 2013; Issued and outstanding shares: none at September 30, 2014 and December 31, 2013	-	-
Common stock, $ 0.001 par value - Authorized shares: 50,000,000 shares at September 30, 2014 and December 31, 2013; Issued and outstanding shares: 21,540,317 and 22,349,780 shares at September 30, 2014 and December 31, 2013, respectively	22	22
Additional paid-in capital	354,694	350,494
Treasury stock	(125,329)	(118,749)
Accumulated other comprehensive loss	(1,433)	(821)
Accumulated deficit	(86,329)	(83,535)
Total stockholders' equity	141,625	147,411
Total liabilities and stockholders' equity	$ 185,529	$ 192,265

Note: The balance sheet at December 31, 2013 has been derived from the audited financial statements on that date.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	**2013**	**2014**	**2013**
Revenues	$36,715	$35,381	$105,877	$115,723
Cost of revenues (1)	22,187	21,576	63,554	70,050
Gross profit	14,528	13,805	42,323	45,673
Operating expenses:				
Research and development, net (2)	8,083	8,147	24,313	26,481
Sales and marketing (3)	2,892	2,767	8,925	8,492
General and administrative (4)	2,580	2,576	7,941	9,046
Intangible assets amortization	397	418	1,191	1,254
Total operating expenses	13,952	13,908	42,370	45,273
Operating income (loss)	576	(103)	(47)	400
Financial income, net	186	512	895	1,837
Income before taxes on income	762	409	848	2,237
Taxes on income (income tax benefit)	(11)	11	(25)	(83)
Net income	$773	$398	$873	$2,320
Net income per share:				
Basic	$0.04	$0.02	$0.04	$0.10
Diluted	$0.03	$0.02	$0.04	$0.10
Weighted average number of shares used in per share computations of net income:				
Basic	21,830	22,522	22,064	22,159
Diluted	23,073	23,048	22,829	22,723

(1) Includes equity-based compensation expense in the amount of $71 and $65 for the three months ended September 30, 2014 and 2013, respectively, and equity-based compensation expense in the amount of $237 and $191 for the nine months ended September 30, 2014 and 2013,respectively.

(2) Includes equity-based compensation expense in the amount of $568 and $474 for the three months ended September 30, 2014 and 2013, respectively, and equity-based compensation expense in the amount of $1,869 and $1,412 for the nine months ended September 30, 2014 and 2013, respectively

(3) Includes equity-based compensation expense in the amount of $150 and $115 for the three months ended September 30, 2014 and 2013, respectively, and equity-based compensation expense in the amount of $481 and $383 for the nine months ended September 30, 2014 and 2013, respectively.

(4) Includes equity-based compensation expense in the amount of $507 and $391 for the three months ended September 30, 2014 and 2013, respectively, and equity-based compensation expense in the amount of $1,613 and $1,147 for the nine months ended September 30, 2014 and 2013, respectively.

See notes to condensed consolidated financial statements.

DSP GROUP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (U.S. dollars in thousands)

	Three months ended September 30,	
	2014	**2013**
Net income:	$773	$398
Other comprehensive loss:		
Available-for-sale securities:		
Changes in unrealized gains/losses	(404)	459
Reclassification adjustments for losses (gains) included in net income (loss)	3	(183)
Net change	(401)	276
Cash flow hedges:		
Changes in unrealized gains/losses	(528)	93
Reclassification adjustments for losses (gains) included in net income (loss)	97	(292)
Net change	(431)	(199)
Change in unrealized components of defined benefit plans:		
Amortization of actuarial loss and prior service benefit	3	3
Net change	3	3
Foreign currency translation adjustments, net	5	7
Other comprehensive income (loss)	(824)	87
Comprehensive income (loss)	$(51)	$485

See notes to condensed consolidated financial statements.

