

INPHI Corp
Form 10-K
March 10, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(Mark
One)

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

For the fiscal year ended December 31, 2014

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

Commission file number 001-34942

Inphi Corporation

(Exact Name of Registrant as Specified in Its Charter)

Delaware **77-0557980**
(State or Other Jurisdiction (I.R.S. Employer
of Incorporation or Organization) Identification No.)

2953 Bunker Hill Lane, Suite 300, Santa Clara, California 95054

(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: (408) 217-7300

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

Title of Class	Name of Exchange on Which Registered
Common Stock, \$0.001 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required

to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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

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

As of June 30, 2014, the aggregate market value of the Registrant's common stock held by non-affiliates of the Registrant was approximately \$458 million, based on the closing price of the common stock as reported on the New York Stock Exchange for that date.

The total number of shares outstanding of the Registrant's common stock, \$0.001 par value per share, as of February 28, 2015 was 37,864,922.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates by reference certain information from the registrant's definitive proxy statement for the 2015 Annual Meeting of Stockholders to be filed no later than 120 days after the conclusion of the registrant's fiscal year ended December 31, 2014.

INPHI CORPORATION

ANNUAL REPORT ON FORM 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2014

TABLE OF CONTENTS

	Page
PART I	
Item 1. Business	1
Item 1A. Risk Factors	8
Item 1B. Unresolved Staff Comments	24
Item 2. Properties	24
Item 3. Legal Proceedings	24
Item 4. Mine Safety Disclosures	26
PART II	
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	27
Item 6. Selected Consolidated Financial Data	29
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	31
Item 7A. Quantitative and Qualitative Disclosures about Market Risk	44
Item 8. Financial Statements and Supplementary Data	46
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	78
Item 9A. Controls and Procedures	78
Item 9B. Other Information	78
PART III	
Item 10. Directors, Executive Officers and Corporate Governance	78
Item 11. Executive Compensation	79
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	79
Item 13. Certain Relationships and Related Transactions, and Director Independence	79
Item 14. Principal Accountant Fees and Services	79
PART IV	
Item 15. Exhibits and Financial Statement Schedules	79

PART I

Item 1. Business

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this report, the terms “may,” “might,” “will,” “objective,” “intend,” “should,” “could,” “can,” “would,” “believe,” “estimate,” “predict,” “potential,” “plan,” or the negative of these terms, and similar expressions intended to identify forward-looking statements. These statements are statements that relate to future periods and include statements regarding our anticipated trends and challenges in our business and the markets in which we operate, including the market for 40G and 100G high-speed analog semiconductor solutions, our plans for future products, expansion of our product offerings and enhancements of existing products, our expectations regarding our expenses and revenue, sources of revenue, our tax benefits, the features and benefits of our products and services, our technological capabilities and expertise, timing of the development of our products, the status and anticipated impact of the Cortina integration, our collaborative relationships with industry and technology leaders, OEMs, systems manufacturers and standard bodies and the anticipated benefits thereof, our anticipated cash needs and our estimates regarding our capital requirements and our needs for additional financing, our anticipated growth and growth strategies, our ability to retain and attract customers, particularly in light of our dependence on a limited number of customers for a substantial portion of our revenue, our strategies regarding sales and marketing, manufacturing, research and development, intellectual property and the anticipated benefits thereof, our expectations regarding competition, interest rate sensitivity, adequacy of our disclosure controls, our legal proceedings and warranty claims. These forward-looking statements involved known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these or any other forward-looking statements. These risks and uncertainties include, but are not limited to, those risks discussed below, as well as factors affecting our results of operations, our ability to manage our growth, our ability to sustain or increase profitability, demand for our solutions, the effect of declines in average selling prices for our products, our ability to compete, our ability to rapidly develop new technology and introduce new products, our ability to safeguard our intellectual property, trends in the semiconductor industry and fluctuations in general economic conditions, and the risks set forth throughout this Report, including the risks set forth under Part I, “Item 1A, Risk Factors”. Readers are cautioned not to place undue reliance on these forward-looking statements, which are based on current expectations and reflect management's opinions only as of the date hereof. These forward-looking statements speak only as of the date of this Report. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any changes in events, conditions or circumstances on which any such statement is based.

All references to “Inphi,” “we,” “us” or “our” mean Inphi Corporation.

Inphi®, iMB™ and the Inphi logo are trademarks or service marks owned by Inphi. All other trademarks, service marks and trade names appearing in this report are the property of their respective owners.

Overview

Our Company

We are a fabless provider of high-speed analog and mixed signal semiconductor solutions for the communications, datacenter and computing markets. We often refer to our business as covering various data transport segments from “fiber to memory”. Our analog and mixed signal semiconductor solutions provide high signal integrity at leading-edge data speeds while reducing system power consumption. Our semiconductor solutions are designed to address bandwidth bottlenecks in networks, maximize throughput and minimize latency in computing environments and enable the rollout of next generation communications, datacenter and computing infrastructures. Our solutions provide a vital high-speed interface between analog signals and digital information in high-performance systems such as telecommunications transport systems, enterprise networking equipment, datacenters and enterprise servers, storage platforms, test and measurement equipment and military systems. We provide 40G and 100G high-speed analog semiconductor solutions for the communications market and high-speed memory interface solutions for the computing market.

On October 3, 2014, we completed the acquisition of Cortina Systems, Inc. including its high-speed interconnect and optical transport product lines (Cortina) for approximately \$52.5 million in cash and approximately 5.3 million shares of our common stock in accordance with the Agreement and Plan of Merger dated July 30, 2014 as amended by Amendment No. 1 to the Agreement and Plan of Merger dated September 25, 2014. We acquired Cortina to expand the Company’s market share in high-speed optical and networking interconnects.

We leverage our proprietary high-speed analog and mixed signal processing expertise and our deep understanding of system architectures to address data bottlenecks in current and emerging communications, enterprise network, computing and storage architectures. We develop these solutions as a result of our competitive strengths, including our system-level simulation capabilities, analog design expertise, strong relationships with industry leaders, extensive broad process technology experience and high-speed package modeling and design expertise. We use our core technology and strength in high-speed analog design to enable our customers to deploy next generation communications and computing systems that operate with high performance at high speed. We believe we are at the forefront of developing semiconductor solutions that deliver 100G speeds throughout the network infrastructure, including core, metro and the datacenter. Furthermore, our analog signal processing expertise enables us to improve throughput in computing systems. For example, some of our computing products enable up to four times the memory capacity on server platforms while using the current generation of memory devices.

We have ongoing, informal collaborative discussions with industry and technology leaders such as Advanced Micro Devices, Inc. (AMD), Alcatel-Lucent, ARM Ltd., Ciena Corporation, Cisco Systems, Inc., Huawei Technologies Co., Ltd., Juniper Networks Inc., Intel Corporation, Micron Technology, Inc., Samsung and SK Hynix Inc. to design architectures and products that solve bandwidth bottlenecks in existing and next generation communications and computing systems. Although, we generally do not have any formal collaboration agreements with these entities, we often engage in informal discussions with these entities with respect to anticipated technological challenges, next generation customer requirements and industry conventions and standards. We help define industry conventions and standards within the markets we target by collaborating with technology leaders, original equipment manufacturers or OEMs, systems manufacturers and standards bodies. Our products are designed into systems sold by OEMs, including Alcatel-Lucent, Ciena, Cisco, Dell Inc., EMC Corporation, H3C Technologies, Hewlett-Packard Company, Huawei, International Business Machines Corporation (IBM), Juniper and Oracle Corporation. We believe we are one of a limited number of suppliers to these OEMs for the type of products we sell, and in some cases we may be the sole supplier for certain applications. We sell both directly to these OEMs and to other intermediary systems or module manufacturers that, in turn, sell to these OEMs.

Our Business

Our semiconductor solutions leverage our deep understanding of high-speed analog and mixed signal processing and our system architecture knowledge to address data bottlenecks in current and emerging network and datacenter architectures. We design and develop our products for the communications and computing markets, which typically have two to three year design cycles, and product life cycles of five or more years. We believe our leadership position in developing high-speed analog semiconductors is a result of the following core strengths:

System-Level Simulation Capabilities. We design our high-speed analog semiconductor solutions to be critical components in complex systems. In order to understand and solve system problems, we work closely with systems vendors to develop proprietary component, channel and system simulation models. We use these proprietary simulation and validation tools to accurately predict system performance prior to fabricating the semiconductor or alternately, to identify and optimize critical semiconductor parameters to satisfy customer system requirements. We

use these simulation and validation capabilities to reduce our customers' time to market and engineering investments, thus enabling us to establish differentiated design relationships with our customers.

Analog Design Expertise. We believe that we are a leader in developing broadband analog semiconductors operating at high frequencies of up to 100 GHz. High-speed analog circuit design is extremely challenging because, as frequencies increase, semiconductors are increasingly sensitive to temperature, power supply noise, process variation and interaction with neighboring circuit elements. Development of components that work robustly at high frequencies requires an understanding of analog circuit design, including electromagnetic theory and practical experience in implementation and testing. Our analog design expertise has enabled us to design and commercially ship several first in the world technologies including the first 100G linear transimpedance amplifier, or TIA, that is now being widely deployed in volume globally in Long Haul networking infrastructures. We also launched the industry's first complementary metal oxide semiconductor, or CMOS, based 100G physical layers or PHYs and clock and data recovery, or CDRs, for Ethernet and optical transport network applications. These high speed serial PHYs, are designed in a generic CMOS process to target much lower power compared to silicon germanium or SiGe based products, while reducing the design footprint and improving manufacturability.

Strong Relationships with Industry Leaders. We develop many of our high-speed analog semiconductor solutions for applications and systems that are driven by industry leaders in the communications, datacenter and computing markets. Through our established relationships with industry leaders, we have repeatedly demonstrated the ability to address their technological challenges. As a result, we are designed into several of their current systems and believe we are well-positioned to develop high-speed analog semiconductor solutions for their emerging architectures. For instance, our high-speed memory interface designs have been validated for Intel's Xeon® Core i7® and next generation platforms. We have ongoing, informal collaborative discussions with communication and networking companies such as Alcatel-Lucent, Cisco, Ciena, Huawei, and Juniper, among others to address their next generation 100G efforts. Specifically, we engage in informal discussions with these entities with respect to anticipated technological challenges, next generation customer requirements and industry conventions and standards. As a result of our development efforts with industry leaders, we help define industry conventions and standards within the markets we target by collaborating with technology leaders, OEMs and systems manufacturers, as well as standards bodies such as the Joint Electronic Device Engineering Councils, or JEDEC, and the Institute of Electrical and Electronic Engineers, or IEEE, and the Optical Internetworking Forum, or OIF, to establish industry standards.

Broad Process Technology. We employ process technology experts, device technologists and circuit designers who have extensive experience in many process technologies including CMOS, SiGe and III-V technologies such as gallium arsenide, or GaAs, or indium phosphide, or InP. We have developed specific internal models and design kits for each process to support a uniform design methodology across all of our semiconductor solutions. For example, our products using 40 nanometer CMOS technology require development of accurate models for sub-circuits such as integrated phase lock loop, or PLLs, varactors and inductors. As another example, for III-V materials-based processes, in-house model development is a necessity and we believe also provides a substantial competitive advantage because these processes have complex material and device interactions. Combined with our fabless manufacturing strategy, our design expertise, proprietary model libraries and uniform design methodology allow us to use the best possible materials and substrates to design and develop our semiconductor solutions. We believe that our ability to design high-speed analog semiconductors in a wide range of materials and process technologies allows us to provide superior performance, power, cost and reliability for a specific set of market requirements.

High-Speed Package Modeling and Design. We have developed deep expertise in high-speed package modeling and design, since introducing the first high-speed 50 GHz MUX and DEMUX product in 2001. At high frequencies, the interaction between an analog device, its package and the external environment can significantly affect product performance. Accurately modeling and developing advanced packaging allows semiconductor solutions to address this challenge. Due to the advanced nature of this work, there is a limited supply of engineers with experience in high-speed package modeling and design, and therefore, this required expertise can be difficult to acquire for companies that have not invested in developing such a skill set. We have developed an infrastructure to simulate electrical, mechanical and thermal properties of devices and packages that we integrate within our semiconductor design process and implement at our third-party packaging providers. Modeling is an inherently iterative process, and since our model libraries are used extensively by our circuit designers, the accuracy and value of these models increases over time. Our current packaging and modeling techniques enable us to deliver semiconductors that are energy efficient, offer high-speed processing and enable advanced signal integrity, all in a small footprint.

We believe that our system-level simulation capabilities, our analog design and broad process technology design capabilities as well as our strengths in packaging enable us to differentiate ourselves by delivering advanced high-speed analog signal processing solutions. For example, we believe we are the first vendor who has successfully commercialized 100G Ethernet PHYs and CDRs in standard CMOS process. Within the server market, we have applied our analog signal processing expertise to develop our isolation memory buffer, or iMB™ technology, which is designed to expand the memory capacity in existing server and computing platforms. Adoption of the iMB™ allows up to four times the memory capacity to be installed in a server platform, while using the current generation of memory devices.

We believe the key benefits that our solutions provide to our customers are as follows:

High Performance. Our high-speed analog semiconductor solutions are designed to meet the specific technical requirements of our customers in their respective end-markets. In many cases, our close design relationships and deep engineering expertise put us in a position where we are one of a limited group of semiconductor vendors that can provide the necessary solution. For instance, in the broadband communications market, we believe our products achieve the highest signal integrity and attain superior signal transmission distance at required error-free or low error

rates. In the computing and datacenter market, we believe our products achieve industry leading data transfer rates at the smallest die size.

Low Power and Small Footprint. In each of the end markets that we serve, the power budget of the overall system is a key consideration for systems designers. Power consumption greatly impacts system operation cost, footprint and cooling requirements, and is increasingly becoming a point of focus for our customers. We believe that our high speed analog signal processing solutions enable our customers to implement system architectures that reduce overall system power consumption. We also believe that, at high frequencies, our high-speed analog semiconductor devices typically consume less power than competitors' standard designs, which often incorporate power-consuming digital signal processing to perform data transfer functions, thereby further reducing overall system power consumption. In addition, in many of our applications, we are able to design and deliver semiconductors that have a smaller footprint and therefore reduce the overall system size.

Faster Time to Market. Our customers compete in markets that require high-speed, reliable semiconductors that can be integrated into their systems as soon as new market opportunities develop. To meet our customers' time-to-market requirements, we work closely with them early in their design cycles and are actively involved in their development processes. Over the past ten years, we have developed methodologies and simulation environments that accurately predict the behavior of complex integrated circuits within various communications systems. In addition, we have developed an extensive internal library of proven building block circuits such as amplifiers, phase frequency detectors and transmitters that are reused to shorten design cycles and reduce risk.

Products

Our products address bandwidth bottlenecks throughout the network communications and computing infrastructure markets – from “fiber to memory”, as depicted in the illustration below. For instance, our products find application in devices such as dense wavelength division multiplexers that enable core and aggregation networks as well as less complex optical interface links within data center communication infrastructures. In addition, our high-speed memory interface products can be found in servers where they allow CPUs to better utilize available memory resources.

As of December 31, 2014, we have a wide range product portfolio, including products that have commercially shipped, products for which we have shipped engineering samples and products under development, that perform a wide range of functions such as amplifying, encoding, multiplexing, demultiplexing, retiming and buffering data and clock signals at speeds up to 100 Gbps. These products are key enablers for servers, routers, switches, storage and other equipment that process, store and transport data traffic. We introduced 15 and 20 new products in 2014 and 2013, respectively. The acquisition of Cortina added approximately 130 products in our portfolio which includes high-speed interconnect and optical transport products. We design and develop our products for the communications and computing markets, which typically have two to three year design cycles, and product life cycles as long as five years or more.

In 2011, we began to ship in production volume a new “ultra-low voltage” version of our integrated PLL and register buffer, which is shipping in the form of product number INSSTE32882UV-GS02, or the GS02UV product. Sales of the GS02UV product comprised 15%, 39% and 45% of our total revenue in 2014, 2013 and 2012, respectively. In 2012, we introduced and began to ship in commercial volume a dual, differential input linear transimpedance/variable-gain amplifier that we identify as product number IN3250TA-SO2D. Sales of

IN3250TA-SO2D product comprised 14% of our total revenue in 2014. In 2010, we introduced and began to ship in commercial volume a dual, differential linear transimpedance amplifier which we identify as product number 2850TA-SO1D. Sales of 2850TA-SO1D product comprised 10% and 14% of our total revenue in 2013 and 2012, respectively. There were no other products that generated more than 10% of our total revenue in 2014, 2013 or 2012.

Customers

We sell our products directly to OEMs and indirectly to OEMs through module manufacturers, original design manufacturers or ODMs and sub-systems providers. We work closely with technology leaders, including microprocessor, memory vendors, communications equipment and optical module companies, to design architectures and products that help solve bandwidth bottlenecks in and between systems. These technology leaders often design our products into reference designs, which they provide to their customers and suppliers. For example, in the server market we work closely with major CPU manufacturers to address the bottleneck between the CPU and the increasing amount of memory attached to it. These CPU manufacturers then provide their server CPU customers and memory module partners with a validation report, including validation of our memory interface products. These server OEMs and memory module companies then design our memory interface products into their production systems. Ultimately, our sales into these servers are to memory module companies, including Micron, Samsung, SK Hynix and others. In the networking market, we work closely with OEMs to deliver high performance communication links. These OEMs design our product into their systems and then require their ODM and electronics manufacturing services suppliers to purchase and use that specific product from us. We also work directly with optical module manufacturers to design our products into their modules, which they sell to OEMs.

We work closely with our customers throughout design cycles that often last two to three years and we are able to develop long-term relationships with them as our technology becomes embedded in their products. As a result, we believe we are well-positioned to not only be designed into their current systems, but also to continually develop next generation high-speed analog semiconductor solutions for their future products. During the year ended December 31, 2014, we sold our products to more than 160 customers.

Sales to customers in Asia accounted for 71%, 71% and 65% of our total revenue in 2014, 2013 and 2012, respectively. Because many of our customers or their OEM manufacturers are located in Asia, we anticipate that a majority of our future revenue will continue to come from sales to that region. Although a large percentage of our sales are made to customers in Asia, we believe that a significant number of the systems designed by these customers and incorporating our semiconductor products are then sold to end users outside Asia.

We currently rely, and expect to continue to rely, on a limited number of customers for a significant portion of our revenue. In the year ended December 31, 2014, sales to Samsung, including its subcontractors accounted for 18% of our total revenue, respectively, and our 10 largest customers collectively accounted for 61% of our total revenue. In the year ended December 31, 2013, sales to Samsung, including its subcontractors and SK Hynix, including its subcontractor accounted for 20% and 16% of our total revenue, respectively, and our 10 largest customers collectively accounted for 70% of our total revenue. In addition, sales directly and through distributors to Micron accounted for 11% of our total revenue in the year ended December 31, 2013. No other single customer directly or indirectly accounted for more than 10% of our total revenue in 2014 or 2013.

Sales and Marketing

Our design cycle from initial engagement to volume shipment is typically two to three years, with product life cycles in the markets we serve ranging from two to 10 years or more. For many of our products, early engagement with our customers' technical staff is necessary for success. To ensure an adequate level of early engagement, our application and development engineers work closely with our customers to identify and propose solutions to their systems challenges.

In addition to our direct customers, we work closely with technology leaders such as Intel, ARM and AMD for the computing and storage markets and Alcatel-Lucent, Ciena, Cisco, Huawei and Juniper for the networking and communications market to anticipate and solve next generation challenges facing our customers. As part of the sales and product development process, we often design our products in close collaboration with these industry leaders and help define their architecture. We also participate actively in setting industry standards with organizations such as IEEE, JEDEC and OIF to have a voice in the definition of future market trends.

We sell our products worldwide through multiple channels, including our direct sales force and a network of sales representatives and distributors. For the year ended December 31, 2014, 84% of our revenue was generated by our direct sales team and third-party sales representatives. We operate direct sales offices in Japan, Korea, Singapore, and the United States and employ sales personnel that cover our direct customers and manage our channel partners. We utilize ten sales representatives and/or distributors in Asia, three distributors in Europe, two distributors in Israel, two distributors in Japan and seven sales representatives and three distributors in North America. Our channel network includes more than 150 sales professionals to support our products and customers, including 12 in Japan, 40 in Asia (other than Japan), 50 in North America and 20 in Europe, the Middle East and Africa, or EMEA. All of these sales professionals are sales agents and are employed by our distributors and sales representatives except for 30 sales agents who are our direct employees, including four in Japan, 13 in Asia, ten in North America and three in EMEA. We believe these distributors and sales representatives have the requisite technical experience in our target markets and are able to leverage existing relationships and understanding of our customers' products to effectively sell our products. Given the breadth of our target markets, customers and products, we provide our direct and indirect sales teams with regular training and share product information with our customers and sales team using web-based tools.

Manufacturing

We operate a fables business model and use third-party foundries and assembly and test manufacturing contractors to manufacture, assemble and test our semiconductor products. We also inspect and test parts in our Westlake Village, California, facility. This outsourced manufacturing approach allows us to focus our resources on the design, sale and marketing of our products. In addition, we believe outsourcing many of our manufacturing and assembly activities provides us the flexibility needed to respond to new market opportunities, simplifies our operations and significantly reduces our capital requirements.

We subject our third-party manufacturing contractors to qualification requirements in order to meet the high quality and reliability standards required of our products. We carefully qualify each of our partners and processes before applying the technology to our products. Our engineers work closely with our foundries and other contractors to increase yield, lower manufacturing costs and improve product quality.

Wafer Fabrication. We currently utilize a wide range of semiconductor processes to develop and manufacture our products. Each of our foundries tends to specialize in a particular semiconductor wafer process technology. We choose the semiconductor process and foundry that we believe provides the best combination of performance attributes for any particular product. For most of our products, we utilize a single foundry for semiconductor wafer production. Our principal foundries are Taiwan Semiconductor Manufacturing Company Ltd., or TSMC, in Taiwan, Sumitomo Electric Device Innovations Inc., or SEDI, in Japan, WIN Semiconductors Corp. in Taiwan, and TowerJazz Semiconductor Ltd. in North America.

Package and Assembly. Upon the completion of processing at the foundry, the finished wafers are shipped to our third-party assemblers for packaging and assembly. Currently, our principal packaging and assembly contractors are Orient Semiconductor Electronics Ltd., or OSE in Taiwan, STATS ChipPAC Ltd. in Korea, Kyocera Corporation in North America and Japan, Signetics Corporation in Korea, Amkor Technology in Korea and ASEM Technology in Malaysia.

Test. At the last stage of integrated circuit production, our third-party test service providers test the packaged and assembled integrated circuits. Currently, OSE in Taiwan, Advanced Semiconductor Engineering or ASE in California, STATS ChipPAC in Korea, Evans Analytical Group or EAG in North America, Signetics Corporation in Korea, Amkor Technology in Korea, ASEM Technology in Malaysia and Presto Engineering in North America are our test partners. We also perform testing in our Westlake Village, California, facility.

We are committed to maintaining the highest level of quality in our products. Our objective is that our products meet all of our customer requirements, are delivered on-time and function reliably throughout their useful lives. As part of our total quality assurance program, our quality management system has been certified to ISO 9001:2008 standards. Our manufacturing partners are also ISO 9001 certified.

Research and Development

We focus our research and development efforts on developing products that address bandwidth bottlenecks in networks and minimize latency in computing environments. We believe that our continued success depends on our ability to both introduce improved versions of our existing products and to develop new products for the markets that we serve. We devote a portion of our resources to expanding our core technology including efforts in system-level simulation, high-speed analog design, supporting a broad range of process technologies and high-speed package modeling and design.

We develop models that are used as an input to a combination of proprietary and commercially available simulation tools. We use these tools to predict overall system performance based on the performance of our product. After our product is manufactured, we perform system measurements and refine our model set to improve the model's accuracy

and predictive ability. As a result, our models and simulation tools have improved over time and we have been able to very accurately predict overall system performance prior to fabricating a part.

We have assembled a core team of experienced engineers and systems designers in three design centers located in the United States, Singapore and United Kingdom. Our technical team typically has, on average, more than 23 years of industry experience with more than 60% having advanced degrees and more than 16% having Ph.Ds. These engineers and designers are involved in advancing our core technologies, as well as applying these core technologies to our product development activities across a number of areas including telecommunications transport systems, enterprise networking equipment, datacenters and enterprise servers, storage platforms, test and measurement and military systems. In 2014, 2013 and 2012, our research and development expenses were \$70.9 million, \$50.5 million and \$40.1 million, respectively.

Competition

The global semiconductor market in general, and the communications and computing markets in particular, are highly competitive. We expect competition to increase and intensify as more and larger semiconductor companies enter our markets. Increased competition could result in price pressure, reduced profitability and loss of market share, any of which could materially and adversely affect our business, revenue and operating results.

Currently, our competitors range from large, international companies offering a wide range of semiconductor products to smaller companies specializing in narrow markets. Our primary competitors include Analog Devices, Inc., Avago Technologies Ltd., Broadcom Corporation, Integrated Device Technology, Inc., or IDT, M/A-COM Technology Solutions Inc., Montage Technology Group Limited, RF Micro Devices, Inc., PMC-Sierra, Inc., Semtech Corp. and Texas Instruments Incorporated, as well as other smaller analog signal processing companies. We expect competition in our target markets to increase in the future as existing competitors improve or expand their product offerings.

Our ability to compete successfully depends on elements both within and outside of our control, including industry and general economic trends. During past periods of downturns in our industry, competition in the markets in which we operate intensified as our customers reduced their purchase orders. Many of our competitors are significantly larger, have greater financial, technical, marketing, distribution, customer support and other resources, are more established than we are, and have significantly better brand recognition and broader product offerings with which to withstand similar adverse economic or market conditions in the future. These developments may materially and adversely affect our current and future target markets and our ability to compete successfully in those markets.

We compete or plan to compete in different target markets to various degrees on the basis of a number of principal competitive factors, including:

• product performance;

• power budget;

• features and functionality;

• customer relationships;

• size;

• ease of system design;

• product roadmap;

• reputation and reliability;

• customer support; and

• price.

We believe we compete favorably with respect to each of these factors. We maintain our competitive position through our ability to successfully design, develop and market complex high-speed analog solutions for the customers that we serve.

Intellectual Property

We rely on a combination of intellectual property rights, including patents, trade secrets, copyrights and trademarks, and contractual protections, to protect our core technology and intellectual property. As of December 31, 2014, we had 393 issued and allowed patents in the United States and other patent applications pending in the United States. The 393 issued and allowed patents in the United States expire in the years beginning in 2015 through 2034. Many of our issued patents and pending patent applications relate to high-speed circuit and package designs.

We may not receive competitive advantages from any rights granted under our patents, and our patent applications may not result in the issuance of any patents. In addition, any future patent may be opposed, contested, circumvented, designed around by a third party or found to be unenforceable or invalidated. Others may develop technologies that are similar or superior to our proprietary technologies, duplicate our proprietary technologies or design around patents owned or licensed by us.

In addition to our own intellectual property, we also use third-party licensors for certain technologies embedded in our semiconductor solutions. These are typically non-exclusive contracts provided under paid-up licenses. These licenses are generally perpetual or automatically renewed for so long as we continue to pay any maintenance fees that may be due. To date, maintenance fees have not constituted a significant portion of our capital expenditures. We have entered into a number of licensing arrangements pursuant to which we license third-party technologies. We do not believe our business is dependent to any significant degree on any individual third-party license.

We generally control access to and use of our confidential information through the use of internal and external controls, including contractual protections with employees, contractors and customers. We rely in part on United States and international copyright laws to protect our mask work. All employees and consultants are required to execute confidentiality agreements in connection with their employment and consulting relationships with us. We also require them to agree to disclose and assign to us all inventions conceived or made in connection with the employment or consulting relationship.

Despite our efforts to protect our intellectual property, unauthorized parties may still copy or otherwise obtain and use our software, technology or other information that we regard as proprietary intellectual property. In addition, we intend to expand our international operations, and effective patent, copyright, trademark and trade secret protection may not be available or may be limited in foreign countries.

The semiconductor industry is characterized by vigorous protection and pursuit of intellectual property rights and positions, which has resulted in protracted and expensive litigation for many companies. We have in the past received and, particularly as a public company, we expect that in the future we may receive, communications from various industry participants alleging our infringement of their patents, trade secrets or other intellectual property rights. Any lawsuits could subject us to significant liability for damages, invalidate our proprietary rights and harm our business and our ability to compete. Any litigation, regardless of success or merit, could cause us to incur substantial expenses, reduce our sales and divert the efforts of our technical and management personnel. In the event we receive an adverse result in any litigation, we could be required to pay substantial damages, seek licenses from third parties, which may not be available on reasonable terms or at all, cease sale of products, expend significant resources to develop alternative technology or discontinue the use of processes requiring the relevant technology.

Employees

At December 31, 2014, we employed 446 full-time equivalent employees, including 280 in research, product development and engineering, 64 in sales and marketing, 39 in general and administrative management and 63 in manufacturing engineering and operations. We consider relations with our employees to be good and have never experienced a work stoppage. None of our employees are either represented by a labor union or subject to a collective bargaining agreement.

Other

We were incorporated in Delaware in November 2000 as TCom Communications, Inc. and changed our name to Inphi Corporation in February 2001. Our principal executive offices are located at 2953 Bunker Hill Lane, Suite 300, Santa Clara, California 95054. Our telephone number at that location is (408) 217-7300. Our website address is www.inphi.com. Information on our website is not part of this report and should not be relied upon in determining whether to make an investment decision. The inclusion of our website address in this report does not include or incorporate by reference into this report any information on our website.

We electronically file our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, with the SEC. The public may read or copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is <http://www.sec.gov>. You may obtain a free copy of our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K and amendments to those reports with the SEC on our website.

Item 1A. Risk Factors

Risks Related to Our Business

Our revenue and operating results can fluctuate from period to period, which could cause our share price to fluctuate.

Our revenue and operating results have fluctuated in the past and may fluctuate from period to period in the future due to a variety of factors, many of which are beyond our control. Factors relating to our business that may contribute to these fluctuations include the following factors, as well as other factors described elsewhere in this report:

- the receipt, reduction or cancellation of orders by customers;

- fluctuations in the levels of component inventories held by our customers;
- the gain or loss of significant customers;

- market acceptance of our products and our customers' products;

- our ability to develop, introduce and market new products and technologies on a timely basis;

- the timing and extent of product development costs;

- new product announcements and introductions by us or our competitors;

- incurrence of research and development and related new product expenditures;

- fluctuations in sales by module manufacturers who incorporate our semiconductor solutions in their products, such as memory modules;

- cyclical fluctuations in our markets;

- fluctuations in our manufacturing yields;

- significant warranty claims, including those not covered by our suppliers;
- changes in our product mix or customer mix;
- intellectual property disputes; and
- loss of key personnel or the inability to attract qualified engineers.

As a result of these and other factors, the results of any prior quarterly or annual periods should not be relied upon as indications of our future revenue or operating performance. Fluctuations in our revenue and operating results could cause our share price to decline.

We have an accumulated deficit and have incurred net losses in the past. We may incur net losses in the future.

As of December 31, 2014, we had an accumulated deficit of \$89.2 million. We have incurred net losses in each year through 2008. We also generated net loss of \$22.6 million, \$13.2 million and \$20.7 million for the years ended December 31, 2014, 2013 and 2012, respectively. We generated net income of \$1.9 million for the year ended December 31, 2011. We may continue to incur net losses in the future.

We depend on a limited number of customers for a substantial portion of our revenue, and the loss of, or a significant reduction in orders from, one or more of our major customers could negatively impact our revenue and operating results. In addition, if we offer more favorable prices to attract or retain customers, our average selling prices and gross margins would decline.

