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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, 2007

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)

Registrant's 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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. Large Accelerated Filer  Accelerated Filer  Non-accelerated Filer

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

As of May 31, 2007, the number of outstanding shares of the registrant's common stock, \$0.001 par value, was 43,595,452.

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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>2007</u>	<u>June 30,</u> <u>2006</u>
	<u>(unaudited)</u>	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 93,585	\$101,481
Marketable investments	42,708	19,725
Accounts receivable, net	6,010	4,631
Prepaid expenses and other current assets	2,223	3,157
Total current assets	<u>144,526</u>	<u>128,994</u>
Equipment, furniture and property, net	4,978	2,718
Intangible assets, net	4,171	5,044
Other assets	13,519	11,813
	<u>\$167,194</u>	<u>\$147,939</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 256	\$ 1,313
Accrued liabilities	13,596	8,287
Deferred revenue	2,475	2,143
Total current liabilities	<u>16,327</u>	<u>11,743</u>
Long-term liabilities	5,161	2,966
	<u>21,488</u>	<u>14,709</u>
Stockholders' equity:		
Common stock	43	43
Preferred stock	—	—
Additional paid-in capital	238,941	232,855
Accumulated other comprehensive income	395	142
Accumulated deficit	<u>(93,673)</u>	<u>(99,810)</u>
Total stockholders' equity	<u>145,706</u>	<u>133,230</u>
	<u>\$167,194</u>	<u>\$147,939</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,	
	2007	As Restated (1) 2006	2007	As Restated (1) 2006
<b>Revenue:</b>				
Royalties	\$10,733	\$ 9,334	\$33,128	\$26,318
Contract revenue	8,342	8,163	26,502	19,497
Total revenue	19,075	17,497	59,630	45,815
<b>Costs and expenses:</b>				
Research and development	8,596	6,981	25,281	20,665
Sales and marketing	5,400	4,808	15,479	13,769
General and administrative	4,978	3,051	13,867	9,262
Acquired in-process research and development	—	—	—	570
Total costs and expenses	18,974	14,840	54,627	44,266
Operating income	101	2,657	5,003	1,549
Other income, net	1,844	1,149	4,817	2,977
Income before income taxes	1,945	3,806	9,820	4,526
Provision for income taxes	708	837	3,672	980
Net income	<u>\$ 1,237</u>	<u>\$ 2,969</u>	<u>\$ 6,148</u>	<u>\$ 3,546</u>
Net income per basic share	<u>\$ 0.03</u>	<u>\$ 0.07</u>	<u>\$ 0.14</u>	<u>\$ 0.08</u>
Net income per diluted share	<u>\$ 0.03</u>	<u>\$ 0.07</u>	<u>\$ 0.13</u>	<u>\$ 0.08</u>
Shares used in computing net income per basic share	<u>43,535</u>	<u>43,088</u>	<u>43,510</u>	<u>42,732</u>
Shares used in computing net income per diluted share	<u>46,384</u>	<u>45,303</u>	<u>45,729</u>	<u>44,486</u>

(1) See Note 2, "Restatement of Condensed Consolidated Financial Statements," in Notes to Condensed Consolidated Financial Statements—Unaudited.

See accompanying notes.

**MIPS TECHNOLOGIES, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)**  
(In thousands)

	Nine Months Ended March 31,	
	2007	2006 As Restated (1)
<b>Operating activities:</b>		
Net income	\$ 6,148	\$ 3,546
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,596	1,189
Stock-based compensation	6,081	6,662
Acquired in-process research and development	—	570
Amortization of intangibles	1,020	921
Other non-cash charges	(781)	(581)
Changes in operating assets and liabilities:		
Accounts receivable	(1,379)	(2,202)
Prepaid expenses and other current assets	930	130
Other assets	(2,483)	(1,283)
Accounts payable	(1,057)	(1,116)
Accrued compensation	1,406	(1,281)
Other current accrued liabilities	2,183	(225)
Income tax payable	1,528	548
Deferred revenue	444	(752)
Long-term liabilities	2,083	560
Net cash provided by operating activities	<u>17,719</u>	<u>6,686</u>
<b>Investing activities:</b>		
Purchases of short-term investments	(57,190)	(39,315)
Maturities of short-term investments	35,000	40,000
Capital expenditures	(3,856)	(1,642)
Acquisition of First Silicon Solutions, Inc., net of cash acquired	—	(3,557)
Investment in private company	—	(500)
Restricted cash	—	(668)
Net cash used in investing activities	<u>(26,046)</u>	<u>(5,682)</u>
<b>Financing activities:</b>		
Net proceeds from issuance of common stock	386	4,504
Net cash provided by financing activities	386	4,504
Effect of exchange rate on cash	45	(62)
Net increase (decrease) in cash and cash equivalents	(7,896)	5,446
Cash and cash equivalents, beginning of period	<u>101,481</u>	<u>91,686</u>
Cash and cash equivalents, end of period	<u>93,585</u>	<u>\$ 97,132</u>
<b>Supplemental disclosures of cash transaction:</b>		
Income taxes paid	\$ 2,165	\$ 889

(1) See Note 2, "Restatement of Condensed Consolidated Financial Statements," in Notes to Condensed Consolidated Financial Statements—Unaudited.

See accompanying notes.

## MIPS TECHNOLOGIES, INC.

### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

#### Note 1. Description of Business and Basis of Presentation

We are a leading provider of industry-standard processor architectures and cores for digital consumer and business applications. We design and license high performance 32- and 64-bit architectures and cores, which offer smaller dimensions and higher performance in embedded processors. Our technology is utilized in many high-growth embedded markets including digital set-top boxes, digital televisions, DVD recordable devices, broadband access devices, digital cameras, laser printers and network routers.

**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 adjustments) 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, 2006 has been derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles. However, we believe that 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, 2006, included in our 2006 Annual Report on Form 10-K. In this Form 10-Q as reported in the 2006 Annual Report on 10-K, we are restating our condensed consolidated statements of operations for the three- and nine-months ended March 31, 2006 and condensed consolidated statement of cash flows for the nine-months ended March 31, 2006, as a result of an independent stock option investigation commenced by the Special Committee as described in Note 2, "Restatement of Condensed Consolidated Financial Statements." We have made certain other adjustments to the historical consolidated financial statements to correct errors identified during the preparation of the restated financial statements.

**Use of Estimates.** The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires us 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 inevitably will differ from those estimates, and such differences may be material to the financial statements.

**Revenue Recognition.** We derive revenue from license fees for the transfer of proven and reusable intellectual property components or from engineering services. We enter into licensing agreements that provide licensees the right to incorporate MIPS' intellectual property components in their products with terms and conditions that have historically varied by licensee. Revenue earned under contracts with our licensees is classified as either contract revenue or royalties. We recognize revenue in accordance with Staff Accounting Bulletin (SAB) No. 104, *Revenue Recognition*, and for multiple deliverable arrangements we follow the guidance in EITF 00-21, *Revenue Arrangements with Multiple Deliverables*, to determine whether there is more than one unit of accounting. To the extent that the deliverables are separable into multiple units of accounting, we then allocate the total fee on such arrangements to the individual units of accounting using the residual method. We then recognize revenue for each unit of accounting depending on the nature of the deliverable(s) comprising the unit of accounting (principally following SAB No. 104).