DSP GROUP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (U.S. dollars in thousands)

	Nine months ended September 30,	
	2014	2013
Net income:	$873	$2,320
Other comprehensive income (loss):		
Available-for-sale securities:		
Changes in unrealized gains/losses	(134)	(537)
Reclassification adjustments for (gains) losses included in net income	(62)	(726)
Net change	(196)	(1,263)
Cash flow hedges:		
Changes in unrealized gains/losses	(516)	355
Reclassification adjustments for losses (gains) included in net income	92	(695)
Net change	(424)	(340)
Change in unrealized components of defined benefit plans:		
Amortization of actuarial loss and prior service benefit	9	8
Net change	9	8
Foreign currency translation adjustments, net	(1)	(19)
Other comprehensive loss	(612)	(1,614)
Comprehensive income	$261	$706

See notes to condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(U.S. dollars in thousands)

	Nine Months Ended September 30,	
	2014	**2013**
Net cash provided by operating activities	$3,734	$4,973
Investing activities		
Purchase of marketable securities	(50,205)	(53,331)
Proceeds from maturity of marketable securities	9,896	15,180
Proceeds from sales of marketable securities	40,821	27,814
Increase in restricted deposits	(327)	-
Purchases of property and equipment	(1,002)	(925)
Net cash provided used in investing activities	(817)	(11,262)
Financial activities		
Purchase of treasury stock	(12,484)	-
Issuance of treasury stock for cash upon exercise of stock options	514	1,848
Net cash provided by (used in) financing activities	(11,970)	1,848
Increase (decrease) in cash and cash equivalents	$(9,053)	$(4,441)
Cash (erosion) due to exchange rate differences	(16)	28
Cash and cash equivalents at the beginning of the period	$23,578	$21,684
Cash and cash equivalents at the end of the period	$14,509	$17,271

See notes to condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED STATEMENTS OF STOCKHOLDERS' EQUITY

(UNAUDITED)

(U.S. dollars and shares in thousands)

Three Months Ended September 30, 2013	**Number of Common Stock**	**Common Stock**	**Additional Paid-In Capital**	**Treasury Stock**	**Accumulated deficit**	**Other Comprehensive Income (Loss)**	**Total Stockholders' Equity**
Balance at June 30, 2013	22,172	$ 22	$ 348,423	$ (120,829)	$ (80,297)	$ (713)	$ 146,606
Net income	-	-	-	-	398	-	398
Change in accumulated other comprehensive income	-	-	-	-	-	87	87
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	184	*)	-	1,802	(984)	-	818
Issuance of treasury stock upon exercise of stock options, stock appreciation rights and restricted share units by employees and directors	202	1	-	1,985	(1,362)	-	624
Equity-based compensation	-	-	1,045	-	-	-	1,045
Balance at September 30, 2014	**22,558**	**$ 23**	**$ 349,468**	**$ (117,042)**	**$ (82,245)**	**$ (626)**	**$ 149,578**
Three Months Ended September 30, 2014							
Balance at June 30, 2014	21,843	$ 22	$ 353,398	$ (122,713)	$ (86,092)	$ (609)	$ 144,006
Net income	-	-	-	-	773	-	773
Change in accumulated other comprehensive income	-	-	-	-	-	(824)	(824)
Purchase of treasury stock	(505)	(1)	-	(4,588)	-	-	(4,589)
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	124	1	-	1,217	(329)	-	889
	78	*)	-	755	(681)	-	74

Issuance of treasury stock upon exercise of stock options, stock appreciation rights and restricted share units by employees and directors							
Equity-based compensation	-	-	1,296	-	-	-	1,296
Balance at September 30, 2014	**21,540**	**$ 22**	**$ 354,694**	**$ (125,329)**	**$ (86,329)**	**$ (1,433)**	**$ 141,625**

(*) Represents an amount lower than $1.

See notes to condensed consolidated financial statements.

DSP GROUP, INC.

