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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2001

OR

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

For the transition period from to .

Commission file number 000-24487

MIPS Technologies, Inc.

(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
Incorporation or organization)

77-0322161
(I.R.S. Employer
Identification Number)

1225 CHARLESTON ROAD, MOUNTAIN VIEW, CA 94043-1353
(Address of principal executive offices)

Registrants' telephone number, including area code: **(650) 567-5000**

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

As of May 1, 2001, the number of outstanding shares of the Registrant's Class A common stock, \$.001 par value, was 13,870,841. As of May 1, 2001, the number of outstanding shares of the Registrant's Class B common stock, \$.001 par value, was 25,064,149.

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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

MIPS TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	<u>March 31,</u> <u>2001</u>	<u>June 30,</u> <u>2000</u>
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 110,730	\$ 84,359
Accounts receivable	12,629	9,175
Prepaid expenses and other current assets	9,019	8,002
	<u>132,378</u>	<u>101,536</u>
Total current assets		
Equipment and furniture, net	8,681	6,742
Other assets	1,211	974
	<u>142,270</u>	<u>109,252</u>
	\$	\$
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 4,363	\$ 2,270
Accrued liabilities	17,205	10,180
Deferred revenue	2,677	4,598
	<u>24,245</u>	<u>17,048</u>
Total current liabilities		
Stockholders' equity:		
Common stock	39	38
Additional paid-in capital	160,528	153,627
Accumulated deficit	(42,542)	(61,461)
	<u>118,025</u>	<u>92,204</u>
Total stockholders' equity		
	<u>\$ 142,270</u>	<u>\$ 109,252</u>

See accompanying notes.

MIPS TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

(In thousands, except per share data)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2001	2000	2001	2000
Revenue:				
Royalties	\$ 16,106	\$ 18,149	\$ 34,204	\$ 43,620
Contract revenue	11,733	8,812	35,932	23,781
Total revenue	27,839	26,961	70,136	67,401
Costs and expenses:				
Cost of contract revenue	—	—	250	500
Research and development	9,543	6,801	24,867	20,054
Sales and marketing	4,272	2,642	11,414	7,011
General and administrative	2,557	1,387	6,801	5,518
Total costs and expenses	16,372	10,830	43,332	33,083
Operating income	11,467	16,131	26,804	34,318
Other income, net	1,651	1,119	4,883	2,581
Income before income taxes	13,118	17,250	31,687	36,899
Provision for income taxes	4,767	6,900	12,194	14,809
Net income	\$ 8,351	\$ 10,350	\$ 19,493	\$ 22,090
Basic net income per share	\$ 0.22	\$ 0.27	\$ 0.50	\$ 0.58
Diluted net income per share	\$ 0.21	\$ 0.26	\$ 0.48	\$ 0.55
Shares used in computing basic net income per share	38,778	38,196	38,659	37,908
Shares used in computing diluted net income per share	40,262	40,437	40,585	39,901

See accompanying notes.

MIPS TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(In thousands)

	Nine Months Ended March 31,	
	2001	2000
Operating activities:		
Net income	\$ 19,493	\$ 22,090
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	2,754	1,767
Other non-cash charges	87	202
Changes in operating assets and liabilities:		
Accounts receivable	(3,454)	(7,063)
Accounts payable	2,093	(6,151)
Other assets and liabilities, net	3,769	7,594
Net cash provided by operating activities	24,742	18,439
Cash used in investing activities—capital expenditures	(4,694)	(2,555)
Financing activities—net proceeds from issuance of common stock	6,648	13,479
Foreign currency translation adjustment	(325)	(159)
Net increase in cash and cash equivalents	26,371	29,204
Cash and cash equivalents, beginning of period	84,359	49,916
Cash and cash equivalents, end of period	\$ 110,730	\$ 79,120

See accompanying notes.