We derive revenue from license fees for currently available technology or from engineering services for technology under development. Each of these types of contracts includes a nonexclusive license for the underlying intellectual property. Fees for contracts for currently available technology include: license fees relating to our intellectual property, including processor designs; maintenance and support, typically for one year; and royalties payable following the sale by our licensees of products incorporating the licensed technology. Generally, our customers pay us a single upfront fee that covers the license and first year maintenance and support. Our deliverables in these arrangements include (a) processor designs and

related intellectual property and (b) maintenance and support. The license for our intellectual property, which includes processor designs, has standalone value and can be used by the licensee without maintenance and support. Further, objective and reliable evidence of fair value exists for maintenance and support based on specified renewal rates. Accordingly, (a) license fees and (b) maintenance and support fees are each treated as separate units of accounting. Total upfront fees are allocated to the license of processor designs and related intellectual property and maintenance and support using the residual method. Designs and related intellectual property are initially delivered followed by maintenance and support. Objective and reliable evidence of the fair value exists for maintenance and support. However, no such evidence of fair value exists for processor designs and related intellectual property. Consistent with the residual method, the amount of consideration allocated to processor designs and related intellectual property equals the total arrangement consideration less the fair value of maintenance and support, which is based on specified renewal rates. Following the guidance in SAB No. 104, fees for or allocated to licenses to currently available technology are recorded as revenue upon the execution of the license agreement when there is persuasive evidence of an arrangement, fees are fixed or determinable, delivery has occurred and collectibility is reasonably assured. We assess the credit worthiness of each customer when a transaction under the agreement occurs. If collectibility is not considered reasonably assured, revenue is recognized when the fee is collected. Other than maintenance and support, there is no continuing obligation under these arrangements after delivery of the intellectual property.

Contracts relating to technology under development also can involve delivery of a license to intellectual property, including processor designs. However, in these arrangements we undertake best-efforts engineering services intended to further the development of certain technology that has yet to be developed into a final processor design. Rather than paying an upfront fee to license completed technology, customers in these arrangements pay us milestone fees as we perform the engineering services. If the development work results in completed technology in the form of a processor design and related intellectual property, the customer is granted a license to such completed technology at no additional fee. These contracts typically include the purchase of first year maintenance and support commencing upon the completion of a processor design and related intellectual property for an additional fee, which fee is equal to the renewal rate specified in the arrangement. The licensee is also obligated to pay us royalties following the sale by our licensee of products incorporating the licensed technology. We continue to own the intellectual property that we develop and we retain the fees for engineering services regardless of whether the work performed results in a completed processor design. Fees for engineering services in contracts for technology under development, which contracts are performed on a best efforts basis, are recognized as revenue as services are performed; however, we limit the amount of revenue recognized to the aggregate amount received or currently due pursuant to the milestone terms. As engineering activities are best-efforts and at-risk and because the customer must pay an additional fee for the first year of maintenance and support if the activities are successful, the maintenance and support is a contingent deliverable that is not accounted for upfront under contracts relating to technology under development.

Under our maintenance and support arrangements, we provide unspecified upgrades, bug fixes and technical support. No other upgrades, products or other post-contract support are provided. These arrangements are renewable annually by the customer. Maintenance and support revenue is recognized at its fair value ratably over the period during which the obligation exists, typically 12 months. The fair value of any maintenance and support obligation is established based on the specified renewal rate for such support and maintenance and generally priced as a percentage of license fees.

We classify all revenue that involves the sale of a licensee's products as royalty revenue. Royalty revenue is recognized in the quarter in which a report is received from a licensee detailing the shipments of products incorporating our intellectual property components, which is generally in the quarter following the sale of the licensee's product to its customer. Royalties are calculated either as a percentage of the revenue received by the seller on sales of such products or on a per unit basis. We periodically engage a third party to perform royalty audits of our licensees, and if these audits indicate any over- or under-reported royalties, we account for the results when they are identified.

**Stock-Based Compensation.** We account for stock-based compensation in accordance with SFAS No. 123 revised 2004 *Share-Based Payment* (SFAS No. 123R). Compensation cost recognized during the three-month and nine-month periods ended March 31, 2007 and 2006, includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of July 1, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123 amortized on an accelerated basis over the options' vesting period, and (b) compensation cost for all share-based payments granted subsequent to July 1, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123R amortized on a straight-line basis over the options' vesting period.

The following table shows total stock-based employee compensation expense included in the condensed consolidated statement of operations for the three-months and nine-months periods ended March 31, 2007 and 2006 (in thousands):

	Three Months Ended March 31, 2007	Three Months Ended March 31, 2006 <u>As Restated (1)</u>	Nine Months Ended March 31, 2007	Nine Months Ended March 31, 2006 <u>As Restated (1)</u>
<b>Costs and expenses:</b>				
Research and development	\$ 871	\$ 602	\$ 2,374	\$ 3,327
Sales and marketing	721	463	1,821	1,464
General and administrative	659	490	1,887	1,818
<b>Total stock-based compensation expense</b>	<b>\$ 2,251</b>	<b>\$ 1,555</b>	<b>\$ 6,082</b>	<b>\$ 6,609</b>

(1) See Note 2, "Restatement of Condensed Consolidated Financial Statements," in Notes to Condensed Consolidated Financial Statements—Unaudited.

There was no capitalized stock-based employee compensation cost as of March 31, 2006. There were no material recognized tax benefits during the first nine months of fiscal 2007.

For restricted common stock issued at discounted prices, we recognize compensation expense over the vesting period for the difference between the exercise or purchase price and the fair market value on the measurement date. Total compensation expense recognized in our financial statements for restricted stock awards was \$35,000 and \$106,000 for the three-month and nine-month periods ended March 31, 2007 and \$26,000 and \$164,000 for the three-month and nine-month periods ended March 31, 2006.

## Note 2. Restatement of Condensed Consolidated Financial Statements

**Restatement of Previously Issued Financial Statements.** In our 2006 Annual Report on Form 10-K, we restated our consolidated balance sheet as of June 30, 2005, and the related consolidated statements of operations, stockholder's equity, and cash flows for each of the fiscal years ended June 30, 2005 and June 30, 2004, and the first three quarters of 2006 as a result of an independent stock option investigation by the Special Committee of our Board of Directors. As a result, we have recorded net additional non-cash stock-based compensation expense and related tax effects of \$32.0 million recorded in fiscal years 1999 to 2006 with regard to past stock option grants with approximately 99% of the expense being recorded in years prior to fiscal 2004. We have made certain other adjustments to the consolidated financial statements to correct errors identified during the preparation of the restated financial statements.

In this Form 10-Q as reported in the 2006 Annual Report on Form 10-K, we are restating our condensed consolidated statements of operations for the three- and nine-months ended March 31, 2006 and condensed consolidated statement of cash flows for the nine-months ended March 31, 2006, as a result of an independent stock option investigation commenced by the Special Committee. We have made certain other adjustments to the historical consolidated financial statements to correct errors identified during the preparation of the restated financial statements. These adjustments included: (1) a calculation error under FAS123R in the fair value of options which were the subject of a settlement of our Denmark lawsuit in the amount of \$2.1 million related to the first quarter of fiscal year 2006; (2) a realized foreign exchange gain of \$280,000 in fiscal year 2005 related to the reconciliation of the currency translation adjustments from the closure of our Denmark entity; (3) calculation errors related to the accretion of interest on certain investments increasing interest income by \$13,000 in fiscal 2003, \$43,000 in fiscal 2004, \$59,000 in fiscal 2005 and \$45,000 cumulative in the first three quarters of fiscal 2006; (4) calculation errors noted in our federal and state research and development tax credits which impacted our income tax provision expense resulting in an increase of \$220,000 in fiscal 2000, a decrease of \$317,000 in fiscal 2001, a decrease of \$17,000 in fiscal 2002 and an increase of \$2,200,000 in fiscal 2003; and (5) errors in our income tax provision calculation related to foreign income taxes resulting in reductions of income tax expense in the amount of \$90,000 in fiscal 2004, \$88,000 in fiscal 2005 and \$118,000 in the second quarter of fiscal 2006.