For the year ended December 31, 2014, sales to Samsung, including its subcontractors, accounted for 18% of our total revenue, and our 10 largest customers collectively accounted for 61% of our total revenue. For the year ended December 31, 2013, sales to Samsung, including its subcontractors, and SK Hynix, including its subcontractor, accounted for 20% and 16% of our total revenue, respectively, and our 10 largest customers collectively accounted for 70% of our total revenue. In addition, sales directly and through distributors to Micron accounted for 11% of our total revenue in the year ended December 31, 2013. Some of our customers, including Samsung, SK Hynix and Micron, use our products primarily in high-speed memory devices. We believe our operating results for the foreseeable future will continue to depend on sales to a relatively small number of customers. In the future, these customers may decide not to purchase our products at all, may purchase fewer products than they did in the past or may alter their purchasing patterns.

In addition, our relationships with some customers may deter other potential customers who compete with these customers from buying our products. To attract new customers or retain existing customers, we may offer these customers favorable prices on our products. In that event, our average selling prices and gross margins would decline. The loss of a key customer, a reduction in sales to any key customer or our inability to attract new significant customers could negatively impact our revenue and materially and adversely affect our results of operations.

We do not have long-term purchase commitments from our customers and if our customers cancel or change their purchase commitments, our revenue and operating results could suffer.

Substantially all of our sales to date, including sales to Samsung, SK Hynix and Micron, have been made on a purchase order basis. We do not have any long-term commitments with any of our customers. As a result, our customers may cancel, change or delay product purchase commitments with little or no notice to us and without penalty. This in turn could cause our revenue to decline and materially and adversely affect our results of operations.

We may face claims of intellectual property infringement, which could be time-consuming, costly to defend or settle and result in the loss of significant rights and which could harm our relationships with our customers and distributors.

The semiconductor industry is characterized by companies that hold patents and other intellectual property rights and that vigorously pursue, protect and enforce intellectual property rights. From time to time, third parties may assert against us and our customers and distributors their patent and other intellectual property rights to technologies that are important to our business.

Claims that our products, processes or technology infringe third-party intellectual property rights, regardless of their merit or resolution, could be costly to defend or settle and could divert the efforts and attention of our management and technical personnel. For example, Netlist, Inc. filed suit against us in the United States District Court, Central District of California, in September 2009, alleging that our iMB™ and certain other memory module components infringe three of Netlist's patents. For more details, see Part I, "Item 3, Legal Proceedings."

Infringement claims also could harm our relationships with our customers or distributors and might deter future customers from doing business with us. We do not know whether we will prevail in these proceedings given the complex technical issues and inherent uncertainties in intellectual property litigation. If any pending or future proceedings result in an adverse outcome, we could be required to:

- cease the manufacture, use or sale of the infringing products, processes or technology;

- pay substantial damages for infringement;

- expend significant resources to develop non-infringing products, processes or technology, which may not be successful;

- license technology from the third-party claiming infringement, which license may not be available on commercially reasonable terms, or at all;

- cross-license our technology to a competitor to resolve an infringement claim, which could weaken our ability to compete with that competitor; or
 - pay substantial damages to our customers or end users to discontinue their use of or to replace infringing technology sold to them with non-infringing technology, if available.

Any of the foregoing results could have a material adverse effect on our business, financial condition and results of operations.

Winning business is subject to lengthy competitive selection processes that require us to incur significant expenditures prior to generating any revenue or without any guarantee of any revenue related to this business. Even if we begin a product design, a customer may decide to cancel or change its product plans, which could cause us to generate no revenue from a product. If we fail to generate revenue after incurring substantial expenses to develop our products, our business and operating results would suffer.

We are focused on winning more competitive bid processes, known as “design wins,” that enable us to sell our high-speed analog semiconductor solutions for use in our customers’ products. These selection processes typically are lengthy and can require us to incur significant design and development expenditures and dedicate scarce engineering resources in pursuit of a single customer opportunity. We may not win the competitive selection process and may never generate any revenue despite incurring significant design and development expenditures. Failure to obtain a design win could prevent us from offering an entire generation of a product. This could cause us to lose revenue and require us to write off obsolete inventory, and could weaken our position in future competitive selection processes. Even after securing a design win, we may experience delays in generating revenue from our products as a result of the lengthy development cycle typically required. Our customers generally take a considerable amount of time to evaluate our products. Our design cycle from initial engagement to volume shipment is typically two to three years.

The delays inherent in these lengthy sales cycles increase the risk that a customer will decide to cancel, curtail, reduce or delay its product plans or adopt a competing design from one of our competitors, causing us to lose anticipated revenue. In addition, any delay or cancellation of a customer’s plans could materially and adversely affect our financial

results, as we may have incurred significant expense without generating any revenue. Finally, our customers' failure to successfully market and sell their products could reduce demand for our products and materially and adversely affect our business, financial condition and results of operations. If we were unable to generate revenue after incurring substantial expenses to develop any of our products, our business would suffer.

Our customers require our products and our third-party contractors to undergo a lengthy and expensive qualification process which does not assure product sales. If we are unsuccessful in or delayed in qualifying any of our products with a customer, our business and operating results would suffer.

Prior to purchasing our products, our customers require that both our products and our third-party contractors undergo extensive qualification processes, which involve testing of our products in the customers' systems, as well as testing for reliability. This qualification process may continue for several months. However, qualification of a product by a customer does not assure any sales of the product to that customer. Even after successful qualification and sales of a product to a customer, a subsequent revision in our third party contractors' manufacturing process or our selection of a new supplier may require a new qualification process with our customers, which may result in delays and in our holding excess or obsolete inventory. After our products are qualified, it can take several months or more before the customer commences volume production of components or systems that incorporate our products. Despite these uncertainties, we devote substantial resources, including design, engineering, sales, marketing and management efforts, to qualifying our products with customers in anticipation of sales. If we are unsuccessful or delayed in qualifying any of our products with a customer, sales of those products to the customer may be precluded or delayed, which may impede our growth and cause our business to suffer.

The complexity of our products could result in undetected defects and we may be subject to warranty claims and product liability, which could result in a decrease in customers and revenue, unexpected expenses and loss of market share. In addition, our product liability insurance may not adequately cover our costs arising from products defects or otherwise.

Our products are sold as components or as modules for use in larger electronic equipment sold by our customers. A product usually goes through an intense qualification and testing period performed by our customers before being used in production. We primarily outsource our product testing to third parties and also perform some testing in our Westlake Village, California, facility. We inspect and test parts, or have them inspected and tested in order to screen out parts that may be weak or potentially suffer a defect incurred through the manufacturing process. From time to time, we are subject to warranty or product liability claims that may require us to make significant expenditures to defend these claims or pay damage awards. For example, in September 2010, we were informed of a claim related to repair and replacement costs in connection with shipments of over 4,000 integrated circuits made by us during the summer and fall of 2009. We assessed, provided and accumulated additional warranty reserves based on estimated, probable costs to replace these units. Based on our standard warranty provisions, we provided replacement parts to the customer for the known and suspected failures that had occurred. In June 2012, we entered into a settlement agreement with the customer in which we paid \$1.75 million in July 2012.

Generally, our agreements seek to limit our liability to the replacement of the part or to the revenue received for the product, but these limitations on liability may not be effective or sufficient in scope in all cases. If a customer's equipment fails in use, the customer may incur significant monetary damages including an equipment recall or associated replacement expenses, as well as lost revenue. The customer may claim that a defect in our product caused the equipment failure and assert a claim against us to recover monetary damages. The process of identifying a defective or potentially defective product in systems that have been widely distributed may be lengthy and require significant resources. We may test the affected product to determine the root cause of the problem and to determine appropriate solutions. We may find an appropriate solution or a temporary fix while a permanent solution is being determined. If we are unable to determine the root cause, find an appropriate solution or offer a temporary fix, we may delay shipment to customers. As a result, we may incur significant replacement costs and contract damage claims from our customers as well as harm to our reputation. In certain situations, circumstances might warrant that we consider incurring the costs or expense related to a recall of one of our products in order to avoid the potential claims that may be raised should the customer reasonably rely upon our product only to suffer a failure due to a design or manufacturing process defect. Defects in our products could harm our relationships with our customers and damage our reputation. Customers may be reluctant to buy our products, which could harm our ability to retain existing customers and attract new customers and our financial results. In addition, the cost of defending these claims and satisfying any arbitration award or judicial judgment with respect to these claims could harm our business prospects and financial condition. Although we carry product liability insurance, this insurance may not adequately cover our costs arising from defects in our products or otherwise.

We rely on our relationships with industry and technology leaders to enhance our product offerings and our inability to continue to develop or maintain such relationships in the future would harm our ability to remain competitive.

We develop many of our semiconductor products for applications in systems that are driven by industry and technology leaders in the communications and computing markets. We also work with OEMs, system manufacturers and standards bodies to define industry conventions and standards within our target markets. We believe these relationships enhance our ability to achieve market acceptance and widespread adoption of our products. If we are unable to continue to develop or maintain these relationships, our semiconductor solutions would become less desirable to our customers, our sales would suffer and our competitive position could be harmed.

If we fail to accurately anticipate and respond to market trends or fail to develop and introduce new or enhanced products to address these trends on a timely basis, our ability to attract and retain customers could be impaired and our competitive position could be harmed.

We operate in industries characterized by rapidly changing technologies and industry standards as well as technological obsolescence. We have developed products that may have long product life cycles of 10 years or more, as well as other products in more volatile high growth or rapidly changing areas, which may have shorter life cycles of only two to three years. We believe that our future success depends on our ability to develop and introduce new technologies and products that generate new sources of revenue to replace, or build upon, existing product revenue

streams that may be dependent upon limited product life cycles. If we are not able to repeatedly introduce, in successive years, new products that ship in volume, our revenue will likely not grow and may decline significantly and rapidly. In 2009, we successfully introduced and began to ship a new product in production which we identify as product number INSSTE32882-GS04, or the GS04 product, and which consists of an integrated PLL and register buffer. Sales of the GS04 product comprised 18% of our total revenue in 2010. In 2010, we also began to ship in production volume a “low voltage” version of our integrated PLL and register buffer, which is shipping in the form of product number INSSTE32882LV-GS02, or the GS02 product. Sales of the GS02 product comprised 38% and 32% of our total revenue in 2011 and 2010, respectively. In 2011, we began to ship in production volume a new “ultra-low voltage” version of our integrated PLL and register buffer, which is shipping in the form of product number INSSTE32882UV-GS02, or the GS02UV product. Sales of the GS02UV product comprised 15%, 39% and 45% of our total revenue in 2014, 2013 and 2012, respectively. In 2010, we introduced and began to ship in commercial volume a dual, differential linear transimpedance amplifier that we identify as product number 2850TA-SO1D. Sales of 2850TA-SO1D product comprised 10% and 14% of our total revenue in 2013 and 2012, respectively. In 2012, we introduced and began to ship in commercial volume a dual, differential input linear transimpedance/variable-gain amplifier that we identify as product number IN3250TA-SO2D. Sales of IN3250TA-SO2D product comprised 14% of our total revenue in 2014. There were no other products that generated more than 10% of our total revenue in 2014, 2013 or 2012.

The GS02 and GS04 products matured in 2012 and 2011, respectively and as a result, sales of both products declined and were supplanted in part by newer parts which we developed. This underscores the importance of the need for us to continually develop and introduce new products to diversify our revenue base as well as generate new revenue to replace and build upon the success of previously introduced products which may be rapidly maturing.

To compete successfully, we must design, develop, market and sell new or enhanced products that provide increasingly higher levels of performance and reliability while meeting the cost expectations of our customers. The introduction of new products by our competitors, the delay or cancellation of a platform for which any of our semiconductor solutions are designed, the market acceptance of products based on new or alternative technologies or the emergence of new industry standards could render our existing or future products uncompetitive from a pricing standpoint, obsolete and otherwise unmarketable. Our failure to anticipate or timely develop new or enhanced products or technologies in response to technological shifts could result in decreased revenue and our competitors winning design wins. In particular, we may experience difficulties with product design, manufacturing, marketing or certification that could delay or prevent our development, introduction or marketing of new or enhanced products. Although we believe our products are fully compliant with applicable industry standards, proprietary enhancements may not in the future result in full conformance with existing industry standards under all circumstances. Due to the interdependence of various components in the systems within which our products and the products of our competitors operate, customers are unlikely to change to another design, once adopted, until the next generation of a technology. As a result, if we fail to introduce new or enhanced products that meet the needs of our customers or penetrate new markets in a timely fashion, and our designs do not gain acceptance, we will lose market share and our competitive position, very likely on an extended basis, and operating results will be adversely affected.

If sufficient market demand for 100G solutions does not develop or develops more slowly than expected, or if we fail to accurately predict market requirements or market demand for 100G solutions, our business, competitive position and operating results would suffer.

We are currently investing significant resources to develop semiconductor solutions supporting 100G data transmission rates in order to increase the number of such solutions in our product line. If we fail to accurately predict market requirements or market demand for 100G semiconductor solutions, or if our 100G semiconductor solutions are not successfully developed or competitive in the industry, our business will suffer. If 100G networks are deployed to a lesser extent or more slowly than we currently anticipate, we may not realize any benefits from our investment. As a result, our business, competitive position, market share and operating results would suffer.

Our target markets may not grow or develop as we currently expect and are subject to market risks, any of which could materially harm our business, revenue and operating results.

To date, a substantial portion of our revenue has been attributable to demand for our products in the communications and computing markets and the growth of these overall markets. These markets have fluctuated in size and growth in

recent times. Our operating results are impacted by various trends in these markets. These trends include the deployment and broader market adoption of next generation technologies, such as 100G and 100Gbe CMOS CDR and Serdes, in communications and enterprise networks, timing of next generation network upgrades, the introduction and broader market adoption of next generation server platforms, timing of enterprise upgrades and the introduction and deployment of high-speed memory interfaces in computing platforms. We are unable to predict the timing or direction of the development of these markets with any accuracy. In addition, because some of our products are not limited in the systems or geographic areas in which they may be deployed, we cannot always determine with accuracy how, where or into which applications our products are being deployed. If our target markets do not grow or develop in ways that we currently expect, demand for our semiconductor products may decrease and our business and operating results could suffer.

We rely on a limited number of third parties to manufacture, assemble and test our products, and the failure to manage our relationships with our third-party contractors successfully could adversely affect our ability to market and sell our products and our reputation. Our revenue and operating results would suffer if these third parties fail to deliver products or components in a timely manner and at reasonable cost or if manufacturing capacity is reduced or eliminated as we may be unable to obtain alternative manufacturing capacity.

We operate an outsourced manufacturing business model. As a result, we rely on third-party foundry wafer fabrication and assembly and test capacity. We also perform testing in our Westlake Village, California, facility. We generally use a single foundry for the production of each of our various semiconductors. Currently, our principal foundries are SEDI, TSMC, TowerJazz Semiconductor Ltd., and WIN Semiconductors. We also use third-party contract manufacturers for a significant majority of our assembly and test operations, including Kyocera, OSE, ASE, Presto, EAG, AIC and STATS ChipPAC.

Relying on third-party manufacturing, assembly and testing presents significant risks to us, including the following:

- failure by us, our customers or their end customers to qualify a selected supplier;

- capacity shortages during periods of high demand;
- reduced control over delivery schedules and quality;
- shortages of materials;
- misappropriation of our intellectual property;
- limited warranties on wafers or products supplied to us; and
- potential increases in prices.

The ability and willingness of our third-party contractors to perform is largely outside our control. If one or more of our contract manufacturers or other outsourcers fails to perform its obligations in a timely manner or at satisfactory quality levels, our ability to bring products to market and our reputation could suffer. For example, if that manufacturing capacity is reduced or eliminated at one or more facilities, including as a response to the recent worldwide decline in the semiconductor industry, or any of those facilities are unable to keep pace with the growth of our business, we could have difficulties fulfilling our customer orders and our revenue could decline. In addition, if these third parties fail to deliver quality products and components on time and at reasonable prices, we could have difficulties fulfilling our customer orders, our revenue could decline and our business, financial condition and results of operations would be adversely affected.

Additionally, as many of our fabrication and assembly and test contractors are located in the Pacific Rim region, principally in Taiwan, our manufacturing capacity may be similarly reduced or eliminated due to natural disasters, political unrest, war, labor strikes, work stoppages or public health crises, such as outbreaks of H1N1 flu. This could cause significant delays in shipments of our products until we are able to shift our manufacturing, assembly or test from the affected contractor to another third-party vendor. There can be no assurance that alternative capacity could be obtained on favorable terms, if at all.

Our costs may increase substantially if the wafer foundries that supply our products do not achieve satisfactory product yields or quality.

The wafer fabrication process is an extremely complicated process where the slightest changes in the design, specifications or materials can result in material decreases in manufacturing yields or even the suspension of production. From time to time, our third-party wafer foundries have experienced, and are likely to experience manufacturing defects and reduced manufacturing yields related to errors or problems in their manufacturing

processes or the interrelationship of their processes with our designs. In some cases, our third-party wafer foundries may not be able to detect these defects early in the fabrication process or determine the cause of such defects in a timely manner. We may incur substantial research and development expense for prototype or development stage products as we qualify the products for production.

Generally, in pricing our semiconductors, we assume that manufacturing yields will continue to increase, even as the complexity of our semiconductors increases. Once our semiconductors are initially qualified with our third-party wafer foundries, minimum acceptable yields are established. We are responsible for the costs of the wafers if the actual yield is above the minimum. If actual yields are below the minimum we are not required to purchase the wafers. The minimum acceptable yields for our new products are generally lower at first and increase as we achieve full production. Unacceptably low product yields or other product manufacturing problems could substantially increase the overall production time and costs and adversely impact our operating results on sales of our products. Product yield losses will increase our costs and reduce our gross margin. In addition to significantly harming our operating results and cash flow, poor yields may delay shipment of our products and harm our relationships with existing and potential customers.

We do not have any long-term supply contracts with our contract manufacturers or suppliers, and any disruption in our supply of products or materials could have a material adverse affect on our business, revenue and operating results.

We currently do not have long-term supply contracts with any of our third-party contract manufacturers. We make substantially all of our purchases on a purchase order basis, and our contract manufacturers are not required to supply us products for any specific period or in any specific quantity. We expect that it would take approximately nine to 12 months to transition from our current foundry or assembly services to new providers. Such a transition would likely require a qualification process by our customers or their end customers. We generally place orders for products with some of our suppliers several months prior to the anticipated delivery date, with order volumes based on our forecasts of demand from our customers. Accordingly, if we inaccurately forecast demand for our products, we may be unable to obtain adequate and cost-effective foundry or assembly capacity from our third-party contractors to meet our customers' delivery requirements, or we may accumulate excess inventories. On occasion, we have been unable to adequately respond to unexpected increases in customer purchase orders and therefore, were unable to benefit from this incremental demand. None of our third-party contract manufacturers have provided any assurance to us that adequate capacity will be available to us within the time required to meet additional demand for our products.

Our foundry vendors and assembly and test vendors may allocate capacity to the production of other companies' products while reducing deliveries to us on short notice. In particular, other customers that are larger and better financed than us or that have long-term agreements with our foundry vendor or assembly and test vendors may cause our foundry vendor or assembly and test vendors to reallocate capacity to those customers, decreasing the capacity available to us. We do not have long-term supply contracts with our third-party contract manufacturers and if we enter into costly arrangements with suppliers that include nonrefundable deposits or loans in exchange for capacity commitments, commitments to purchase specified quantities over extended periods or investment in a foundry, our operating results could be harmed. We may not be able to make any such arrangement in a timely fashion or at all, and any arrangements may be costly, reduce our financial flexibility, and not be on terms favorable to us. Moreover, if we are able to secure foundry capacity, we may be obligated to use all of that capacity or incur penalties. These penalties may be expensive and could harm our financial results. To date, we have not entered into such arrangements with our suppliers. If we need another foundry or assembly and test subcontractor because of increased demand, or if we are unable to obtain timely and adequate deliveries from our providers, we might not be able to cost effectively and quickly retain other vendors to satisfy our requirements.

Many of our customers depend on us as the sole source for a number of our products. If we are unable to deliver these products as the sole supplier or as one of a limited number of suppliers, our relationships with these customers and our business would suffer.

A number of our customers do not have alternative sources for our semiconductor solutions and depend on us as the sole supplier or as one of a limited number of suppliers for these products. Since we outsource our manufacturing to third-party contractors, our ability to deliver our products is substantially dependent on the ability and willingness of our third-party contractors to perform, which is largely outside our control. A failure to deliver our products in sufficient quantities or at all to our customers that depend on us as a sole supplier or as one of a limited number of suppliers may be detrimental to their business and, as a result, our relationship with the customer would be negatively impacted. If we are unable to maintain our relationships with these customers after such failure, our business and financial results may be harmed.

If we are unable to attract, train and retain qualified personnel, particularly our design and technical personnel, we may not be able to execute our business strategy effectively.

Our future success depends on our ability to attract and retain qualified personnel, including our management, sales and marketing, and finance, and particularly our design and technical personnel. We do not know whether we will be able to retain all of these personnel as we continue to pursue our business strategy. Historically, we have encountered difficulties in hiring qualified engineers because there is a limited pool of engineers with the expertise required in our field. Competition for these personnel is intense in the semiconductor industry. As the source of our technological and product innovations, our design and technical personnel represent a significant asset. The loss of the services of one or more of our key employees, especially our key design and technical personnel, or our inability to attract and retain qualified design and technical personnel, could harm our business, financial condition and results of operations.

We may not be able to effectively manage our growth, and we may need to incur significant expenditures to address the additional operational and control requirements of our growth, either of which could harm our business and operating results.

To effectively manage our growth, we must continue to expand our operational, engineering and financial systems, procedures and controls and to improve our accounting and other internal management systems. This may require substantial managerial and financial resources, and our efforts in this regard may not be successful. Our current systems, procedures and controls may not be adequate to support our future operations. If we fail to adequately manage our growth, or to improve our operational, financial and management information systems, or fail to effectively motivate or manage our new and future employees, the quality of our products and the management of our operations could suffer, which could adversely affect our operating results.

We face intense competition and expect competition to increase in the future. If we fail to compete effectively, it could have an adverse effect on our revenue, revenue growth rate, if any, and market share.

The global semiconductor market in general, and the communications and computing markets in particular, are highly competitive. We compete or plan to compete in different target markets to various degrees on the basis of a number of principal competitive factors, including product performance, power budget, features and functionality, customer relationships, size, ease of system design, product roadmap, reputation and reliability, customer support and price. We expect competition to increase and intensify as more and larger semiconductor companies enter our markets. Increased competition could result in price pressure, reduced profitability and loss of market share, any of which could materially and adversely affect our business, revenue and operating results.

Currently, our competitors range from large, international companies offering a wide range of semiconductor products to smaller companies specializing in narrow markets. Our primary competitors include Analog Devices, Inc., Avago Technologies Ltd., Broadcom Corporation, Integrated Device Technology, Inc., M/A-COM Technology Solutions Inc., Montage Technology Group Limited, PMC-Sierra, Inc., Semtech Corp., RF Micro Devices, Inc. and Texas Instruments Incorporated, as well as other analog signal processing companies. We expect competition in the markets in which we participate to increase in the future as existing competitors improve or expand their product offerings.

Our ability to compete successfully depends on elements both within and outside of our control, including industry and general economic trends. During past periods of downturns in our industry, competition in the markets in which we operate intensified as our customers reduced their purchase orders. Many of our competitors have substantially greater financial and other resources with which to withstand similar adverse economic or market conditions in the future. These developments may materially and adversely affect our current and future target markets and our ability to compete successfully in those markets.

We use a significant amount of intellectual property in our business. Monitoring unauthorized use of our intellectual property can be difficult and costly and if we are unable to protect our intellectual property, our business could be adversely affected.

Our success depends in part upon our ability to protect our intellectual property. To accomplish this, we rely on a combination of intellectual property rights, including patents, copyrights, trademarks and trade secrets in the United States and in selected foreign countries where we believe filing for such protection is appropriate. Effective protection of our intellectual property rights may be unavailable, limited or not applied for in some countries. Some of our products and technologies are not covered by any patent or patent application, as we do not believe patent protection of these products and technologies is critical to our business strategy at this time. A failure to timely seek patent protection on products or technologies generally precludes us from seeking future patent protection on these products or technologies. We cannot guarantee that:

- any of our present or future patents or patent claims will not lapse or be invalidated, circumvented, challenged or abandoned;
- our intellectual property rights will provide competitive advantages to us;
- our ability to assert our intellectual property rights against potential competitors or to settle current or future disputes will not be limited by our agreements with third parties;
- any of our pending or future patent applications will be issued or have the coverage originally sought;

- our intellectual property rights will be enforced in jurisdictions where competition may be intense or where legal protection may be weak;
- any of the trademarks, copyrights, trade secrets or other intellectual property rights that we presently employ in our business will not lapse or be invalidated, circumvented, challenged or abandoned; or
- we will not lose the ability to assert our intellectual property rights against or to license our technology to others and collect royalties or other payments.

In addition, our competitors or others may design around our protected patents or technologies. Effective intellectual property protection may be unavailable or more limited in one or more relevant jurisdictions relative to those protections available in the United States, or may not be applied for in one or more relevant jurisdictions. If we pursue litigation to assert our intellectual property rights, an adverse decision in any of these legal actions could limit our ability to assert our intellectual property rights, limit the value of our technology or otherwise negatively impact our business, financial condition and results of operations.

Monitoring unauthorized use of our intellectual property is difficult and costly. Unauthorized use of our intellectual property may have occurred or may occur in the future. Although we have taken steps to minimize the risk of this occurring, any such failure to identify unauthorized use and otherwise adequately protect our intellectual property would adversely affect our business. Moreover, if we are required to commence litigation, whether as a plaintiff or defendant, not only would this be time-consuming, but we would also be forced to incur significant costs and divert our attention and efforts of our employees, which could, in turn, result in lower revenue and higher expenses.

We also rely on contractual protections with our customers, suppliers, distributors, employees and consultants, and we implement security measures designed to protect our trade secrets. We cannot assure you that these contractual protections and security measures will not be breached, that we will have adequate remedies for any such breach or that our suppliers, employees or consultants will not assert rights to intellectual property arising out of such contracts.

In addition, we have a number of third-party patent and intellectual property license agreements. Some of these license agreements require us to make one-time payments or ongoing royalty payments. We cannot guarantee that the third-party patents and technology we license will not be licensed to our competitors or others in the semiconductor industry. In the future, we may need to obtain additional licenses, renew existing license agreements or otherwise replace existing technology. We are unable to predict whether these license agreements can be obtained or renewed or the technology can be replaced on acceptable terms, or at all.

Average selling prices of our products generally decrease over time, which could negatively impact our revenue and gross margins.

Our operating results may be impacted by a decline in the average selling prices of our semiconductors. If competition increases in our target markets, we may need to reduce the average unit price of our products in anticipation of competitive pricing pressures, new product introductions by us or our competitors and for other reasons. If we are unable to offset any reductions in our average selling prices by increasing our sales volumes or introducing new products with higher margins, our revenue and gross margins will suffer. To maintain our revenue and gross margins, we must develop and introduce new products and product enhancements on a timely basis and continually reduce our costs as well as our customers' costs. Failure to do so would cause our revenue and gross margins to decline.

We are subject to order and shipment uncertainties, and differences between our estimates of customer demand and product mix and our actual results could negatively affect our inventory levels, sales and operating results.

Our revenue is generated on the basis of purchase orders with our customers rather than long-term purchase commitments. In addition, our customers can cancel purchase orders or defer the shipments of our products under certain circumstances. Our products are manufactured using semiconductor foundries according to our estimates of

customer demand, which requires us to make separate demand forecast assumptions for every customer, each of which may introduce significant variability into our aggregate estimates. It is difficult for us to forecast the demand for our products, in part because of the complex supply chain between us and the end-user markets that incorporate our products. Due to our lengthy product development cycle, it is critical for us to anticipate changes in demand for our various product features and the applications they serve to allow sufficient time for product development and design. We have limited visibility into future customer demand and the product mix that our customers will require, which could adversely affect our revenue forecasts and operating margins. Moreover, because some of our target markets are relatively new, many of our customers have difficulty accurately forecasting their product requirements and estimating the timing of their new product introductions, which ultimately affects their demand for our products. Our failure to accurately forecast demand can lead to product shortages that can impede production by our customers and harm our customer relationships. Conversely, our failure to forecast declining demand or shifts in product mix can result in excess or obsolete inventory. For example, some of our customers may cancel purchase orders or delay the shipment of their products that incorporate our products as a result of component shortages they may experience due to the earthquakes and tsunami in Japan, or likewise with respect to the flooding in Thailand, which may result in excess or obsolete inventory and impact our sales and operating results. In addition, the rapid pace of innovation in our industry could also render significant portions of our inventory obsolete. Excess or obsolete inventory levels could result in unexpected expenses or increases in our reserves that could adversely affect our business, operating results and financial condition. In contrast, if we were to underestimate customer demand or if sufficient manufacturing capacity were unavailable, we could forego revenue opportunities, potentially lose market share and damage our customer relationships. In addition, any significant future cancellations or deferrals of product orders or the return of previously sold products due to manufacturing defects could materially and adversely impact our profit margins, increase our write-offs due to product obsolescence and restrict our ability to fund our operations.

We rely on third-party sales representatives and distributors to assist in selling our products. If we fail to retain or find additional sales representatives and distributors, or if any of these parties fail to perform as expected, it could reduce our future sales.

In 2014, we derived 84% of our total revenue from sales by our direct sales team and third-party sales representatives. In addition, in 2014 and 2013, approximately 16% of our sales were made through third-party distributors, respectively. Two of our distributors, which sell solely to Micron, accounted for 11% our total revenue in 2013. We are unable to predict the extent to which these third-party sales representatives and distributors will be successful in marketing and selling our products. Moreover, many of these third-party sales representatives and distributors also market and sell competing products, which may affect the extent to which they promote our products. Even where our relationships are formalized in contracts, our third-party sales representatives and distributors often have the right to terminate their relationships with us at any time. Our future performance will also depend, in part, on our ability to attract additional third-party sales representatives and distributors who will be able to market and support our products effectively, especially in markets in which we have not previously sold our products. If we cannot retain our current distributors or find additional or replacement third-party sales representatives and distributors, our business, financial condition and results of operations could be harmed. Additionally, if we terminate our relationship with a distributor, we may be obligated to repurchase unsold products. We record a reserve for estimated returns and price credits. If actual returns and credits exceed our estimates, our operating results could be harmed.

The facilities of our third-party contractors and distributors are located in regions that are subject to earthquakes and other natural disasters.

The facilities of our third-party contractors and distributors are subject to risk of catastrophic loss due to fire, flood or other natural or man-made disasters. A number of our facilities and those of our contract manufacturers are located in areas with above average seismic activity and also subject to typhoons and other Pacific storms. Several foundries that manufacture our wafers are located in Taiwan, Japan and California, and a majority of our third-party contractors who assemble and test our products are located in Asia. In addition, our headquarters are located in California. The risk of an earthquake in the Pacific Rim region or California is significant due to the proximity of major earthquake fault lines. Any catastrophic loss to any of these facilities would likely disrupt our operations, delay production, shipments and revenue and result in significant expenses to repair or replace the facility. In particular, any catastrophic loss at our California locations would materially and adversely affect our business.

We rely on third-party technologies for the development of our products and our inability to use such technologies in the future would harm our ability to remain competitive.