CONDENSED STATEMENTS OF STOCKHOLDERS' EQUITY

(UNAUDITED)

(U.S. dollars and shares in thousands)

	Number of Common Stock	Common Stock	Additonal Paid-In Capital	Treasury Stock	Accumulated deficit	Other Comprehensive Income (Loss)	Total Stockholders' Equity
Nine Months Ended September 30, 2013							
Balance at December 31, 2012	21,674	$ 22	$ 346,335	$ (125,724)	$ (79,394)	$ 988	$ 142,227
Net income		-	-	-	2,320		2,320
Change in accumulated other comprehensive income		-	-	-	-	(1,614)	(1,614)
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	374	*)	-	3,669	(2,005)	-	1,664
Issuance of treasury stock upon exercise of stock options, stock appreciation rights and restricted share units by employees and directors	510	1	-	5,013	(3,166)	-	1,848
Equity-based compensation	-	-	3,133	-	-	-	3,133
Balance at September 30, 2013	**22,558**	**$ 23**	**$ 349,468**	**$ (117,042)**	**$ (82,245)**	**$ (626)**	**$ 149,578**
Nine Months Ended September 30, 2014							
Balance at December 31, 2013	22,350	$ 22	$ 350,494	$ (118,749)	$ (83,535)	$ (821)	$ 147,411
Net income		-	-	-	873		873
Change in accumulated other comprehensive income		-	-	-	-	(612)	(612)
Purchase of treasury stock	(1,414)	(1)	-	(12,483)	-	-	(12,484)
Issuance of treasury stock upon purchase of common stock under employee stock purchase plan	311	1	-	3,031	(1,309)	-	1,723

Issuance of treasury stock upon exercise of stock options, stock appreciation rights and restricted share units by employees and directors	293	*)	-	2,872	(2,358)	-	514
Equity-based compensation	-	-	4,200	-	-	-	4,200
Balance at September 30, 2014	**21,540**	**$ 22**	**$ 354,694**	**$ (125,329)**	**$ (86,329)**	**$ (1,433)**	**$ 141,625**

(*) Represents an amount lower than $1.

See notes to condensed consolidated financial statements.

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DSP GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(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 and nine months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. 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, 2013.

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:

	September 30, 2014	**December 31, 2013**
	(Unaudited)	(Audited)
Work-in-process	$ 7,311	$ 5,412
Finished goods	6,597	6,922
	$ 13,908	$ 12,334

Inventory write-off amounted to $48 for the nine months ended September 30, 2014. For the nine months ended September 30, 2013, the Company recorded $177 of income due to the utilization of inventory that was written off in the past.

NOTE c—NET income PER SHARE

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

	Three months ended		**Nine months ended**	
	September 30,		**September 30,**	
	2014	**2013**	**2014**	**2013**
	Unaudited			
Net income	$773	$398	$873	$2,320
Net income per share:				
Basic	$0.04	$0.02	$0.04	$0.10
Diluted	$0.03	$0.02	$0.04	$0.10
Weighted average number of shares of common stock outstanding during the period used to compute basic net income per share (in thousands)	21,830	22,522	22,064	22,159
Incremental shares attributable to exercise of outstanding options, stock appreciation rights and restricted shares units (assuming proceeds would be used to purchase treasury stock) (in thousands)	1,243	526	765	564
Weighted average number of shares of common stock used to compute diluted net income per share (in thousands)	23,073	23,048	22,829	22,723

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 on securities are included in financial income, net. The following is a summary of available-for-sale securities and short term deposits at September 30, 2014 and December 31, 2014:

	Amortized cost		Unrealized gains (losses), net		Estimated fair value	
	September 30, 2014	December 31, 2013	September 30, 2014	December 31, 2013	September 30, 2014	December 31, 2013
	(Unaudited)	(Audited)	(Unaudited)	(Audited)	(Unaudited)	(Audited)
Short -term deposits	$2,755	$2,911	$-	$ -	$2,755	$2,911
U.S. GSE securities	4,315	3,093	2	(11)	4,317	3,082
Corporate obligations	96,006	98,444	(589)	(380)	95,417	98,064
	$103,076	$104,448	$(587)	$ (391)	$102,489	$104,057