MIPS TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—UNAUDITED

Note 1. Description of Business and Basis of Presentation

Formation of MIPS Technologies, Inc. (MIPS). MIPS Technologies' predecessor, MIPS Computer Systems, Inc., was founded in 1984 and was engaged in the design and development of RISC processors for the computer systems and embedded markets. Silicon Graphics, Inc. adopted the MIPS architecture for its computer systems in 1988 and acquired MIPS Computer Systems, Inc. in 1992. Following the acquisition, Silicon Graphics continued the MIPS processor business through its MIPS Group (a division of Silicon Graphics), which focused primarily on the development of high-performance processors for Silicon Graphics' workstations and servers. In order to increase the focus of the MIPS Group on the design and development of processor applications dedicated to the embedded market, in December 1997, Silicon Graphics initiated a plan to separate the business of the MIPS Group from its other operations.

In April 1998, our Board of Directors approved a transaction pursuant to which Silicon Graphics transferred to us the assets and liabilities related to the design and development of processor intellectual property for embedded market applications. From the closing of our initial public offering on July 6, 1998 and until June 20, 2000, we were a majority owned subsidiary of Silicon Graphics. On June 20, 2000, Silicon Graphics distributed all of its remaining interest in us in the form of a stock dividend of Class B common stock to its stockholders.

Basis of Presentation. The unaudited results of operations for the interim periods shown in these financial statements are not necessarily indicative of operating results for the entire fiscal year. In our opinion, the condensed consolidated financial statements include all adjustments (consisting only of normal recurring accruals) necessary to present fairly the financial position, results of operations and cash flows for each interim period shown.

The condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") applicable to interim financial information. Certain information and footnote disclosures included in financial statements prepared in accordance with generally accepted accounting principles have been omitted in these interim statements as allowed by such SEC rules and regulations. The balance sheet at June 30, 2000 has been derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles. However, we believe that the disclosures are adequate to make the information presented not misleading. The unaudited condensed consolidated financial statements included in this Form 10-Q should be read in conjunction with the audited consolidated financial statements and related notes for the fiscal year ended June 30, 2000, included in our 2000 Annual Report on Form 10-K.

Note 2. Computation of Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share amounts):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2001	2000	2001	2000
Numerator:				
Net income	\$ 8,351	\$ 10,350	\$ 19,493	\$ 22,090
Denominator:				
Weighted-average shares of common stock outstanding	38,817	38,211	38,690	37,923
Less: Weighted-average shares subject to repurchase	(39)	(15)	(31)	(15)
Shares used in computing basic net income per share	38,778	38,196	38,659	37,908
Effect of dilutive securities—employee stock options and shares subject to repurchase	1,484	2,241	1,926	1,993
Shares used in computing diluted net income per share	40,262	40,437	40,585	39,901
Basic net income per share	\$ 0.22	\$ 0.27	\$ 0.50	\$ 0.58
Diluted net income per share	\$ 0.21	\$ 0.26	\$ 0.48	\$ 0.55
Potentially dilutive securities excluded from diluted net income per share computation because they are anti-dilutive	1,940	—	1,170	17

Note 3. Comprehensive Income

For the three and nine month periods ended March 31, 2001 and 2000, the currency translation adjustment was not material and, therefore, total comprehensive income closely approximated net income in each period presented.

Note 4. Contingencies

On October 28, 1999, we filed suit against Lexra, Inc. in the United States District Court for the Northern District of California for infringement of two United States patents. We subsequently amended our suit to cover two subsequently released Lexra products.

On November 12, 1999, Lexra, Inc. filed counterclaims against us seeking a declaratory judgment that the two asserted patents are invalid and not infringed. Lexra has also asserted claims for common law unfair competition, intentional interference with business relations, and statutory unfair competition, all purportedly based on the allegation that our claims of patent infringement have been made in bad faith. On April 25, 2001, the Court conducted a hearing to consider arguments from the parties regarding the appropriate interpretation of the disputed patent claim terms. We anticipate a ruling from the Court concerning these terms in the near future. Discovery is currently ongoing in the lawsuit, but the Court has not yet set a trial date. In addition, Lexra has filed a request with the Patent and Trademark Office seeking re-examination of one of the patents at issue in this litigation. The Patent and Trademark Office has indicated that it will conduct a re-examination of the patent.

From time to time, we receive communications from third parties asserting patent or other rights covering our products and technologies. Based upon our evaluation, we may take no action or we may seek to obtain a license. There can be no assurance in any given case that a license will be available on

terms we consider reasonable, or that litigation will not ensue. In addition, from time to time, we evaluate possible infringement claims against third parties and may assert such claims, if appropriate.