We rely on third parties for technologies that are integrated into our products, such as wafer fabrication and assembly and test technologies used by our contract manufacturers, as well as licensed architecture technologies. If we are unable to continue to use or license these technologies on reasonable terms, or if these technologies fail to operate properly, we may not be able to secure alternatives in a timely manner or at all, and our ability to remain competitive would be harmed. In addition, if we are unable to successfully license technology from third parties to develop future products, we may not be able to develop such products in a timely manner or at all.

Our business would be adversely affected by the departure of existing members of our senior management team and other key personnel.

Our success depends, in large part, on the continued contributions of our senior management team, in particular, the services of certain key personnel, including Dr. Loi Nguyen, one of our founders and our Vice President of Optical Interconnect. In February 2011, our Chief Technology Officer resigned and we promoted our Vice President of Engineering for New Business Initiatives to serve as our new Chief Technology Officer. Changes in our management team could negatively affect our operations and our relationships with our customers, employees and market leaders. In addition, we have not entered into non-compete agreements with members of our senior management team. The loss of any member of our senior management team or key personnel could harm our ability to implement our business strategy and respond to the rapidly changing market conditions in which we operate.

Potential future acquisitions could be difficult to integrate, divert attention of key personnel, disrupt our business, dilute stockholder value and impair our operating results.

As part of our business strategy, we have pursued and may continue to pursue acquisitions in the future that we believe will complement our business, semiconductor solutions or technologies. Any acquisition involves a number of risks, many of which could harm our business, including:

- difficulties in integrating the operations, technologies, products, existing contracts, accounting and personnel of the target company;
- realizing the anticipated benefits of any acquisition;
- difficulties in transitioning and supporting customers, if any, of the target company;
 - diversion of financial and management resources from existing operations;
- the price we pay or other resources that we devote may exceed the value we realize, or the value we could have realized if we had allocated the purchase price or other resources to another opportunity;
- potential loss of key employees, customers and strategic alliances from either our current business or the target company's business;
- assumption of unanticipated problems or latent liabilities, such as problems with the quality of the target company's products;
- inability to generate sufficient revenue to offset acquisition costs;
- dilutive effect on our stock as a result of any equity-based acquisitions;
- inability to successfully complete transactions with a suitable acquisition candidate; and
- in the event of international acquisitions, risks associated with accounting and business practices that are different from applicable U.S. practices and requirements.

Acquisitions also frequently result in the recording of goodwill and other intangible assets that are subject to potential impairments, which could harm our financial results. As a result, if we fail to properly evaluate acquisitions or investments, we may not achieve the anticipated benefits of any such acquisitions, and we may incur costs in excess of what we anticipate. The failure to successfully evaluate and execute acquisitions or investments or otherwise adequately address these risks could materially harm our business and financial results.

Our portfolio of marketable securities is significant and subject to market, interest and credit risk that may reduce its value.

We maintain a significant portfolio of marketable securities. Changes in the value of this portfolio could adversely affect our earnings. In particular, the value of our investments may decline due to increases in interest rates, downgrades of money market funds, U.S. Treasuries, municipal bonds, corporate bonds, certificates of deposit and asset backed securities included in our portfolio, instability in the global financial markets that reduces the liquidity of securities included in our portfolio, declines in the value of collateral underlying the asset-backed securities included in our portfolio and other factors. Each of these events may cause us to record charges to reduce the carrying value of our investment portfolio or sell investments for less than our acquisition cost. Although we attempt to mitigate these risks by investing in high quality securities and continuously monitoring our portfolio's overall risk profile, the value of our investments may nevertheless decline.

Tax benefits that we receive may be terminated or reduced in the future, which would increase our costs.

In 2010, we began to expand our international presence to take advantage of the opportunity to recruit additional engineering design talent, as well as to more closely align our operations geographically with our customers and suppliers in Asia. In certain international jurisdictions, we have also entered into agreements with local governments to provide us with, among other things, favorable local tax rates if certain minimum criteria are met. These agreements may require us to meet several requirements as to investment, headcount and activities to retain this status. We currently believe that we will be able to meet all the terms and conditions specified in these agreements. However, if adverse changes in the economy or changes in technology affect international demand for our products in an unforeseen manner or if we fail to otherwise meet the conditions of the local agreements, we may be subject to additional taxes, which in turn would increase our costs.

Changes in our effective tax rate may harm our results of operations. A number of factors may increase our future effective tax rates, including:

- the jurisdictions in which profits are determined to be earned and taxed;

Edgar Filing: INPHI Corp - Form 10-K

- the resolution of issues arising from tax audits with various tax authorities;
- changes in the measurement of our deferred tax assets and liabilities and in deferred tax valuation allowances;
- changes in the value of assets or services transferred or provided from one jurisdiction to another;
- adjustments to income taxes upon finalization of various tax returns;
- increases in expenses not deductible for tax purposes, including write-offs of acquired in-process research and development and impairments of goodwill in connection with acquisitions;
- changes in available tax credits;
- changes in tax laws or the interpretation of such tax laws, and changes in U.S. generally accepted accounting principles; and
 - a decision to repatriate non-U.S. earnings for which we have not previously provided for U.S. taxes.

We are subject to additional regulatory compliance requirements, including Section 404 of the Sarbanes-Oxley Act of 2002, as a result of being a public company and our management has limited experience managing a public company.

As a public company, we will incur significant legal, accounting and other expenses that we did not incur as a private company. Our management team and other personnel will need to devote a substantial amount of time to new compliance initiatives and we may not successfully or efficiently manage our transition into a public company. We expect rules and regulations such as the Sarbanes-Oxley Act of 2002 to increase our legal and finance compliance costs and to make some activities more time-consuming and costly. We will need to hire a number of additional employees with public accounting and disclosure experience in order to meet our ongoing obligations as a public company. For example, Section 404 of the Sarbanes-Oxley Act of 2002 requires that our management report on, and our independent registered public accounting firm attest to, the effectiveness of our internal control over financial reporting in our annual report on Form 10-K starting fiscal year ended December 31, 2011. Section 404 compliance has in the past and may continue to divert internal resources and require significant amount of time and effort to complete. If we fail to do so, or if in the future our Chief Executive Officer, Chief Financial Officer or independent registered public accounting firm determines that our internal controls over financial reporting are not effective as defined under Section 404, we could be subject to sanctions or investigations by The New York Stock Exchange, or NYSE, the Securities and Exchange Commission, or the SEC, or other regulatory authorities. Furthermore, investor perceptions of our company may suffer, and this could cause a decline in the market price of our stock. Irrespective of compliance with Section 404, any failure of our internal controls could have a material adverse effect on our stated results of operations and harm our reputation. If we are unable to implement these changes effectively or efficiently, it could harm our operations, financial reporting or financial results and could result in an adverse opinion on internal

controls from our independent auditors.

Risks Related to Cortina Acquisition

Future sales of shares by existing stockholders, including former Cortina stockholders, could cause our stock price to decline.

We filed a registration statement to register the shares issued in connection with the Cortina acquisition for sale into the public market by the selling stockholders. These shares, if sold in the market all at once or at about the same time, could depress the market price during the period the registration statement remains effective and also could affect our ability to raise equity capital.

We have pursued and may continue to pursue acquisition opportunities such as our acquisition of Cortina and may not realize the anticipated benefits of any such acquisitions, which in turn could harm our business and operating results.

We may be unable to successfully integrate Cortina's high-speed interconnect and optical transport business or realize the anticipated benefits of the acquisition. The successful integration of Cortina as well as the retention of personnel require significant attention from our management and could result in a diversion of resources from our existing business, which in turn could have an adverse effect on our business operations. We may not be successful in these efforts. We may not achieve the anticipated benefits of any acquired assets or businesses, such as Cortina, due to a number of factors including: unanticipated costs or liabilities associated with the acquisition, incurrence of acquisition-related costs, harm to our relationships with existing customers as a result of the acquisition, harm to our brands and reputation, the loss of key employees in the acquired businesses, use of resources that are needed in other parts of our business, and use of substantial portions of our available cash to consummate the acquisition. In addition, our ability to impose appropriate internal controls, including accurate forecasting, accounting integration of inventory, costs and reporting, to successfully manage any acquired businesses will require significant investments of resources and management time. Finally, acquisitions could result in the use of substantial amounts of cash, potentially dilutive issuances of equity securities, the occurrence of significant goodwill impairment charges, amortization expenses for other intangible assets and exposure to potential unknown liabilities of the acquired business.

Our business, particularly the high-speed interconnect and optical transport business, is dependent on capital expenditures by service providers, and any downturn that they experience could negatively impact our business.

Our business, particularly the high-speed interconnect and optical transport business we acquired in connection with our acquisition of Cortina, depends on continued capital expenditures by service providers and is subject to the cyclicity of such expenditures. Our communications semiconductor products are sold primarily to network equipment vendors that in turn sell their equipment to service providers. If the demand for our customers' products

declines or fails to increase, as a result of lower capital expenditures by service providers or any other factors, demand for our products will be similarly affected. The global economic downturn caused a significant reduction in capital spending on communications network equipment. While we are beginning to see improvement, there are no guarantees that this growth will continue, which could result in market volatility or another downturn. If there is another downturn, our business, operating results and financial condition may be materially harmed.

Cortina's high-speed interconnect and optical transport business has historically relied on a small number of key customers for a substantial portion of its revenue, and the loss of one or more of these key customers or the diminished demand for these products from one or more such key customers could negatively affect our ability to realize the anticipated benefits of our acquisition of Cortina.

A small number of customers have historically accounted for a substantial portion of Cortina's revenues from its high-speed interconnect and optical transport business in any particular period. We anticipate that our relationships with these key customers will continue to be important to this business, and we expect that this customer concentration will increase in the future. We have no long-term volume purchase commitments from our key customers. These customers may decide not to purchase our products at all, may purchase fewer products than they did in the past or may otherwise alter their purchasing patterns. Reductions, delays and cancellation of orders from our key customers or the loss of one or more key customers would significantly reduce our revenue and profits.

The failure of our distributors to perform as expected could materially reduce our future revenue or negatively impact our reported financial results.

Cortina's high-speed interconnect and optical transport business has historically relied on a number of distributors, in particular Arrow Electronics, Inc., Dragon Technology Distribution (HK) Limited and Brilliant Technologies Company, to help generate customer demand, provide technical support and other value-added services to its customers, fill customer orders and stock its products. These distributors do not sell those products exclusively, and to the extent they choose to emphasize a competitor's products over our products, our results of operations could be harmed. Our contracts with these distributors may be terminated by either party with notice. Our distributors are located all over the world, and are of various sizes and financial conditions. Lower sales, lower earnings, debt downgrades, the inability to access capital markets and higher interest rates could potentially affect our distributors' operations. Further, our distributors have contractual rights to return unsold inventory to us, and, if this were to happen, we could incur significant cost in finding alternative sales channels for these products or through write-offs. Any adverse condition experienced by our distributors could negatively impact their level of support for our products or the rate at which they make payments to us and, consequently, could harm our results of operations. We rely on accurate and timely sales reports from our distributors in order for our financial results to represent the actual sales that our distributors make for us in any given period. Any inaccuracies or delays in these reports could negatively affect our ability to produce accurate and timely financial reports and to recognize revenue. We also rely on distributors for sales forecasts, and any inaccuracies in such forecasts could impair the accuracy of our projections and planned operations.

Risks Related to Our Industry

We may be unable to make the substantial and productive research and development investments, which are required to remain competitive in our business.

The semiconductor industry requires substantial investment in research and development in order to develop and bring to market new and enhanced technologies and products. Many of our products originated with our research and development efforts and have provided us with a significant competitive advantage. Our research and development expense was \$70.9 million in 2014, \$50.5 million in 2013 and \$40.1 million in 2012. We are committed to investing in new product development in order to remain competitive in our target markets. We do not know whether we will have sufficient resources to maintain the level of investment in research and development required to remain competitive. In addition, we cannot assure you that the technologies which are the focus of our research and development expenditures will become commercially successful.

Our business, financial condition and results of operations could be adversely affected by worldwide economic conditions, as well as political and economic conditions in the countries in which we conduct business.

Our business and operating results are impacted by worldwide economic conditions. Uncertainty about current global economic conditions may cause businesses to continue to postpone spending in response to tighter credit, unemployment or negative financial news. This in turn could have a material negative effect on the demand for our semiconductor products or the products into which our semiconductors are incorporated. Multiple factors relating to our international operations and to particular countries in which we operate could negatively impact our business, financial condition and results of operations. These factors include:

- changes in political, regulatory, legal or economic conditions;
- restrictive governmental actions, such as restrictions on the transfer or repatriation of funds and foreign investments and trade protection measures, including export duties and quotas and customs duties and tariffs;
- disruptions of capital and trading markets;
- changes in import or export requirements;
- transportation delays;
- civil disturbances or political instability;
 - geopolitical turmoil, including terrorism, war or political or military coups;
- public health emergencies;
- differing employment practices and labor standards;
- limitations on our ability under local laws to protect our intellectual property;
- local business and cultural factors that differ from our customary standards and practices;
- nationalization and expropriation;

- changes in tax or intellectual property laws;
- currency fluctuations relating to our international operating activities; and
- difficulty in obtaining distribution and support.

A significant portion of our products are manufactured, assembled and tested outside the United States. Any conflict or uncertainty in these countries, including due to natural disasters, public health concerns, political unrest or safety concerns, could harm our business, financial condition and results of operations. In addition, if the government of any country in which our products are manufactured or sold sets technical standards for products manufactured in or imported into their country that are not widely shared, it may lead some of our customers to suspend imports of their products into that country, require manufacturers in that country to manufacture products with different technical standards and disrupt cross-border manufacturing relationships which, in each case, could harm our business.

Changes in current or future laws or regulations or the imposition of new laws or regulations, including new or changed tax regulations, environmental laws and export control laws, or new interpretations thereof, by federal or state agencies or foreign governments could impair our ability to compete in international markets.

Changes in current laws or regulations applicable to us or the imposition of new laws and regulations in the United States or other jurisdictions in which we do business, such as China, Japan, Korea, Singapore and Taiwan, could materially and adversely affect our business, financial condition and results of operations. For example, we have entered into agreements with local governments to provide us with, among other things, favorable local tax rates if certain minimum criteria are met, as discussed in our risk factor entitled “Tax benefits that we received may be terminated or reduced in the future, which would increase our costs.” These agreements may require us to meet several requirements as to investment, headcount and activities to retain this status. If we fail to otherwise meet the conditions of the local agreements, we may be subject to additional taxes, which in turn would increase our costs. In addition, potential future U.S. tax legislation could impact the tax benefits we effectively realize under these agreements.

Due to environmental concerns, the use of lead and other hazardous substances in electronic components and systems is receiving increased attention. In response, the European Union passed the Restriction on Hazardous Substances, or RoHS, Directive, legislation that limits the use of lead and other hazardous substances in electrical equipment. The RoHS Directive became effective July 1, 2006. We believe that our current product designs and material supply chains are in compliance with the RoHS Directive. If our product designs or material supply chains are deemed not to be in compliance with the RoHS Directive, we and our third party manufacturers may need to redesign products with components meeting the requirements of the RoHS Directive and we may incur additional expense as well as loss of market share and damage to our reputation.

In addition, we are subject to export control laws, regulations and requirements that limit which products we sell and where and to whom we sell our products. In some cases, it is possible that export licenses would be required from U.S. government agencies for some of our products in accordance with the Export Administration Regulations and the International Traffic in Arms Regulations. We may not be successful in obtaining the necessary export licenses in all instances. Any limitation on our ability to export or sell our products imposed by these laws would adversely affect our business, financial condition and results of operations. In addition, changes in our products or changes in export and import laws and implementing regulations may create delays in the introduction of new products in international markets, prevent our customers from deploying our products internationally or, in some cases, prevent the export or import of our products to certain countries altogether. While we are not aware of any other current or proposed export

or import regulations which would materially restrict our ability to sell our products in countries such as China, Japan, Korea, Singapore or Taiwan, any change in export or import regulations or related legislation, shift in approach to the enforcement or scope of existing regulations, or change in the countries, persons or technologies targeted by these regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential customers with international operations. In such event, our business and results of operations could be adversely affected.

Our product or manufacturing standards could also be impacted by new or revised environmental rules and regulations or other social initiatives. For instance, the SEC adopted new disclosure requirements in 2012 relating to the sourcing of certain minerals from the Democratic Republic of Congo and certain other adjoining countries. Those new rules, which will require reporting starting 2014, could adversely affect our costs, the availability of minerals used in our products and our relationships with customers and suppliers. Also, since our supply chain is complex, we may face reputational challenges with our customers, stockholders, and other stakeholders if we are unable to sufficiently verify the origins for any conflict minerals used in the products that we sell.

We are subject to the cyclical nature of the semiconductor industry, which has suffered and may suffer from future recessionary downturns.

The semiconductor industry is highly cyclical and is characterized by constant and rapid technological change, rapid product obsolescence and price erosion, evolving standards and wide fluctuations in product supply and demand. The industry experienced a significant downturn during the current global recession. These downturns have been characterized by diminished product demand, production overcapacity, high inventory levels and accelerated erosion of average selling prices. The most recent downturn and any future downturns could negatively impact our business and operating results. Furthermore, any upturn in the semiconductor industry could result in increased competition for access to third-party foundry and assembly capacity. We are dependent on the availability of this capacity to manufacture and assemble our integrated circuits. None of our third-party foundry or assembly contractors has provided assurances that adequate capacity will be available to us in the future.

Our products must conform to industry standards in order to be accepted by end users in our markets.

Our products comprise only a part of larger electronic systems. All components of these systems must uniformly comply with industry standards in order to operate efficiently together. These industry standards are often developed and promoted by larger companies who are industry leaders and provide other components of the systems in which our products are incorporated. In driving industry standards, these larger companies are able to develop and foster product ecosystems within which our products can be used. We work with a number of these larger companies in helping develop industry standards with which our products are compatible. If larger companies do not support the same industry standards that we do, or if competing standards emerge, market acceptance of our products could be adversely affected, which would harm our business.

Some industry standards may not be widely adopted or implemented uniformly, and competing standards may still emerge that may be preferred by our customers. Products for communications and computing applications are based on industry standards that are continually evolving. Our ability to compete in the future will depend on our ability to identify and ensure compliance with these evolving industry standards. The emergence of new industry standards could render our products incompatible with products developed by other suppliers or make it difficult for our products to meet the requirements of certain OEMs. As a result, we could be required to invest significant time and effort and to incur significant expense to redesign our products to ensure compliance with relevant standards. If our products are not in compliance with prevailing industry standards for a significant period of time, we could miss opportunities to achieve crucial design wins. We may not be successful in developing or using new technologies or in developing new products or product enhancements that achieve market acceptance. Our pursuit of necessary technological advances may require substantial time and expense.

Risks Related to our Common Stock

The trading price and volume of our common stock is subject to price volatility.

The trading price of our common stock has experienced wide fluctuations. For example, since our initial public offering through December 31, 2014, the closing price of our common stock has ranged from \$7.20 to \$26.63. Volatility in the market price of our common stock may occur in the future. The market price of shares of our common stock could be subject to wide fluctuations in response to many risk factors listed in this report and others beyond our control, including:

- actual or anticipated fluctuations in our financial condition and operating results;

Edgar Filing: INPHI Corp - Form 10-K

- changes in the economic performance or market valuations of other companies that provide high-speed analog semiconductor solutions;
- loss of a significant amount of existing business;
- actual or anticipated changes in our growth rate relative to our competitors;
 - actual or anticipated fluctuations in our competitors' operating results or changes in their growth rates;
- issuance of new or updated research or reports by securities analysts;
- our announcement of actual results for a fiscal period that are higher or lower than projected results or our announcement of revenue or earnings guidance that is higher or lower than expected;
- regulatory developments in our target markets affecting us, our customers or our competitors;
- fluctuations in the valuation of companies perceived by investors to be comparable to us;
- share price and volume fluctuations attributable to inconsistent trading volume levels of our shares;
- sales or expected sales of additional common stock;
- terrorist attacks or natural disasters or other such events impacting countries where we or our customers have operations; and
- general economic and market conditions.

Furthermore, the stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies. These fluctuations often have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry fluctuations, as well as general economic, political and market conditions such as recessions, interest rate changes or international currency fluctuations, may cause the market price of shares of our common stock to decline. In the past, companies that have experienced volatility in the market price of their stock have been subject to securities class action litigation. We may be the target of this type of litigation in the future. Securities litigation against us could result in substantial costs and divert our management's attention from other business concerns, which could seriously harm our business.

Due to the nature of our compensation program, our executive officers can sell shares of our common stock, often pursuant to trading plans established under Rule 10b5-1 of the Exchange Act. As a result, sales of common stock by our executive officers may not be indicative of their respective opinions of our performance at the time of sale or of our potential future performance. Nonetheless, the market price of our stock may be affected by sales of shares by our executive officers.

If securities or industry analysts do not publish research or reports about our business, or if they change their recommendations regarding our stock adversely, our stock price and trading volume could decline.

The trading market for our common stock will be influenced by the research and reports that industry or securities analysts publish about us or our business. If one or more of the analysts who cover us downgrade our stock, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

We may not be able to obtain capital when desired on favorable terms, if at all, or without dilution to our stockholders and our failure to raise capital when needed could prevent us from executing our growth strategy.

We believe that our existing cash and cash equivalents, investments in marketable securities, and cash flows from our operating activities, will be sufficient to meet our anticipated cash needs for at least the next 12 to 18 months. We operate in an industry, however, that makes our prospects difficult to evaluate. It is possible that we may not generate sufficient cash flow from operations or otherwise have the capital resources to meet our future capital needs. If this occurs, we may need additional financing to execute on our current or future business strategies, including to:

- invest in our research and development efforts by hiring additional technical and other personnel;
- expand our operating infrastructure;
- acquire complementary businesses, products, services or technologies; or
 - otherwise pursue our strategic plans and respond to competitive pressures.

If we raise additional funds through the issuance of equity or convertible debt securities, the percentage ownership of our stockholders could be significantly diluted, and these newly-issued securities may have rights, preferences or privileges senior to those of existing stockholders. If we raise additional funds by obtaining loans from third parties, the terms of those financing arrangements may include negative covenants or other restrictions on our business that could impair our operational flexibility, and would also require us to incur interest expense. We have not made arrangements to obtain additional financing and there is no assurance that additional financing will be available on terms favorable to us, or at all. If adequate funds are not available or are not available on acceptable terms, if and when needed, our ability to fund our operations, take advantage of unanticipated opportunities, develop or enhance our products, or otherwise respond to competitive pressures could be significantly limited.

Delaware law and our corporate charter and bylaws contain anti-takeover provisions that could delay or discourage takeover attempts that stockholders may consider favorable.

Provisions in our certificate of incorporation and bylaws, may have the effect of delaying or preventing a change of control or changes in our management. These provisions include the following:

- the right of our board of directors to elect a director to fill a vacancy created by the expansion of our board of directors;
 - the classification of our board of directors so that only a portion of our directors are elected each year, with each director serving a three-year term;
- the requirement for advance notice for nominations for election to our board of directors or for proposing matters that can be acted upon at a stockholders' meeting;
- the ability of our board of directors to alter our bylaws without obtaining stockholder approval;
- the ability of our board of directors to issue, without stockholder approval, up to 10,000,000 shares of preferred stock with rights set by our board of directors, which rights could be senior to those of common stock;
- the required approval of holders of at least two-thirds of the shares entitled to vote at an election of directors to adopt, amend or repeal our bylaws or amend or repeal the provisions of our certificate of incorporation regarding the election and removal of directors and the ability of stockholders to take action by written consent; and
- the elimination of the right of stockholders to call a special meeting of stockholders and to take action by written consent.

In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law. These provisions may prohibit or restrict large stockholders, in particular those owning 15% or more of our outstanding voting stock, from merging or combining with us. These provisions in our certificate of incorporation and bylaws and under Delaware law could discourage potential takeover attempts and could reduce the price that investors might be willing to pay for shares of our common stock in the future and result in our market price being lower than it would without these provisions.

We do not currently intend to pay dividends on our common stock and, consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.

We have never declared or paid any cash dividends on our common stock and do not currently intend to do so for the foreseeable future. We currently intend to invest our future earnings, if any, to fund our growth. Therefore, you are not likely to receive any dividends on your common stock for the foreseeable future and the success of an investment in shares of our common stock will depend upon any future appreciation in their value. There is no guarantee that shares of our common stock will appreciate in value or even maintain the price at which our stockholders have purchased their shares.

Item 1b. *Unresolved Staff Comments*

None.

Item 2. *Properties*

We lease 57,914 square feet of office space in Santa Clara, California which currently serve as our principal executive office which will expire on August 17, 2019. We also lease 40,522 square feet of office space in Westlake Village, California under a lease that will expire on December 31, 2017. Our Singapore subsidiary currently leases 6,374 square feet of office space in Singapore under a lease that expires on April 30, 2017. Our United Kingdom subsidiary currently leases office space in Northamptonshire, England under a lease that expires on March 30, 2016. We also occupy space in Folsom, California, consisting of 14,254 square feet under a lease that expires on May 31, 2015, and space in Raleigh, North Carolina, consisting of 15,440 square feet under a lease that expires on September 30, 2015. Our Canada subsidiary currently leases 13,951 square feet in Ottawa, Canada under a lease that expires on October 31, 2016. We believe that current facilities, are sufficient to meet our needs for the foreseeable future. For additional information regarding our obligations under property leases, see Note 15 of Notes to Consolidated Financial Statements, included in Part II, “Item 8, Financial Statements and Supplementary Data”.

Item 3. *Legal Proceedings* –

We are currently a party to the following legal proceedings:

Netlist, Inc. v. Inphi Corporation, Case No. 09-cv-6900 (C.D. Cal.)

On September 22, 2009, Netlist filed suit in the United States District Court, Central District of California, or the Court, asserting that we infringe U.S. Patent No. 7,532,537. Netlist filed an amended complaint on December 22, 2009, further asserting that we infringe U.S. Patent Nos. 7,619,912 and 7,636,274, collectively with U.S. Patent No. 7,532,537, the patents-in-suit, and seeking both unspecified monetary damages to be determined and an injunction to prevent further infringement. These infringement claims allege that our iMB™ and certain other memory module components infringe the patents-in-suit. We answered the amended complaint on February 11, 2010 and asserted that we do not infringe the patents-in-suit and that the patents-in-suit are invalid. In 2010, we filed *inter partes* requests for reexamination with the United States Patent and Trademark Office (the “USPTO”), asserting that the patents-in-suit are invalid.

On August 27, 2010, the USPTO ordered the request for *Inter Partes* Reexamination for U.S. Patent No. 7,636,274 and found a substantial new question of patentability based upon each of the different issues that we raised as the reexamination requestor. On September 27, 2011, the Patent Office issued a First Office Action based on the Netlist '274 Patent Reexamination Request and rejected 91 of its 97 claims. On October 27, 2011, Netlist responded to the USPTO determination by amending some but not all of the claims, adding new claims and making arguments as to the validity of the rejected claims in view of the cited references. We provided rebuttable comments to the USPTO on November 28, 2011. On March 12, 2012, the Examiner issued an Action Closing Prosecution, indicating that the claims pending contain allowable subject matter, and Netlist did not respond to the Action Closing Prosecution in the time provided by the USPTO. On June 22, 2012, the USPTO issued a Right of Appeal Notice, and on July 23, 2012, we filed a Notice of Appeal. We filed the Appeal Brief on September 24, 2012 and Netlist filed its Responsive Brief on October 24, 2012. The parties received an Examiner's Answer dated April 16, 2013 from the USPTO that maintained the rejections set forth on the Right of Appeal Notice dated June 22, 2012. We filed a Rebuttal Brief on May 16, 2013 and a Request for Oral Hearing on June 7, 2013. The appeal hearing took place on November 20, 2013. The Patent Trial and Appeal Board (PTAB) issued its decision on January 16, 2014, finding the Examiner erred in declining to adopt 8 of the 9 different rejections that had been proposed by us. We requested a rehearing of the decision not to adopt the remaining one rejection that had been proposed by us and was not adopted by the PTAB on February 18, 2014. In papers dated March 18, 2014, Netlist provided rebuttal comments to the request for rehearing and also requested re-opening of prosecution with respect to the claims that the PTAB had rejected, and in that request to re-open prosecution amended the independent claims that stood rejected. We filed comments with respect to these proposed amended claims on April 17, 2014, which were refiled in a slightly different form on September 5, 2014. On June 26, 2014, the PTAB issued a decision on the request for rehearing, which included a rejection of further claims pursuant to our request and on July 28, 2014 Netlist provided a response to the USPTO cancelling those claims that had been rejected in the decision on the request for rehearing. On September 26, 2014, the PTAB remanded the proceedings back to the Examiner, with instructions to consider part, but not all, of our comments that had been previously filed on September 5, 2014. On October 10, 2014, we filed a Petition to the Director of the USPTO seeking reconsideration of the PTAB remand of September 26, 2014, and requesting that all of the comments that we had previously filed on September 5, 2014 should have been entered for consideration by the Examiner. The USPTO denied this Petition and a communication from the Examiner, with instructions to consider part, but not all, of our comments that had been previously filed on September 5, 2014 is expected as the next substantive step of the proceeding, as prosecution otherwise remains closed. The proceeding is expected to continue in accordance with established *Inter Partes* Reexamination procedures. We may consider filing an appeal to any determination made by the USPTO with the Federal Circuit Court of Appeals.

On September 8, 2010, the USPTO ordered the request for *Inter Partes* Reexamination for U.S. Patent No. 7,532,537 and found a substantial new question of patentability based upon different issues that we raised as the reexamination requestor. The USPTO accompanied this Reexamination Order of U.S. Patent No. 7,532,537 with its own evaluation of the validity of this patent, and rejected some but not all of claims. In a response dated October 8, 2010, Netlist responded to the USPTO determination by amending some but not all of the claims, adding new claims and making arguments as to why the claims were not invalid in view of the cited references. We provided rebuttable comments to the USPTO on November 8, 2010 along with a Petition requesting an increase in the number of allowed pages of the rebuttable comments. On January 20, 2011, the USPTO granted the Petition in part. We then filed updated rebuttal comments on January 27, 2011 in compliance with the granted Petition. The USPTO has considered these updated rebuttal comments, and in a communication dated June 15, 2011, continued to reject all the previously rejected claims. The USPTO also rejected all the claims newly added in the October 8, 2010 Netlist response. In a further communication dated June 21, 2011, the USPTO issued an Action Closing Prosecution indicating that it would confirm the patentability of four claims and reject all the other pending claims. On August 22, 2011, Netlist responded

to the Action Closing Prosecution by further amending some claims and making arguments as to the validity of the rejected claims in view of the cited references. We submitted rebuttal comments on September 21, 2011. In a further communication dated February 7, 2012, the USPTO issued a Right of Appeal Notice, which also indicated that the previous amendments to claim made by Netlist would be entered, and that the current pending claims, as amended, were patentable. We filed a Notice of Appeal at the USPTO on March 8, 2012, within the time period provided for filing the Notice of Appeal and Netlist did not file Notice of Cross-Appeal. We filed its Appeal Brief on May 8, 2012, and Netlist filed its Responsive Brief on July 2, 2012. The parties received an Examiner's Answer dated April 16, 2013 from the USPTO that maintained the rejections set forth on the Right of Appeal Notice dated February 7, 2012. We filed a Rebuttal Brief on May 16, 2013 and a Request for Oral Hearing on June 7, 2013. The appeal hearing took place in front of the PTAB on November 20, 2013. The PTAB issued its decision on January 16, 2014, affirming the Examiner's decision as to all of the challenged claims. On February 18, 2014, we made a request for rehearing of the decision, and in papers dated March 18, 2014, Netlist provided rebuttal comments to the request for rehearing. On August 13, 2014, the PTAB denied our request for rehearing, and on October 15, 2014, we filed a Notice of Appeal to the Court of Appeals for the Federal Circuit. An Appeal Brief was filed with the Court of Appeals for the Federal Circuit on February 3, 2015 and an Opposition Brief filed by Netlist in the Court of Appeals for the Federal Circuit is expected as the next substantive step of the proceeding, as prosecution otherwise remains closed. The proceeding is expected to continue in accordance with established *Inter Partes* Reexamination procedures.