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The amortized cost of short and long-term deposits and available-for-sale debt securities at September 30, 2014, by contractual maturities, is shown below:

	Amortized cost	Unrealized gains (losses) Gains	Losses	Estimated fair value
Due in one year or less	$ 9,266	$ 9	$ -	$ 9,275
Due after one year to five years	93,810	125	(721)	93,214
	$ 103,076	$ 134	$ (721)	$ 102,489

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 September 30, 2014, 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.

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.

The total fair value of marketable securities with outstanding unrealized losses as of September 30, 2014 amounted to $68,921. Of the $721 unrealized losses outstanding as of September 30, 2014 and presented in the table above, a portion of which in the amount of $149, was related to marketable securities that were in a loss position for more than 12 months and the remaining portion in the amount of $572 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 nine months ended September 30, 2014 and 2013 were $9,896 and $15,180, respectively. Proceeds from sales of available-for-sale marketable securities during the nine months ended September 30, 2014 and 2013 were $40,821 and $27,814, respectively. Net realized gains from the sale of available-for sale marketable securities for the nine months ended September 30, 2014 and 2013 were $62 and $726, respectively. The Company determines realized gains or losses on the sale of available-for-sale marketable securities based on a specific identification method.

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. Tax provision for the three and nine months ended September 30, 2014 and September 30, 2013 does not include tax benefits associated with equity-based compensation expenses. During the three and nine months ended September 30, 2014, the Company did not record any significant changes to its deferred tax assets due to its current estimation of future taxable income.

The total amount of net unrecognized tax benefits was $1,833 and $1,892 at September 30, 2014 and December 31, 2013, respectively. The Company accrues interest and penalties, relating to unrecognized tax benefits, in its provision for income taxes. At September 30, 2014 and December 31, 2013, the Company had accrued interest and penalties relating to unrecognized tax benefits of $432 and $408, respectively.

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.

Sales to Hong Kong-based VTech Holdings Ltd. (“VTech”) represented 34% and 35% of the Company’s total revenues for the three months ended September 30, 2014 and 2013, respectively. Sales to VTech represented 36% of the Company’s total revenues for both the nine months ended September 30, 2014 and 2013.

Revenues derived from sales through one distributor, Tomen Electronics Corporation (“Tomen Electronics”), accounted for 22% and 24% of the Company’s total revenues for the three months ended September 30, 2014 and 2013, respectively. Tomen Electronics accounted for 21% and 18% of the Company's total revenues for the nine months ended September 30, 2014 and 2013, respectively. The Japanese market and the OEMs that operate in that market are among the largest suppliers in the world with significant market share in the U.S. market for residential wireless products. Tomen Electronics sells the Company’s products to a limited number of customers. One customer, Panasonic Communications Co., Ltd. (“Panasonic”), has continually accounted for a majority of the sales of Tomen Electronics. Sales to Panasonic through Tomen Electronics generated 17% and 18% of the Company’s total revenues for the three months ended September 30, 2014 and 2013, respectively. Sales to Panasonic through Tomen Electronics generated 15% and 13% of the Company’s total revenues for the nine months ended September 30, 2014 and 2013, respectively.

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 September 30, 2014, the Company had outstanding foreign exchange forward contracts in the amount of $3,450 and outstanding option contracts in the amount of $11,725. These hedging contracts do not contain any credit-risk-related contingency features. See Note K for information on the fair value of these hedging contracts.

The fair value of derivative assets and derivative liabilities were $32 and $456, respectively, at September 30, 2014. The Company recorded a net amount of $424 in accrued expenses and other accounts payable in the condensed consolidated balance sheets at September 30, 2014.