The following table presents the effects of the stock-based compensation related to the stock option investigation and associated income tax adjustments and certain other adjustments to our previously reported condensed consolidated statements of operations (in thousands, except per share amounts):

	Three Months Ended March 31, 2006			Nine Months Ended March 31, 2006		
	As Reported	Adjustments	As Restated	As Reported	Adjustments (1)	As Restated
<b>Revenue:</b>						
Royalties	\$ 9,334	\$ —	\$ 9,334	\$26,318	\$ —	\$26,318
Contract revenue	8,163	—	8,163	19,497	—	19,497
Total revenue	17,497	—	17,497	45,815	—	45,815
<b>Costs and expenses:</b>						
Research and development	7,071	(90)	6,981	22,788	(2,123)	20,665
Sales and marketing	4,799	9	4,808	13,724	45	13,769
General and administrative	3,195	(144)	3,051	9,281	(19)	9,262
Acquired in-process research and development	—	—	—	570	—	570
Total costs and expenses	15,065	(225)	14,840	46,363	(2,097)	44,266
Operating income (loss)	2,432	225	2,657	(548)	2,097	1,549
Other income, net	1,120	29	1,149	2,932	45	2,977
Income before income taxes	3,552	254	3,806	2,384	2,142	4,526
Provision (benefit) for income taxes	1,327	(490)	837	1,089	(109)	980
Net income	<u>\$ 2,225</u>	<u>\$ 744</u>	<u>\$ 2,969</u>	<u>\$ 1,295</u>	<u>2,251</u>	<u>\$ 3,546</u>
<b>Per basic share amounts:</b>						
Net income per basic share	<u>\$ 0.05</u>	<u>\$ 0.02</u>	<u>\$ 0.07</u>	<u>\$ 0.03</u>	<u>\$ 0.05</u>	<u>\$ 0.08</u>
<b>Per diluted share amounts:</b>						
Net income per diluted share	<u>\$ 0.05</u>	<u>\$ 0.02</u>	<u>\$ 0.07</u>	<u>\$ 0.03</u>	<u>\$ 0.05</u>	<u>\$ 0.08</u>
Shares used in computing net income per basic share	<u>43,103</u>	<u>43,088</u>	<u>43,088</u>	<u>42,750</u>	<u>42,732</u>	<u>42,732</u>
Shares used in computing net income per diluted share	<u>45,367</u>	<u>45,303</u>	<u>45,303</u>	<u>44,562</u>	<u>44,486</u>	<u>44,486</u>

- (1) Adjustment of \$2.1 million in research and development primarily pertains to a calculation error under FAS 123R in the fair value of options which were the subject of a settlement of our Denmark lawsuit. The impact of this error before income taxes was \$2.1 million related to the first quarter of fiscal 2006.

The following table presents the effects of the stock-based compensation and related tax adjustments and certain other adjustments to our previously reported condensed consolidated statement of cash flows (in thousands, except per share amounts):

	Nine Months Ended March 31, 2006		
	As Reported	Adjustments (1)	As Restated
<b>Operating Activities:</b>			
Net income	\$ 1,295	\$ 2,251	\$ 3,546
<b>Adjustments to reconcile net income (loss) to cash provided by operations:</b>			
Depreciation	1,189	—	1,189
Stock based compensation	8,860	(2,198)	6,662
Acquired in-process research and development	570	—	570
Amortization of intangibles and deferred compensation	921	—	921
Other non-cash charges	(552)	(29)	(581)
<b>Changes in operating assets and liabilities:</b>			
Accounts receivable	(2,202)	—	(2,202)
Prepaid expenses and other current assets	130	—	130
Other assets	(1,283)	—	(1,283)
Accounts payable	(1,116)	—	(1,116)
Accrued compensation	(1,281)	—	(1,281)
Other current accrued liabilities	(211)	(14)	(225)
Income tax payable	658	(110)	548
Deferred revenue	(752)	—	(752)
Long-term liabilities	560	—	560
Net cash provided by operating activities	6,786	(100)	6,686
<b>Investing activities:</b>			
Purchases of marketable investments	(39,315)	—	(39,315)
Maturities of marketable investments	40,000	—	40,000
Capital expenditures	(1,642)	—	(1,642)
Acquisition of First Silicon Solutions, Inc., net of cash acquired	(3,657)	100	(3,557)
Investment in private company	(500)	—	(500)
Restricted cash	(668)	—	(668)
Net cash used in investing activities	(5,782)	100	(5,682)
<b>Financing activities:</b>			
Net proceeds from issuance of common stock	4,504	—	4,504
Net cash provided by financing activities	4,504	—	4,504
Effect of exchange rate on cash	(62)	—	(62)
Net increase (decrease) in cash and cash equivalents	5,446	—	5,446
Cash and cash equivalents, beginning of year	91,686	—	91,686
Cash and cash equivalents, end of year	<u>\$ 97,132</u>	<u>\$ —</u>	<u>\$ 97,132</u>
<b>Supplemental disclosures of cash transactions:</b>			
Income taxes paid	\$ 179	\$ —	\$ 179

- (1) Adjustment of \$2.2 million in stock-based compensation primarily pertains to a calculation error under FAS 123R in the fair value of options which were the subject of a settlement of our Denmark lawsuit. The impact of this error before income taxes was \$2.1 million during the first quarter of fiscal 2006.

### Note 3. Computation of Earnings Per Share

**Earnings per Share.** We follow the provisions of SFAS No. 128, *Earnings per Share* (SFAS No. 128). SFAS No. 128 requires the presentation of basic and fully diluted earnings per share. Basic earnings per share is computed by dividing income available to common stockholders by the weighted average number of common shares that were outstanding during the period. Diluted earnings per share is computed giving effect to all dilutive potential common shares that were outstanding for any periods presented in these financial statements.

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,	
	2007	2006 As Restated (1)	2007	2006 As Restated (1)
<b>Numerator:</b>				
Net income	\$ 1,237	\$ 2,969	\$ 6,148	\$ 3,546
<b>Denominator:</b>				
Weighted-average shares of common stock outstanding	43,595	43,178	43,570	42,837
Less: Weighted-average shares subject to repurchase	(60)	(90)	(60)	(105)
Shares used in computing net income per basic share	<u>43,535</u>	<u>43,088</u>	<u>43,510</u>	<u>42,732</u>
Effect of dilutive securities-employee stock options and shares subject to repurchase	2,849	2,215	2,219	1,754
Shares used in computing net income per diluted share	<u>46,384</u>	<u>45,303</u>	<u>45,729</u>	<u>44,486</u>
Net income per basic share	<u>\$ 0.03</u>	<u>\$ 0.07</u>	<u>\$ 0.14</u>	<u>\$ 0.08</u>
Net income per diluted share	<u>\$ 0.03</u>	<u>\$ 0.07</u>	<u>\$ 0.13</u>	<u>\$ 0.08</u>
Potentially dilutive securities excluded from net income per diluted share because they are anti-dilutive	5,163	7,928	7,904	8,062

(1) See Note 2, "Restatement of Condensed Consolidated Financial Statements."