On September 8, 2010, the USPTO ordered the request for *Inter Partes* Reexamination for U.S. Patent No. 7,619,912 and found a substantial new question of patentability based upon different issues that we raised as the reexamination requestor. The USPTO accompanied this Reexamination Order of U.S. Patent No. 7,619,912 with its own evaluation of the validity of this patent, and initially determined that all of the claims were patentable based upon our request for *Inter Partes* Reexamination. Netlist did not comment upon this Reexamination Order. The USPTO on February 28, 2011 also merged the Proceedings of our Reexamination of U.S. Patent No. 7,619,912, bearing Control No. 90/001,339 with Inter Partes Reexamination Proceeding 95/000,578 filed October 20, 2010 on behalf of SMART Modular Technologies, Inc. and Inter Partes Reexamination Proceeding 95/000,579 filed October 21, 2010 on behalf of Google, Inc. In each of these other Reexamination Proceedings, the USPTO had indicated that there existed a substantial new question of patentability with respect to certain claims of U.S. Patent No. 7,619,912, but had not accompanied the Reexamination Orders related thereto with its own evaluation of the validity of this patent, indicating that such evaluation would be forthcoming at a later time. This further evaluation was received in an Office Action dated April 4, 2011, in which the Examiner rejected a substantial majority of the claims based upon a number of different rejections, including certain of the rejections originally proposed by the Company in its Request for Reexamination. This Office Action also indicated that one claim was deemed to be patentable over the prior art of record in the merged Reexamination Proceedings. After seeking and obtaining an extension of time to respond to the Office Action dated April 4, 2011, Netlist served its response on July 5, 2011, which added new claims and made arguments as to why the originally filed claims were not invalid in view of the cited references. Each of the merged Reexamination Requestors, including us, submitted rebuttal comments by August 29, 2011. The USPTO considered this Netlist response and each of the rebuttal comments, and in an Office Action dated October 14, 2011, continued to reject most, but not all of the previously rejected claims, as well as rejected claims that had been added by Netlist in its July 5, 2011 response. After seeking and obtaining an extension of time to respond to the Office Action dated October 14, 2011, Netlist served its response on January 13, 2012, which response made amendments based upon subject matter that had been indicated as allowable in the Office Action dated October 14, 2011, added other new claims and made arguments as to why all of these claims should be allowed. The three different merged Reexamination Requestors, including us, timely submitted rebuttal comments on or about February 13, 2012. The USPTO issued a Non-final Office Action on November 13, 2012, rejecting some claims and indicating that others contained allowable subject matter. On January 14, 2013, Netlist filed a Response to the Non-final Office Action which presented further claim amendments and evidence supporting its positions regarding patentability. Rebuttal comments from us and the other Requestors were filed on February 13, 2013. On March 21, 2014, the USPTO issued an Action Closing Prosecution in which the USPTO indicated that certain of the pending claims were allowable and other of the pending claims were rejected, and on June 18, 2014 issued a Right of Notice of Appeal. By July 18, 2014, we as well as other Requestors each filed Notices of Appeal, and Netlist filed a Cross Appeal on July 30, 2014. By September 30, 2014, each of the Requestors as well as Netlist had filed their respective Appeal Briefs, and by October 30, 2014 each of the Requestors as well as Netlist had filed their respective Responses to the previously filed Appeal Briefs. Reply Briefs by Requestors and Netlist were filed on or before February 18, 2015 and consideration by the USPTO will be the next substantive step of the proceeding, as currently prosecution otherwise will remain closed. The merged proceeding is expected to continue in accordance with established *Inter Partes* Reexamination procedures.

The reexamination proceedings could result in a determination that the patents-in-suit, in whole or in part, are valid or invalid, as well as modifications of the scope of the patents-in-suit.

Based on these papers the Court in January 2014 ordered a continued stay of the proceedings, took the litigation off the active court calendar, and requested that the parties file a joint status report on May 1, 2014 and every 120 days

thereafter advising the Court as to status of the reexamination proceedings at which times, the Court could decide to maintain or lift the stay.

While we intend to defend the foregoing lawsuit vigorously, litigation, whether or not determined in our favor or settled, could be costly and time-consuming and could divert management's attention and resources, which could adversely affect our business.

Based on the nature of the litigation, we are currently unable to predict the final outcome of this lawsuit and therefore, cannot determine the likelihood of loss nor estimate a range of possible loss. However, because of the nature and inherent uncertainties of litigation, should the outcome of these actions be unfavorable, our business, financial condition, results of operations or cash flows could be materially and adversely affected.

As a result of acquisition of Cortina, we are currently working to settle a patent dispute involving Cortina and Vitesse Semiconductor Corporation (Vitesse). The patent dispute involves a certain patent family owned by Vitesse associated with error correction. We are currently in discussion with Vitesse in good faith to settle the dispute. We believe that the probable liability of this claim would be \$750,000 which we recorded as of the acquisition date and December 31, 2014. Based on the Agreement and Plan of Merger dated July 30, 2014, we would be indemnified for future settlement arising from this claim, up to an amount of \$750,000. Accordingly, we recorded an indemnification asset in the amount of \$750,000 as of the acquisition date. However, because of the nature and inherent uncertainties, should the outcome of the settlement be unfavorable, our business, financial condition, results of operations or cash flows could be materially and adversely affected.

We are not currently a party to any other material litigation. The semiconductor industry is characterized by frequent claims and litigation, including claims regarding patent and other intellectual property rights as well as improper hiring practices. We may from time to time become involved in litigation relating to claims arising from our ordinary course of business. These claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

Item 5. *Market For Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*

Market for Registrant’s Common Equity

Our common stock is traded on the New York Stock Exchange under the symbol “IPHI”. The following table sets forth the range of high and low sales prices for our common stock in each quarter:

2014	Low	High
Fourth Quarter	\$12.41	\$19.14
Third Quarter	12.57	17.17
Second Quarter	13.49	16.35
First Quarter	10.87	16.56

2013	Low	High
Fourth Quarter	\$10.88	\$14.88
Third Quarter	10.59	13.85
Second Quarter	8.62	11.53
First Quarter	7.95	10.95

As of February 28, 2015, we had approximately 66 holders of record of our common stock. This number does not include the number of persons whose shares are in nominee or in “street name” accounts through brokers.

We have never declared or paid any cash dividends on shares of our capital stock. We expect to retain all of our earnings to finance the expansion and development of our business and we do not currently intend to pay any cash dividends on our capital stock in the foreseeable future. Our board of directors will determine future dividends, if any.

Director and Executive Officers have currently and may from time to time in the future, establish pre-set trading plans in accordance with Rule 10b5-1 promulgated under the Securities Exchange Act of 1934.

Securities Authorized for Issuance under Equity Compensation Plans

Information regarding the securities authorized for issuance under our equity compensation plans can be found under Part III, “Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters”.

Share Performance Graph

The following information is not deemed to be “soliciting material” or to be “filed” with the Securities and Exchange Commission or subject to Regulation 14A or 14C under the Securities Exchange Act of 1934 or to the liabilities of Section 18 of the Securities Exchange Act of 1934, and will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent we specifically incorporate it by reference into such a filing.

Set forth below is a line graph showing the cumulative total stockholder return (change in stock price plus reinvested dividends) assuming the investment of \$100 on November 11, 2010 (the day of our initial public offering) in each of our common stock, the S&P 500 Index and PHLX Semiconductor Index for the period commencing on November 11, 2010 and ending on December 31, 2014. The comparisons in the table are required by the Securities and Exchange Commission and are not intended to forecast or be indicative of future performance of our common stock.

Item 6. Selected Consolidated Financial Data

The following selected consolidated financial data should be read together with Part II, “Item 7., Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our consolidated financial statements and related notes included elsewhere in this report. The selected balance sheet data as of December 31, 2014 and 2013, and the selected statements of operations data for each of the years ended December 31, 2014, 2013, and 2012 have been derived from our audited financial statements included elsewhere in this report. The selected balance sheet data as of December 31, 2012, 2011 and 2010 and the selected statements of operations data for the years ended December 31, 2011 and 2010 have been derived from our audited financial statements not included in this report. Historical results are not necessarily indicative of the results to be expected in the future.

	Year Ended December 31,				
	2014	2013	2012	2011	2010
	(in thousands, except share and per share data)				
Statement of Operations Data:					
Revenue ^{(1) (4)}	\$ 156,142	\$ 102,664	\$ 91,206	\$ 79,297	\$ 83,193
Cost of revenue ^{(1) (2)}	70,488	37,095	32,684	28,687	29,438
Gross profit	85,654	65,569	58,522	50,610	53,755
Operating expense:					
Research and development ^{(1) (2)}	70,863	50,516	40,102	28,565	23,781
Sales and marketing ^{(1) (2)}	20,003	15,741	14,052	12,700	8,823
General and administrative ^{(1) (2)}	16,153	11,614	12,300	9,141	9,212
Total operating expense	107,019	77,871	66,454	50,406	41,816
Income (loss) from operations	(21,365)	(12,302)	(7,932)	204	11,939
Interest and other income (expense)	495	876	914	509	(50)
Income (loss) before income taxes	(20,870)	(11,426)	(7,018)	713	11,889
Provision (benefit) for income taxes ⁽³⁾	1,738	1,752	13,673	(1,218)	(14,242)
Net income (loss)	\$(22,608)	\$(13,178)	\$(20,691)	\$1,931	\$26,131
Net income (loss) allocable to common and participating common securities	\$(22,608)	\$(13,178)	\$(20,691)	\$1,931	\$5,326
Earnings per share:					
Basic	\$(0.69)	\$(0.45)	\$(0.73)	\$0.07	\$1.03
Diluted	\$(0.69)	\$(0.45)	\$(0.73)	\$0.07	\$0.61
Weighted-average shares used in computing earnings per share:					
Basic	32,707,868	29,493,005	28,378,680	26,799,237	5,086,169
Diluted	32,707,868	29,493,005	28,378,680	29,367,423	8,546,537

(1) On October 3, 2014, we completed the acquisition of Cortina, including its high-speed interconnect and optical transport product lines for approximately \$52.5 million in cash and approximately 5.3 million shares of our common stock in accordance with the Agreement and Plan of Merger dated July 30, 2014 as amended by Amendment No. 1 to the Agreement and Plan of Merger dated September 25, 2014. The results of operations of

Cortina and estimated fair value of assets acquired and liabilities assumed were included in our consolidated financial statements from the acquisition date. This acquisition resulted in a significant change in our statement of operations in 2014 which includes:

- (i) Charge to cost of goods sold resulting from the step-up inventory acquired from Cortina; and
- (ii) Charge to cost of goods sold and operating expenses from amortization of acquired intangibles

Footnotes continued on the following page.

	As of December 31,				
	2014	2013	2012	2011	2010
	(in thousands)				
Balance Sheet Data:					
Cash and cash equivalents	\$30,366	\$31,667	\$30,161	\$29,696	\$110,172
Investments in marketable securities	38,908	90,890	91,107	89,283	—
Working capital	108,372	129,013	131,310	129,395	116,887
Total assets	278,710	182,342	170,074	172,628	158,957
Total liabilities	39,536	22,949	17,109	14,224	16,271
Total stockholders' equity (deficit)	239,174	159,393	152,965	158,404	142,686

Footnotes continued from the prior page.

(2) Stock-based compensation expense is included in our results of operations as follows:

	As of December 31,				
	2014	2013	2012	2011	2010
	(in thousands)				
Operating expenses:					
Cost of revenue	\$1,260	\$1,086	\$726	\$315	\$107
Research and development	12,420	8,586	5,833	3,214	1,381
Sales and marketing	4,079	3,204	2,660	2,054	526
General and administrative	4,701	4,102	3,240	1,609	691

The provision (benefit) for income taxes for the year ended December 31, 2012 included the establishment of valuation allowance against deferred tax assets. The provision (benefit) for income taxes for the year ended (3) December 31, 2010 included the releases and reversals of valuation allowances against deferred tax assets provided in prior periods. Please see note 9 to the notes to our consolidated financial statements.

Samsung, together with associated entities, held over 13% of our outstanding shares of common stock before our initial public offering. After our initial public offering in November 2010, Samsung, together with associated (4) entities, holds less than 10% of our outstanding shares of common stock. As a result of decline in ownership below 10% of our common stock, we no longer consider Samsung a related party. Revenues from Samsung were \$27,940 for the year ended December 31, 2010.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Management's Discussion and Analysis of Financial Condition and Results of Operations and this report contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this report, the terms "may," "might," "will," "objective," "intend," "should," "could," "can," "would," "expect," "believe," "potential," "plan," or the negative of these terms, and similar expressions intended to identify forward-looking statements. These statements are statements that relate to future periods and include statements regarding our anticipated trends and challenges in our business and the markets in which we operate, including the market for 40G and 100G high-speed analog semiconductor solutions, our plans for future products, expansion of our product offerings and enhancements of existing products, our expectations regarding our expenses and revenue, sources of revenue, our tax benefits, the benefits of our products and services, our technological capabilities and expertise, timing of the development of our products, the status and anticipated impact of the Cortina acquisition, our anticipated cash needs and our estimates regarding our capital requirements and our needs for additional financing, our anticipated growth and growth strategies, our ability to retain and attract customers, particularly in light of our dependence on a limited number of customers for a substantial portion of our revenue, our expectations regarding competition, interest rate sensitivity, adequacy of our disclosure controls, our legal proceedings and warranty claims. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these or any other forward-looking statements. These risks and uncertainties include, but are not limited to, those risks discussed below, as well as factors affecting our results of operations, our ability to manage our growth, our ability to sustain or increase profitability, demand for our solutions, the effect of declines in average selling prices for our products, our ability to compete, our ability to rapidly develop new technology and introduce new products, our ability to safeguard our intellectual property, trends in the semiconductor industry and fluctuations in general economic conditions, and the risks set forth throughout this Report, including the risks set forth under Part I, "Item 1A, Risk Factors". Readers are cautioned not to place undue reliance on these forward-looking statements, which are based on current expectations and reflect management's opinions only as of the date hereof. These forward-looking statements speak only as of the date of this Report. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any changes in events, conditions or circumstances on which any such statement is based.

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes that are included elsewhere in this Annual Report on Form 10-K.

Overview

We are a fabless provider of high-speed analog and mixed signal semiconductor solutions for the communications, datacenter and computing markets. We often refer to our business as covering various data transport segments from "fiber to memory". Our analog and mixed signal semiconductor solutions provide high signal integrity at leading-edge data speeds while reducing system power consumption. Our semiconductor solutions are designed to address bandwidth bottlenecks in networks, maximize throughput and minimize latency in computing environments and

enable the rollout of next generation communications, datacenter and computing infrastructures. Our solutions provide a vital high-speed interface between analog signals and digital information in high-performance systems such as telecommunications transport systems, enterprise networking equipment, datacenter and enterprise servers, storage platforms, test and measurement equipment and military systems. We provide 40G and 100G high-speed analog semiconductor solutions for the communications market and high-speed memory interface solutions for the computing market. We have a wide range product portfolio with many products sold in communication and datacenter markets as of December 31, 2014. We have ongoing, informal collaborative discussions with industry and technology leaders such as AMD, Cisco, Alcatel-Lucent, Ciena, Dell Incorporated, Huawei, Intel, Juniper, Micron, Neophotonics, Samsung and other data center companies to design architectures and products that solve bandwidth bottlenecks in existing and next generation communications and computing systems. Although we do not have any formal agreements with these entities, we engage in informal discussions with these entities with respect to anticipated technological challenges, next generation customer requirements and industry conventions and standards. We help define industry conventions and standards within the markets we target by collaborating with technology leaders, OEMs, systems manufacturers and standards bodies.

The history of our product development and sales and marketing efforts is as follows:

From 2000 to 2002, we were primarily engaged in the development of our core high-speed analog products and proprietary system architecture models to address bottlenecks in emerging network architectures. Specifically, during this period, we developed and shipped our 50 GHz MUX and DEMUX products. During this period, we also began development work on our initial 40G products.

In 2003, we introduced and shipped 13G, 25G and 50G logic products, 20G MUX and 40G transimpedance amplifiers and modulator drivers for the communications, test and measurement and military markets. During this period, we also began the development of our first generation high-speed PLLs and register solution used primarily in conjunction with double data rate 2, or DDR2, modules for the computing market.

In 2005, we introduced and shipped our high-speed PLLs and register solution used primarily in conjunction with DDR2 modules for the computing market.

In 2006, we began development of our second generation single chip high-speed PLLs and register solution to be used primarily in conjunction with double data rate 3, or DDR3, modules for the computing market and were the first to introduce this product to the market. In addition, we introduced and shipped track-and-hold amplifiers for the communications market.

In 2007, we began volume shipments of our high-speed PLLs and register solution used primarily in conjunction with DDR2 modules, and continued development of our single chip high-speed PLLs and register solution, used primarily in conjunction with DDR3 modules.

In 2008, we began volume shipments of our 40G drivers for the communications market and commenced shipments of our high-speed PLLs and register solution used primarily in conjunction with DDR3 modules for the computing market.

In 2009, due to the launch of Intel's Nehalem-based platform servers, we began volume shipments of our single chip high-speed PLLs and register solution to be used primarily in conjunction with DDR3 modules. We also shipped engineering samples of the first generation of our isolation memory buffer, or iMB™, for the computing market. We also began development of our second generation iMB™ product, the architecture for which has been adopted by the Joint Electronic Device Engineering Council, or JEDEC, and development of our low power CMOS SerDes product for next generation 100G Ethernet in enterprise networks.

- In 2010, we began to ship in production volume a “low voltage” version of our integrated PLL and register buffer. We also shipped engineering samples of the second generation iMB™ product. We also introduced and began to ship in commercial volume the industry's first transimpedance ampliform for 100G reconfigurable colorless networks, which we identify as product number 2850TA-SO1D.

In 2011, we began to ship in production volume a new “ultra-low voltage” version of our integrated PLL and register buffer and the second generation of iMB™. We also shipped engineering samples of our iPHY 100 Gbe CMOS CDR and SerDes Gearbox products.

In 2012, we started shipping samples of the IN3250TA, our second-generation transimpedance amplifier, or TIA, for 100G reconfigurable colorless networks. We also introduced the industry's first quad linear driver designed for linear transmitters to enable next-generation 100G/400G coherent systems to address the need for higher speed, higher performance networking infrastructure. We also began shipping in production volume our lowest power integrated phase lock loop and register buffer, which is shipping in the form of product number INSSTE32882XV. We also announce the availability of the world's first production ready 100G CMOS PHY/SerDes Gearbox products for next-generation data center, enterprise and service provider line cards.

In 2013, we introduced the second generation 100G CMOS SerDes gearbox integrated circuit, or GB IC, for data center, enterprise and service provider line cards. The new GB IC with Tri-rate™ foundation is designed to enable seamless support of 10G, 40G and 100G Ethernet and optical transport network on a single line card. We also began shipping an improved version of iMB™ which delivers up to 35% improvement in LRDIMM bandwidth for 768BG memory capacities and 40% improvement in memory bandwidth for servers up to 512GB memory capacities. We also introduced the next generation high speed memory interface product, DDR4 register for the computing market. We also began shipping the industry's first quad linear driver designed for linear transmitters to enable next-generation 100G/400G coherent systems to address the need for higher speed, higher performance networking infrastructure.

In 2014, we completed the acquisition of Cortina Systems Inc. which expands our market share of the high-speed optical and networking interconnects. This added more than 130 products in our portfolio which includes high-speed interconnect and optical transport products. We also started sampling the IN3252TA, the industry's first 32 Gbps dual high gain linear/variable-gain amplifier. The IN3252TA is designed specifically to address the demanding requirements for 100G coherent transmission for the Metro market. We also announced the availability of a new iKON™ family of 100G Clock and Data Recovery Retimer integrated circuits (IC) targeted at next-generation 2-Terabit line cards. The first product in this series, the IN112525-LC 100G CMOS CDR Retimer IC, is designed to accelerate deployment for higher density 100G in service center and data center networks. We also announced the availability of IN3216DZ, the first single chip quad channel linear Mach Zehnder driver in bare die form to address the network needs for 100G coherent systems in small form factors for the metro market. Specifically designed to be co-packaged with MZ modulators, the IN3216DZ will reduce size and cost of 100G coherent systems to enable higher density metro solutions. We also started sampling 45GBaud Linear Coherent Product Family, the industry's first linear ICs enabling 400G coherent solutions for next-generation metro to long haul applications. The initial product offerings includes IN4514SZ, a high-performance octal linear differential to single-ended Mach-Zehnder Modulator Driver and IN4550TA, a quad linear TIA/VGA Amplifier.

Our products are designed into systems sold by OEMs, including Alcatel-Lucent, Ciena, Cisco, Dell, EMC, HP, IBM, Juniper and Oracle. We believe we are one of a limited number of suppliers to these OEMs for the types of products we sell, and in some cases we may be the sole supplier for certain applications. We sell both directly to these OEMs and to module manufacturers, original design manufacturers, or ODMs, and subsystems providers that, in turn, sell to these OEMs. During the year ended December 31, 2014, we sold our products to more than 160 customers. A significant portion of our revenue has been generated by a limited number of customers. Sales to Samsung, including its subcontractors, accounted for 18% and 20% of our total revenue for the years ended December 31, 2014 and 2013, respectively. Sales directly and through distributors to Micron accounted for 11% of our total revenue for the year ended December 31, 2013. In addition, sales to SK Hynix, including its subcontractor, accounted for 16% of our total revenue for the year ended December 31, 2013. Substantially all of our sales to date, including our sales to Samsung, Micron and SK Hynix, are made on a purchase order basis. Since the beginning of 2006, we have shipped more than 100 million high-speed analog semiconductors. Our total revenue increased to \$156.1 million for the year ended December 31, 2014 from \$102.7 million for the year ended December 31, 2013. The increase in revenue for the year ended December 31, 2014 was partially due to the acquisition of Cortina Systems as of October 3, 2014. As of December 31, 2014, our accumulated deficit was \$89.2 million.

Sales to customers in Asia accounted for 71%, 71% and 65% of our total revenue in 2014, 2013 and 2012, respectively. Because many of our customers or their OEM manufacturers are located in Asia, we anticipate that a majority of our future revenue will continue to come from sales to that region. Although a large percentage of our sales are made to customers in Asia, we believe that a significant number of the systems designed by these customers are then sold to end users outside Asia.

In April 2010, we received approval from the government of Singapore to set up an international headquarters from which to conduct our international operations. Because of its geographic alignment with suppliers and customers, we established our operations in Singapore to become a new international headquarters office for receiving and fulfilling orders for product shipped to locations outside the United States. Singapore has a strong university system and an established group of technology-based companies from which to recruit new engineers. We intend to build a team of engineering capability in Singapore both for development as well as testing associated with manufacturing. International operations in Singapore commenced on May 1, 2010 and during 2010, we transitioned our international operations from the United States to our Singapore subsidiary. As of December 31, 2014, our Singapore subsidiary leases 6,374 square feet of office space and employs 25 full time employees.

Demand for new features changes rapidly. It is difficult for us to forecast the demand for our products, in part because of the complex supply chain between us and the end-user markets that incorporate our products. Due to our lengthy product development cycle, it is critical for us to anticipate changes in demand for our various product features and the applications they serve to allow sufficient time for product development and design. Our failure to accurately forecast demand can lead to product shortages that can impede production by our customers and harm our customer relationships. Conversely, our failure to forecast declining demand or shifts in product mix can result in excess or obsolete inventory.

Although revenue generated by each design win and the timing of the recognition of that revenue can vary significantly, we consider ongoing design wins to be a key factor in our future success. We consider a design win to occur when an OEM or contract manufacturer notifies us that it has selected our products to be incorporated into a product or system under development. The design win process is typically lengthy, and as a result, our sales cycles will vary based on the market served, whether the design win is with an existing or new customer and whether our product is under consideration for inclusion in a first or subsequent generation product. In addition, our customers' products that incorporate our semiconductors can be complex and can require a substantial amount of time to define, design and produce in volume. As a result, we can incur significant design and development expenditures in circumstances where we do not ultimately recognize, or experience delays in recognizing revenue. Our customers generally order our products on a purchase order basis. We do not have any long-term purchase commitments (in excess of one year) from any of our customers. Once our product is incorporated into a customer's design, however, we believe that our product is likely to continue to be purchased for that design throughout that product's life cycle because of the time and expense associated with redesigning the product or substituting an alternative semiconductor. Our design cycle from initial engagement to volume shipment is typically two to three years. Product life cycles in the markets we serve typically range from two to 10 years or more and vary by application.

As a result of the Cortina acquisition, on October 16, 2014, the Compensation Committee of the Board of Directors granted one-time employment restricted stock unit awards of 1,000,000 shares to certain Cortina employees who entered employment with us commencing upon the closing of the acquisition. The awards vest over four years contingent upon continuous service.

Summary of Consolidated Financial Results

As discussed in more detail below, for the year ended December 31, 2014, compared to the year ended December 31, 2013, we delivered the following financial performance. The financial results for the year ended December 31, 2014, include the results of operations of Cortina from the acquisition date to December 31, 2014 and the effect of purchase price accounting.

Total revenues increased by \$53.5 million, or 52%, to \$156.1 million.

Gross profit as a percentage of revenue decreased from 64% to 55%.

Total operating expenses increased by \$29.1 million, or 37%, to \$107.0 million.

Loss from operations increased by \$9.1 million, to loss of \$21.4 million.

Provision for income tax was consistent from prior year.

Diluted loss per share increased by \$0.24, to (\$0.69).

The increase in our revenue for the year ended December 31, 2014 was a result of an increase in consumption of our dual linear TIAs, quad linear driver products, iPHY products, iMBTM high-speed interconnect and optical transport products.

The decline in gross margin was due to the amortization of inventory fair value step-up related to the acquired Cortina inventories, sold during the fourth quarter of 2014 and amortization of the acquired intangibles.

Total operating expenses increased due primarily to an increase in headcount and stock-based compensation. Our expenses primarily consist of personnel costs, which include compensation, benefits, payroll related taxes and stock-based compensation. In 2014, we hired 95 new employees, primarily in the engineering department. In addition, the acquisition of Cortina added 145 employees in the fourth quarter of 2014. We expect expenses to continue to increase in absolute dollars as we continue to invest resources to develop more products, to support the growth of our business. Our diluted loss per share increased primarily due to increase in operating expenses offset partially by increase in revenue.

Critical Accounting Policies and Significant Management Estimates

Our consolidated financial statements are prepared in accordance with U.S. Generally Accepted Accounting Principles, or GAAP. In connection with the preparation of our consolidated financial statements, we are required to make assumptions and estimates about future events, and apply judgments that affect the reported amounts of assets, liabilities, revenue, expenses and the related disclosures. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that management believes to be relevant at the time our consolidated financial statements are prepared. On a regular basis, we review the accounting policies, assumptions,

estimates and judgments to ensure that our consolidated financial statements are presented fairly and in accordance with GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ from our assumptions and estimates, and such differences could be material.

Our significant accounting policies are discussed in note 1 of the notes to our consolidated financial statements. We believe that the following accounting estimates are the most critical to aid in fully understanding and evaluating our reported financial results, and they require our most difficult, subjective or complex judgments, resulting from the need to make estimates about the effect of matters that are inherently uncertain. We have reviewed these critical accounting estimates and related disclosures with our audit committee.

Revenue Recognition

Our products are fully functional at the time of shipment and do not require production, modification or customization. We recognize revenue from product sales when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collection is reasonably assured. Our fee is considered fixed or determinable at the execution of an agreement, based on specific products and quantities to be delivered at specified prices, which is evidenced by a customer purchase order or other persuasive evidence of an arrangement. Our agreements with non-distributor customers do not include rights of return or acceptance provisions. Product revenue is recognized upon shipment of product to customers, net of accruals for estimated sales returns and allowances, which to date, have not been significant.

Approximately 16% of our sales were made through third-party distributors in 2014. Sales to distributors are included in deferred revenue and we include the related costs in inventory until sales and delivery to the end customers occurs. Distributor arrangements, allow for limited price protection and rights of stock rotation on product unsold by the distributors. The price protection rights allow distributors the right to a credit in the event of declines in the price of our product that they hold prior to the sale to a specific end customer. In the event that we reduce the selling price of products held by distributors, deferred revenue related to distributors with price protection rights is reduced upon notification to the customer of the price change. Additionally, distributors may receive a credit for the price discounts associated with the distributors' customers that purchased those products. We estimate the extent of these distributor price discounts at each reporting period to reduce accounts receivable and deferred revenue, but we do not issue these discounts to the distributor until the inventory is sold to the distributors' customers. Revenue recognition on product sales through distributors is highly dependent on receiving pertinent and accurate data from our distributors in a timely fashion. Distributors provide us periodic data prior to the release of our consolidated financial statements regarding the product, price, quantity and end customer when products are resold, as well as the quantities of our products they still have in stock.

We monitor collectability of accounts receivable primarily through review of the accounts receivable aging. Our policy is to record an allowance for doubtful accounts based on specific collection issues we have identified, aging of underlying receivables and historical experience of uncollectible balances. As of December 31, 2014 and 2013, our allowance for doubtful accounts was \$165,000 and \$152,000, respectively.

We have not made any material changes in the accounting methodology we use to record the allowance for doubtful accounts during the past three years. If actual results are not consistent with the assumptions and estimates used, for example, if the financial condition of the customer deteriorated, we may be required to record additional expense that could materially negatively impact our operating results. To date, however, substantially all of our receivables have been collected within following quarter.

Inventory Valuation

We value our inventory, which includes materials, labor and overhead, at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost, on a first-in, first-out basis. We periodically write-down our inventory to the lower of cost or market based on our estimates that consider historical usage and future demand. These factors are impacted by market and economic conditions, technology changes, new product introductions and changes in strategic direction. The calculation of our inventory valuation requires management to make assumptions and to apply judgment regarding forecasted customer demand and technological obsolescence that may turn out to be inaccurate. Inventory valuation reserves were \$1,949,000 and \$1,479,000 as of December 31, 2014 and 2013, respectively. Inventory valuation reserves, once established, are not reversed until the related inventory has been sold or scrapped.

We have not made any material changes in the accounting methodology we use to record inventory reserves during the past three years. We do not believe there is a reasonable likelihood that there will be a material change in the future estimates or assumptions that we use to calculate our inventory reserve. However, if estimates regarding customer demand are inaccurate or changes in technology affect demand for certain products in an unforeseen manner, we may be exposed to losses or gains that could be material.

Product Warranty

Our products are under warranty against defects in material and workmanship generally for a period of one or two years. We accrue for estimated warranty cost at the time of sale based on anticipated warranty claims and actual historical warranty claims experience including knowledge of specific product failures that are outside of our typical experience. The warranty obligation is determined based on product failure rates, cost of replacement and failure analysis cost. We monitor product returns for warranty-related matters and monitor both a specific and general accrual

for the related warranty expense based on specific circumstances and general historical experience. Our warranty obligation requires management to make assumptions regarding failure rates and failure analysis costs. If actual warranty costs differ significantly from these estimates, adjustments may be required in the future, which would adversely affect our gross margins and operating results. The warranty liability as of December 31, 2014 and 2013, were \$110,000 and \$40,000, respectively.