The amount recorded as expense in research and development expenses, sales and marketing expenses and general and administrative expenses in the condensed consolidated statements of income for the nine months ended September 30, 2014 that resulted from the above referenced hedging transactions was $72, $7 and $13, respectively. The amount recorded as expense in research and development expenses, sales and marketing expenses and general and administrative expenses in the condensed consolidated statements of income for the three months ended September 30, 2014 that resulted from the above referenced hedging transactions was $76, $8 and $13, respectively.

The fair value of the outstanding derivative instruments at September 30, 2014 and December 31, 2013 is summarized below:

	Balance Sheet Location	Fair Value of Derivative Instruments As of September 30, 2014	As of December 31, 2013
Derivative Assets			
Foreign exchange forward contracts and put options	Accrued expenses and other accounts payable (*)	$ 424	$ -
Total		$ 424	$ -

*) Estimated to be reclassified into earnings for the remainder of 2014 and in 2015.

The effect of derivative instruments in cash flow hedging transactions on income and other comprehensive income (“OCI”) for the three and nine months ended September 30, 2013 and 2012 is summarized below:

Gains (Losses) on Derivatives Recognized in OCI	
for the three months	for the nine months

	ended September 30,		ended September 30,	
	2014	**2013**	**2014**	**2013**
Foreign exchange forward contracts	$(528)	$ 93	$(516)	$355

	Gains (Losses) Reclassified from OCI into Income				
		for the three months ended September 30,		for the nine months ended September 30,	
	Location	**2014**	**2013**	**2014**	**2013**
Foreign exchange forward contracts	Operating expenses	$(97)	$292	$(92)	$695

NOTE h—CONTINGENCIES

From time to time, the Company may become involved in litigation relating to claims arising from its ordinary course of business. Also, 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—ACCOUNTING FOR EQUITY-BASED COMPENSATION

Grants for Three Months ended September 30, 2013:

The weighted-average estimated fair value of restricted stock units (“RSUs”) granted during the three months ended September 30, 2014 and September 30, 2013 was $8.87 and $7.58 per share with the following weighted-average assumptions (annualized percentages):

	Three months ended September 30, 2014	Three months ended September 30, 2013
Pre-vest cancellation rate	4.57%	3.66%

Employee Stock Benefit Plans

As of September 30, 2013, 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 September 30, 2014, approximately 404,000 shares of common stock remain available for grant under the Company’s employee stock purchase plan and 566,000 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, SAR and RSU grants pursuant to its equity incentive plans:

	Number of Options/SARs/RSUs	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years) (3)	Aggregate Value (*)
	in thousands			**in thousands**
Outstanding at June 30, 2014	6,173	$ 7.20		
RSUs granted	5	-		
Options / SARs/RSUs cancelled/forfeited/expired	(89)	$ 17.49		
Options / SARs / RSUs exercised	(153)	$ 4.89		
Outstanding at September 30, 2014 (1)	5,937	$ 7.10	3.02	$ 13,853
Exercisable at September 30, 2014 (2)	4,233	$ 8.28	2.35	$ 5,738

(*) Calculation of aggregate intrinsic value is based on the share price of the Company's common stock on September 30, 2014 ($8.87 per share).

(1) Due to the ceiling imposed on the SAR grants, the outstanding amount equals to a maximum of 4,432 shares of the Company's common stock issuable upon exercise. SAR grants made prior to January 1, 2009 are convertible for a maximum number of shares of the Company's common stock equal to 50% of the SAR units subject to the grant. SAR grants made on or after January 1, 2009 and before January 1, 2010 are convertible for a maximum number of shares of the Company's common stock equal to 75% of the SAR units subject to the grant. SAR grants made on or after January 1, 2010 and before January 1, 2012 are convertible for a maximum number of shares of the Company's common stock equal to 66.67% of the SAR units subject to the grant. 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 SAR units subject to the grant.

(2) Due to the ceiling imposed on the SAR grants, the currently exercisable amount equals to a maximum of 2,920 shares of the Company's common stock exercisable.