We are not aware of any pending disputes, including that discussed above that we believe would adversely affect our business, results of operations or financial condition.

Note 5. Recent Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Financial Instruments and for Hedging Activities" (later replaced by SFAS No. 137), which provides comprehensive and consistent standards for the recognition and measurement of derivatives and hedging activities. As a result, we were required to adopt SFAS 133 as of July 1, 2000. The adoption of this statement did not have a material impact on our consolidated financial statements.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). SAB 101 summarizes the SEC staff's views in applying generally accepted accounting principles to revenue recognition. We are currently in the process of evaluating SAB 101 and what effect it may have on our financial statements. We have not yet determined whether the adoption of SAB 101 will have a material impact on our financial position or results of operations. In the event that the adoption of SAB 101 requires us to report a change in accounting principle related to our revenue recognition policy, we would be required to report such change in the quarter ending June 30, 2001.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

You should read the following discussion and analysis together with our unaudited condensed consolidated financial statements and the notes to those statements included elsewhere in this report. This discussion may contain forward-looking statements that involve risks and uncertainties. These forward-looking statements within this Quarterly Report on Form 10-Q are identified by words such as "believes," "anticipates," "expects," "intends," "may" and other similar expressions. Our actual results could differ materially from those indicated in these forward-looking statements as a result of certain factors, including those described under "Factors That May Affect Our Business," and other risks affecting our business. We undertake no obligation to update any forward-looking statements included in this discussion.

Results of Operations

Revenue. Our revenue consists of royalties and contract revenue earned under contracts with our licensees. We generate royalties from the sale by our licensees of products incorporating our technology including royalties from Nintendo relating to sales of Nintendo 64 video game players and related cartridges. Royalties may be calculated as a percentage of the revenue received by the seller on sales of such products or on a per unit basis. Contract revenue includes technology license fees and engineering service fees. We receive license fees for the use of technology that we have developed internally and, in some cases, which we have licensed from third parties. License fees are typically recognized upon the execution of the license agreement and transfer of intellectual property provided no further significant performance obligations exist. Fees related to engineering services, which are performed on a best efforts basis, are recognized as revenue when the defined milestones are achieved and collectibility of the milestone payment is probable. The technology we develop is generally licensed to multiple customers.

Total revenue for the third quarter of fiscal 2001 was \$27.8 million and for the first nine months of fiscal 2001 was \$70.1 million compared to \$27.0 million and \$67.4 million for the comparable periods in fiscal 2000. Total revenue excluding royalties from Nintendo 64 game products was \$15.9 million and \$47.0 million in the third quarter and first nine months of fiscal 2001 and grew 40% during the third quarter of fiscal 2001 and 51% during the first nine months of fiscal 2001 over the comparable periods in fiscal 2000. Royalties for the third quarter of fiscal 2001 were \$16.1 million and for the first nine months of fiscal 2001 were \$34.2 million compared to \$18.1 million and \$43.6 million for the comparable periods in fiscal 2000. The decreases in both periods were due primarily to lower royalties derived from sales of Nintendo products. As the Nintendo 64 video game product line continues further into its life cycle, we expect that sales of such products and the related royalties we receive will generally trend downward, subject to seasonal fluctuations and the impact of particular game titles introduced by Nintendo from time to time. Royalties excluding royalties from Nintendo 64 game products grew 65% in the third quarter of fiscal 2001 and 50% in the first nine months of fiscal 2001 over the comparable periods in fiscal 2000. Contract revenue for the third quarter of fiscal 2001 was \$11.7 million and for the first nine months of fiscal 2001 was \$35.9 million compared to \$8.8 million and \$23.8 million for the same periods in fiscal 2000. The increases in both periods were the result of technology license fees from new agreements and engineering service fees earned upon our achievement of defined milestones. We expect that contract revenue, except for seasonal fluctuations in royalties, will be greater than 50% of our total revenue for the next several years.

Cost of Contract Revenue. Our cost of contract revenue consists of sublicense fees payable to third parties. We incur an obligation to pay these fees when we sublicense technology to our customers that we have licensed from third parties. Sublicense fees are recorded as cost of contract revenue when the obligation is incurred, which is typically the same period in which the related revenue is recognized.