On November 3, 2014, we received a claim notification from an insurance company asserting a claim of approximately \$4,000,000 for field installation repair and replacement costs incurred by a customer in 2011. We believe that we had fulfilled our contractual obligation to provide warranty repair and replacement, but referred the matter to our insurance carrier at the request of the insurance company. As of December 31, 2014, we believe the liability under this claim is not probable. Nevertheless, resolutions of third-party claims are inherently uncertain and as such, an unfavorable outcome could ultimately impact our business, cash flow and results of operations.

In September 2010, we were informed of a claim related to repair and replacement costs in connection with shipments of over 4,000 integrated circuits made by us during the summer and fall of 2009. We also assessed, provided and accumulated additional warranty reserves based on estimated, probable costs to replace units. In March 2010, we developed additional tests to screen out the wafer die that might be susceptible to a suspected type of failure ultimately related to the lack of a manufacturing process design rule and resumed shipments to the customer. Based on our standard warranty provisions, we provided replacement parts to the customer for the known and suspected failures that had occurred. In 2012, based on additional review investigation and settlement discussions with the customer, we booked an additional warranty cost of \$750,000. This amount was recorded as a reduction to revenue. In June 2012, we entered into a settlement agreement with the customer in which we paid \$1,750,000 in July 2012.

Business combinations

We use the acquisition method of accounting for business combinations and recognize assets acquired and liabilities assumed measured at their fair values on the date acquired. This requires us to recognize separately from goodwill the assets acquired and the liabilities assumed at their acquisition date fair values. Goodwill as of the acquisition date is measured as the excess of consideration transferred over the net of the acquisition date fair values of the assets acquired and the liabilities assumed. While we use our best estimates and assumptions to accurately value assets acquired and liabilities assumed at the acquisition date as well as contingent consideration, where applicable, our estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, we adjust the assets acquired and liabilities assumed with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recognized in our consolidated statements of operations.

Accounting for business combinations requires our management to make significant estimates and assumptions, especially at the acquisition date, including our estimates for intangible assets, contractual obligations assumed and pre-acquisition contingencies, where applicable. Although we believe the assumptions and estimates we have made in the past have been reasonable and appropriate, they are based, in part, on historical experience and information obtained from the management of the acquired companies and are inherently uncertain. Critical estimates in valuing certain of the intangible assets we have acquired include, but are not limited to: future expected cash flows from product sales, customer contracts and acquired technologies, expected costs to develop in-process research and development into commercially viable products, estimated cash flows from the projects when completed, and discount rates. Unanticipated events and circumstances may occur that may affect the accuracy or validity of such assumptions, estimates or actual results.

Goodwill and Purchased Intangible Assets

Goodwill is recorded as the difference, if any, between the aggregate consideration paid for an acquisition and the fair value of the acquired net tangible and intangible assets. The amounts and useful lives assigned to intangible assets acquired, other than goodwill, impact the amount and timing of future amortization. The value of our intangible assets, including goodwill, could be impacted by future adverse changes such as: (a) any future declines in our operating results, (b) a decline in the valuation of technology company stocks, including the valuation of our common stock, (c) a further significant slowdown in the worldwide economy or the semiconductor industry, (d) any failure to meet the performance projections included in our forecasts of future operating results or (e) the abandonment of any of our acquired in-process research and development projects. We evaluate goodwill and purchased intangible assets deemed to have indefinite lives, on an annual basis in the fourth quarter or more frequently if we believe indicators of impairment exist. Significant management judgment is required in performing periodic impairment tests. The testing for a potential impairment of goodwill involves a two-step process. The first step involves comparing the estimated fair values of our reporting unit with the book values, including goodwill. If the estimated fair value exceeds book value, goodwill is considered not to be impaired and no additional steps are necessary. If, however, the fair value of the reporting unit is less than book value, then the carrying amount of the goodwill is compared with its implied fair value. The estimate of implied fair value of goodwill may require valuations of certain internally generated and unrecognized intangible assets such as our technology, customer relationships, patents and trademarks. If the carrying amount of goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to the excess. If our actual results, or the plans and estimates used in future impairment analyses, are lower than the original estimates used to assess the recoverability of these assets, we could incur additional impairment charges. The acquisition of Cortina on October 3, 2014 increased our goodwill and identifiable intangible assets by \$3,530,000 and \$82,410,000, respectively. See note 2 to the notes to our consolidated financial statements.

Stock-Based Compensation

We account for stock-based compensation in accordance with authoritative guidance which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors based on the grant date fair values of the awards. The fair value of stock option awards is estimated using the Black-Scholes

option pricing model. The fair value of restricted stock units is based on the fair market value of our common stock on the date of grant. The value of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in our consolidated statements of operations. We elected to treat share-based payment awards with graded vesting schedules and time-based service conditions as a single award and recognize stock-based compensation expense on a straight-line basis (net of estimated forfeitures) over the requisite service period. Stock-based compensation expenses are classified in the consolidated statement of operations based on the department to which the related employee reports.

We account for stock options issued to non-employees in accordance with the guidance for equity-based payments to non-employees. Stock option awards to non-employees are accounted for at fair value using the Black-Scholes option pricing model. Our management believes that the fair value of stock options is more reliably measured than the fair value of the services received. The fair value of the unvested portion of the options granted to non-employees is re-measured each period. The resulting increase in value, if any, is recognized as expense during the period the related services are rendered.

The Black-Scholes option pricing model requires management to make assumptions and to apply judgment in determining the fair value of our awards. The most significant assumptions and judgments include estimating the fair value of underlying stock, expected volatility and expected term. In addition, the recognition of stock-based compensation expense is impacted by estimated forfeiture rates.

We estimated the expected volatility from the historical volatilities of several unrelated public companies within the semiconductor industry because our common stock has limited trading history. When selecting the public companies used in the volatility calculation, we selected companies in the semiconductor industry with comparable characteristics to us, including stage of development, lines of business, market capitalization, revenue and financial leverage. The weighted average expected life of options was calculated using the simplified method. This decision was based on the lack of relevant historical data due to our limited experience and the lack of active market for our common stock. The risk-free interest rate is based on the U.S. Treasury yields in effect at the time of grant for periods corresponding to the expected term of the options. The expected dividend rate is zero based on the fact that we have not historically paid dividends and have no intention to pay cash dividends in the foreseeable future. The forfeiture rate is established based on the historical average period of time that options were outstanding and adjusted for expected changes in future exercise patterns.

We do not believe there is a reasonable likelihood that there will be material changes in the estimates and assumptions we use to determine stock-based compensation expense. In the future, if we determine that other option valuation models are more reasonable, the stock-based compensation expense that we record in the future may differ significantly from what we have recorded using the Black-Scholes option pricing model.

Income Taxes

Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax rates and laws that will be in effect when and where the differences are expected to reverse. We record a valuation allowance to reduce deferred tax assets to the amount that we believe is more likely than not to be realized. In assessing the need for a valuation allowance, we consider all positive and negative evidence, including scheduled reversals of deferred tax liabilities, historical levels of income, projections of future income, expectations and risk associated with estimates of future taxable income and ongoing prudent and practical tax planning strategies. To the extent that we believe it is more likely than not that some portion of our deferred tax assets will not be realized, we would increase the valuation allowance against deferred tax assets. The determination of recording or releasing a tax valuation allowance is made, in part, pursuant to an assessment performed by management regarding the likelihood that we will generate sufficient future taxable income against which the benefits of our deferred tax assets may or may not be realized. This assessment requires management to exercise significant judgment and make estimates with respect to our ability to generate revenue, gross profits, operating income and taxable income in future periods. Among other factors, management must make assumptions regarding current and projected overall business and semiconductor industry conditions, operating efficiencies, our ability to timely develop, introduce and consistently manufacture new products to meet our customers' needs and specifications, our ability to adapt to technological changes and the competitive environment, which may impact our ability to generate taxable income and, in turn, realize the value of our deferred tax assets. Although, we believe that the judgment we used is reasonable, actual results can differ due to a change in market conditions, changes in tax laws and other factors.

We have valuation allowance against deferred tax assets for the years ended December 31, 2014, 2013 and 2012. The decision to establish the valuation allowance in 2012 was due to negative evidence that includes our cumulative losses in U.S., Singapore and Taiwan after considering permanent tax differences and the passage of new California tax law requiring use of single sales factor which reduces the amount of California taxable income starting 2013.

In accordance with FASBs guidance on Accounting for Uncertainty in Income Taxes, we perform a comprehensive review of uncertain tax positions regularly. The guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken, or expected to be taken, in a tax return. We determine the tax liability for uncertain tax positions based on a two-step process. The first step is to determine whether it is more likely than not based on technical merits that each income tax position would be sustained upon examination. The second step is to measure the tax benefit as the largest amount that has a greater than 50% likelihood of being realized upon ultimate settlement with a tax authority that has full knowledge of all relevant information. The assessment of each tax position requires significant judgment and estimates. We believe our tax return positions are fully supported, but tax authorities could challenge certain positions, which may not be fully sustained. All tax positions are periodically analyzed and adjusted as a result of events, such as the resolution of tax audits, issuance of new regulations or new case law, negotiations with tax authorities, and expiration of statutes of limitations.

Results of Operations and Key Operating Metrics

The following describes the line items in the statements of operations, which we consider to be our key operating metrics.

Revenue. We generate revenue from sales of our semiconductor products to end customers. A portion of our products is sold indirectly to customers through distributors.

We design and develop high-speed analog semiconductor solutions for the communications and computing markets. Our revenue is driven by various trends in these markets. These trends include the deployment and broader market adoption of next generation 100G technologies in communications and enterprise networks, the timing of next generation network and enterprise server upgrades in different geographic locations worldwide, the introduction and broader market adoption of next generation server platforms such as Intel’s Haswell-based platform, and the deployment of high-speed memory interfaces in server and computing platforms.

Our revenue is also impacted by changes in the number and average selling prices of our semiconductor products. Our products are typically characterized by a life cycle that begins with higher average selling prices and lower volumes, followed by broader market adoption, higher volumes, and average selling prices that are lower than initial levels.

We operate in industries characterized by rapidly changing technologies and industry standards as well as technological obsolescence. Our revenue growth is dependent on our ability to continually develop and introduce new products to meet the changing technology and performance requirements of our customers, diversify our revenue base and generate new revenue to replace, or build upon, the success of previously introduced products which may be rapidly maturing. As a result, our revenue is impacted to a more significant extent by product life cycles for a variety of products and to a much lesser extent, if any, by any single product. In 2011, we began to ship in production volume a new “ultra-low voltage” version of our integrated PLL and register buffer, which is shipping in the form of product number INSSTE32882UV-GS02, or the GS02UV product. Sales of the GS02UV product comprised 15%, 39% and 45% of our total revenue in 2014, 2013 and 2012, respectively. In 2010, we introduced and began to ship in commercial volume a dual, differential linear TIA, which we identify as product number 2850TA-SO1D. Sales of 2850TA-SO1D product comprised 10% and 14% of our total revenue in 2013 and 2012, respectively. In 2012, we introduced and began to ship in commercial volume a dual, differential input linear transimpedance/variable-gain amplifier that we identify as product number IN3250TA-SO2D. Sales of IN3250TA-SO2D product comprised 14% of our total revenue in 2014. In 2015, we expect that revenue from sales of IN3250TA-SO2D will be significant.

The following table is based on the geographic location to which our product is initially shipped. In most cases this will differ from the ultimate location of the end user of a product containing our technology. For sales to our distributors, their geographic location may be different from the geographic locations of the ultimate end customer. Sales by geography for the periods indicated were:

	Year Ended December 31,		
	2014	2013	2012
	(in thousands)		
China	\$54,312	\$23,039	\$20,724
United States	22,918	22,389	21,582
Korea	10,123	21,818	17,424

Other	68,789	35,418	31,476
	\$156,142	\$102,664	\$91,206

In 2013, we were shipping products to a customer in Korea. However, in 2014, this customer requested to ship majority of the products to their facility in China, which resulted in a significant shift in revenue between China and Korea. In addition, the increase in shipments to China was due to revenue generated from Cortina during the fourth quarter of 2014.

Cost of revenue. Cost of revenue includes cost of materials such as wafers processed by third-party foundries, costs associated with packaging and assembly, test and shipping, cost of personnel, including stock-based compensation, as well as equipment associated with manufacturing support, logistics and quality assurance, warranty costs, write down of inventories, amortization of production mask costs, amortization of developed technology, amortization of step-up values of inventory, overhead and other indirect costs, such as allocated occupancy and information technology, or IT, costs.

As some semiconductor products mature and unit volumes increase, their average selling prices may decline. These declines are often paired with improvements in manufacturing yields and lower wafer, assembly and test costs, which offset some of the margin reduction that results from lower prices. However, our gross profit, period over period, may fluctuate as a result of changes in average selling prices due to new product introductions or existing product transitions into larger scale commercial volumes, manufacturing costs as well as our product mix.

Research and development. Research and development expense includes personnel-related expenses, including salaries, stock-based compensation and employee benefits. It also includes pre-production engineering mask costs, software license expenses, prototype wafer, packaging and test costs, design and development costs, testing and evaluation costs, depreciation expense and other indirect costs. All research and development costs are expensed as incurred. We enter into development agreements with some of our customers. Recoveries from nonrecurring engineering services are recorded as an offset to product development expense incurred in support of this effort since these activities do not represent an earning process core to our business and serve as a mechanism to partially recover development expenditures. These reimbursements are recognized upon completion and acceptance by the customer of contract deliverables or milestones. We expect research and development expense to increase in absolute dollars as we continue to invest resources to develop more products and enhance our existing product portfolio.

Sales and marketing. Sales and marketing expense consists primarily of salaries, stock-based compensation, employee benefits, travel, promotions, trade shows, marketing and customer support, commission payments to employees, depreciation expense and other indirect costs. We expect sales and marketing expense to increase in absolute dollars to support the growth of our business and promote our products to current and potential customers.

General and administrative. General and administrative expense consists primarily of salaries, stock-based compensation, employee benefits and expenses for executive management, legal, and finance. In addition, general and administrative expenses include fees for professional services and other indirect costs. We expect general and administrative expense to increase in absolute dollars due to the general growth of our business and the costs associated with becoming a public company for, among other things, SEC reporting and compliance, director fees, insurance, transfer agent fees and similar expenses.

Provision (benefit) for income taxes. For the year ended December 31, 2012, we recorded provision for income taxes of \$13.7 million, which reflects an effective tax rate of 195%. The effective tax rate of 195% differs from the statutory rate of 35% primarily due to the full valuation allowance established against net deferred tax assets and, to a lesser extent, foreign income taxes provided at lower rates, geographic mix in profitability, recognition of research and development credits and unrecognized tax benefits. For the year ended December 31, 2013, we recorded provision for income taxes of \$1.8 million, which reflects an effective tax rate of 15%. The effective tax rate of 15% differs from the statutory rate of 34% primarily due to the an increase in valuation allowance, foreign income taxes provided at lower rates, geographic mix in profitability, unrecognized tax benefits and recognition of research and development credits. For the year ended December 31, 2014, we recorded provision for income taxes of \$1.7 million, which reflects an effective tax rate of 8%. The effective tax rate of 8% differs from the statutory rate of 34% primarily due to increase in valuation allowance, foreign income taxes provided at lower rates, geographic mix in profitability, unrecognized tax benefits, transaction cost adjustment and recognition of research and development credits.

The following table sets forth a summary of our statement of operations for the periods indicated:

	Year Ended December 31,		
	2014	2013	2012
	(in thousands)		
Total revenue	\$156,142	\$102,664	\$91,206
Cost of revenue	70,488	37,095	32,684
Gross profit	85,654	65,569	58,522
Operating expense:			
Research and development	70,863	50,516	40,102
Sales and marketing	20,003	15,741	14,052
General and administrative	16,153	11,614	12,300
Total operating expenses	107,019	77,871	66,454
Loss from operations	(21,365)	(12,302)	(7,932)
Interest and other income	495	876	914

Edgar Filing: INPHI Corp - Form 10-K

Loss before income taxes	(20,870)	(11,426)	(7,018)
Provision for income taxes	1,738	1,752	13,673
Net loss	\$(22,608)	\$(13,178)	\$(20,691)

The following table sets forth a summary of our statement of operations as a percentage of each line item to the revenue:

	Year Ended		
	December 31,		
	2014	2013	2012
Total revenue	100%	100 %	100 %
Cost of revenue	45	36	36
Gross profit	55	64	64
Operating expense:			
Research and development	45	49	44
Sales and marketing	13	16	15
General and administrative	10	11	14
Total operating expenses	68	76	73
Loss from operations	(13)	(12)	(9)
Interest and other income	-	1	1
Loss before income taxes	(13)	(11)	(8)
Provision (benefit) for income taxes	1	2	15
Net loss	(14)%	(13)%	(23)%

Comparison of the Years Ended December 31, 2014, 2013 and 2012**Revenue**

Year Ended December 31,			Change	2013			
2014	2013	2012	2014		Amount	%	
			Amount	%	Amount	%	
(dollars in thousands)							
Total revenue	\$156,142	\$102,664	\$91,206	\$53,478	52%	\$11,458	13%

Total revenue for the year ended December 31, 2014 increased by \$53.5 million due to year over year increase in average selling price of 63%, partially offset by a decrease in the number of units sold of 7%. The increase in average selling price was due to product mix, mainly from sales of our higher priced products including dual linear TIA, quad linear driver products, iMB™, high-speed interconnect and optical transport products. For the year ended December 31, 2014, the number of units sold decreased by 7% mainly from decrease in consumption of our other high speed memory interface products. We believe the reduction in the unit consumption of high speed memory is the natural result of migration to higher capacity DiMM cards at economic prices made possible in part by the availability of higher capacity DRAM at economic prices. In effect, a requirement for the same or more memory capacity can now be placed on a single card, thereby naturally absorbing the same or more aggregate memory requirement into a smaller number of cards.

Total revenue for the year ended December 31, 2013 increased by \$11.5 million due to year over year increase in number of units sold and average selling price of 7% and 4%, respectively. The increase in number of units sold was due to sale of high speed memory interface products, dual, differential linear TIA, iPHY 100Gbe CMOS gearbox products and iMB™. The increase in average selling price of 4% was due to product mix. In addition, revenue increased by \$0.8 million due to provision for estimated settlement of a warranty claim with a customer that was several years old, which was recorded as a reduction in revenue for the year ended December 31, 2012.

Cost of Revenue and Gross Profit

Year Ended December 31,			Change	2013		
2014	2013	2012	2014		Amount	%
			Amount	%	Amount	%

	(dollars in thousands)							
Cost of revenue	\$70,488	\$37,095	\$32,684	\$33,393	90 %	\$4,411	13 %	
Gross profit	85,654	65,569	58,522	20,085	31 %	7,047	12 %	
Gross profit as a percentage of revenue	55 %	64 %	64 %	—	(9%)	—	—	

Cost of revenue and gross profit for the year ended December 31, 2014 increased by \$33.4 million and \$20.1 million, respectively, compared to the prior year primarily due to increase in revenue from sales our dual linear TIA, quad linear driver products, iMB™, high-speed interconnect and optical transport products which generated higher margin. Product costs as a percentage of revenue decreased due to the amortization of inventory fair value step-up related to the acquired Cortina inventories, sold during the fourth quarter of 2014 and amortization of the acquired intangibles.

Cost of revenue and gross profit for the year ended December 31, 2013 increased by \$4.4 million and \$7.0 million, respectively, compared to the prior year, primarily due to increase in the number of units purchased by customers of our high speed memory interface products, TIA, iPHY 100Gbe CMOS gearbox products and iMB™, consistent with the overall increase in revenue. Product costs as a percentage of revenue were relatively unchanged compared to the prior year.

Research and Development

	Year Ended December 31,			Change		2013	
	2014	2013	2012	2014	%	Amount	%
	(dollars in thousands)						
Research and development	\$70,863	\$50,516	\$40,102	\$20,347	40 %	\$10,414	26 %

Research and development expense for the year ended December 31, 2014 increased by \$20.3 million due to the increase in research and development headcount from new employees hired in 2014 and as a result of the acquisition of Cortina, which resulted in a \$12.9 million and \$3.8 million increase in personnel costs and stock-based compensation expense, respectively. Consulting fees and CAD software tool license expense increased by \$2.2 million and \$2.0 million, respectively, primarily due to an increase in headcount and engineering activities. In addition, external test services and pre-production engineering mask costs increased by \$2.0 million. Depreciation and allocated expenses increased by \$5.2 million, primarily, due to an increase in equipment and research and development activities. The increases were partially offset by higher reimbursement from customers related to research and development contracts of \$9.3 million due to new development contracts entered with the customers in 2014. The increase in research and development expense was primarily driven by acquisition of Cortina and our strategy to continue to expand our product offerings and enhance our existing products.

Research and development expense for the year ended December 31, 2013 increased by \$10.4 million primarily due to the increase in research and development headcount, which resulted in a \$7.5 million increase in personnel costs and stock-based compensation expense and \$1.5 million increase in CAD software tool license expense. In addition, total reimbursement from customers related to research and development contracts was lower by \$1.5 million due to expiration of a contract in 2012. The increases were partially offset by a decrease in consulting expenses by \$1.6 million, in turn due to the hiring of engineers. The increase in research and development expense was driven by our strategy to continue to expand our product offerings and enhance our existing products.

Sales and Marketing

	Year Ended December 31,			Change		2013	
	2014	2013	2012	2014 Amount	%	Amount	%
(dollars in thousands)							
Sales and marketing	\$20,003	\$15,741	\$14,052	\$4,262	27%	\$1,689	12%

Sales and marketing expense for the year ended December 31, 2014 increased by \$4.3 million, primarily due to an increase in personnel costs, including stock-based compensation expense of \$3.2 million, to support increasing sales activities from new developed products and from the Cortina acquisition.

Sales and marketing expense for the year ended December 31, 2013 increased primarily due to an increase in personnel costs, including stock-based compensation expense and consulting fees of \$1.6 million, to support increasing sales activities.

General and Administrative

	Year Ended December 31,			Change		2013	
	2014	2013	2012	2014 Amount	%	Amount	%
	(dollars in thousands)						
General and administrative	\$16,153	\$11,614	\$12,300	\$4,539	39%	\$(686)	(6%)

General and administrative expenses for the year ended December 31, 2014 increased primarily due to increase in outside legal fees of \$1.8 million in connection with the acquisition of Cortina. In addition, personnel costs and stock-based compensation expense increased by \$1.6 million due to new hires from Cortina and stock grants awarded in 2014.

General and administrative expenses for the year ended December 31, 2013 decreased primarily due to accrual of provisional costs related to employment and other related claims, as well as associated costs of \$1.0 million we recorded during the year ended December 31, 2012. In addition, outside legal fees decreased by \$0.4 million, primarily related to reduced expenditures for litigation matters described in Note 15 of the notes to our financial statements. The decreases were partially offset by increase in stock-based compensation expense of \$0.9 million.

Provision (benefit) for Income Taxes

	Year Ended December 31,			Change		
				2014	2013	
	2014	2013	2012	Amount [%]	Amount	%
	(dollars in thousands)					
Provision (benefit) for income taxes	\$1,738	\$1,752	\$13,673	\$(14)	—\$(11,921)	N/M

For the year ended December 31, 2014, we recorded a provision for income taxes of \$1.7 million, which reflects an effective tax rate of 8%. The effective tax rate of 8% differs from the statutory rate of 34% primarily due to the change in valuation allowance, foreign income taxes provided at lower rates, geographic mix in profitability, unrecognized tax benefits, transaction costs adjustments and recognition of research and development credits.

For the year ended December 31, 2013, we recorded a provision for income taxes of \$1.8 million, which reflects an effective tax rate of 15%. The effective tax rate of 15% differs from the statutory rate of 34% primarily due to the change in valuation allowance, foreign income taxes provided at lower rates, geographic mix in profitability, unrecognized tax benefits and recognition of research and development credits.

For the year ended December 31, 2012, we recorded a provision for income taxes of \$13.7 million, which reflects an effective tax rate of 195%. The effective tax rate of 195% differs from the statutory rate of 35% primarily due to full valuation allowance established against deferred tax assets and, to a lesser extent, foreign income taxes provided at lower rates, geographic mix in profitability and recognition of research and development credits. We established full valuation allowance against deferred tax assets for the year ended December 31, 2012. The decision to establish the valuation allowance was due to negative evidence which includes the passage of California tax law requiring the use of single sales factor, which reduces the amount of California taxable income starting 2013 and our recent cumulative losses in U.S., Singapore and Taiwan after considering permanent tax differences.

We operate under tax holiday in Singapore, which is effective through May 2020. The tax holiday is conditional upon our meeting certain employment, activities and investment thresholds. There was no impact of the Singapore tax holiday on our Singapore taxes in 2014, 2013 and 2012. The benefit of tax holidays has no material impact on diluted earnings per share.

Liquidity and Capital Resources

As of December 31, 2014, we had cash and cash equivalents and investments in marketable securities of \$69.3 million. Our primary uses of cash are to fund operating expenses, purchase inventory and acquire property and equipment. Cash used to fund operating expenses is impacted by the timing of when we pay these expenses, as reflected in the changes in our outstanding accounts payable and accrued expenses. Our primary sources of cash are cash receipts on accounts receivable from our revenue. Aside from the growth in amounts billed to our customers, net cash collections of accounts receivable are impacted by the efficiency of our cash collections process, which can vary from period to period, depending on the payment cycles of our major customers.

The following table summarizes our cash flows for the periods indicated:

	Years Ended December 31,		
	2014	2013	2012
	(in thousands)		
Net cash provided by operating activities	\$8,386	\$18,658	\$6,468
Net cash used in investing activities	(11,744)	(20,098)	(10,509)
Net cash provided by financing activities	2,057	2,946	4,506
Net increase (decrease) in cash and cash equivalents	\$(1,301)	\$1,506	\$465

Net Cash Provided by Operating Activities

Net cash provided by operating activities in 2014 primarily reflected depreciation and amortization of \$10.9 million, stock-based compensation of \$22.5 million, abandonment of assets of \$1.2 million, amortization of intangibles of \$3.2 million, amortization of deferred tax charge of \$0.9 million, amortization of premiums on marketable securities of \$0.8 million, decrease in inventories of \$10.1 million and increase in deferred revenue of \$5.4 million offset by net loss of \$22.6 million, increase in accounts receivable by \$8.7 million, increase in prepaid expenses by \$3.3 million, decrease in accounts payable and accrued expenses by \$10.3 million and decrease in other liabilities of \$1.7 million. Our inventories, net of acquired inventories from Cortina acquisition decreased due to shipments to customers. Our deferred revenue increased due to acquisition of Cortina and distributors increased their inventory level for shipment to customers in the first quarter of 2015. Accounts receivable increased due to higher shipments made in the last month of the quarter, including Cortina's products. Our prepaid expenses and other assets increased as a result of new subscriptions with vendors and related prepayments. Our accounts payable and accrued expenses, net of assumed liabilities from Cortina acquisition, decreased due to payment to vendors and employees. Other liabilities decreased due to amortization of advance payment received from a customer in 2013.

We completed the acquisition of Cortina for approximately \$52.5 million in cash and approximately 5.3 million shares of our common stock. At the closing of the Cortina acquisition, solely for purposes of convenience, Cortina also provided cash to the Company of approximately \$17.2 million and simultaneously directed the Company to use the cash to make certain post-acquisition payments of either acquisition- related, or pre- acquisition obligations that the Definitive Agreement between the Company and Cortina would not have required the Company to assume. As a clarification to our previous disclosures and comments in our earnings call, the amount of Cortina cash acquired by the Company of \$17.2 million reduces the amount of cash paid for the acquisition of Cortina of \$52.5 million as presented on the statement of cash flows under GAAP, and as a result, the amount reported in the statement of cash flows for the acquisition of Cortina is \$35.3 million for the year ended December 31, 2014. In addition, in discussing our preliminary fourth quarter results, we disclosed estimated cash flows from operations in the fourth quarter of approximately \$16 million, which was exclusive of the post-acquisition payments related to Cortina of \$17.2 million and thus the amount was disclosed on a non-GAAP basis. As the post-acquisition payments were made in the year ended December 31, 2014 and related to operating cash flow activities, the amounts paid have been reflected in the cash flow from operations in the statement of cash flows under GAAP for the year ended December 31, 2014.

Net cash provided by operating activities in 2013 primarily reflected depreciation and amortization of \$7.5 million, stock-based compensation of \$17.0 million, impairment charge of \$0.5 million, amortization of deferred tax charge of \$0.9 million, amortization of premiums on marketable securities of \$1.0 million, change in income tax receivable/payable by \$3.0 million, increase in accounts payable and accrued expenses of \$2.0 million, increase in deferred revenue of \$0.6 million and other liabilities of \$1.3 million offset by net loss of \$13.2 million and increase in inventories of \$1.9 million. Our accounts payable and accrued expenses increased as a result of increased production volume and employee related expenses. Our deferred revenue increased as distributors increased their inventory level for shipment to customers in the first quarter of 2014. Other liabilities increased due to advance payment received from a customer, which will be used in 2014. Our inventories increased a result of growing production for expected delivery to customers in the first quarter of 2014.

Net cash provided by operating activities in 2012 primarily reflected depreciation and amortization of \$4.9 million, stock-based compensation of \$12.5 million, deferred income taxes of \$10.0 million, amortization of deferred tax charge of \$1.0 million, amortization of premiums on marketable securities of \$1.2 million, change in income tax receivable/payable by \$2.7 million, decrease in inventories of \$0.8 million and increase in accounts payable and accrued expenses of \$1.5 million offset by net loss of \$20.7 million, excess tax benefit related to stock-based compensation of \$2.1 million, increase in accounts receivable of \$4.4 million and decrease in deferred revenue of \$0.8 million. Our inventories decreased due to shipments to customers. Our accounts payable and accrued expenses increased as a result of increased production volume and employee related expenses. Accounts receivable increased due to shipments made in the last month of the quarter. Our deferred revenue decreased as distributors reduced their inventory levels shipped parts to end customers to meet their demand.

Net Cash Used in Investing Activities

In 2014, net cash used in investing activities consisted of cash used to purchase investment in marketable securities of \$38.6 million, acquisition of Cortina of \$35.3 million, net of cash acquired, purchases of property and equipment of \$21.2 million, mainly for laboratory, production and computer equipment and leasehold improvements for our offices, purchase of minority interest in an early stage private company for \$5.0 million and purchase of patents for \$1.6 million offset by sales and maturities of marketable securities of \$89.9 million

In 2013, net cash used in investing activities consisted of cash used to purchase investment in marketable securities of \$43.1 million, purchases of property and equipment of \$16.6 million, mainly for laboratory and production equipment and leasehold improvements for our offices in California, purchase of minority interest in an early stage private company for \$2.6 million offset by sales and maturities of marketable securities of \$42.2 million.

In 2012, net cash used in investing activities consisted of cash used to purchase investment in marketable securities of \$47 million and purchases of property and equipment of \$8.4 million, mainly for laboratory and production equipment and leasehold improvements for our offices in California, offset by sales and maturities of marketable securities of \$44.7 million.

Net Cash Provided by Financing Activities

Net cash provided by financing activities in 2014, consisted primarily of proceeds from exercise of stock options and employee stock purchase plan of \$7.0 million. This was offset, in part, by the minimum tax withholding paid on behalf of employees for restricted stock units of \$5.0 million.

Net cash provided by financing activities in 2013, consisted primarily of proceeds from exercise of stock options and employee stock purchase plan of \$5.1 million. This was offset, in part, by the minimum tax withholding paid on behalf of employees for restricted stock units of \$2.2 million.

Net cash provided by financing activities in 2012, consisted primarily of \$2.8 million proceeds from exercise of stock options and employee stock purchase plan and excess tax benefit related to stock-based compensation of \$2.1 million. This was offset, in part, by the minimum tax withholding paid on behalf of employees for restricted stock units of \$0.3 million.