#### Note 4. Comprehensive Income (Loss)

Total comprehensive income (loss) includes net income (loss) and other comprehensive income, which primarily comprises unrealized gains and losses from foreign currency adjustments. Total comprehensive income for the third quarter and the first nine months of fiscal 2007 was \$1.3 million and \$6.4 million compared to total comprehensive income of \$3.0 million and \$3.5 million for the comparable periods in the prior year.

#### Note 5. Investment and Acquisition

On September 2, 2005, we acquired First Silicon Solutions, Inc. (FS2), a design services and development tools company based in Lake Oswego, Oregon. FS2's products and services will provide value to our customer base by improving de-bugging capability and accelerating time to market of their products. We acquired all of the outstanding FS2 stock for an initial purchase consideration of \$4.5 million, including approximately \$140,000 of acquisition-related costs. The purchase consideration was paid in cash. We did not assume any of the options of FS2. An escrow account holds 15% of the initial cash consideration to cover claims we may have under the merger agreement for a minimum of 18 months. We agreed to pay an additional amount of up to \$4.0 million in contingent payments over a three-year period following the acquisition date based upon annual revenue and project completion milestones. In accordance with EITF 95-8: *Accounting for Contingent Consideration Paid to the Shareholders for an Acquired Enterprise in a Purchase Business Combination*, any such payments based on achievement of annual revenue milestones will be additional purchase consideration and will be recorded as goodwill. Any such payments based on completion of project milestones will be recorded as operating expense.

The preliminary purchase price was allocated as follows:

Intangible assets acquired	\$3,220
Acquired in-process research and development	570
Net tangible assets	477
Goodwill	263
<b>Total assets acquired</b>	<b><u>\$4,530</u></b>

Additional contingent consideration based on completion of project milestones of \$100,000 was earned during the quarter ended December 31, 2005. This contingent consideration was recorded as additional operating expense. Additional contingent consideration based on completion of project milestones of \$100,000 was earned during the second quarter of fiscal year 2007. This contingent consideration was recorded as additional operating expense.

The fair value of the intangible assets, including developed technology, customer relationships and trade name was determined by estimating the present value of cash flows from those assets based on the assumptions of our management, industry assumptions and market data. The estimated useful life of the developed technology of five years was determined based on our estimates of the product life cycles in the current and expected market place. The estimated useful life of the customer relationships of six years was determined based on our experience in the industry and with this customer pool. The useful life of the trade name of three years was determined based on industry experience. These assets are being amortized on a straight line basis over their estimated useful lives.

The fair value of the in-process technology was determined by estimating the present value of the net cash flows we believed would result from the acquired technology. Because technological feasibility of certain of the acquired technology had not been established and no future alternative use for the in-process technology existed at the time of the acquisition, we recorded a charge of \$570,000 for the acquired in-process research and development expense upon completion of the acquisition.

The operating results of FS2 beginning on the acquisition date of September 2, 2005 are included in these financial statements.

In fiscal 2006, we acquired equity interests in two privately-held companies for \$4.5 million that were accounted for under the cost method. The investments are included in other assets on the consolidated balance sheet.

#### Note 6. Purchased Intangible Assets

All of our purchased intangible assets, except goodwill, are subject to amortization. Purchased intangible assets subject to amortization consisted of the following as of March 31, 2007 and June 30, 2006 (in thousands):

	March 31, 2007			June 30, 2006		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Developed and core technology	\$ 6,062	\$ (3,418)	\$ 2,644	\$ 6,062	\$ (2,736)	\$ 3,326
Customer relationships	1,310	(346)	964	1,310	(182)	1,128
Tradename	110	(58)	52	110	(31)	79
Purchased intangible assets	<u>\$ 7,482</u>	<u>\$ (3,822)</u>	<u>\$ 3,660</u>	<u>\$ 7,482</u>	<u>\$ (2,949)</u>	<u>\$ 4,533</u>

The estimated future amortization expense of purchased intangible assets as of March 31, 2007 is approximately \$291,000, \$1,164,000, \$925,000, \$690,000 and \$388,000 for the remaining three months of fiscal 2007 and for fiscal years 2008, 2009, 2010 and 2011 respectively, and approximately \$201,000 for years following fiscal 2011. Amortization expense for purchased intangible assets was \$291,000 in the third quarter of fiscal 2007 and \$873,000 for the first nine months of fiscal 2007 compared to \$291,000 and \$771,000 for the comparable periods of fiscal 2006.

Goodwill, as of March 31, 2007 and June 30, 2006 was \$511,000.

#### Note 7. Interest Income

Interest income reported under Other income, net was \$1.9 million and \$5.0 million for the three-month and nine-month periods ended March 31, 2007 compared to \$1.2 million, and \$3.1 million in the comparable periods of fiscal 2006.

## Note 8. Commitments and Contingencies

### *Purchase Commitments with Suppliers*

We have outstanding purchase orders for ongoing operations of approximately \$7.4 million as of March 31, 2007. Payment of these obligations are subject to the provision of services or products.

### *Litigation*

On April 30, 2003, our Swiss subsidiary, MIPS Technologies International AG, or MIPS AG, through which we conducted our operations in Denmark, terminated the employment of 55 employees in connection with the closure of our Denmark design center. Of these, 45 employees filed claims against MIPS AG in the County Court of Ballerup, Denmark (subsequently transferred to the Maritime and Commercial Court of Copenhagen, Denmark). Subsequently, 13 of these employees agreed to withdraw their claims. On the termination date, the remaining 32 employees of MIPS AG held options to purchase an aggregate of 724,830 shares of our common stock, of which options to purchase 413,552 shares were vested and options to purchase 311,278 shares were unvested. The exercise price of these options ranged from \$2.94 to \$25.50 per share. Under our stock option plans, unvested options expire upon termination of employment and vested options expire three months after the termination of employment.

In September 2005, we reached a settlement with each of the 32 former Danish employees and the union that represented them. Pursuant to the settlement, each of the 32 former employees will retain a substantial portion of his or her options and relinquish claims to the balance of the options and any other claims regarding the options. In the first quarter of fiscal 2006, approximately \$3.3 million was expensed which represents the estimated fair value of options reinstated pursuant to the settlement. As a result of the settlement, the Danish lawsuit was withdrawn in October 2005 and MIPS Technologies, Inc. withdrew the lawsuit filed on April 11, 2005 in the U.S. federal court (Northern District of California) against the terminated employees who had pending Danish claims against MIPS AG. As a result, MIPS Technologies, Inc. and MIPS AG no longer have any litigation pending with respect to this matter.