Cost of contract revenue was zero for the third quarter and \$250,000 for the first nine months of fiscal 2001, compared to no cost of contract revenue in the third quarter of fiscal 2000 and \$500,000 for the first nine months of fiscal 2000. We expect that in future periods cost of contract revenue will be minimal.

Research and Development. Costs incurred with respect to technology we develop internally and engineering services we perform which are not directly related to any particular licensee, license agreement or license fee, are recorded as research and development expense.

Research and development expenses for the third quarter of fiscal 2001 were \$9.5 million and for the first nine months of fiscal 2001 were \$24.9 million compared with research and development expenses of \$6.8 million and \$20.1 million for the comparable periods in fiscal 2000. The increases in research and development expenses in both periods were due to the addition of resources and tools to support various project development activities, including the addition of 19 employees to the development team during the past twelve months. These increases were partially offset by lower requirements for contractors needed to meet project milestones. We expect research and development expenses to increase in the foreseeable future as we continue to develop new designs for the digital consumer and business products markets and the embedded processor market.

Sales and Marketing. Sales and marketing expenses for the third quarter of fiscal 2001 were \$4.3 million and for the first nine months of fiscal 2001 were \$11.4 million compared to \$2.6 million and \$7.0 million for the comparable periods in fiscal 2000. The increases in sales and marketing expenses in both periods were due to additional resources hired to support our increasing licensing and third party tools and applications activities. We increased our sales and marketing staff to 54 persons as of March 31, 2001, from 32 persons as of March 31, 2000, to support this growth.

General and Administrative. General and administrative expenses for the third quarter of fiscal 2001 were \$2.6 million and for the first nine months of fiscal 2001 were \$6.8 million compared to \$1.4 million and \$5.5 million for the comparable periods in fiscal 2000. The increases in general and administrative expenses in both periods were primarily due to increased legal expense required to support our ongoing patent and licensing activity.

Other Income, Net. For the third quarter of fiscal 2001, other income, net, was \$1.7 million and for the first nine months of fiscal 2001 was \$4.9 million, compared to other income, net, of \$1.1 million and \$2.6 million for the comparable periods in fiscal 2000. The increases in both periods were primarily due to interest income earned from the investment of cash generated from our operating activities and from proceeds on the issuance of common stock under our stock plans.

Income Taxes. We recorded a provision for income taxes of \$4.8 million for the third quarter of fiscal 2001 and \$12.2 million for the first nine months of fiscal 2001, compared to \$6.9 million and \$14.8 million for the same periods in fiscal 2000. The estimated annual income tax rate of 38.5% in fiscal 2001 is lower than the effective tax rate of 40% in fiscal 2000 due to benefits derived from foreign income at rates below the US statutory rate and other US incentives.

Financial Condition

At March 31, 2001, we had cash and cash equivalents of \$110.7 million and total working capital of \$108.1 million.

Our operating activities provided net cash of \$24.7 million for the nine months ended March 31, 2001 compared to \$18.4 million for the comparable period in the prior year. During the nine month period ended March 31, 2001, net cash provided by operating activities consisted mainly of net income, a net increase in other assets and liabilities and the benefit of non-cash depreciation expenses, partially offset by an increase in accounts receivable. The net increase in other assets and liabilities in fiscal

2001 was primarily due to the tax provision, offset by a decrease in deferred revenue. The increase in accounts receivable reflects the timing of the invoicing and collection of license fees owed us under licensing agreements. During the nine months ended March 31, 2000, net cash provided by operations consisted primarily of net income and a net increase in other assets and liabilities, offset by an increase in accounts receivable and a decrease in accounts payable. The net increase in other assets and liabilities in fiscal 2000 was primarily due to the tax provision and an increase in deferred revenue and was partially offset by a decrease in accrued liabilities. The increase in accounts receivable reflects the timing of the invoicing and collection of license fees owed us under licensing agreements. The decrease in accounts payable was due to a payment of taxes due to Silicon Graphics for our fiscal 1999 tax liability incurred under a tax sharing agreement with Silicon Graphics.