Operating and Capital Expenditure Requirements

Our principal source of liquidity as of December 31, 2014 consisted of \$69.3 million of cash, cash equivalents and investments in marketable securities. Based on our current operating plan, we believe that our existing cash and cash equivalents and investments in marketable securities from operations will be sufficient to finance our operational cash needs through at least the next 12 months. In the future, we expect our operating and capital expenditures to increase as we increase headcount, expand our business activities and grow our end customer base which will result in higher needs for working capital. Our ability to generate cash from operations is also subject to substantial risks described in Part I, "Item 1A., Risk Factors." If any of these risks occur, we may be unable to generate or sustain positive cash flow from operating activities. We would then be required to use existing cash and cash equivalents to support our working capital and other cash requirements. If additional funds are required to support our working capital requirements, acquisitions or other purposes, we may seek to raise funds through debt financing or from other sources. If we raise additional funds through the issuance of equity or convertible debt securities, the percentage ownership of our stockholders could be significantly diluted, and these newly-issued securities may have rights, preferences or privileges senior to those of existing stockholders. If we raise additional funds by obtaining loans from third parties, the terms of those financing arrangements may include negative covenants or other restrictions on our business that could impair our operating flexibility, and would also require us to incur interest expense. We can provide no assurance that additional financing will be available at all or, if available, that we would be able to obtain additional financing on terms favorable to us.

Contractual Obligations, Commitments and Contingencies

The following table summarizes our outstanding contractual obligations as of December 31, 2014:

	Payments due by period				
Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years	
	(in thousands)				
Operating lease obligations	\$33,263	\$15,131	\$15,129	\$3,003	—

As of December 31, 2014, we recorded a liability for our uncertain tax position of \$4.5 million. We are unable to reasonably estimate the timing of payments in individual years due to uncertainties in the timing of the effective settlement of tax positions.

We depend upon third party subcontractors to manufacture our wafers. Our subcontractor relationships typically allow for the cancellation of outstanding purchase orders, but require payment of all expenses incurred through the date of cancellation. As of December 31, 2014, the total value of open purchase orders for wafers was approximately \$10.3 million.

Off-Balance Sheet Arrangements

Since our inception, we have not engaged in any off-balance sheet arrangements, such as the use of structured finance, special purpose entities or variable interest entities.

Recent Authoritative Accounting Guidance

See Note 1 of the notes to our consolidated financial statements for information regarding recently issued accounting pronouncements.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

Interest Rate Sensitivity

We had cash and cash equivalents and investments in marketable securities of \$69.3 million and \$122.6 million at December 31, 2014 and December 31, 2013, respectively, which was held for working capital purposes. Our exposure to market interest-rate risk relates primarily to our investment portfolio. We do not use derivative financial instruments to hedge the market risks of our investments. We manage our total portfolio to encompass a diversified pool of investment-grade securities to preserve principal and maintain liquidity. We place our investments with high-quality issuers, money market funds and debt securities. Our investment portfolio as of December 31, 2014 consisted of money market funds, U.S. Treasuries, municipal bonds, corporate bonds, certificates of deposit and asset backed securities. Investments in both fixed rate and floating rate instruments carry a degree of interest rate risk. Fixed rate securities may have their market value adversely impacted due to an increase in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates or if the decline in fair value of our publicly traded debt investments is judged to be other-than-temporary. We may suffer losses in principal if we are forced to sell securities that have declined in market value due to changes in interest rates. However, because any debt securities we hold are classified as available-for-sale, no gains or losses are realized in the income statement due to changes in interest rates unless such securities are sold prior to maturity or unless declines in value are determined to be other-than-temporary. These securities are reported at fair value with the related unrealized gains and losses, net of applicable taxes, included in accumulated other comprehensive income (loss), reported in a separate component of

stockholders' equity. Although, we currently expect that our ability to access or liquidate these investments as needed to support our business activities will continue, we cannot ensure that this will not change. We believe that, if market interest rates were to change immediately and uniformly by 10% from levels at December 31, 2014, the impact on the fair value of these securities or our cash flows or income would not be material.

In a declining interest rate environment, as short-term investments mature, reinvestment occurs at less favorable market rates. Given the short-term nature of certain investments, the current interest rate environment may negatively impact our investment income.

Our cash and cash equivalents and investment in marketable securities at December 31, 2014 consisted of \$54.4 million held domestically, with the remaining balance of \$14.9 million held by foreign subsidiaries. There may be adverse tax effects upon repatriation of these funds to the United States. We do not plan to repatriate cash balances from foreign subsidiaries to fund our operations in the United States.

Foreign Currency Risk

To date, our international customer and vendor agreements have been denominated almost exclusively in United States dollars. Accordingly, we have limited exposure to foreign currency exchange rates and do not currently enter into foreign currency hedging transactions.

Item 8. *Financial Statements and Supplementary Data*

Index to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm	47
Consolidated Balance Sheets	48
Consolidated Statements of Operations	49
Consolidated Statements of Comprehensive Income (Loss)	50
Consolidated Statements of Stockholders' Equity	51
Consolidated Statements of Cash Flows	52
Notes to Consolidated Financial Statements	53

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Inphi Corporation:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, comprehensive income (loss), stockholders' equity and cash flows present fairly, in all material respects, the financial position of Inphi Corporation and its subsidiaries at December 31, 2014 and 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Annual Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become

inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As described in Management's Annual Report on Internal Control over Financial Reporting appearing under Item 9A, management has excluded Cortina Systems, Inc. from its assessment of internal control over financial reporting as of December 31, 2014 because it was acquired by the Company in a purchase business combination during 2014. We have also excluded Cortina Systems, Inc. from our audit of internal control over financial reporting. Cortina Systems, Inc. is a wholly-owned subsidiary whose total assets and total revenues represent 19% and 13%, respectively of the related consolidated financial statement amounts as of and for the year ended December 31, 2014.

/s/PricewaterhouseCoopers LLP

San Jose, CA

March 10, 2015

Inphi Corporation**Consolidated Balance Sheets**

(in thousands, except share and per share amounts)

	December 31,	
	2014	2013
Assets		
Current assets:		
Cash and cash equivalents	\$30,366	\$31,667
Investments in marketable securities	38,908	90,890
Accounts receivable, net	36,914	13,073
Inventories	26,650	6,767
Deferred tax assets	678	1,099
Income tax receivable	204	240
Prepaid expenses and other current assets	6,779	2,361
Total current assets	140,499	146,097
Property and equipment, net	35,498	22,460
Goodwill	9,405	5,875
Identifiable intangible assets, net	80,773	—
Deferred tax charge	3,261	4,200
Other assets, net	9,274	3,710
Total assets	\$278,710	\$182,342
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$7,884	\$7,280
Deferred revenue	7,110	1,686
Accrued employee expenses	9,492	4,626
Other accrued expenses	4,952	1,611
Other current liabilities	2,689	1,881
Total current liabilities	32,127	17,084
Other long-term liabilities	7,409	5,865
Total liabilities	39,536	22,949
Commitments and contingencies (Note 15)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized; no shares issued	—	—
Common stock, \$0.001 par value; 500,000,000 shares authorized; 37,310,963 and 30,244,439 issued and outstanding at December 31, 2014 and 2013, respectively	37	30
Additional paid-in capital	327,475	225,007
Accumulated deficit	(89,190)	(66,582)
Accumulated other comprehensive income	852	938
Total stockholders' equity	239,174	159,393

Total liabilities and stockholders' equity

\$278,710 \$182,342

The accompanying notes are an integral part of these consolidated financial statements.

Inphi Corporation**Consolidated Statements of Operations**

(in thousands, except share and per share amounts)

	Year Ended December 31,		
	2014	2013	2012
Revenue	\$156,142	\$102,664	\$91,206
Cost of revenue	70,488	37,095	32,684
Gross profit	85,654	65,569	58,522
Operating expenses:			
Research and development	70,863	50,516	40,102
Sales and marketing	20,003	15,741	14,052
General and administrative	16,153	11,614	12,300
Total operating expenses	107,019	77,871	66,454
Loss from operations	(21,365)	(12,302)	(7,932)
Interest and other income	495	876	914
Loss before income taxes	(20,870)	(11,426)	(7,018)
Provision for income taxes	1,738	1,752	13,673
Net loss	\$(22,608)	\$(13,178)	\$(20,691)
Earnings per share:			
Basic	\$(0.69)	\$(0.45)	\$(0.73)
Diluted	\$(0.69)	\$(0.45)	\$(0.73)
Weighted-average shares used in computing earnings per share:			
Basic	32,707,868	29,493,005	28,378,680
Diluted	32,707,868	29,493,005	28,378,680

The accompanying notes are an integral part of these consolidated financial statements.

Inphi Corporation**Consolidated Statements of Comprehensive Income (Loss)****(in thousands)**

	Year Ended December 31,		
	2014	2013	2012
Net loss	\$(22,608)	\$(13,178)	\$(20,691)
Other comprehensive income (loss):			
Available for sale investments:			
Change in unrealized gain, net of \$45, \$(80) and \$176 tax expense (benefit) in 2014, 2013 and 2012, respectively	11	(88)	364
Realized loss (gain) reclassified into earnings, net of tax	(97)	(45)	(68)
Comprehensive loss	\$(22,694)	\$(13,311)	\$(20,395)

The accompanying notes are an integral part of these consolidated financial statements.

Inphi Corporation**Consolidated Statements of Stockholders' Equity**

(in thousands, except share amounts)

	Common Stock		Additional	Accumulated	Other	Total
	Shares	Amount	Paid-in Capital	Deficit	Comprehensive Income	Stockholders' Equity
Balance at December 31, 2011	27,882,223	\$ 28	\$ 190,314	\$ (32,713)	\$ 775	\$ 158,404
Issuance of common stock from exercise of stock options	670,734	1	1,827	—	—	1,828
Issuance of common stock from restricted stock unit grant, net of shares withheld for tax	76,001	—	(325)	—	—	(325)
Issuance of common stock from employee stock purchase plan	101,088	—	943	—	—	943
Income tax benefit from stock option exercises	—	—	51	—	—	51
Stock-based compensation expense	—	—	12,459	—	—	12,459
Net loss	—	—	—	(20,691)	—	(20,691)
Other comprehensive income, net	—	—	—	—	296	296
Balance at December 31, 2012	28,730,046	\$ 29	\$ 205,269	\$ (53,404)	\$ 1,071	\$ 152,965
Issuance of common stock from exercise of stock options and warrant	854,379	1	2,904	—	—	2,905
Issuance of common stock from restricted stock unit grant, net of shares withheld for tax	380,940	—	(2,180)	—	—	(2,180)
Issuance of common stock from employee stock purchase plan	279,074	—	2,221	—	—	2,221
Income tax benefit adjustment from stock option exercises	—	—	(185)	—	—	(185)
Stock-based compensation expense	—	—	16,978	—	—	16,978
Net loss	—	—	—	(13,178)	—	(13,178)
Other comprehensive loss, net	—	—	—	—	(133)	(133)
Balance at December 31, 2013	30,244,439	\$ 30	\$ 225,007	\$ (66,582)	\$ 938	\$ 159,393
Issuance of common stock from exercise of stock options	788,196	1	4,297	—	—	4,298
Issuance of common stock from restricted stock unit grants, net of shares withheld for tax	738,862	1	(4,965)	—	—	(4,964)
Issuance of common stock from employee stock purchase plan	264,886	—	2,668	—	—	2,668
	—	—	55	—	—	55

Edgar Filing: INPHI Corp - Form 10-K

Income tax benefit from stock option exercises						
Stock-based compensation expense	—	—	22,460	—	—	22,460
Issuance of stock from Cortina acquisition	5,274,580	5	77,953	—	—	77,958
Net loss	—	—	—	(22,608)	—	(22,608)
Other comprehensive income, net	—	—	—	—	(86)	(86)
Balance at December 31, 2014	37,310,963	\$ 37	\$ 327,475	\$ (89,190)	\$ 852	\$ 239,174

The accompanying notes are an integral part of these consolidated financial statements.

Inphi Corporation**Consolidated Statements of Cash Flows****(in thousands)**

	Year Ended December 31,		
	2014	2013	2012
Cash flows from operating activities			
Net loss	\$(22,608)	\$(13,178)	\$(20,691)
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	14,114	7,508	4,908
Stock-based compensation	22,460	16,978	12,459
Abandonment of asset	1,195	516	—
Deferred income taxes	487	(163)	9,954
Amortization of deferred tax charge	938	938	963
Excess tax benefit related to stock-based compensation	(55)	—	(2,060)
Amortization of premiums on marketable securities	800	983	1,161
Other noncash items	2	(46)	112
Changes in assets and liabilities:			
Accounts receivable	(8,686)	644	(4,442)
Inventories	10,119	(1,873)	822
Prepaid expenses and other assets	(3,255)	(578)	(164)
Income tax payable/receivable	(576)	3,045	2,657
Accounts payable	(1,302)	379	682
Accrued expenses	(9,006)	1,645	847
Deferred revenue	5,424	603	(846)
Other liabilities	(1,665)	1,257	106
Net cash provided by operating activities	8,386	18,658	6,468
Cash flows from investing activities			
Purchases of property and equipment	(21,171)	(16,578)	(8,383)
Proceeds from sale of property and equipment	—	—	237
Purchases of marketable securities	(38,557)	(43,125)	(47,030)
Sales and maturities of marketable securities	89,872	42,226	44,667
Purchase of patents	(1,580)	—	—
Acquisition of Cortina, net of cash acquired	(35,308)	—	—
Purchase of cost-method investment in private company	(5,000)	(2,621)	—
Net cash used in investing activities	(11,744)	(20,098)	(10,509)
Cash flows from financing activities			
Proceeds from exercise of stock options and warrants	4,298	2,905	1,828
Excess tax benefit related to stock-based compensation	55	—	2,060
Proceeds from employee stock purchase plan	2,668	2,221	943
Minimum tax withholding paid on behalf of employees for restricted stock units	(4,964)	(2,180)	(325)
Net cash provided by financing activities	2,057	2,946	4,506

Edgar Filing: INPHI Corp - Form 10-K

Net increase (decrease) in cash and cash equivalents	(1,301)	1,506	465
Cash and cash equivalents at beginning of year	31,667	30,161	29,696
Cash and cash equivalents at end of year	\$30,366	\$31,667	\$30,161
 Supplemental Cash Flow Information			
Acquisition of Cortina Systems, Inc. in exchange for common stock	\$77,958	\$—	\$—
Income taxes paid	\$715	\$59	\$99

The accompanying notes are an integral part of these consolidated financial statements.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

1. Organization and Summary of Significant Accounting Policies

Inphi Corporation (the “Company”), a Delaware corporation, was incorporated in November 2000. The Company is a fabless provider of high-speed analog and mixed signal semiconductor solutions for the communications, datacenter and computing markets. The Company’s semiconductor solutions are designed to address bandwidth bottlenecks in networks, maximize throughput and minimize latency in computing environments and enable the rollout of next generation communications, datacenter and computing infrastructures. In addition, the semiconductor solutions provide a vital high-speed interface between analog signals and digital information in high-performance systems such as telecommunications transport systems, enterprise networking equipment, datacenter and enterprise servers, storage platforms, test and measurement equipment and military systems.

On October 3, 2014, the Company completed the acquisition of Cortina Systems, Inc. including its high-speed interconnect and optical transport product lines (Cortina) for approximately \$52,509 in cash and approximately 5.3 million shares of the Company’s common stock in accordance with the Agreement and Plan of Merger dated July 30, 2014 as amended by Amendment No. 1 to the Agreement and Plan of Merger dated September 25, 2014.

The Company is subject to certain risks and uncertainties and believes changes in any of the following areas could have a material adverse effect on the Company’s future financial position or results of operations or cash flows: ability to sustain profitable operations due to history of losses and accumulated deficit, dependence on limited number of customers for a substantial portion of revenue, product defects, risks related to intellectual property matters, lengthy sales cycle and competitive selection process, lengthy and expensive qualification process, ability to develop new or enhance products in a timely manner, market development of and demand for the Company’s products, reliance on third parties to manufacture, assemble and test products and ability to compete.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”) and include the accounts of Inphi, Cortina and subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Business Combinations

The Company accounts for acquisitions of business using the purchase method of accounting, which requires the Company to recognize separately from goodwill the assets acquired and the liabilities assumed at their acquisition date fair values. While the Company uses its best estimates and assumptions to accurately value assets acquired and liabilities assumed at the acquisition date as well as contingent consideration, where applicable, the estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the assets acquired and liabilities assumed with the corresponding offset to goodwill. Upon the conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the consolidated statements of operations.

Accounting for business combinations requires management to make significant estimates and assumptions, especially at the acquisition date including our estimates for intangible assets, contractual obligations assumed and pre-acquisition contingencies where applicable. Although, the Company believes the assumptions and estimates we have made in the past have been reasonable and appropriate, they are based in part on historical experience and information obtained from the management of the acquired companies and are inherently uncertain. Critical estimates in valuing certain of the intangible assets we have acquired include future expected cash flows from product sales, customer contracts and acquired technologies, expected costs to develop in-process research and development (IPR&D) into commercially viable products and estimated cash flows from the projects when completed and discount rates. Unanticipated events and circumstances may occur that may affect the accuracy or validity of such assumptions, estimates or actual results.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

On an ongoing basis, management evaluates its estimates, including those related to (i) the collectibility of accounts receivable and allowance for distributors' price discounts; (ii) write down for excess and obsolete inventories; (iii) warranty obligations; (iv) the value assigned to and estimated useful lives of long-lived assets; (v) the realization of tax assets and estimates of tax liabilities and tax reserves; (vi) the valuation of equity securities; (vii) amounts recorded in connection with acquisitions; (viii) recoverability of intangible assets and goodwill and (ix) the recognition and disclosure of contingent liabilities. These estimates are based on historical data and experience, as well as various other factors that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. The Company engages third party valuation specialists to assist with estimates related to the valuation of financial instruments and assets associated with various contractual arrangements, and valuation of assets acquired in connection with acquisitions. Such estimates often require the selection of appropriate valuation methodologies and models, and significant judgment in evaluating ranges of assumptions and financial inputs. Actual results may differ from those estimates under different assumptions or circumstances.

Foreign Currency Translation

The Company and its subsidiaries use the U.S. dollar as its functional currency. Foreign currency assets and liabilities are remeasured into U.S. dollars at the end-of-period exchange rates except for non-monetary assets and liabilities, which are remeasured at historical exchange rates. Revenue and expenses are remeasured at the exchange rate in effect during the period the transaction occurred, except for those expenses related to balance sheet amounts, which are remeasured at historical exchange rates. Gains or losses from foreign currency transactions are included in the Consolidated Statements of Operations as part of "Other income (expense)". Foreign currency gain or loss in 2014, 2013 and 2012 were not material.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original or remaining maturity of three months or less at the date of purchase to be cash equivalents. The Company maintains its cash and cash equivalents with major financial institutions and, at times, such balances with any one financial institution may exceed Federal Deposit Insurance Corporation insurance limits. Cash equivalents primarily consist of money market funds.

Fair Market Value of Financial Instruments

The carrying amount reflected in the balance sheet for cash and cash equivalents, accounts receivable, prepaid and other current assets, accounts payable, accrued expenses and other current liabilities, approximate fair value due to the short-term nature of these financial instruments.

Investments in Marketable Securities

Investments in marketable securities consist of available-for-sale securities. These investments are recorded at fair value with changes in fair value, net of applicable taxes, recorded as unrealized gains (losses) as a component of accumulated other comprehensive income in stockholders' equity. Realized gains and losses and declines in value judged to be other-than-temporary on available-for-sale securities are included in Other (expense) income, net. The cost basis for realized gains and losses on available-for-sale securities is determined on a specific identification basis. Investments are made based on our investment policy which restricts the types of investments that can be made. The Company classified available-for-sale securities as short-term as the investments are available to be used in current operations.

Inventories

Inventories are stated at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost, on a first-in, first-out basis. Inventories are reduced for write downs based on periodic reviews for evidence of slow-moving or obsolete parts. The write-down is based on comparison between inventory on hand and estimated future sales for each specific product. Once written down, inventory write downs are not reversed until the inventory is sold or scrapped. Inventory write downs are also established when conditions indicate that the net realizable value is less than cost due to physical deterioration, obsolescence, changes in price level or other causes. Inventory valuation reserves were \$1,949 and \$1,479, as of December 31, 2014 and 2013, respectively.

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)****Property and Equipment**

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is provided on property and equipment over the estimated useful lives on a straight-line basis. Leasehold improvements are amortized on a straight-line basis over the shorter of their estimated useful lives or lease terms. Repairs and maintenance are charged to expense as incurred. Useful lives by asset category are as follows:

<u>Asset Category</u>	<u>Years</u>
Office equipment	3 years
Software	3 years
Leasehold improvements	Shorter of lease term or estimated useful life
Production equipment	2 years
Computer equipment	5 years
Lab equipment	5 years
Furniture and fixtures	7 years

Equipment Under Capital Leases

The Company leases certain of its equipment under capital lease agreements. The assets and liabilities under capital leases are initially recorded at the fair value of the assets under lease. The capital lease obligation outstanding at December 31, 2014 was \$142, payable in 2015.

Intangible Assets

Intangible assets represent rights acquired for developed technology, customer relationships, trade mark, patents and IPR&D in connection with the acquisition of Cortina. Intangible assets with finite useful lives are amortized over periods ranging from five to ten years using a method that reflects the pattern in which the economic benefits of the intangible asset are consumed, or if that pattern cannot be reliably determined, using a straight-line amortization method. Acquired IPR&D is capitalized and amortization commences upon completion of the underlying projects. If

any of the projects are abandoned, the Company would be required to impair the related IPR&D asset.

Impairment of Long-lived Assets and Goodwill

Long-lived Assets

The Company assesses the impairment of long-lived assets, which consist primarily of property and equipment and intangible assets, whenever events or changes in circumstances indicate that such assets might be impaired and the carrying value may not be recoverable. Events or changes in circumstances that may indicate that an asset is impaired include significant decreases in the market value of an asset, significant underperformance relative to expected historical or projected future results of operations, a change in the extent or manner in which an asset is utilized, significant declines in the estimated fair value of the overall Company for a sustained period, shifts in technology, loss of key management or personnel, changes in the Company's operating model or strategy and competitive forces.

If events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable and the expected undiscounted future cash flows attributable to the asset are less than the carrying amount of the asset, an impairment loss equal to the excess of the asset's carrying value over its fair value is recorded. Fair value is determined based on the present value of estimated expected future cash flows using a discount rate commensurate with the risk involved, quoted market prices or appraised values, depending on the nature of the assets.

Goodwill

Goodwill is recorded when the consideration paid for a business acquisition exceeds the fair value of net tangible and intangible assets acquired. Goodwill is measured and tested for impairment on an annual basis during the fourth fiscal quarter or more frequently if the Company believes indicators of impairment exist.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

The performance of the test involves a two-step process. The first step requires comparing the fair value of the reporting unit to its net book value, including goodwill. As the Company has only one reporting unit, the fair value of the reporting unit is determined by taking the market capitalization of the Company as determined through quoted market prices and adjusted for control premiums and other relevant factors. A potential impairment exists if the fair value of the reporting unit is lower than its net book value. The second step of the process is only performed if a potential impairment exists, and it involves determining the difference between the fair value of the reporting unit's net assets other than goodwill and the fair value of the reporting unit. If the difference is less than the net book value of goodwill, impairment exists and is recorded. In the event that the Company determines that the value of goodwill has become impaired, the Company will record an accounting charge for the amount of impairment during the fiscal quarter in which the determination is made. The Company has not been required to perform this second step of the process because the fair value of the reporting unit has significantly exceeded its book value at every measurement date. The guidance also provides the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. There was no impairment of goodwill in 2014, 2013 and 2012.

Internal Use Software Costs

Certain external computer software costs acquired for internal use are capitalized. Training costs and maintenance are expensed as incurred, while upgrades and enhancements are capitalized if it is probable that such expenditures will result in additional functionality. Capitalized costs are included within property and equipment.

Revenue Recognition

The Company's products are fully functional at the time of shipment and do not require additional production, modification, or customization. The Company recognizes revenue when there is persuasive evidence of an arrangement, delivery has occurred, the fee is fixed or determinable, and collection is reasonably assured. The Company's sales arrangements do not include multiple elements.

Product revenue is recognized upon shipment of product to customers, net of accruals for estimated sales returns and allowances, which to date, have not been significant. However, some of the Company's sales are made through distributors under arrangements that allow for price protection or rights of return on product unsold by the distributors. Product revenue on sales made through distributors with rights of return or price protection is deferred until the distributors sell the product to end customers. Sales to distributors are included in deferred revenue and the Company includes the related costs in inventory until sale to the end customers occurs. Price protection rights allow distributors the right to a credit in the event of declines in the price of the Company's product that they hold prior to the sale to an end customer. In the event that the Company reduces the selling price of products held by distributors, deferred revenue related to distributors with price protection rights is reduced upon notification to the customer of the price change. Additionally, certain distributors may receive a credit for the price discounts associated with the distributors' customers that purchased those products. The Company estimates the extent of these distributor price discounts at each reporting period to reduce accounts receivable and deferred revenue, but does not issue these discounts to the distributor until the inventory is sold to the distributors' customers. The Company's sales to direct customers are made primarily pursuant to standard purchase orders for delivery of products. The Company generally allows customers to cancel or change purchase orders within limited notice periods prior to the scheduled shipment.

Cost of Revenue

Cost of revenue includes cost of materials, such as wafers processed by third-party foundries, cost associated with packaging and assembly, test and shipping, cost of personnel, including stock-based compensation, and equipment associated with manufacturing support, logistics and quality assurance, warranty cost, write down of inventories, amortization of production mask costs, amortization of developed technology, amortization of step-up values of inventory, overhead and an allocated portion of occupancy costs.

Warranty

The Company's products are under warranty against defects in material and workmanship generally for a period of one or two years. The Company accrues for estimated warranty cost at the time of sale based on anticipated warranty claims and actual historical warranty claims experience including knowledge of specific product failures that are outside of the Company's typical experience. The warranty obligation is determined based on product failure rates, cost of replacement and failure analysis cost. If actual warranty costs differ significantly from these estimates, adjustments may be required in the future. As of both December 31, 2014 and 2013, the warranty liability was \$110 and \$40, respectively.

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

The following table sets forth changes in warranty accrual included in other accrued expenses in the Company's consolidated balance sheets:

	Year Ended December 31,		
	2014	2013	2012
Beginning balance	\$40	\$ 40	\$ 40
Warranty liabilities assumed in acquisition	79	—	—
Settlements	(9)	—	—
	\$110	\$ 40	\$ 40

On November 3, 2014, the Company received a claim notification from an insurance company asserting a claim of approximately \$4,000 for field installation repair and replacement costs incurred by a customer in 2011. The Company believes that it had fulfilled its contractual obligation to provide warranty repair and replacement, but has referred the matter to its insurance carrier at the request of the insurance company. As of December 31, 2014, the Company believes that the liability under this claim is not probable. Nevertheless, resolutions of third-party claims are inherently uncertain and as such, an unfavorable outcome could ultimately impact the Company's business, cash flow and results of operations.

In 2010, the Company was informed of a claim related to repair and replacement costs in connection with shipments of over 4,000 integrated circuits made by the Company during the summer and fall of 2009. The Company assessed, provided and accumulated additional warranty reserves based on estimated, probable costs to replace units. In 2012, based on additional investigation and discussions with the customer, the Company booked an additional warranty cost of \$750. This amount was recorded as a reduction to revenue. In June 2012, the Company entered into a settlement agreement with the customer in which the Company paid \$1,750 in July 2012.

Research and Development Expense

Research and development expense consists of costs incurred in performing research and development activities including salaries, stock-based compensation, employee benefits, occupancy costs, pre-production engineering mask

costs, overhead costs and prototype wafer, packaging and test costs. Research and development costs are expensed as incurred. The Company enters into development agreements with some of our customers. Recoveries from nonrecurring engineering services are recorded as an offset to product development expense incurred in support of this effort since these activities do not represent an earning process core to our business and serve as a mechanism to partially recover development expenditures. These reimbursements are recognized upon completion and acceptance by the customer of contract deliverables or milestones. The Company recorded approximately \$10,250, \$1,000 and \$2,484 as offset to research and development expense for the years ended December 31, 2014, 2013 and 2012, respectively.

Sales and Marketing Expense

Sales and marketing expense consists of salaries, stock-based compensation, employee benefits, travel and trade show costs. The Company expenses sales and marketing costs as incurred. Advertising expenses for the years ended December 31, 2014, 2013 and 2012 were not material.

General and Administrative Expense

General and administrative expense consists of salaries, stock-based compensation, employee benefits and expenses for executive management, legal and finance. In addition, general and administrative expense includes fees for professional services and occupancy costs. These costs are expensed as incurred.

Income Taxes

Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company must also make judgments in evaluating whether deferred tax assets will be recovered from future taxable income. To the extent that it believes that recovery is not likely, the Company must establish a valuation allowance. The carrying value of the Company's net deferred tax asset is based on whether it is more likely than not that the Company will generate sufficient future taxable income to realize these deferred tax assets. A valuation allowance is established for deferred tax assets which the Company does not believe meet the "more likely than not" criteria. The Company's judgments regarding future taxable income may change over time due to changes in market conditions, changes in tax laws, tax planning strategies or other factors. If the Company's assumptions and consequently its estimates change in the future, the valuation allowance the Company has established may be increased or decreased, resulting in a material respective increase or decrease in income tax expense (benefit) and related impact on the Company's reported net income (loss).

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

In accordance with FASBs guidance on Accounting for Uncertainty in Income Taxes, the Company performs a comprehensive review of uncertain tax positions regularly. In this regard, an uncertain tax position represents an expected treatment of a tax position taken in a filed tax return, or planned to be taken in a future tax return or claim, which has not been reflected in measuring income tax expense for financial reporting purposes. Until these positions are sustained by the taxing authorities, the Company does not recognize the tax benefits resulting from such positions and reports the tax effects as a liability for uncertain tax positions in our consolidated financial statements. The Company recognizes potential interest and penalties on uncertain tax positions within provision (benefit) for income taxes on the consolidated statement of operations.

Stock-Based Compensation

Stock-based compensation for stock option and restricted stock units issued to the Company's employees is measured at the grant date based on the fair value of the award and is recognized as expense over the requisite service period, which is the vesting period, on a straight-line basis. The fair value of restricted stock units is based on the fair market value of the Company's common stock on the date of grant. The Company uses the Black-Scholes option-pricing model for valuing stock option awards granted to employees and directors at the grant date. Determining the fair value of stock option awards at the grant date requires the input of various assumptions, including fair value of the underlying common stock, expected future share price volatility, expected term, risk-free interest rate and dividend rate. Changes in these assumptions can materially affect the fair value of the options. The Company based its estimate of expected volatility on the estimated volatility of similar entities whose share prices are publicly available. The risk-free interest rate is based on the U.S. Treasury yields in effect at the time of grant for periods corresponding to the expected life of the options. The weighted average expected life of options was calculated using the simplified method. This decision was based on the lack of relevant historical data due to the Company's limited experience. The expected dividend yield is zero because the Company has not historically paid dividends and has no present intention to pay dividends. The Company establishes the estimated forfeiture rates based on historical experience. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service period which is equal to the vesting period.

The Company has elected to treat share-based payment awards with graded vesting schedules and time-based service conditions as single awards and recognizes stock-based compensation expense on a straight-line basis (net of estimated forfeitures) over the requisite service period.