Three actions seeking to assert derivative claims on behalf of MIPS have been filed in the United States District Court for the Northern District of California. The shareholder-plaintiffs in each of these actions seek to assert claims against current and former officers and directors related to our historic stock option grant practices. Each action alleges that the individual defendants breached their fiduciary duties and violated federal securities laws as a result of backdating stock option grants, insider trading and the dissemination of false financial statements. Each action asserts that the individual defendants' conduct injured MIPS and gives rise to numerous causes of action on behalf of MIPS under the federal securities laws and state law. Plaintiffs seek to recover, on behalf of MIPS, monetary damages, various equitable remedies, attorneys' fees and costs. The individual actions are:

- *Steger v. Bourgoin, et. al.*, No. C-06-06699, filed on October 27, 2006, and brought against John Bourgoin, Jack Browne, Kenneth L. Coleman, Sandy Creighton, Kevin C. Eichler, Fred M. Gibbons, Anthony B. Holbrook, William M. Kelly, Lavi Lev, and Derek Meyer as individual defendants and MIPS as nominal defendant;
- *Carco v. Holbrook, et. al.*, No. C-07-0661, filed on February 1, 2007, and brought against Anthony B. Holbrook, John E. Bourgoin, Mervin S. Kato, Kate Hunt Rundle, Brad Holtzinger, Mark Tyndall, Jack Browne, Sandy Creighton, Kevin C. Eichler, G. Michael Uhler, Robert R. Herb, Fred M. Gibbons, Benjamin A. Horowitz, Kenneth L. Coleman and William M. Kelly as individual defendants and MIPS as nominal defendant; and
- *Michaels v. Bourgoin, et. al.*, No. C-07-0771, filed on February 6, 2007, and brought against John E. Bourgoin, Sandy Creighton, Kevin C. Eichler, Lavi Lev, Derek Meyer, Kenneth L. Coleman, Fred M. Gibbons, Anthony B. Holbrook and William M. Kelly as individual defendants and MIPS as nominal defendant.

By order of the court dated April 12, 2007, the three actions were consolidated into a single action entitled *In re MIPS Technologies, Inc. Derivative Litigation*. Pursuant to the court's order, a consolidated complaint was due by May 29, 2007 and discovery in the consolidated action was stayed pending resolution of a motion to dismiss the consolidated complaint due to plaintiffs' lack of standing to sue on MIPS' behalf. On May 25, 2007, the parties jointly submitted to the court a stipulation and proposed order extending the time for lead plaintiff to file a consolidated complaint until July 16, 2007. It is not known when or on what basis these matters will be resolved.

On December 1, 2006, MIPS Technologies, Inc. filed a lawsuit in the United States District Court for the Northern District of California against Trident Microsystems, Inc. asserting patent and trademark infringement and unfair competition. This action sought various forms of relief including a permanent injunction from further infringement of the company's intellectual property, compensatory and enhanced damages, and attorneys' fees. In early April 2007, the parties entered into an agreement that settled the lawsuit and filed documentation with the Court stipulating to its dismissal. On April 9, 2007, we issued a press release reporting that the parties had reached agreement on the lawsuit, that the suit had been dismissed, and that Trident Microsystems had licensed the MIPS32 24KEc Pro Core.

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.

### Note 9. Stock-Based Compensation

Activity under our Stock Option Plans for the nine months ending March 31, 2007 is summarized as follows:

	<u>Number of Shares</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Aggregate Intrinsic Value</u> (in thousands)
Outstanding at July 1, 2006	13,047,917	\$ 7.49		
Options granted	1,935,275	\$ 6.92		
Options exercised	(86,035)	\$ 4.49		
Options canceled	(857,809)	\$ 8.25		
Outstanding at March 31, 2007	<u>14,039,348</u>	\$ 7.39	5.51	\$ 33,893
Exercisable at March 31, 2007	<u>9,818,700</u>	\$ 7.75	5.14	\$ 23,618

Aggregate intrinsic value represents the value of our closing stock price on the last trading day of the period in excess of the exercise price multiplied by the number of options outstanding or exercisable. The intrinsic value of options exercised represents the value of our closing stock price on the exercise date in excess of the exercise price multiplied by the number of options exercised. The total intrinsic value for the nine months ended March 31, 2007 and 2006 was \$200,000 and \$2.5 million.

Nonvested share activity under our Stock Options Plans for the nine-month period ended March 31, 2007 is summarized as follows:

	<u>Non-vested Number of Shares</u>	<u>Weighted Average Grant-Date Fair Value</u>
Nonvested balance at July 1, 2006	90,000	\$ 4.72
Vested	(30,000)	\$ 4.72
Cancelled	—	—
Nonvested balance at March 31, 2007	<u>60,000</u>	\$ 4.72

As of March 31, 2007, \$194,000 of total unrecognized compensation costs related to nonvested awards is expected to be recognized over a weighted average period of 1.4 years. The total fair value of shares vested during the nine-month period ended March 31, 2006 was \$202,000.

**Grant Date Fair Values.** The weighted average fair value has been estimated at the date of grant using a Black-Scholes option-pricing model. In fiscal 2006, we refined the method of estimating the volatility of our common stock which we believe provides a more reasonable forecast. For stock options, we estimated volatility by considering both the implied volatility derived from publicly traded options to purchase our common stock and historical stock volatility. As a result of the adjustment to our term and vesting schedule in July 2005 for stock options awarded under our 1998 and 2002 Plans, we do not believe that we are able to rely on our historical exercise and post-vested termination activity to provide relevant data for estimating our expected term for use in determining the fair value of these options. Therefore, as allowed by Staff Accounting Bulletin (SAB) No. 107, *Share-Based Payment*, we have opted to use the simplified method for estimating our expected term equal to the midpoint between the vesting period and the contractual term. Prior to fiscal 2006, we estimated volatility and the expected life based solely on historical activity. The change in our assumptions did not have a significant impact on the fair value of our stock options granted in fiscal 2006. The following are significant weighted average assumptions used for estimating the fair value of the activity under our stock option plans:

	Employee Stock Options Nine Months Ended March 31,		Employee Stock Purchase Plan Nine Months Ended March 31,	
	2007	2006	2007(1)	2006
Expected life (in years)	4.2	4.2	—	.5
Risk-free interest rate	4.83%	4.27%	—	4.37%
Expected volatility	.63	.75	—	.63
Dividend yield	0.00%	0.00%	—	0.00%
Grant date fair value	\$ 3.68	\$ 4.01	—	\$ 1.84

(1) There were no employee stock purchases made in the first nine months of fiscal 2007.

Included in the condensed consolidated statement of operations for the three-month and nine-month periods ended March 31, 2007 is zero and \$162,000 in stock-based compensation expense related to the amortization of options granted under our Employee Stock Purchase and Supplemental Stock Purchase Plans and \$74,000 and \$293,000 in the comparable periods in fiscal 2006.

#### Note 10. Income Taxes

We recorded an income tax provision of \$708,000 for the three-month period ended March 31, 2007 and \$837,000 for the comparable period in fiscal 2006. For the nine-month period ended March 31, 2007, we recorded an income tax provision of \$3.7 million and \$980,000 for the comparable period in fiscal 2006.

Our estimated annual effective income tax rate of 38% for fiscal 2007 primarily consists of US federal and state taxes and foreign taxes on income earned in certain foreign jurisdictions and withholding taxes, offset in part by the availability of certain foreign tax credits and general business tax credits. The actual tax rate of 36% for the three-month period ended March 31, 2007 and 37% for the nine-month period ended March 31, 2007 differs from the estimated annual effective tax rate of 38% due to discrete items recorded during the periods for non-deductible acquisition costs related to our acquisition of First Silicon Solutions. The estimated annual effective income tax rate of 22%, before discrete items, recorded for the three and nine-month periods ended March 31, 2006 is lower than the applicable statutory rate primarily due to the availability of foreign tax credits and general business tax credit carryovers from prior years.