Net cash used in investing activities was \$4.7 million for the nine months ended March 31, 2001 compared to \$2.6 million for the comparable period in the prior year. Net cash used in investing activities in both periods represents equipment purchases and licensing of computer aided design tools used in development. Capital expenditures have been, and future expenditures are anticipated to be, primarily for facilities, equipment to support expansion of our operations and licensing of computer aided design tools used in development.

Net cash provided by financing activities was \$6.6 million for the nine months ended March 31, 2001 compared to \$13.5 million for the comparable period in the prior year. Net cash provided in both periods resulted primarily from the exercise of employee stock options.

Our future liquidity and capital requirements are expected to vary significantly from quarter to quarter, depending on numerous factors, including, among others:

- the cost, timing and success of product development efforts;
- the cost and timing of sales and marketing activities;
- the extent to which our existing and new technologies gain market acceptance;
- the level and timing of contract revenues and royalties;
- competing technological and market developments; and
- the cost of maintaining and enforcing patent claims and other intellectual property rights.

We believe that cash generated by our operations, together with our existing cash balance, will be sufficient to meet our projected operating and capital requirements for the foreseeable future. However, we may in the future be required to raise additional funds through public or private financing, strategic relationships or other arrangements. Additional equity financing may be dilutive to holders of our common stock, and debt financing, if available, may involve restrictive covenants. Moreover, strategic relationships, if necessary to raise additional funds, may require that we relinquish our rights to certain of our technologies. Our failure to raise capital when needed could adversely affect our business, results of operations and financial condition.

On June 20, 2000, Silicon Graphics distributed all of the shares of our common stock that it owned in a transaction intended to be tax-free to Silicon Graphics and its stockholders. Our ability to issue additional shares of our common stock in connection with acquisitions or to raise equity capital during the 30-month period following this distribution is limited under the terms of a distribution tax indemnification agreement that we entered into with Silicon Graphics. The agreement contains covenants under which we may not issue capital stock in an acquisition or private or public offering within the 30-month period following the tax-free distribution, except:

- pursuant to the exercise of employee, director or consultant stock options or awards and

- for the issuance of up to a cumulative amount of 10% of our outstanding stock at the time of the tax-free distribution unless certain conditions are met.

Factors That May Affect Our Business

Factors negatively affecting sales of Nintendo 64 video game players and related cartridges could adversely affect us. Royalties from Nintendo and NEC Corporation relating to Nintendo 64 video game players and related cartridges accounted for 43% of our total revenue for the third quarter of fiscal 2001 and 33% for the first nine months of fiscal 2001 compared to 58% and 54% for the comparable periods in the prior year. We anticipate that royalties related to Nintendo 64 game products, while continuing to represent an important portion of our total revenue for the next few quarters, will continue to decline. If we cannot replace these lost revenues, our revenue will decline. The market for home entertainment products is competitive and the introduction of new products or technologies, as well as shifting consumer preferences and generally uncertain economic conditions, could negatively impact the amount and timing of sales of Nintendo 64 game products.

We must diversify our sources of revenue to offset the decline in revenue we derive from sales of Nintendo video game products. The next generation Nintendo video game system will not incorporate our technology. Our ability to diversify our sources of revenue is uncertain and will depend on whether our processors and related designs are selected for design into a broader range of both digital consumer and business products, which we refer to as design wins. Our ability to achieve design wins is subject to several risks and uncertainties, including:

- the potentially limited opportunities for design wins with respect to certain digital consumer products, such as video game products, due to a limited number of product manufacturers and the length of product life cycles; and
- the risk that the performance, functionality, price and power characteristics of our designs may not satisfy those that are critical to specific digital consumer and business product applications.

Even if our technology is incorporated into new products, we cannot be certain that any such products will ultimately be brought to market, achieve commercial acceptance or generate meaningful royalties for us.

We depend on semiconductor companies and manufacturers of digital consumer and business products to adopt our technology and use it in the products they sell. The adoption and continued use of our technology by semiconductor companies and digital consumer and business product manufacturers is essential to our continued success. We face numerous risks in obtaining agreements with semiconductor companies and digital consumer and business product manufacturers on terms consistent with our business model, including:

- investing the time and money required to build a relationship with a potential licensee;
- potential competition with the internal design teams of semiconductor companies and digital consumer and business product manufacturers;
- potential difficulties in persuading large semiconductor companies and digital consumer and business product manufacturers to work with us, to rely on us for critical technology, and to disclose to us proprietary manufacturing technology; and
- potential difficulties in persuading potential licensees to bear certain development costs associated with our technology and to produce embedded processors using our technology.