The Company recognizes non-employee stock-based compensation expenses based on the estimated fair value of the equity instrument determined using the Black-Scholes option-pricing model. Management believes that the fair value of the stock options is more reliably measured than the fair value of the services received. The fair value of each non-employee variable stock award is re-measured each period until a commitment date is reached, which is generally the vesting date.

Earnings per Share

Basic earnings per share is calculated by dividing income allocable to common stockholders (after the reduction for any preferred stock dividends assuming current income for the period had been distributed) by the weighted average number of shares of common stock outstanding, net of shares subject to repurchase by the Company, during the period. Diluted earnings per share is calculated by dividing the net income allocable to common stockholders by the weighted average number of common shares outstanding, adjusted for the effects of potentially dilutive common stock, which are comprised of stock options, restricted stock units and employee share purchase plan.

Segment Information

The Company operates in one segment related to the design, development and sale of high speed analog connectivity components that operate to maintain, amplify and improve signal integrity at high speeds in a wide variety of applications. The Company's chief operating decision-maker is its Chief Executive Officer, who reviews operating results on an aggregate basis and manages the Company's operations as a single operating segment.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

Recent Accounting Pronouncements

In January 2014, the Company adopted the guidance on the “Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists.” The guidance provides that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The assessment of whether a deferred tax asset is available is based on the unrecognized tax benefit and deferred tax asset that exist at the reporting date and should be made presuming disallowance of the tax position at the reporting date. The amendments in this update do not require new recurring disclosures. The adoption of this guidance had no impact on the Company’s financial statements.

In May 2014, the Financial Accounting Standards Board issued guidance on “Revenue from Contracts with Customers.” The new revenue recognition guidance provides a five-step analysis of transactions to determine when and how revenue is recognized. The guidance requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The new guidance is effective for the Company on January 1, 2017. Early application is not permitted. The new guidance permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that the new revenue recognition guidance will have on the consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor determined the effect of the standard on the ongoing financial reporting.

In November 2014, the Financial Accounting Standards Board, issued authoritative guidance that provides guidance on whether and at what threshold an acquired business or not-for-profit organization can apply pushdown accounting. This guidance provides an option to apply pushdown accounting in the separate financial statements of an acquired entity upon the occurrence of an event in which an acquirer obtains control of the acquired entity. The guidance is effective on November 18, 2014. After the effective date, an acquired entity can make an election to apply the guidance to future change-in-control events or to its most recent change-in-control event. However, if the financial statements for the period in which the most recent change-in-control event occurred already have been issued or made available to be issued, the application of this guidance would be a change in accounting principle. The adoption of this guidance is not expected to have any significant impact in the consolidated financial statements.

2. Acquisition

On October 3, 2014, the Company completed the acquisition of Cortina Systems, Inc. including its high-speed interconnect and optical transport product lines for approximately \$52,509 in cash and approximately 5.3 million shares. The Company did not acquire as part of the merger, Cortina Systems, Inc.'s access and digital Home business, which Cortina Systems, Inc. divested prior to the closing of the acquisition. The Company acquired Cortina to expand the Company's market share of the high-speed optical and networking interconnects. Cash of \$16,500 was placed in an escrow fund for up to 12 months following the closing for the satisfaction of certain potential indemnification claims. The consolidated financial statements include the results of operations of Cortina as of the acquisition date.

The fair value of consideration transferred is shown in the table below:

Cash	\$ 52,509
Common stock	77,958
	\$ 130,467

The acquisition has been accounted for using the acquisition method of accounting which requires, among other things, that assets acquired and liabilities assumed be recognized at their fair values as of the acquisition date. As additional information becomes available, the Company may revise its preliminary purchase price allocation during the remainder of the measurement period (which will not exceed 12 months from the acquisition date). Any such revisions or changes may be material.

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

The following table summarizes the preliminary purchase price allocation as of the acquisition date:

Cash	\$17,201
Receivables	15,155
Inventories	30,002
Other current assets	1,685
Property and equipment	4,751
Identifiable intangible assets	80,660
In-process research and development	1,750
Other noncurrent assets	366
Accounts payable, accrued expenses and other current liabilities	(22,796)
Deferred tax liabilities, noncurrent	(725)
Other liabilities	(1,112)
Total identifiable net assets	126,937
Goodwill	3,530
Net assets acquired	\$130,467

As of the acquisition date, the fair value of receivables, other assets, accounts payable and accrued expenses approximated the book value acquired.

The following table summarizes the estimated fair value of intangible assets and their estimated useful lives as of the date of acquisition:

	Estimated	Estimated
	Fair	Useful
	Value	Life
		(Years)
Developed technology	\$ 71,570	5-8
Customer relationships	8,170	10
Trade name	920	5
In-process research and development	1,750	—

\$ 82,410

Developed technology was valued using the multi-period excess earnings method under the income approach. This method involves discounting the direct cash flow expected to be generated by the technologies over their remaining lives, net of returns on contributory assets. The estimated useful life was determined based on the technology cycle related to each product family and its expected contribution to forecast revenue. Customer relationships were valued using the incremental cash flow approach which involved discounting management's estimate of the incremental revenues afforded by having the existing customer relationships in place as of the acquisition date, net of operating expense, taxes and returns on contributory assets. The estimated useful life was determined based on the estimated customer product or program ramp-up period required to develop the similar existing customer revenue base. Trade name was valued based on application of relief-from-royalty approach under the income approach. This method is based on the application of a royalty rate to forecasted revenue. The estimated useful life was determined based on the expected life of the trade names, the history of the trade names and the cash flows anticipated over the forecasted periods. In-process research and development was valued using the multi-period excess earnings method under the income approach, with the additional inclusion of estimated costs required to complete the projects.

The Company capitalized \$1,750 of IPR&D costs related to the Cortina acquisition. Upon completion of the project, the related IPR&D assets will be amortized over their estimated useful lives. If the project are abandoned, the Company will be required to impair the related IPR&D asset. The significant assumptions underlying the valuation of IPR&D are:

Estimated percent complete	5	%
Estimated time to complete	18	months
Estimated cost to complete	\$12,548	
Discount rate	26.5	%

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

As of December 31, 2014, the projects are expected to be completed in March 2016 and will commence commercial production in 2016.

Goodwill is calculated as the excess of the consideration transferred over the net assets recognized and is attributable to the workforce of Cortina. Goodwill is not amortized and is not deductible for tax purposes.

The Company incurred acquisition costs of \$1,091 which are included in general and administrative expense in the consolidated statement of income for the year ended December 31, 2014.

Cortina contributed revenue of \$21,018 and pre-tax loss of \$10,018 to the Company for the period from October 3, 2014 to December 31, 2014.

Pro Forma Information

The following unaudited pro forma financial information presents a summary of the Company's consolidated results of operations for the year ended December 31, 2014 and the year ended December 31, 2013, assuming the Cortina acquisition had been completed as of January 1, 2013. The pro forma information includes adjustments to amortization and depreciation for intangible assets and property and equipment acquired, amortization of the purchase accounting effect on inventory acquired from Cortina, and interest income for reduction in short-term investments to fund the acquisition.

Pro Forma Year Ended December 31, 2014 (unaudited)	Pro Forma Year Ended December 31, 2013 (unaudited)
---	---

Revenue	\$ 224,116	\$ 191,966
Net loss	\$ (8,500)	\$ (28,427)
Earnings per share – basic	\$ (0.23)	\$ (0.82)
Earnings per share – diluted	\$ (0.23)	\$ (0.82)

The unaudited pro forma consolidated results were prepared using the acquisition method of accounting and are based on the historical financial information of the Company and Cortina, reflecting the results of operations for the year ended December 31, 2014 and 2013. The unaudited pro forma consolidated results are not necessarily indicative of what our consolidated results of operations actually would have been had we completed the acquisition as of the beginning of the period presented. In addition, the unaudited pro forma consolidated results do not purport to project the future results of operations of the combined company nor do they reflect the expected realization of any cost savings associated with the acquisition.

3. Investments

The following table summarizes the investments by investment category:

	December 31, 2014			
	Cost	Gross	Gross	Fair Value
		Unrealized Gain	Unrealized Loss	
Available-for-sale securities:				
US treasury securities	\$2,056	\$ 1	\$ —	\$2,057
Municipal bonds	19,686	43	(17)	19,712
Corporate notes/bonds	16,381	32	(21)	16,392
Asset backed securities	750	—	(3)	747
Total investments	\$38,873	\$ 76	\$ (41)	\$38,908

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

	December 31, 2013			
		Gross		Gross
	Cost	Unrealized Gain	Unrealized Loss	Fair Value
Available-for-sale securities:				
US treasury securities	\$25,061	\$ 11	\$ —	\$25,072
Municipal bonds	34,912	105	(34)	34,983
Corporate notes/bonds	28,565	105	(22)	28,648
Certificate of deposit	1,500	1	—	1,501
Asset backed securities	685	1	—	686
Total investments	\$90,723	\$ 223	\$ (56)	\$90,890

As of December 31, 2014, we had 22 investments that were in an unrealized loss position. The gross unrealized losses on these investments at December 31, 2014 were primarily due to changes in interest rates and determined to be temporary in nature. The Company reviews the investments to identify and evaluate investments that have an indication of possible other-than-temporary impairment. Factors considered in determining whether a loss is other-than-temporary include the length of time and extent to which fair value has been less than the cost basis, the financial condition and near-term prospects of the investee, and the intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value.

The realized gain related to the Company's available-for-sale investment, which was reclassified from other comprehensive income, was included in other income in the consolidated statements of income.

The contractual maturities of available-for-sale securities at December 31, 2014 are presented in the following table:

	Cost	Fair Value
Due in one year or less	\$13,613	\$13,656
Due between one and five years	25,260	25,252
	\$38,873	\$38,908

In 2014 and 2013, the Company used cash to purchase a minority interest in an early stage private company for \$5,000 and \$2,621, respectively. The Company's ownership in the entity is less than 10% and the Company does not have significant influence, therefore, the investment is accounted for under the cost method and included in other assets in the Company's consolidated balance sheets.

4. Concentrations

Financial instruments that subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents and trade accounts receivable. The Company extends differing levels of credit to customers and does not require collateral deposits. As of December 31, 2014 and 2013, the Company has allowance for doubtful accounts of \$165 and \$152, respectively. As of December 31, 2014, the Company has allowance for distributors' price discount of \$2,206.

The following table summarizes the significant customers' and distributors' accounts receivable and revenue as a percentage of total accounts receivable and total revenue, respectively:

	December 31,	
Accounts Receivable	2014	2013
Customer A	*	11%
Customer B	*	*
Customer C	18%	*

Inphi Corporation**Notes to Consolidated Financial Statements**

(Dollars in thousands except share and per share amounts)

Revenue	Year Ended December 31,		
	2014	2013	2012
Customer A	13%	12%	19%
Customer B	*	15	15
Customer C	*	*	*

*Less than 10% of total accounts receivable or total revenue

Certain other customers are distributors that sell the Company's products exclusively to what would be a "Customer D" above if we were able to include the sales made to those distributors. In the aggregate, revenue to such end customer, including revenue made through distributors as a percentage of total revenue was 11% and 14% for the years ended December 31, 2013 and 2012, respectively. In addition, certain other customers are subcontractors of customers A and B above. In the aggregate, revenue to Customer A, including its subcontractors as a percentage of total revenue was 18%, 20% and 23% for the years ended December 31, 2014, 2013 and 2012, respectively. In the aggregate, revenue to Customer B, including its subcontractor as a percentage of total revenue was 16% and 15% for the years ended December 31, 2013 and 2012, respectively.

5. Inventories

Inventories consist of the following:

	December 31,	
	2014	2013
Raw materials	\$5,803	\$670
Work in process	2,409	2,001
Finished goods	18,438	4,096
	\$26,650	\$6,767

Finished goods include amounts held by distributors of \$2,798 and \$543 as of December 31, 2014 and 2013, respectively.

6. Property and Equipment, net

Property and equipment consist of the following:

	December 31,	
	2014	2013
Laboratory and production equipment	\$48,522	\$34,443
Office, software and computer equipment	15,855	8,649
Furniture and fixtures	1,762	834
Leasehold improvements	5,212	3,952
	71,351	47,878
Less accumulated depreciation	(35,853)	(25,418)
	\$35,498	\$22,460

Depreciation and amortization expense for the years ended December 31, 2014, 2013 and 2012 was \$10,897, \$7,508 and \$4,908, respectively.

As of December 31, 2014 and 2013, computer software costs included in property and equipment were \$4,582 and \$2,815, respectively. Amortization expense of capitalized computer software costs was \$614, \$283 and \$280 for the years ended December 31, 2014, 2013 and 2012, respectively.

Inphi Corporation**Notes to Consolidated Financial Statements**

(Dollars in thousands except share and per share amounts)

7. Goodwill and Identifiable Intangible Assets

The following table presents details of identifiable intangible assets:

	December 31, 2014		
	Gross	Accumulated Amortization	Net
Developed technology	\$71,570	\$ 2,857	\$68,713
Customer relationships	8,170	201	7,969
Trade name	920	46	874
Patents	1,579	112	1,467
In-process research and development	1,750	—	1,750
	\$83,989	\$ 3,216	\$80,773

The following table presents amortization of intangible assets for the year ended December 31, 2014:

Cost of goods sold	\$2,857
Sales and marketing	201
General and administrative	158
	\$3,216

Based on the amount of intangible assets subject to amortization at December 31, 2014, the expected amortization expense for each of the next five fiscal years and thereafter is as follows:

2015	\$12,730
2016	12,704
2017	12,678

2018	12,645
2019	11,075
Thereafter	17,191
	\$79,023

The weighted-average amortization periods remaining by intangible asset category were as follows (in years):

Developed technology	6.27
Customer relationship	9.75
Others	10.71

During the year ended December 31, 2014, goodwill increased by \$3,530 as a result of Cortina acquisition.

8. Other Long-term Liabilities

Other long-term liabilities consist of the following:

	December 31,	
	2014	2013
Deferred rent	\$1,930	\$1,471
Income tax payable	4,687	3,295
Deferred tax liabilities	792	1,099
	\$7,409	\$5,865

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)****9. Income Taxes**

Loss before income taxes consists of the following:

	Year Ended December 31,		
	2014	2013	2012
United States	\$(2,684)	\$(2,507)	\$(2,852)
Foreign	(18,186)	(8,919)	(4,166)
Total	\$(20,870)	\$(11,426)	\$(7,018)

Income tax provision (benefit) consisted of the following:

	Year Ended December		
	31,		
	2014	2013	2012
Current:			
U.S. Federal	\$350	\$1,816	\$3,760
U.S. State	55	1	(132)
Foreign	846	98	91
	1,251	1,915	3,719
Deferred:			
U.S. Federal	895	(135)	4,842
U.S. State	—	—	5,088
Foreign	(408)	(28)	24
	487	(163)	9,954
Total	\$1,738	\$1,752	\$13,673

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

Income tax provision (benefit) differed from the amounts computed by applying the U.S. federal income tax rate of 34% in 2014 and 2013 and 35% in 2012 to loss before income taxes as a result of the following:

	Year Ended December 31,		
	2014	2013	2012
Provision (benefit) at statutory rate	\$(7,096)	\$(3,886)	\$(2,456)
State income taxes	1,651	303	200
Research and development credits	(7,384)	(5,850)	(1,345)
Change in valuation allowance	5,271	6,781	15,247
Foreign earnings, taxed at different rates	6,381	2,888	1,649
Unrecognized tax benefits	1,713	1,708	1,487
Stock-based compensation	166	142	336
Tax exempt income	(83)	(157)	(197)
Prior year return to provision adjustment	292	(257)	(1,264)
Cortina acquisition transaction cost	444	—	—
Other	383	80	16
	\$1,738	\$1,752	\$13,673

Significant components of the Company's net deferred taxes consist of the following:

	December 31,	
	2014	2013
Deferred tax assets		
Net operating loss carry forwards	\$8,314	\$8,532
Research and development credits	30,637	15,460
Stock-based compensation	6,966	5,192
Accrued expenses and allowances	2,117	1,592
Amortization and depreciation	1,052	—
Other temporary differences	3,461	111
Valuation allowance	(39,682)	(22,448)
Total deferred tax assets	12,865	8,439
Deferred tax liabilities		
Subpart F income on foreign subsidiaries earnings	(5,981)	(5,621)
Acquired intangible assets	(6,157)	—

Amortization and depreciation	—	(2,790)
Other deferred tax liabilities	(820)	—
Total deferred tax liabilities	(12,958)	(8,411)
Deferred tax assets (liabilities), net	\$(93)	\$28

At December 31, 2014 and 2013, the Company has recorded a deferred tax charge of \$3,261 and \$4,200, respectively, which represents the tax on the intercompany transfer of intangible assets in connection with the Company's international reorganization during 2010. The deferred tax charge is being amortized over the estimated useful life of 8 years to income tax expense.

Valuation Allowance

The Company records a valuation allowance to reduce deferred tax assets to the amount that the Company believes is more likely than not to be realized. The determination of recording or releasing tax valuation allowances is made, in part, pursuant to an assessment performed by management regarding the likelihood that the Company will generate sufficient future taxable income against which benefits of the deferred tax assets may or may not be realized. This assessment requires management to exercise significant judgment and make estimates with respect to the Company's ability to generate revenue, gross profits, operating income and taxable income in future periods. Amongst other factors, management must make assumptions regarding overall current and projected business and semiconductor industry conditions, operating efficiencies, the Company's ability to timely develop, introduce and consistently manufacture new products to customers' specifications, acceptance of new products, customer concentrations, technological change and the competitive environment which may impact the Company's ability to generate taxable income and, in turn, realize the value of the deferred tax assets. The Company uses the tax law ordering approach of intraperiod allocation to allocate the benefit of windfall tax benefits based on provisions in the tax law that identify the sequence in which those amounts are utilized for tax purposes. Additionally, when determining whether uncertain tax positions are a source of income for valuation allowance purposes, the Company applies the tax law ordering approach to determine how these liabilities will ultimately be satisfied.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

At December 31, 2012, the Company established full valuation allowances of approximately \$14,827 against certain U.S. deferred tax assets, and valuation allowances of approximately \$853 against deferred tax assets of the Company's subsidiaries in Singapore and Taiwan, to reflect the deferred tax asset at the net amount that is more likely than not to be realized. The decision to establish the valuation allowance in 2012 was due to negative evidence which includes the Company's cumulative losses in U.S., Singapore and Taiwan after considering permanent tax differences, the passage of a California tax law requiring use of single sales factor, which reduces the amount of California taxable income starting 2013. At December 31, 2013, full valuation allowance was recorded on the U.S., Singapore, and Taiwan deferred tax assets. At December 31, 2014, the Company has full valuation allowance recorded against the U.S., Singapore and Canada deferred tax assets, and partial valuation allowance on Taiwan deferred tax assets.

The valuation allowance increased \$17,234, \$6,768 and \$15,247 in the years ended December 31, 2014, 2013 and 2012, respectively.

General Income Tax Disclosures

The Company has net operating loss ("NOL") carryforwards for federal and state income tax purposes of approximately \$67,951 and \$34,904, respectively at December 31, 2014, that will begin to expire in 2022 for federal income tax purposes and in 2015 for state income tax purposes. The Company has additional federal and state NOL carryover as of December 31, 2014 of \$29,204 and \$12,417, respectively, arising from an excess stock option deduction that were not recognized in the financial statements. These excess stock option compensation benefits will be credited to additional paid-in capital when it reduces current taxable income. At December 31, 2014, the Company has NOL carryforwards of \$3,215 for its Taiwan subsidiary which begin to expire in 2019, and capital allowance carryover of \$30,459 for the Singapore subsidiary, which does not expire. A full valuation allowance has been provided on U.S. NOL and Singapore capital allowance carryforwards, and partial valuation allowance has been provided on the Taiwan NOL.

At December 31, 2014, the Company has federal and state research and development ("R&D") tax credit carryforwards of \$21,059 and \$23,853, respectively. The federal tax credits will begin to expire in 2024, unless previously utilized. Some state tax credits will begin to expire in 2022 and some do not expire. A full valuation allowance has been provided on R&D tax credit carryforwards.

Pursuant to Internal Revenue Code sections 382 and 383, use of the Company's NOL and R&D credits generated prior to June 2004 are subject to an annual limitation due to a cumulative ownership percentage change that occurred in that period. The Company has had two changes in ownership, one in December 2000 and the second in June 2004, that resulted in an annual limitation on NOL and R&D credit utilization. The NOL and R&D credit carryover of Cortina, are also subject to annual limitation under Internal Revenue Code sections 382 and 383. The acquisition of Cortina caused an ownership change that resulted in an annual limitation, as well as Cortina's legacy annual limitation amount from ownership changes prior to acquisition. The NOL and R&D credit carryforward which will expire unused due to annual limitation is not recognized for financial statement purposes and is not reflected in the above carryover amounts.

The Company's NOL carryforwards include Cortina's federal and state pre-acquisition NOL of \$49,609 and \$32,033, respectively. These NOL carryforwards will begin to expire in 2024 for federal and 2016 for state. The Company's R&D credit carryforwards included Cortina's federal and state pre-acquisition credits of \$6,033 and \$7,977, respectively. The federal R&D credit carryforward will begin to expire in 2027. While some state tax credits will begin to expire in 2022, most do not expire. In addition, Cortina has \$2,859 capital loss carryover which expires in 2018. The utilization of Cortina's pre-acquisition tax attributes is subject to certain annual limitations under Internal Revenue Code sections 382 and 383. No benefit for these tax attributes was recorded upon the close of the acquisition, as the benefit from these tax attributes did not meet the "more-likely-than-not" standard.

The Company operates under tax holiday in Singapore, which is effective through May 2020. The tax holiday is conditional upon meeting certain employment, activities and investment thresholds. The Singapore tax holiday did not impact the Company's Singapore taxes for the years 2014, 2013, and 2012 due to losses and valuation allowance.

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

The following table summarizes the changes in gross unrecognized tax benefits:

	Year Ended December		
	31,		
	2014	2013	2012
Balance as of January 1	\$8,031	\$6,155	\$4,132
Increases based on tax positions related to the current year	3,102	1,918	1,418
Increase (decreases) based on tax positions of prior year	(61)	(42)	605
Gross increases for acquired unrecognized tax benefits	33,935	—	—
Statute of limitation expirations	(926)	—	—
Balance as of December 31	\$44,081	\$8,031	\$6,155

As of December 31, 2014, the Company had approximately \$4,370 of unrecognized tax benefits that if recognized would affect the effective income tax rate. The Company believes that before the end of next year, it is reasonably possible that the gross unrecognized tax benefit may decrease by approximately \$1,750 due to resolution of the state audit.

The Company recognizes interest and penalties related to unrecognized tax benefits as a component of income tax expense. The Company recorded \$14 interest in the year ended December 31, 2014, and no interest or penalties in the years ended December 31, 2013 and 2012.

The Company files income tax returns in the U.S. federal jurisdiction, various states and certain foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations for tax years ended on or before December 31, 2010 or to California state income tax examinations for tax years ended on or before December 31, 2009. However, to the extent allowed by law, the tax authorities may have the right to examine prior periods where net operating losses or tax credits were generated and carried forward, and make adjustments up to the amount of the net operating loss or credit carryforward.

The Company does not provide for U.S. income taxes on undistributed earnings of its controlled foreign corporations as the Company intends to reinvest these earnings indefinitely outside the United States. At December 31, 2014, certain foreign subsidiaries had cumulative undistributed earnings while others had accumulated deficit. The

cumulative undistributed earnings as of December 31, 2014 was \$3,395 that, if repatriated, is not expected to result in additional tax liability as these earnings would be absorbed by the NOL and research credit carryover. No U.S. deferred tax asset was recorded for the accumulated deficit as it was not apparent as of December 31, 2014, that such deferred tax asset would reverse in the foreseeable future.

The Company paid \$715 for various state and foreign income taxes during the year ended December 31, 2014.

In October 2012, the Company received notification from the California Franchise Tax Board that the 2009 and 2010 California tax returns will be examined. The Company believes it has adequate reserve for its uncertain tax positions, however, there is no assurance that the taxing authorities will not propose adjustments that are different from the Company's expected outcome and such adjustments may impact the provision for income taxes. The California Franchise Tax Board examination is on-going as of report date.

In June 2013, the Singapore subsidiary received notification from the Inland Revenue Authority of Singapore that the 2010 tax return will be reviewed. The review is on-going as of report date.

Inphi Corporation**Notes to Consolidated Financial Statements**

(Dollars in thousands except share and per share amounts)

10. Earnings Per Share

The following shows the computation of basic and diluted earnings per share:

	Year Ended December 31,		
	2014	2013	2012
Numerator			
Net loss	\$(22,608)	\$(13,178)	\$(20,691)
Denominator			
Weighted average common stock	32,707,868	29,495,856	28,391,528
Less weighted average unvested common stock subject to repurchase and unvested restricted stock award	—	(2,851)	(12,848)
Weighted average common stock—basic and diluted	32,707,868	29,493,005	28,378,680
Earnings per share			
Basic	\$(0.69)	\$(0.45)	\$(0.73)
Diluted	\$(0.69)	\$(0.45)	\$(0.73)

The following securities were not included in the computation of diluted earnings per share as inclusion would have been anti-dilutive:

	Year Ended December 31,		
	2014	2013	2012
Common stock options	3,350,112	4,373,642	4,797,873
Warrant to purchase redeemable convertible preferred stock	—	1,696	2,142
Unvested restricted stock award and restricted stock unit	3,705,415	3,030,202	1,608,464
	7,055,527	7,405,540	6,408,479

11. Stock-Based Compensation

In June 2010, the Board of Directors approved the Company's 2010 Stock Incentive Plan (the "2010 Plan"), which became effective in November 2010. The 2010 Plan provides for the grants of restricted stock, stock appreciation rights and stock unit awards to employees, non-employee directors, advisors and consultants. The Board of Directors administers the 2010 Plan, including the determination of the recipient of an award, the number of shares subject to each award, whether an option is to be classified as an incentive stock option or nonstatutory option, and the terms and conditions of each award, including the exercise and purchase prices and the vesting or duration of the award. Options granted under the 2010 Plan are exercisable only upon vesting. At December 31, 2014, 1,570,319 shares of common stock have been reserved for future grants under the 2010 Plan.

Stock Option Awards

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	Year Ended	
	December 31,	
	2013	2012
	2014	
Risk-free interest rate	— 1.41 %	1.32 %
Expected life (in years)	— 6.25	6.22
Dividend yield	— —	—
Expected volatility	— 50 %	50 %

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

The following table summarizes information regarding options outstanding:

	Number of Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding at December 31, 2013	3,883,097	\$ 9.26	6.33	\$ 16,229
Granted	—	—		
Exercised	(788,196)	5.45		
Canceled	(89,307)	12.52		
Outstanding at December 31, 2014	3,005,594	\$ 10.16	6.12	\$ 25,302
Exercisable at December 31, 2014	2,349,476	\$ 9.69	5.82	\$ 20,880
Vested and expected to vest in the future as of December 31, 2014	3,001,391	\$ 10.16	6.12	\$ 25,273

The intrinsic value of options outstanding, exercisable and vested and expected to vest is calculated based on the difference between the exercise price and the fair value of the Company's common stock as of the respective balance sheet dates.

The weighted average grant date fair value per share of stock options granted to employees during the years ended December 31, 2014, 2013 and 2012 was \$0, \$4.82 and \$6.18, respectively.

The total intrinsic value of options exercised during the years ended December 31, 2014, 2013 and 2012 was \$7,800, \$7,313, and \$6,861, respectively. The intrinsic value of exercised options is calculated based on the difference between the exercise price and the fair value of the Company's common stock as of the exercise date. Cash received from the exercise of stock options was \$4,298, \$2,905 and \$1,828, respectively, for the years ended December 31, 2014, 2013 and 2012.

Stock Option Exchange Offer

On September 20, 2012, the Company commenced an offering to eligible employees to voluntarily exchange certain vested and unvested stock option grants. Under the program, eligible employees holding options to purchase the Company's common stock were given the opportunity to exchange certain of their existing options, with exercise prices at or above \$16.63 per share for a predetermined smaller number of stock options to be granted following the expiration of the tender offer with exercise prices equal to the fair market value of one share of the Company's common stock on the day the new awards were issued. Stock options to purchase an aggregate of 508,399 shares with exercise prices ranging from \$16.63 to \$22.07 were eligible for tender at the commencement of the program. The Company's directors and executive officers were not eligible to participate in the program. The program is structured as a value-neutral exchange. The replacement awards would be targeted at providing value that is, in the aggregate, not greater than the fair value of the exchanged stock options. This means that the employees who participate in the program are expected to receive a number of replacement awards with an aggregate value that does not exceed the aggregate value of the stock options surrendered in the exchange. The terms and conditions of the new options, including the vesting schedules, will be substantially the same as the terms and conditions of the options cancelled.

On October 19, 2012, the offer period ended and the Company accepted for exchange and cancellation 464,899 vested and unvested eligible options to purchase common stock, with a weighted average exercise price of \$21.06. In exchange, the Company issued 353,779 vested and unvested options to purchase shares of the Company's common stock with an exercise price of \$8.93, the closing price of the Company's common stock on October 22, 2012. Using the Black-Scholes option pricing model, the Company determined that the fair value of the surrendered stock options on a grant-by-grant basis was approximately equal, as of the date of the exchange, to the fair value of the eligible stock options exchanged, resulting in insignificant incremental share-based compensation.

Restricted Stock Units and Awards

The Company granted restricted stock units (RSUs) to members of the Board of Directors and employees. Most of the Company's outstanding restricted stock units vest over four years with vesting contingent upon continuous service. The Company estimates the fair value of restricted stock units using the market price of the common stock on the date of the grant. The fair value of these awards is amortized on a straight-line basis over the vesting period.

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

The following table summarizes information regarding outstanding restricted stock units:

	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Outstanding at December 31, 2013	3,209,567	\$ 11.69
Granted	2,878,836	13.99
Vested	(1,098,924)	12.61
Canceled	(199,857)	11.92
Outstanding at December 31, 2014	4,789,622	\$ 12.85
Expected to vest in the future as of December 31, 2014	4,712,501	

On October 16, 2014, the Compensation Committee of the Board of Directors granted one-time employment RSU awards of 1,000,000 shares to certain Cortina employees who entered employment with the Company commencing upon the closing of the acquisition. The awards vest over four years with vesting contingent upon continuous service.

The Company granted restricted stock awards (RSAs) to certain members of the Board of Directors. The Company estimates the fair value of the RSAs using the market price of the common stock on the date of the grant. As of December 31, 2011, the Company had 21,425 of which 8,576 RSAs vested during the year ended December 31, 2012, resulting to 12,849 unvested RSAs outstanding as of December 31, 2012. During 2013, 9,998 RSAs vested, resulting to 2,851 unvested RSAs outstanding as of December 31, 2013. All remaining unvested RSAs of 2,851 vested during the year ended December 31, 2014.

Employee Stock Purchase Plan

In December 2011, the Company adopted the Employee Stock Purchase Plan (“ESPP”). Participants purchase the Company's stock using payroll deductions, which may not exceed 15% of their total cash compensation. Pursuant to

the terms of the ESPP, the "look-back" period for the stock purchase price is six months. Offering and purchase periods will begin on February 10 and August 10 of each year. Participants will be granted the right to purchase common stock at a price per share that is 85% of the lesser of the fair market value of the Company's common shares at the beginning or the end of each six-month period.

The ESPP imposes certain limitations upon an employee's right to acquire common stock, including the following: (i) no employee shall be granted a right to participate if such employee immediately after the election to purchase common stock, would own stock possessing 5% or more to the total combined voting power or value of all classes of stock of the Company, and (ii) no employee may be granted rights to purchase more than \$25 fair value of common stock for each calendar year. The maximum aggregate number of shares of common stock available for purchase under the ESPP is one million shares. Total common stock issued under the ESPP during the years ended December 31, 2014, 2013 and 2012 was 264,886, 279,074 and 101,088, respectively.