The amount of income taxes we pay is subject to ongoing audits by federal, state and foreign tax authorities, which often result in proposed assessments. Our future results may include favorable or

unfavorable adjustments to our estimated tax liabilities in the period the assessments are made or resolved or when statutes of limitation on potential assessments expire. As a result, our effective tax rate may fluctuate significantly on a quarterly basis.

**Note 11. Recent Accounting Pronouncements**

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN No. 48). FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with Statement of Financial Accounting Standard (SFAS) No. 109, "Accounting for Income Taxes." This Interpretation prescribes a recognition threshold and measurement attribute of tax positions taken or expected to be taken on a tax return. FIN No. 48 will be effective for MIPS beginning with July 1, 2007. We are currently evaluating the effect that the adoption of FIN No. 48 will have on its results of operations and financial position.

In September 2006, the FASB, issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157), which defines fair value, establishes a framework for measuring fair value and expands disclosures, about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are currently assessing the potential effect, if any, of implementing this standard.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB No. 108), which is effective for fiscal years ending after November 15, 2006. SAB No. 108 provides interpretive guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. We do not expect the adoption of SAB No. 108 to have a material impact on our consolidated financial statements.

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

*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. Forward-looking statements within this Quarterly Report on Form 10-Q include our expectations of decreased royalties, as well as expectations for future levels of operating and other expenses and 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 "Risk Factors," and other risks affecting our business. We undertake no obligation to update any forward-looking statements included in this discussion.*

The discussion and analysis set forth below in this Item 2 reflect the restatement of our financial results as referenced in our Annual Report on Form 10-K for the year ended June 30, 2006 in the "Explanatory Note" immediately preceding Part I Item 1 and further discussed in Item 7, Management's Discussion and Analysis of Results of Operations and Financial Condition and in Note 3, "Restatement of Consolidated Financial Statements" in Notes to Consolidated Financial Statements. In this Form 10-Q, we are restating our condensed consolidated statements of operations for the three- and nine-months ended March 31, 2006 and condensed consolidated statement of cash flows for the nine-month ended March 31, 2006, as a result of an independent stock option investigation commenced by the Special Committee. We have made certain other adjustments to the historical consolidated financial statements to correct errors identified during the preparation of the restated financial statements.

### **Overview**

We are a leading provider of industry-standard processor architectures and cores for digital consumer and business applications. We design and license high performance 32- and 64-bit architectures and cores, which offer smaller dimensions and higher performance in embedded processors. Our technology is utilized in many high-growth embedded markets including digital set-top boxes, digital televisions, DVD recordable devices, broadband access devices, digital cameras, laser printers and network routers.

Revenue in the third quarter of fiscal 2007 increased 9% over the comparable period in fiscal 2006, but decreased 9% sequentially. Contract revenue was flat with the comparable period in fiscal 2006 and decreased 18% sequentially. We expected to complete two agreements during the third quarter that were not completed until the first week of the fourth quarter of fiscal 2007. Of the four new license agreement signed during the quarter, two were for the MIPS32 24K core family and one was for the MIPS32 4K core family. The fourth agreement involved a broad licensing agreement with Broadcom for all of our MIPS 32 cores. Royalty revenue increased 15% over the comparable period in fiscal 2006, but was down 4% sequentially due to a decrease in royalties from pre IPO agreements. Our licensees reported shipping 87 million units during the third quarter of fiscal 2007, an increase of 23% over the comparable period in fiscal 2006 and a decrease of 2.3 million units sequentially. The average royalty per unit decreased from \$0.13 to \$0.12. We expect royalty revenue to decrease slightly in the upcoming quarter due to historical seasonal downward trends following the holiday selling season.

Operating expense in the third quarter of fiscal 2007 increased \$4.1 million or 28% over the comparable period in fiscal 2006 primarily due to an increase of \$1.5 million in salary and benefits expense due to headcount growth and the cost of accounting and legal services of \$1.2 million related to the investigation into our historical stock option practices, and an increase of \$702,000 in stock compensation expense primarily due to a modification expense from the extension of the term of certain options. We will incur additional accounting and legal fees related to the stock option investigation and restatement of our historical financial statements through the remainder of fiscal 2007. We expect our operating expenses for the remainder of fiscal 2007, net of the cost of the investigation, to be higher than the comparable periods in fiscal 2006 as we continue to invest in additional projects to support future growth.

Net income before income tax for the third quarter of fiscal 2007 was \$1.9 million compared to \$3.8 million for the comparable period in fiscal 2006.

Our balance sheet remains strong as our cash, cash equivalents and marketable investments balance increased by \$15.1 million during the first nine months of fiscal 2007 with net cash of \$17.7 million provided from operating activities.

## Results of Operations

*Revenue.* Total revenue consists of royalties and contract revenue. Royalties are based upon sales by licensees of products incorporating our technology. Contract revenue consists of technology license fees generated from new and existing license agreements for developed technology and engineering service fees generated from contracts for technology under development. Technology license fees vary based on, among other things, whether a particular technology is licensed for a single application or for multiple or unlimited applications, and whether the license granted covers a particular design or a broader architecture.

Our revenue in the three-month and nine-month periods ended March 31, 2006 and March 31, 2005 was as follows (in thousands):

	Three Months Ended March 31,			Nine Months Ended March 31,		
	2007	2006	Change in Percent	2007	2006	Change in Percent
Revenue						
Royalties	\$10,733	\$ 9,334	15%	\$33,128	\$26,318	26%
<i>Percentage of Total Revenue</i>	56 %	53 %		56 %	57 %	
Contract Revenue	\$ 8,342	\$ 8,163	2%	\$26,502	\$19,497	36%
<i>Percentage of Total Revenue</i>	44 %	47 %		44 %	43 %	
Total Revenue	<u>\$19,075</u>	<u>\$17,497</u>	<u>9%</u>	<u>\$59,630</u>	<u>\$45,815</u>	<u>30%</u>

The increase in revenue for the third quarter of fiscal 2007 over the comparable period in fiscal 2006 was due to an increase in royalties from post-IPO agreements of \$2.4 million offset in part by a decrease in royalties from pre-IPO agreements of \$1.0 million. Contract revenue for the third quarter of fiscal 2007 increased slightly over the comparable period in fiscal 2006.

The increase in revenue for the first nine months of fiscal 2007 over the comparable period in fiscal 2006 was due to an increase in both contract revenue and royalties. The increase in contract revenue was primarily due to an increase in fees generated from new and existing license agreements for developed technology of \$5.5 million driven by an increase in revenue from MIPS32 24K core family revenue of \$3.1 million, MIPS 64 ISA revenue of \$2.8 million and MIPS 4K core family revenue of \$1.8 million, offset in part by a decrease in the MIPS32 34K core family of \$1.3 million. The increase in fees for developed technology was primarily due to the completion of 21 new license agreements during the first nine months of fiscal 2007 compared to 16 agreements completed in the comparable period of fiscal 2006. Additionally, there was an increase of \$1.0M in maintenance, support and FS2 revenue over the comparable period in fiscal 2006. This increase was offset in part by a decrease of \$1.2 million in contract revenue generated from engineering services contracts for technology under development during the first nine months of fiscal 2007 as we rendered no such services during the first six months of fiscal 2007. The increase in royalties was due to an increase of \$9.2 million in royalties from post-IPO agreements offset in part by a decrease of \$2.4 million in pre-IPO agreements

*Cost and Expenses.* Our cost and expenses for the three-month and nine-month periods ended March 31, 2007 and March 31, 2006 was as follows (in thousands):

	Three Months Ended March 31,			Nine Months Ended March 31,		
	2007	2006 (As Restated) (1)	Change in Percent	2007	2006 (As Restated) (1)	Change in Percent
<b>Cost and Expenses</b>						
Research and Development	\$8,596	\$ 6,981	23%	\$25,281	\$ 20,665	22%
Sales and Marketing	\$5,400	\$ 4,808	12%	\$15,479	\$ 13,769	12%
General and Administrative	\$4,978	\$ 3,051	63%	\$13,867	\$ 9,262	50%

(1) See Note 2, "Restatement of Condensed Consolidated Financial Statements," in Notes to Condensed Consolidated Financial Statements—Unaudited.