We cannot assure you that we will be able to maintain our current relationships or establish new relationships with additional licensees, and any failure by us to do so could have a material adverse effect on our business.

Moreover, we are subject to risks beyond our control that influence the success or failure of a particular semiconductor company or digital consumer and business product manufacturer, including:

- the competition it faces and the market acceptance of its products;
- its engineering, marketing and management capabilities and the technical challenges unrelated to our technology that it faces in developing its products; and
- its financial and other resources.

Generally, our current licensees are not obligated to license new or future generations of our processor designs. In addition, because we do not control the business practices of our licensees, we do not influence the degree to which our licensees promote our technology or set the prices at which the products incorporating our technology are sold.

Our quarterly financial results are subject to significant fluctuations that could adversely affect our stock price. Our quarterly financial results may vary significantly due to a number of factors, many of which are outside of our control. In addition, our revenue components are difficult to predict and may fluctuate significantly from period to period. Because our expenses are largely independent of our revenue in any particular period, it is difficult to accurately forecast our operating results. Our operating expenses are based, in part, on anticipated future revenue and a high percentage of our expenses are fixed in the short term. As a result, if our revenue is below expectations in any quarter, the adverse effect may be magnified by our inability to adjust spending in a timely manner to compensate for the revenue shortfall.

In light of the foregoing, we believe that quarter-to-quarter comparisons of our revenue and operating results may not be a good indication of our future performance. In addition, it is possible that in some future periods our results of operations may be below the expectations of public market analysts and investors. In this event, the price of both our Class A common stock and Class B common stock may fall.

Factors that could cause our revenue and operating results to vary from quarter to quarter include:

- the demand for and average selling prices of semiconductor products that incorporate our technology;
- the financial terms and delivery schedule of our contractual arrangements with our licensees, which may provide for significant up-front payments or payments based on the achievement of certain milestones;
- the relative mix of contract revenue and royalties;
- competitive pressures resulting in lower contract revenue or royalty rates;
- our ability to develop, introduce and market new processor intellectual property;
- the establishment or loss of licensing relationships with semiconductor companies or digital consumer or business product manufacturers;
- the timing of new products and product enhancements by us and our competitors;
- changes in development schedules, research and development expenditure levels and product support by us and digital consumer or business product manufacturers;
- seasonal fluctuations; and

- general economic and market conditions.

We depend on the emerging market for digital consumer and business products and customer acceptance of the products that incorporate our technology. The digital consumer and business products industries are presently the primary markets for our processor, core and related designs. The markets for digital consumer and business products is relatively new and emerging, and our success will depend largely on the level of interest in digital consumer and business products, many of which have only recently been introduced to the market. In addition, the timing and amount of royalties we receive will depend on customer acceptance of the products that incorporate our technology. We cannot assure you that any products that incorporate our technology will achieve commercial acceptance or generate meaningful royalties for us.

Our dependence on the digital consumer and business products industries involves several risks and uncertainties, including:

- changes in customer requirements and preferences;
- the introduction of products by our competitors embodying new technologies or features; and
- the current lack of open industry standards for hardware and software for digital consumer and business products.

If we are unable to develop enhancements and new generations of our intellectual property, we may be unable to achieve design wins. Our future success will depend on our ability to develop enhancements and new generations of our processors, cores and other intellectual property that satisfy the requirements of specific product applications and introduce these new technologies to the marketplace in a timely manner. If our development efforts are not successful or are significantly delayed, or if the characteristics of our processor and related designs are not compatible with the requirements of specific product applications, our ability to achieve design wins would be limited. Our failure to achieve a sufficient number of design wins could adversely affect our business, results of operations and financial condition.