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

Additional information about stock options, SARs and RSUs outstanding and exercisable at September 30, 2014 with exercise prices above $8.87 per share (the closing price of the Company's common stock on September 30, 2014) is as follows (in thousands, except per share amounts):

Exercise Prices	Exercisable Number of Options/ SARs (in thousands)	Weighted Average Exercise Price	Unexercisable Number of Options/ SARs/RSUs (in thousands)	Weighted Average Exercise Price	Total Number of Options/ SARs/RSUs (in thousands)	Weighted Average Exercise Price
Above $8.87	1,373	$ 11.22	124	$ 9.71	1,497	$ 11.09
Less than $8.87	2,860	$ 6.86	1,580	$ 3.73	4,440	$ 5.75
Total	4,233	$ 8.28	1,704	$ 4.17	5,937	$ 7.10

The Company's aggregate equity-based compensation expense for the three months ended September 30, 2014 and 2013 totaled $1,296 and $1,045, respectively. The Company did not recognize any income tax benefits relating to its equity-based compensation expense for the three months ended September 30, 2014 and 2013.

The Company's aggregate equity-based compensation expenses for the nine months ended September 30, 2014 and 2013 totaled $4,200 and $3,133, respectively. The Company did not recognize any income tax benefits relating to its equity-based compensation expense for the nine months ended September 30, 2014 and 2013.

As of September 30, 2014, there was $3,488 of total unrecognized equity-based compensation expenses 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 the remainder of 2014 through 2018.

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 nine months ended September 30, 2014 and 2013 are as follows (in thousands):

	September 30, 2014	September 30, 2013
Components of net periodic benefit cost		
Service cost	$ 12	$ 13
Interest cost	22	27
Expected return on plan assets	(4)	(7)
Net periodic benefit cost	**$ 30**	**$ 33**

The net pension liability as of September 30, 2014 amounted to $927.

NOTE K—FAIR VALUE MEASUREMENTS

Assets and Liabilities Measured at Fair Value on a Recurring Basis:

The Company measures its cash equivalents, short-term deposits, marketable securities and foreign currency derivative contracts at fair value. Cash equivalents, short-term deposits and marketable securities are classified within Level 1 or Level 2 value hierarchies as they are valued using quoted market prices or alternative pricing sources and models utilizing market observable inputs. Foreign currency derivative contracts are classified within Level 2 value hierarchy as the valuation inputs are based on quoted prices and market observable data of similar instruments.

The following table provides information by value level for assets and liabilities that are measured at fair value on a recurring basis as of September 30, 2014:

Description	Balance as of September 30, 2014	Fair Value Measurements Level 1	Level 2	Level 3
Assets:				
Cash equivalents:				
Time deposits	$ 572	-	$ 572	-
Money market mutual funds	$ 1,828	$ 1,828	-	-
Short-term marketable securities and cash deposits:				
Corporate debt securities	$ 6,520	-	$ 6,520	-
Time deposits	$ 2,755	-	$ 2,755	-
Long-term marketable securities:				
U.S. GSE securities	$ 4,317	-	$ 4,317	-
Corporate debt securities	$ 88,897	-	$ 88,897	-
Derivative liabilities	$ (424)	-	$ (424)	-

The following table provides information by value level for assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2013:

Description	Balance as of December 31, 2013	Level 1	Fair Value Measurements Level 2	Level 3
Assets:				
Cash equivalents:				
Time deposits	$ 913	-	$ 913	-
Money market mutual funds	$ 3,762	$ 3,762	-	-

Short-term marketable securities and time deposits:				
U.S. GSE securities	$ 251	-	$ 251	-
Corporate debt securities	$ 10,733	-	$ 10,733	-
Time deposits	$ 2,911	-	$ 2,911	-
Long-term marketable securities:				
U.S. GSE securities	$ 2,831	-	$ 2,831	-
Corporate debt securities	$ 87,331	-	$ 87,331	-

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In addition to the assets and liabilities described above, the Company’s financial instruments also include cash and cash equivalents, restricted and short-term deposits, trade receivables, other accounts receivable, trade payables, accrued expenses and other payables. The fair value of these financial instruments was not materially different from their carrying values at September 30, 2014 due to the short-term maturity of these instruments.