*Research and Development.* Research and development expenses include salaries and contractor and consultant fees, as well as costs related to workstations, software, computer aided design tools, and stock-based compensation expense. The costs we incur with respect to internally developed technology and engineering services are included in research and development expenses as they are incurred and are not directly related to any particular licensee, license agreement or license fee.

The increase in research and development expenses for the third quarter of fiscal 2007 over the comparable period in fiscal 2006 was primarily the result an increase in salary and benefits expense of \$986,000 due to a growth in headcount of 19 employees.

The increase in research and development expenses for the first nine months of fiscal 2007 over the comparable period in fiscal 2006 was primarily the result of an increase in salary and benefits expense of \$2.5 million due to an increase in headcount of 19 employees, an increase in depreciation and amortization expense of \$1.0 million related to an increase in our computer-aided design tool base to support our increasing headcount, an increase in bonus expense of \$880,000 as targets under our fiscal 2007 bonus plans were achieved, and a payment of \$400,000 in fees to a third party for milestones completed under a development agreement. These increases were partially offset by a decrease in stock based compensation expense of \$1.2 million related to the options which were the subject of the Denmark lawsuit settlement agreement reached in September 2005.

*Sales and Marketing.* Sales and marketing expenses include salaries, commissions and costs associated with third party independent software development tools, direct marketing, other marketing efforts and stock-based compensation expense. Our sales and marketing efforts are directed at establishing and supporting our licensing relationships.

The increase in sales and marketing expenses for the third quarter of fiscal 2007 over the comparable period in fiscal 2006 was primarily the result of an increase in salary expense of \$206,000 due to a net increase in headcount of 4 employees, and an increase in bonus and commission expense of \$205,000 primarily due to increased headcount and higher commissions in certain regions as target revenues were exceeded. These increases were offset in part by a decrease in marketing project related costs of \$125,000 due to milestones reached under ongoing projects in the prior period.

The increase in sales and marketing expenses for the first nine months of fiscal 2007 over the comparable period in the prior year was primarily the result an increase in salary expense of \$507,000 due to a net increase in headcount of 4 employees, and an increase in bonus and commission expense of \$837,000 as targets under our fiscal 2007 bonus plans were achieved, as well as higher commissions in certain regions as target revenues were exceeded. These increases were offset in part by a decrease in marketing project related costs of \$210,000 primarily due to milestones reached under ongoing projects in the prior period.

*General and Administrative.* General and administrative expenses comprise salaries, legal fees including those associated with the establishment and protection of our patent, trademark and other intellectual property rights which are integral to our business and expenses related to compliance with the reporting and other requirements of a publicly traded company including directors and officers liability insurance, in addition to stock-based compensation expense.

The increase in general and administrative expenses for the third quarter of fiscal 2007 over the comparable period in fiscal 2006 was primarily the result of the an increase in fees for legal, accounting and audit services of \$1.2 million due to the investigation of our historical stock option practices, as well as an increase in salary expense of \$222,000 due to headcount growth of 5 employees as well as an increase in bonus expense of \$105,000.

The increase in general and administrative expenses in the first nine months of fiscal 2007 was primarily the result of an increase in fees for legal, accounting and audit services of \$2.5 million primarily due to the investigation of our historical stock option practices, as well as an increase in bonus expense of \$725,000 as targets under our fiscal 2007 bonus plans were achieved, and an increase in salary expense of \$500,000 due to headcount growth of 5 employees.

*Acquired In-process Research and Development.* In September 2005, we completed the acquisition of FS2, a design services and development tools company, for cash consideration. The fair value of the in-process technology was determined by estimating the present value of the net cash flows we believed would result from the acquired technology. Because technological feasibility of certain of the acquired technology had not been established and no future alternative use for the in-process technology existed at the time of the acquisition, we recorded a charge in the first quarter of fiscal 2006 of \$570,000 for the acquired in-process research and development expense upon completion of the acquisition.

*Other Income, Net.* Other income, net, for the third quarter of fiscal 2007 was \$1.8 million and for the first nine months of fiscal 2007 was \$4.8 million compared to \$1.1 million and \$3.0 million for the comparable periods in fiscal 2006. The increase in other income was primarily due to an increase in interest and investment income.

#### *Income Taxes.*

We recorded an income tax provision of \$708,000 for the three-month period ended March 31, 2007 and \$837,000 for the comparable period in fiscal 2006. For the nine-month period ended March 31, 2007, we recorded an income tax provision of \$3.7 million and \$980,000 for the comparable period in fiscal 2006.

Our estimated annual effective income tax rate of 38% for fiscal 2007 primarily consists of US federal and state taxes and foreign taxes on income earned in certain foreign jurisdictions and withholding taxes, offset in part by the availability of certain foreign tax credits and general business tax credits. The actual tax rate of 36% for the three-month period ended March 31, 2007 and 37% for the nine-month period ended March 31, 2007 differs from the estimated annual effective tax rate of 38% due to discrete items recorded during the periods for non-deductible acquisition costs related to our acquisition of First Silicon Solutions. The estimated annual effective income tax rate of 22%, before discrete items, recorded for the three and nine-month periods ended March 31, 2006 is lower than the applicable statutory rate primarily due to the availability of foreign tax credits and general business tax credit carryovers from prior years.

The amount of income taxes we pay is subject to ongoing audits by federal, state and foreign tax authorities, which often result in proposed assessments. Our future results may include favorable or unfavorable adjustments to our estimated tax liabilities in the period the assessments are made or resolved or when statutes of limitation on potential assessments expire. As a result, our effective tax rate may fluctuate significantly on a quarterly basis.

#### **Financial Condition**

At March 31, 2007, we had cash, cash equivalents and short-term investments of \$136.3 million and total working capital of \$128.2 million. Our principal requirements for cash are to fund working capital needs, and, to a lesser extent, capital expenditures for equipment purchases, licensing of computer-aided design tools used in our development activities and acquisition of technologies and patents. The following table summarizes selected items (in thousands) from our statement of cash flows for the nine months ended March 31, 2007 and 2006. For complete statements of cash flows for those periods, see the financial statements in Item 1.