Technical innovations of the type critical to our success are inherently complex and involve several risks, including:

- our ability to anticipate and timely respond to changes in the requirements of semiconductor companies, and original equipment manufacturers (OEMs) of digital consumer and business products;
- our ability to anticipate and timely respond to changes in semiconductor manufacturing processes;
- changing customer preferences in the digital consumer and business products markets;
- the emergence of new standards in the semiconductor industry and for digital consumer and business products;
- the significant investment that is often required before commercial viability is determined; and
- the introduction by our competitors of products embodying new technologies or features.

Our failure to adequately address these risks could render our existing processor, core and related designs obsolete and could adversely affect our business, results of operations and financial condition. In addition, we cannot assure you that we will have the financial and other resources necessary to develop processor, core and related designs in the future, or that any enhancements or new generations of the technology that we develop will generate revenue in excess of or sufficient to cover the costs of development.

Our intellectual property may be misappropriated or subject to claims of infringement. We attempt to protect our intellectual property rights through a combination of patent, trademark, copyright and trade secret laws, as well as licensing agreements and employee and third-party nondisclosure and assignment agreements. Our failure to obtain or maintain adequate protection of our intellectual property rights for any reason could have a material adverse effect on our business, results of operations and financial condition.

Policing the unauthorized use of our intellectual property is difficult, and we cannot be certain that the steps we have taken will prevent the misappropriation or unauthorized use of our technologies, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. In addition, we cannot be certain that we will be able to prevent other parties from designing and marketing unauthorized MIPS-based products or that others will not independently develop or otherwise acquire the same or substantially equivalent technologies as ours. Moreover, cross licensing arrangements, in which we license certain of our patents but do not generally transfer know-how or other proprietary information, may facilitate the ability of cross-licensees, either alone or in conjunction with others, to develop competitive products and designs.

We cannot assure you that any of our patent applications will be approved or that any of the patents that we own will not be challenged, invalidated or circumvented by others or be of sufficient scope or strength to provide us with any meaningful protection or commercial advantage. Significant litigation regarding intellectual property rights exists in our industry. We cannot be certain that third parties will not make a claim of infringement against us, our licensees, or their manufacturers' customers in connection with use of our technology. Any claims, even those without merit, could be time consuming to defend, result in costly litigation and/or require us to enter into royalty or licensing agreements. These royalty or licensing agreements, if required, may not be available to us on acceptable terms or at all. A successful claim of infringement against us or one of our licensees in connection with its use of our technology could adversely affect our business.

If we fail to compete effectively in the market for embedded processors, our business will be adversely affected. Competition in the market for embedded processors is intense. We believe that the principal competitive factors in our industry are performance, functionality, price, customizability and power consumption. We cannot assure you that we will be able to compete successfully with respect to these factors or that competitive pressures will not materially and adversely affect our business, results of operations and financial condition. We compete with other designers and developers of processors and cores, as well as semiconductor manufacturers whose product lines include processors for embedded and non-embedded applications. In addition, we may face competition from the producers of unauthorized MIPS-based clones and non-RISC based technology designs.

To remain competitive, we must also differentiate our processors, cores and related designs from those available or under development by the internal design groups of semiconductor companies, including some of our current and prospective licensees. Many of these internal design groups have substantial programming and design resources and are part of larger organizations with substantial financial and marketing resources. These internal design groups may develop products that compete directly with ours or may actively seek to license their own technology to third-party semiconductor companies.

Many of our existing competitors, as well as a number of potential new competitors, have longer operating histories, greater brand recognition, larger customer bases as well as greater financial and marketing resources than we do. This may allow them to respond more quickly than we can to new or emerging technologies and changes in customer requirements. It may also allow them to devote greater resources than we can to the development and promotion of their technologies and products.

We may not be able to recruit and retain the personnel required to succeed. Our future success depends to a significant extent on the continued contributions of our key management, technical, sales

and marketing personnel, many of whom are highly skilled and difficult to replace. We intend to hire additional highly skilled personnel, particularly technical personnel, for our anticipated research and development activities. Competition for qualified personnel, particularly those with significant experience in the semiconductor and processor design industries, is intense. The loss of the services of any of our key personnel or our inability to attract and retain qualified personnel in the future could adversely affect our business, results of operations and financial condition. In particular, our ability to hire and retain qualified engineering personnel is essential to meet our business goals. Our ability to continue to grow successfully requires an effective planning and management process. Our growth has placed, and the recruitment and integration of additional employees will continue to place, a strain on our resources.