NOTE l—STOCKHOLDERS’ EQUITY

During the first nine months of 2014, the Company repurchased 1,414,226 shares of common stock at an average purchase price of $8.83 per share for an aggregate purchase price of $12,484. As of September 30, 2014, 1,203,601 shares of common stock remained authorized for repurchase under the Company's board-authorized share repurchase program.

Repurchases of common stock are accounted for as treasury stock, and result in a reduction of stockholders’ equity. When treasury shares are reissued, the Company accounts for the reissuance in accordance with Accounting Principles Board Opinion No. 6, “Status of Accounting Research Bulletins” and charges the excess of the repurchase cost over issuance price using the weighted average method to accumulated deficit. In the case where the repurchase cost over issuance price using the weighted average method is lower than the issuance price, the Company credits the difference to additional paid-in capital.

During the first nine months of 2014, the Company issued approximately 605,000 shares of common stock out of treasury stock to employees who exercised their stock options, SARs or RSUs, or purchased shares from the Company’s 1993 Employee Stock Purchase Plan.

note M—SEGMENT INFORMATION

Description of segments:

The Company operates under three reportable segments.

The Company's segment information has been prepared in accordance with ASC 280, "Segment Reporting." Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the Company's chief operating decision-maker

(“CODM”) in deciding how to allocate resources and assess performance. The Company's CODM is its Chief Executive Officer, who evaluates the Company's performance and allocates resources based on segment revenues and operating income.

The Company's operating segments are as follows: Home, Office and Mobile. The classification of the Company’s business segments is based on a number of factors that management uses to evaluate, view and run its business operations, which include, but are not limited to, customer base, homogeneity of products and technology.

A description of the types of products provided by each business segment is as follows:

Home - Wireless chipset solutions for converged communication at home. Such solutions include integrated circuits targeted for cordless phones sold in retail or supplied by telecommunication service providers, residential gateway devices supplied by telecommunication service providers which integrate the DECT/CAT-iq functionality and also address home automation applications, as well as fixed-mobile convergence solutions.

Office - Comprehensive solution for Voice-over-IP (VOIP) office products, including office solutions that offer businesses of all size low-cost VOIP terminals with converged voice and data applications.

Mobile - Products for the mobile market that provides voice enhancement and far-end noise elimination targeted for mobile phone and mobile headsets.

Segment data:

The Company derives the results of its business segments directly from its internal management reporting system and by using certain allocation methods. The accounting policies the Company uses to derive business segment results are substantially the same as those the Company uses for consolidation of its financial statements. The CODM measures the performance of each business segment based on several metrics, including earnings from operations. The CODM uses these results, in part, to evaluate the performance of, and to assign resources to, each of the business segments. The Company does not allocate to its business segments certain operating expenses, which it manages separately at the corporate level. These unallocated costs include primarily restructuring charges, amortization of purchased intangible assets, equity-based compensation expenses, proxy contest related expenses incurred during the second quarter of 2013 and certain corporate governance costs.

Selected operating results information for each business segment was as follows for the three months ended September 30, 2014 and 2013:

Three months ended September 30			
Revenues		**Income (loss) from operations**	
2014	**2013**	**2014**	**2013**

Home	$32,292	$33,492	$5,957	$5,381
Office	$4,353	$1,889	$(252)	$(731)
Mobile	$70	$-	$(2,910)	$(2,609)
Total	$36,715	$35,381	$2,795	$2,041

Selected operating results information for each business segment was as follows for the nine months ended September 30, 2014 and 2013:

Nine months ended September 30