The fair value of employee stock purchase plan is estimated at the start of offering period using the Black-Scholes option pricing model with the following average assumptions for the years ended December 31, 2014, 2013 and 2012:

	Year Ended December		
	31,		
	2014	2013	2012
Risk-free interest rate	0.07%	0.10%	0.13%
Expected life (in years)	0.50	0.49	0.50
Dividend yield	—	—	—
Expected volatility	40 %	45 %	81 %
Estimated fair value	\$3.55	\$2.86	\$4.69

Inphi Corporation**Notes to Consolidated Financial Statements**

(Dollars in thousands except share and per share amounts)

Stock-Based Compensation Expense

Stock-based compensation expense is included in the Company's results of operations as follows:

	Year Ended December 31,		
	2014	2013	2012
Cost of revenue	\$1,260	\$1,086	\$726
Research and development	12,420	8,586	5,833
Sales and marketing	4,079	3,204	2,660
General and administrative	4,701	4,102	3,240
	\$22,460	\$16,978	\$12,459

As of December 31, 2014, total unrecognized compensation cost related to unvested stock options and awards prior to the consideration of expected forfeitures, was approximately \$52,068, which is expected to be recognized over a weighted-average period of 2.88 years.

12. Employee Benefit Plan

The Company has established a 401(k) tax-deferred savings plan (the "Plan") which permits participants to make contributions by salary deduction pursuant to Section 401(k) of the Internal Revenue Code of 1986, as amended. The Company may, at its discretion, make matching contributions to the Plan. Furthermore, the Company is responsible for administrative costs of the Plan. The Company has not made contributions to the Plan since its inception.

13. Fair Value Measurements

The guidance on fair value measurements requires fair value measurements to be classified and disclosed in one of the following three categories:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2: Quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability, or

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

The Company measures its investments in marketable securities at fair value using the market approach which uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The Company has cash equivalents which consist of money market funds valued using the amortized cost method, in accordance with Rule 2a-7 under the 1940 Act which approximates fair value.

The following table presents information about assets and liabilities required to be carried at fair value on a recurring basis:

December 31, 2014	Total	Level 1	Level 2
Assets			
Cash equivalents:			
Money market funds	\$1,457	\$—	\$1,457
Investment in marketable securities:			
US treasury securities	2,057	2,057	—
Municipal bonds	19,712	—	19,712
Corporate notes/bonds	16,392	—	16,392
Asset backed securities	747	—	747
	\$40,365	\$2,057	\$38,308

Inphi Corporation**Notes to Consolidated Financial Statements**

(Dollars in thousands except share and per share amounts)

December 31, 2013	Total	Level 1	Level 2
Assets			
Cash equivalents:			
Money market funds	\$5,119	\$—	\$5,119
Investment in marketable securities:			
US treasury securities	25,072	25,072	—
Municipal bonds	34,983	—	34,983
Corporate notes/bonds	28,648	—	28,648
Certificate of deposit	1,501	—	1,501
Asset backed securities	686	—	686
	\$96,009	\$25,072	\$70,937

14. Segment and Geographic Information

The Company operates in one reportable segment. Revenue by region is classified based on the locations to which the product is transported, which may differ from the customer's principal offices.

The following table sets forth the Company's revenue by geographic region:

	Year Ended December 31,		
	2014	2013	2012
China	\$54,312	\$23,039	\$20,724
United States	22,918	22,389	21,582
Korea	10,123	21,818	17,424
Other	68,789	35,418	31,476
	\$156,142	\$102,664	\$91,206

As of December 31, 2014, \$6,153 of long-lived tangible assets are located outside the United States of which \$3,463 are located in Taiwan. As of December 31, 2013, \$5,217 of long-lived tangible assets are located outside the United States of which \$4,694 are located in Taiwan.

15. Commitments and Contingencies

Leases

The Company leases its facility under noncancelable lease agreements expiring in various years through 2019. The Company also licenses certain software used in its research and development activities under a term license subscription and maintenance arrangement.

Future minimum lease payments under noncancelable operating leases having initial terms in excess of one year are as follows:

	December 31, 2014
2015	\$ 15,131
2016	10,749
2017	4,380
2018	1,744
2019	1,259
	\$ 33,263

For the years ended December 31, 2014, 2013 and 2012, lease operating expense was \$8,193, \$5,990 and \$3,980, respectively.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

Noncancelable Purchase Obligations

We depend upon third party subcontractors to manufacture our wafers. Our subcontractor relationships typically allow for the cancellation of outstanding purchase orders, but require payment of all expenses incurred through the date of cancellation. As of December 31, 2014, the total value of open purchase orders for wafers was approximately \$10,278.

Legal Proceedings

Netlist, Inc. v. Inphi Corporation, Case No. 09-cv-6900 (C.D. Cal.)

On September 22, 2009, Netlist filed suit in the United States District Court, Central District of California, or the Court, asserting that the Company infringes U.S. Patent No. 7,532,537. Netlist filed an amended complaint on December 22, 2009, further asserting that the Company infringes U.S. Patent Nos. 7,619,912 and 7,636,274, collectively with U.S. Patent No. 7,532,537, the patents-in-suit, and seeking both unspecified monetary damages to be determined and an injunction to prevent further infringement. These infringement claims allege that the Company's iMB™ and certain other memory module components infringe the patents-in-suit. The Company answered the amended complaint on February 11, 2010 and asserted that the Company does not infringe the patents-in-suit and that the patents-in-suit are invalid. In 2010, Company filed *inter partes* requests for reexamination with the United States Patent and Trademark Office (the "USPTO"), asserting that the patents-in-suit are invalid.

On August 27, 2010, the USPTO ordered the request for *Inter Partes* Reexamination for U.S. Patent No. 7,636,274 and found a substantial new question of patentability based upon each of the different issues that the Company raised as the reexamination requestor. On September 27, 2011, the Patent Office issued a First Office Action based on the Netlist '274 Patent Reexamination Request and rejected 91 of its 97 claims. On October 27, 2011, Netlist responded to the USPTO determination by amending some but not all of the claims, adding new claims and making arguments as to the validity of the rejected claims in view of the cited references. The Company provided rebuttable comments to the USPTO on November 28, 2011. On March 12, 2012, the Examiner issued an Action Closing Prosecution, indicating that the claims pending contain allowable subject matter, and Netlist did not respond to the Action Closing Prosecution in the time provided by the USPTO. On June 22, 2012, the USPTO issued a Right of Appeal Notice, and

on July 23, 2012, the Company filed a Notice of Appeal. The Company filed the Appeal Brief on September 24, 2012 and Netlist filed its Responsive Brief on October 24, 2012. The parties received an Examiner's Answer dated April 16, 2013 from the USPTO that maintained the rejections set forth on the Right of Appeal Notice dated June 22, 2012. The Company filed a Rebuttal Brief on May 16, 2013 and a Request for Oral Hearing on June 7, 2013. The appeal hearing took place on November 20, 2013. The Patent Trial and Appeal Board (PTAB) issued its decision on January 16, 2014, finding the Examiner erred in declining to adopt 8 of the 9 different rejections that had been proposed by us. The Company requested a rehearing of the decision not to adopt the remaining one rejection that had been proposed by the Company and was not adopted by the PTAB on February 18, 2014. In papers dated March 18, 2014, Netlist provided rebuttal comments to the request for rehearing and also requested re-opening of prosecution with respect to the claims that the PTAB had rejected, and in that request to re-open prosecution amended the independent claims that stood rejected. The Company filed comments with respect to these proposed amended claims on April 17, 2014, which were refiled in a slightly different form on September 5, 2014. On June 26, 2014, the PTAB issued a decision on the request for rehearing, which included a rejection of further claims pursuant to the Company's request and on July 28, 2014, Netlist provided a response to the USPTO cancelling those claims that had been rejected in the decision on the request for rehearing. On September 26, 2014, the PTAB remanded the proceedings back to the Examiner, with instructions to consider part, but not all, of the Company's comments that had been previously filed on September 5, 2014. On October 10, 2014, the Company filed a Petition to the Director of the USPTO seeking reconsideration of the PTAB remand of September 26, 2014, and requesting that all of the comments that the Company previously filed on September 5, 2014 should have been entered for consideration by the Examiner. The USPTO denied this Petition and a communication from the Examiner, with instructions to consider part, but not all, of the Company's comments that had been previously filed on September 5, 2014 is expected as the next substantive step of the proceeding, as prosecution otherwise remains closed. The proceeding is expected to continue in accordance with established *Inter Partes* Reexamination procedures. The Company may consider filing an appeal to any determination made by the USPTO with the Federal Circuit Court of Appeals.

Inphi Corporation**Notes to Consolidated Financial Statements****(Dollars in thousands except share and per share amounts)**

On September 8, 2010, the USPTO ordered the request for *Inter Partes* Reexamination for U.S. Patent No. 7,532,537 and found a substantial new question of patentability based upon different issues that the Company raised as the reexamination requestor. The USPTO accompanied this Reexamination Order of U.S. Patent No. 7,532,537 with its own evaluation of the validity of this patent, and rejected some but not all of claims. In a response dated October 8, 2010, Netlist responded to the USPTO determination by amending some but not all of the claims, adding new claims and making arguments as to why the claims were not invalid in view of the cited references. The Company provided rebuttable comments to the USPTO on November 8, 2010 along with a Petition requesting an increase in the number of allowed pages of the rebuttable comments. On January 20, 2011, the USPTO granted the Petition in part. The Company then filed updated rebuttal comments on January 27, 2011 in compliance with the granted Petition. The USPTO has considered these updated rebuttal comments, and in a communication dated June 15, 2011, continued to reject all the previously rejected claims. The USPTO also rejected all the claims newly added in the October 8, 2010 Netlist response. In a further communication dated June 21, 2011, the USPTO issued an Action Closing Prosecution indicating that it would confirm the patentability of four claims and reject all the other pending claims. On August 22, 2011, Netlist responded to the Action Closing Prosecution by further amending some claims and making arguments as to the validity of the rejected claims in view of the cited references. The Company submitted rebuttal comments on September 21, 2011. In a further communication dated February 7, 2012, the USPTO issued a Right of Appeal Notice, which also indicated that the previous amendments to claim made by Netlist would be entered, and that the current pending claims, as amended, were patentable. The Company filed a Notice of Appeal at the USPTO on March 8, 2012, within the time period provided for filing the Notice of Appeal and Netlist did not file Notice of Cross-Appeal. The Company filed its Appeal Brief on May 8, 2012, and Netlist filed its Responsive Brief on July 2, 2012. The parties received an Examiner's Answer dated April 16, 2013 from the USPTO that maintained the rejections set forth on the Right of Appeal Notice dated February 7, 2012. The Company filed a Rebuttal Brief on May 16, 2013 and a Request for Oral Hearing on June 7, 2013. The appeal hearing took place in front of the PTAB on November 20, 2013. The PTAB issued its decision on January 16, 2014, affirming the Examiner's decision as to all of the challenged claims. On February 18, 2014, the Company made a request for rehearing of the decision, and in papers dated March 18, 2014, Netlist provided rebuttal comments to the request for rehearing. On August 13, 2014, the PTAB denied our request for rehearing, and on October 15, 2014, the Company filed a Notice of Appeal to the Court of Appeals for the Federal Circuit. An Appeal Brief was filed with the Court of Appeals for the Federal Circuit on February 3, 2015 and an Opposition Brief filed by Netlist in the Court of Appeals for the Federal Circuit is expected as the next substantive step of the proceeding, as prosecution otherwise remains closed. The proceeding is expected to continue in accordance with established *Inter Partes* Reexamination procedures.

On September 8, 2010, the USPTO ordered the request for *Inter Partes* Reexamination for U.S. Patent No. 7,619,912 and found a substantial new question of patentability based upon different issues that the Company raised as the reexamination requestor. The USPTO accompanied this Reexamination Order of U.S. Patent No. 7,619,912 with its own evaluation of the validity of this patent, and initially determined that all of the claims were patentable based upon the Company's request for *Inter Partes* Reexamination. Netlist did not comment upon this Reexamination Order. The USPTO on February 28, 2011 also merged the Proceedings of our Reexamination of U.S. Patent No. 7,619,912,

bearing Control No. 90/001,339 with Inter Partes Reexamination Proceeding 95/000,578 filed October 20, 2010 on behalf of SMART Modular Technologies, Inc. and Inter Partes Reexamination Proceeding 95/000,579 filed October 21, 2010 on behalf of Google, Inc. In each of these other Reexamination Proceedings, the USPTO had indicated that there existed a substantial new question of patentability with respect to certain claims of U.S. Patent No. 7,619,912, but had not accompanied the Reexamination Orders related thereto with its own evaluation of the validity of this patent, indicating that such evaluation would be forthcoming at a later time. This further evaluation was received in an Office Action dated April 4, 2011, in which the Examiner rejected a substantial majority of the claims based upon a number of different rejections, including certain of the rejections originally proposed by the Company in its Request for Reexamination. This Office Action also indicated that one claim was deemed to be patentable over the prior art of record in the merged Reexamination Proceedings. After seeking and obtaining an extension of time to respond to the Office Action dated April 4, 2011, Netlist served its response on July 5, 2011, which added new claims and made arguments as to why the originally filed claims were not invalid in view of the cited references. Each of the merged Reexamination Requestors, including the Company, submitted rebuttal comments by August 29, 2011. The USPTO considered this Netlist response and each of the rebuttal comments, and in an Office Action dated October 14, 2011, continued to reject most, but not all of the previously rejected claims, as well as rejected claims that had been added by Netlist in its July 5, 2011 response. After seeking and obtaining an extension of time to respond to the Office Action dated October 14, 2011, Netlist served its response on January 13, 2012, which response made amendments based upon subject matter that had been indicated as allowable in the Office Action dated October 14, 2011, added other new claims and made arguments as to why all of these claims should be allowed. The three different merged Reexamination Requestors, including the Company, timely submitted rebuttal comments on or about February 13, 2012. The USPTO issued a Non-final Office Action on November 13, 2012, rejecting some claims and indicating that others contained allowable subject matter. On January 14, 2013, Netlist filed a Response to the Non-final Office Action which presented further claim amendments and evidence supporting its positions regarding patentability. Rebuttal comments from the Company and the other Requestors were filed on February 13, 2013. On March 21, 2014, the USPTO issued an Action Closing Prosecution in which the USPTO indicated that certain of the pending claims were allowable and other of the pending claims were rejected, and on June 18, 2014 issued a Right of Notice of Appeal. By July 18, 2014, the Company as well as other Requestors each filed Notices of Appeal, and Netlist filed a Cross Appeal on July 30, 2014. By September 30, 2014, each of the Requestors as well as Netlist had filed their respective Appeal Briefs, and by October 30, 2014 each of the Requestors as well as Netlist had filed their respective Responses to the previously filed Appeal Briefs. Reply Briefs by Requestors and Netlist were filed on or before February 18, 2015 and consideration by the USPTO will be the next substantive step of the proceeding, as currently prosecution otherwise will remain closed. The merged proceeding is expected to continue in accordance with established *Inter Partes* Reexamination procedures.

The reexamination proceedings could result in a determination that the patents-in-suit, in whole or in part, are valid or invalid, as well as modifications of the scope of the patents-in-suit.

Inphi Corporation

Notes to Consolidated Financial Statements

(Dollars in thousands except share and per share amounts)

Based on these papers the Court in January 2014 ordered a continued stay of the proceedings, took the litigation off the active court calendar, and requested that the parties file a joint status report on May 1, 2014 and every 120 days thereafter advising the Court as to status of the reexamination proceedings at which times, the Court could decide to maintain or lift the stay.

While the Company intends to defend the foregoing lawsuit vigorously, litigation, whether or not determined in the Company's favor or settled, could be costly and time-consuming and could divert management's attention and resources, which could adversely affect the Company's business.

Based on the nature of the litigation, the Company is currently unable to predict the final outcome of this lawsuit and therefore, cannot determine the likelihood of loss nor estimate a range of possible loss. However, because of the nature and inherent uncertainties of litigation, should the outcome of these actions be unfavorable, the Company's business, financial condition, results of operations or cash flows could be materially and adversely affected.

As a result of acquisition of Cortina, the Company is currently working to settle a patent dispute involving Cortina and Vitesse Semiconductor Corporation (Vitesse). The patent dispute involves a certain patent family owned by Vitesse associated with error correction. The Company is currently in discussion with Vitesse in good faith to settle the dispute. The Company believes that the probable liability of this claim would be \$750 which the Company recorded as of the acquisition date and December 31, 2014. Based on the Agreement and Plan of Merger dated July 30, 2014, we would be indemnified for future settlement arising from this claim, up to an amount of \$750. Accordingly, we recorded an indemnification asset in the amount of \$750 as of the acquisition date. However, because of the nature and inherent uncertainties, should the outcome of the settlement be unfavorable, the Company's business, financial condition, results of operations or cash flows could be materially and adversely affected.

Indemnifications

In the ordinary course of business, the Company may provide indemnifications of varying scope and terms to customers, vendors, lessors, investors, directors, officers, employees and other parties with respect to certain matters, including, but not limited to, losses arising out of the Company's breach of such agreements, services to be provided by the Company, or from intellectual property infringement claims made by third-parties. These indemnifications may

survive termination of the underlying agreement and the maximum potential amount of future payments the Company could be required to make under these indemnification provisions may not be subject to maximum loss clauses. The Company has not incurred material costs to defend lawsuits or settle claims related to these indemnifications. Accordingly, the Company has no liabilities recorded for these agreements as of December 31, 2014 and December 31, 2013.

16. Related Party Transactions

In 2007, the Company entered into a software subscription and maintenance agreement with Cadence Design Systems, Inc. (“Cadence”), a related party company. A former member of the Company’s Board of Directors is also the Chief Executive Officer, President and a director of Cadence. The Company committed to pay \$7,000 payable in 16 quarterly payments through May 2011. In December 2010, the software subscription and maintenance agreement was renewed effective June 30, 2011. Under the new agreement, the Company committed to pay \$5,250 payable in 10 quarterly payments through November 2013. In June 2012, the software subscription and maintenance agreement was amended to include new licensed materials effective on September 28, 2012 and expired on December 31, 2013. Under this amendment, the Company committed to pay \$2,129 payable in 5 quarterly payments through November 2013. The Company paid \$2,224 in the year ended December 31, 2012. Operating lease expense related to this agreement included in research and development expense was \$2,467 for the year ended December 31, 2012.

Supplementary Financial Information (Unaudited)**Quarterly Results of Operations****Year Ended December 31, 2014**

	Mar. 31, 2014	Jun. 30, 2014	Sept. 30, 2014	Dec. 31, 2014⁽¹⁾
	(in thousands, except per share amounts)			
Total revenue	\$31,189	\$33,922	\$36,278	\$54,753
Gross profit	20,126	21,626	23,275	20,627
Net income (loss)	(995)	2,634	(6,857)	(17,390)
Basic earnings per share	(0.03)	0.08	(0.22)	(0.47)
Diluted earnings per share	(0.03)	0.08	(0.22)	(0.47)

Year Ended December 31, 2013

	Mar. 31, 2013	Jun. 30, 2013	Sept. 30, 2013	Dec. 31, 2013
	(in thousands, except per share amounts)			
Total revenue	\$22,584	\$24,339	\$26,611	\$29,130
Gross profit	14,292	15,446	16,815	19,016
Net income (loss)	(7,671)	(1,474)	(2,760)	(1,273)
Basic earnings per share	(0.27)	(0.05)	(0.09)	(0.04)
Diluted earnings per share	(0.27)	(0.05)	(0.09)	(0.04)

On October 3, 2014, we completed the acquisition of Cortina, including its high-speed interconnect and optical transport product lines. The results of operations of Cortina and estimated fair value of assets acquired and (1) liabilities assumed were included in our financial statements from the acquisition date. This acquisition resulted in a significant change in our statement of operations in 2014 which includes increase cost of goods sold resulting from the step-up inventory acquired from Cortina and amortization of acquired intangibles.

Item 9 ~~Changes in and Disagreements with Accountants on Accounting and Financial Disclosure~~

None.

Item 9a ~~Controls and Procedures~~

(a) *Evaluation of disclosure controls and procedures.* We maintain “disclosure controls and procedures,” as such term is defined in Rules 13a-15 (e) and 15d – 15(e) under the Securities Exchange Act 1934, or the Exchange Act (as amended), that are designed to provide reasonable assurance that information required to be disclosed by us in reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Our disclosure controls and procedures have been designed to provide reasonable, not absolute assurance. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on their evaluation as of the end of the period covered by this Annual Report on Form 10-K, our Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) *Management’s Annual Report on Internal Control over Financial Reporting.* Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may deteriorate. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, assessed the effectiveness of our internal control over financial reporting as of December 31, 2014. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO, in *Internal Control — Integrated Framework (2013)*. Based on the assessment using those criteria, our management concluded that as of December 31, 2014, our internal control over financial reporting was effective. Our evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2014 did not include the internal controls of Cortina. We excluded Cortina from our assessment of internal controls over financial reporting as of December 31, 2014 because it was acquired in a business combination in October 2014. Cortina is a wholly owned subsidiary of the Company whose total assets and total

revenues represent 19% and 13%, respectively of the related consolidated financial statement amounts as of and for the year ended December 31, 2014. The effectiveness of our internal control over financial reporting as of December 31, 2014 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which is included in Part II “Item 8, Financial Statements and Supplementary Data”.

(c) *Changes in Internal Control over Financial Reporting.* There has been no change in our “internal control over financial reporting” as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, during our most recent fiscal quarter that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9b ~~Other Information~~

None.

PART III

Item 10 —*Directors, Executive Officers and Corporate Governance*

The information required by this item is incorporated by reference from the information under the captions “Election of Directors,” “Section 16(a) Beneficial Ownership Reporting Compliance” and “Corporate Governance” contained in our Proxy Statement to be filed with the Securities and Exchange Commission in connection with the solicitation of proxies for our 2015 Annual Meeting of Stockholders to be held on May 28, 2015, or Proxy Statement.

Item 11 ~~*Executive Compensation*~~

The information required by this item is incorporated by reference from the information under the captions “Election of Director,” “Compensation of Directors,” “Compensation Discussion and Analysis,” “Corporate Governance,” “Compensation Committee Report” and “Executive Compensation” contained in the Proxy Statement.

Item 12 ~~*Security Ownership of Certain Beneficial Owners and Management and Related STOCKholder Matters*~~

The information required by this item is incorporated by reference from the information under the captions “Security Ownership of Certain Beneficial Owners and Management” and “Executive Compensation” contained in the Proxy Statement.

Item 13 ~~*Certain Relationships and Related Transactions, and Director Independence*~~

The information required by this item is incorporated by reference from the information under the captions “Election of Directors,” “Corporate Governance” and “Certain Relationships and Related Person Transactions” contained in the Proxy Statement.

Item 14 — *Principal Accountant Fees and Services*

The information required by this item is incorporated by reference from the information under the captions “Audit Committee Report” and “Ratification of the Appointment of Independent Registered Public Accounting Firm — Principal Accountant Fees and Services” contained in the Proxy Statement.

PART IV

Item 15 ~~*Exhibits and Financial Statement Schedules*~~

¹ Financial Statements. See “Index to Consolidated Financial Statements” under Part II, “Item 8, Financial Statements and Supplementary Data”.

(a) *Documents filed as part of this report:*

(1) Financial Statements

Reference is made to the Index to Consolidated Financial Statements of Inphi Corporation under Part II, “Item 8, Financial Statements and Supplementary Data”.

(2) Financial Statement Schedules

All financial statement schedules have been omitted because they are not applicable or not required or because the information is included elsewhere in the Consolidated Financial Statements or the Notes thereto.

(3) Exhibits

See Item 15(b) below. Each management contract or compensatory plan or arrangement required to be filed has been identified.

(b) *Exhibits*

The exhibits listed in the Exhibit Index below are filed or incorporated by reference as part of this report.

(c) *Financial Statements and Schedules*

Reference is made to Item 15(a)(2) above.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

INPHI CORPORATION

By: /s/ Ford Tamer
Ford Tamer
Chief Executive Officer
(Principal Executive Officer)

Date: March 10, 2015

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Ford Tamer and John Edmunds, and each of them, his true and lawful attorneys-in-fact, each with full power of substitution, for him or her in any and all capacities, to sign any amendments to this report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact or their substitute or substitutes may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Name	Title	Date
/s/ Ford Tamer	Chief Executive Officer	March 10, 2015

Edgar Filing: INPHI Corp - Form 10-K

Ford Tamer	(Principal Executive Officer), President and Director	
/s/ John Edmunds	Chief Financial Officer and Chief Accounting Officer	March 10, 2015
John Edmunds	(Principal Financial and Accounting Officer)	
/s/ Diosdado P. Banatao Diosdado P. Banatao	Chairman of the Board	March 10, 2015
/s/ Chenming C. Hu Chenming C. Hu	Director	March 10, 2015
/s/ David Liddle David Liddle	Director	March 10, 2015
/s/ Bruce McWilliams Bruce McWilliams	Director	March 10, 2015
/s/ Nicholas Brathwaite Nicholas Brathwaite	Director	March 10, 2015
/s/ Sam S. Srinivasan Sam S. Srinivasan	Lead Director	March 10, 2015

EXHIBIT INDEX

Exhibit Number	Description
3(i)	Restated Certificate of Incorporation of the Registrant (incorporated by reference to exhibit 3(i) of the Registrant's annual report on Form 10-K filed with the SEC on March 7, 2011).
3(ii)	Amended and Restated Bylaws of the Registrant (incorporated by reference to the exhibit 3(ii).2 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
4.1	Specimen Common Stock Certificate (incorporated by reference to exhibit 4.1 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
4.2	Amended and Restated Investors' Rights Agreement dated as of August 12, 2010 (incorporated by reference to exhibit 4.2 of the Registrant's annual report on Form 10-K filed with the SEC on March 7, 2011).
10.1+	Inphi Corporation 2000 Stock Option/Stock Issuance Plan (as amended on June 2, 2010) and related form stock option plan agreements (incorporated by reference to exhibit 10.1 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
10.2+	Inphi Corporation 2010 Stock Incentive Plan and related form agreements (incorporated by reference to exhibit 10.2 of the Registrant's annual report on Form 10-K filed with the SEC on March 7, 2011).
10.3+	Form of Indemnification Agreement between the Registrant and its officers and directors (incorporated by reference to exhibit 10.3 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
10.4+	Offer letter dated July 14, 2007 between Young K. Sohn and the Registrant, as amended (incorporated by reference to exhibit 10.4 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
10.5+	Change of Control and Severance Agreement dated June 8, 2010, by and between Young K. Sohn and the Registrant (incorporated by

Edgar Filing: INPHI Corp - Form 10-K

reference to exhibit 10.5 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).

- 10.6+ Offer letter dated December 10, 2007 between John Edmunds and the Registrant, as amended (incorporated by reference to exhibit 10.6 to filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
- 10.7+ Change of Control and Severance Agreement dated June 8, 2010, by and between John Edmunds and the Registrant (incorporated by reference to exhibit 10.7 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
- 10.8+ Offer letter dated October 3, 2007 between Ron Torten and the Registrant, as amended (incorporated by reference to exhibit 10.8 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).
- 10.9+ Offer letter dated February 1, 2012 between Ford Tamer and the Registrant (incorporated by reference to exhibit 10.2 of the Registrant's Current Report on Form 8-K with the SEC on February 3, 2012).
- 10.10+ Change of Control and Severance Agreement dated February 1, 2012 between Ford Tamer and the Registrant (incorporated by reference to exhibit 10.3 of the Registrant's Current Report on Form 8-K with the SEC on February 3, 2012).
- 10.11+ Senior Advisor Agreement dated as of February 1, 2012 by and between Young K. Sohn and the Registrant (incorporated by reference to exhibit 10.1 of the Registrant's Current Report on Form 8-K with the SEC on February 3, 2012).
- 10.12+ Transition Services Agreement dated May 30, 2012 between Ron Torten and the Registrant (incorporated by reference to exhibit 10.1 of the Registrant's Quarterly Report on Form 10-Q for the three months ended June 30, 2012).
- 10.13+ Change of Control and Severance Agreement dated September 4, 2012, by and between Charlie Roach and the Registrant (incorporated by reference to exhibit 10.4 of the Registrant's Quarterly Report on Form 10-Q for the three months ended September 30, 2012).
- 10.14+ Separation Agreement dated as of July 30, 2013 by and between Norman Yeung and the Registrant (incorporated by reference to exhibit 10.1 of the Registrant's Quarterly Report on Form 10-Q for the three months ended September 30, 2013).
- 10.15+ Consulting Agreement effective as of October 18, 2013 by and between Norman Yeung and the Registrant (incorporated by reference to exhibit 10.2 of the Registrant's Quarterly Report on Form 10-Q for the three months ended September 30, 2013).

10.16 Lease Agreement between the Registrant and LBA Realty Fund III—Company VII, LLC dated as of June 4, 2010 (incorporated by reference to exhibit 10.12 filed with Registration Statement on Form S-1 (File No. 333-167564), as amended).

10.17 Lease Agreement between the Registrant and Bayland Corporation dated as of September 20, 2012 (incorporated by reference to exhibit 10.2 of the Registrant's Quarterly Report on Form 10-Q for the three months ended September 30, 2012).

81

- Second
Amendment
to
Lease
Agreement
between
the
Registrant
and
LBA
Realty
Fund
III—Company
VII,
LLC
dated
as
of
September
30,
2012
10.18 (incorporated
by
reference
to
exhibit
10.3
of
the
Registrant’s
Quarterly
Report
on
Form
10-Q
for
the
three
months
ended
September
30,
2012).
- 10.19+ Inphi
Corporation
Employee
Stock

Purchase
Plan
(incorporated
by
reference
to
exhibit
99.1
filed
with
Registration
Statement
on
Form
S-8
(File
No.
333-179270)).

10.20 Agreement
and
Plan
of
Merger
dated
July
30,
2014
by
and
among
the
Company,
Cortina,
Catalina
Acquisition
Corporation,
a
Delaware
corporation
and
wholly
owned
subsidiary
of
the
Company,
and
the
Stockholder's
Agent

(incorporated
by
reference
to
exhibit
2.1
of
the
the
Registrant's
Current
Report
on
Form
8-K
with
the
SEC
on
August
1,
2014).

10.21 Agreement
and
Plan
of
Merger
dated
July
30,
2014
by
and
among
the
Company,
Cortina,
Catalina
Acquisition
Corporation,
a
Delaware
corporation
and
wholly
owned
subsidiary
of
the
Company,
and

the
Stockholder's
Agent,
as
amended
by
Amendment
No.
1
thereto
dated
September
25,
2014
(incorporated
by
reference
to
Exhibit
2.1
of
the
Registrant's
Current
Report
on
Form
8-K
with
the
SEC
on
October
6,
2014).

21.1 List
of
Subsidiaries
(incorporated
by
reference
to
the
exhibit
of
the
same
number
filed
with

	Registration Statement on Form S-1 (File No. 333-167564), as amended).
23.1	Consent of PricewaterhouseCoopers LLP, independent registered public accounting firm.
24.1	Power of Attorney (see page 73 of this report).
31.1	Certificate of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
31.2	Certificate of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
32.1(1)	Certificate of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
32.2(1)	Certificate of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
101.INS	XBRL Instance Document

101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

+Indicates management contract or compensatory plan.

(1) The material contained in Exhibit 32.1 and Exhibit 32.2 is not deemed “filed” with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language contained in such filing, except to the extent that the registrant specifically incorporates it by reference.