Factors that negatively affect our licensees could adversely affect our business. To date, a significant portion of our total revenue has been derived from a limited number of companies. Accordingly, factors negatively affecting a particular licensee could adversely affect our results of operations and financial condition if such licensee accounts for a significant portion of our revenue at the time. We are subject to many risks beyond our control that influence the success of our licensees, including, for example, the highly competitive environment in which they operate, the market for their products, their engineering capabilities and their financial and other resources.

Revenue from our top two licensees excluding Nintendo represented an aggregate of 17% of our total revenue in the third quarter and 19% in the first nine months of fiscal 2001 compared to 23% and 17% of our total revenue in the comparable periods during the prior year. We may experience similar revenue concentration in the future, although the identity of the particular licensees that will account for this revenue concentration may vary from period to period depending on the addition or expiration of contracts, the nature and timing of payments due under our contracts and the volumes and prices at which our licensees sell products incorporating our technology.

Our revenue is subject to fluctuations in currency exchange rates. A substantial portion of our revenue has been, and is expected to continue to be, derived from customers located outside the United States, primarily in Japan. To date, substantially all of our revenue from international customers has been denominated in U.S. dollars. However, to the extent that the sales by our licensees to their customers are denominated in foreign currencies, the royalties we receive on such sales could be subject to fluctuations in currency exchange rates. In addition, if the effective price of the technology we sell to our licensees were to increase due to fluctuations in foreign currency exchange rates, demand for our technology could fall, which would, in turn, reduce our royalties. Because we cannot predict the amount of non-U.S. dollar denominated revenue earned by our licensees, we have not historically attempted to mitigate the effect that currency fluctuations may have on our revenue, and we do not presently intend to do so in the future.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to interest rate risk on investments of our excess cash. The primary objective of our investment activities is to preserve capital. To achieve this objective and minimize the exposure due to adverse shifts in interest rates, we invest in high quality short-term maturity commercial paper and money market funds operated by reputable financial institutions in the United States. Due to the nature of our investments, we believe that we do not have a material interest rate risk exposure.

We are exposed to fluctuations in currency exchange rates because a substantial portion of our revenue has been, and is expected to continue to be, derived from customers located outside the United States, primarily in Japan. To date, substantially all of our revenue from international customers has been denominated in U.S. dollars. Because we cannot predict the amount of non-U.S. dollar denominated revenue earned by our licensees, we have not historically attempted to mitigate the effect that currency fluctuations may have on our revenue, and we do not presently intend to do so in the future.

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On October 28, 1999, we filed suit against Lexra, Inc. in the United States District Court for the Northern District of California for infringement of two United States patents. We subsequently amended our suit to cover two subsequently released Lexra products. On November 12, 1999, Lexra, Inc. filed counterclaims against us seeking a declaratory judgment that the two asserted patents are invalid and not infringed. Lexra has also asserted claims for common law unfair competition, intentional interference with business relations, and statutory unfair competition, all purportedly based on the allegation that our claims of patent infringement have been made in bad faith. On April 25, 2001, the Court conducted a hearing to consider arguments from the parties regarding the appropriate interpretation of the disputed patent claim terms. We anticipate a ruling from the Court concerning these terms in the near future. Discovery is currently ongoing in the lawsuit, but the Court has not yet set a trial date. In addition, Lexra has filed a request with the Patent and Trademark Office seeking re-examination of one of the patents at issue in this litigation. The Patent and Trademark Office has indicated that it will conduct a re-examination of the patent.

From time to time, we receive communications from third parties asserting patent or other rights covering our products and technologies. Based upon our evaluation, we may take no action or we may seek to obtain a license. There can be no assurance in any given case that a license will be available on terms we consider reasonable, or that litigation will not ensue. In addition, from time to time, we evaluate possible infringement claims against third parties and may assert such claims, if appropriate.

We are not aware of any pending disputes including that discussed above that we believe would adversely affect our business, results of operations or financial condition.

ITEMS 2, 3, 4, 5 AND 6 ARE NOT APPLICABLE AND HAVE BEEN OMITTED.

QuickLinks

PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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