	Nine Months Ended March 31,	
	2007	2006 (As Restated) (1)
<b>Net cash provided by operating activities</b>	<b>\$ 17,719</b>	<b>\$ 6,686</b>
Net income	6,148	3,546
Depreciation	1,596	1,189
Stock-based compensation	6,081	6,662
Acquired in-process research and development	—	570
Amortization of intangibles	1,020	921
Accounts receivable	(1,379)	(2,202)
Other assets	(2,483)	(1,283)
Other current accrued liabilities	2,183	(225)
Income tax payable	1,528	548
Accrued compensation	1,406	(1,281)
Long-term liabilities	2,083	560
<b>Net cash used in investing activities</b>	<b>\$ (26,046)</b>	<b>\$ (5,682)</b>
Net maturities (purchases) of short-term investments	(22,190)	685
Capital expenditures	(3,856)	(1,642)
Acquisition of FS2, net of cash acquired	—	(3,557)
Restricted cash	—	(668)
Investment in private company	—	(500)
<b>Net cash provided by financing activities</b>	<b>\$ 386</b>	<b>\$ 4,504</b>
Net proceeds from issuance of common stock	386	4,504
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>\$ (7,896)</b>	<b>\$ 5,446</b>

(1) See Note 2, “Restatement of Condensed Consolidated Financial Statements,” in Notes to Condensed Consolidated Financial Statements—Unaudited.

For the nine-month period ended March 31, 2007, our operating activities provided net cash of \$17.7 million primarily reflecting our net income and non-cash charges including stock-based compensation under SFAS No. 123R, depreciation expense and amortization of intangibles and deferred compensation. Reported cash flow was provided by increases in long-term liabilities due to a \$2.1 million accrual for extended payment terms on a Computer Aided Design Time-Based License (“CAD TBL”), as well as an increase in accrued compensation primarily due to accruals under our bonus plans, and an increase in other current accrued liabilities due to higher accruals of legal and accounting fees and higher accruals for CAD TBLs and maintenance contracts. In addition, cash flow was provided by an increase in taxes payable due to our provision. The net cash provided by these sources was partially offset by an increase in other assets relating primarily to a \$3.1 million purchase of a CAD TBL and an increase in accounts receivable due to new license agreements signed near the end of the quarter.

For the nine-month period ended March 31, 2006, our operating activities provided net cash of \$6.7 million primarily reflecting our net income and adjustments for in-process research and development charges related to the FS2 acquisition and by non-cash charges including stock-based compensation under SFAS No. 123R, depreciation expense and amortization of intangibles. In addition, cash was generated by an increase in income taxes payable due to tax provisions for the period. The net cash provided by these sources was partially offset by an increase in accounts receivable due to new license agreements signed near the end of the quarter, an increase in other assets primarily due to prepaid royalties of \$700,000 and an increase in the cash surrender value on life insurance policies of \$631,000, and a decrease in accrued compensation which included \$1.0 million in executive bonus payments from our prior fiscal year,

Net cash used in investing activities was \$26.0 million for the nine months ended March 31, 2007, which included net purchases of short-term investments and purchases of equipment and computer-aided design tools used in our development activities. This compared to net cash used in investing activities of \$5.7 million for the nine months ended March 31, 2006 which included cash used for the acquisition of FS2 of \$3.6 million, \$668,000 for the establishment of an escrow account related to the acquisition, and an investment of \$500,000 in a private company, along with purchases of equipment and computer-aided design tools used in our development activities offset slightly by net maturities of short-term investments.

Net cash provided by financing activities was \$386,000 for the nine months ended March 31, 2007 compared to net cash provided of \$4.5 million for the comparable period in the prior year. Net cash provided by financing activities during the nine-month period ended March 31, 2007 and March 31, 2006 was primarily attributable to purchases under our employee stock plans.

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

- the cost, timing and success of product development efforts;
- the level and timing of contract revenues and royalties;
- the cost of maintaining and enforcing patent claims and other intellectual property rights and other litigation;
- level and timing of restructuring activities; and
- whether cash would be used to complete any acquisitions.

We believe that we have sufficient cash 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 have a material adverse effect on our business, results of operations and financial condition.

## Contractual Obligations

Our contractual obligations as of March 31, 2007 were as follows:

### **Payments due by period (in thousands)**

	<u>Total</u>	<u>Less than 1 year</u>	<u>1-3 years</u>	<u>3-5 years</u>	<u>More than 5 years</u>
Operating lease obligations (1)	\$ 4,279	\$ 1,759	\$ 2,162	\$ 318	\$ 40
Purchase obligations (2)	7,436	5,353	2,083	—	—
Other long-term liabilities reflected on our balance sheet (3)	2,123	—	2,123	—	—
<b>Total</b>	<b><u>\$13,838</u></b>	<b><u>\$ 7,112</u></b>	<b><u>\$ 6,368</u></b>	<b><u>\$ 318</u></b>	<b><u>\$ 40</u></b>

- (1) We lease office facilities under noncancelable operating leases that expire through 2009. In connection with a lease, we have entered into a letter of credit as a security deposit with a financial institution for \$264,000, which is guaranteed by a time-based certificate of deposit.

- (2) These are primarily outstanding purchase orders for ongoing operations. Payments of these obligations are subject to the provision of services or products. Purchase obligations have increased by approximately \$3.7 million since June 30, 2006 primarily due to the purchase of a CAD TBL in August 2006.
- (3) Long-term liability to employees under a deferred compensation plan. The employees elect distributions under this plan.

#### **Critical Accounting Policies and Estimates**

We prepare our financial statements in conformity with U.S. generally accepted accounting principles, which require us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. We regularly evaluate our accounting estimates and assumptions. We base our estimates and assumptions on historical experience and on various other factors that we believe 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. Actual results inevitably will differ from the estimates, and such differences may require material adjustments to our financial statements. We believe there have been no significant changes to the items that we disclosed as our critical accounting policies and estimates in our discussion and analysis of financial condition and results of operations in our 2006 Form 10-K.

#### **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, municipal bonds, 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 outside the United States. 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.

#### **ITEM 4. CONTROLS AND PROCEDURES**

Our chief executive officer and our chief financial officer have concluded, based on the evaluation of the effectiveness of our disclosure controls and procedures by our management, with the participation of our chief executive officer and our chief financial officer, as of the end of the period covered by this report, that our disclosure controls and procedures (as such term is defined under Rule 12a-15(e) under the Exchange Act) were not effective as of March 31, 2007, because of the material weaknesses described in Part II, Item 9A, in our 2006 Annual Report on Form 10-K. In that section, we describe two material weaknesses in our internal control over financial reporting as a result of errors found during the preparation of the restated financial statements with regards to the process of accounting for a complex non-routine transaction and the process of accounting for income taxes. Specifically, we lacked adequate controls to ensure that the assumptions used in the determination of the fair value calculation were properly determined on options that were the subject of a settlement with former employees in Denmark during the first quarter of fiscal 2006. Second, we lacked adequate controls relating to the oversight and review of tax provision, including a timely lack of reconciliation of certain tax accounts and review of those reconciliations for income tax expense and deferred tax assets and liabilities.

We have an on-going process of analyzing and improving our internal controls, including those related to the material weaknesses identified by management. We expect to develop and implement a plan to remediate the material weaknesses described above. With regard to the process of accounting for a complex non-routine transaction, our remediation plan is expected to include enhancing our internal controls to provide additional oversight and review of the accounting for complex non-routine transactions, including consultations with experts in a timely manner and documentation of the process followed for transactions in adherence to the policy. With regard to the process of accounting for income taxes, our remediation plan is expected to include: (a) consideration and implementation of additional review of tax provision and reconciliations by qualified personnel experienced in application of tax rules and regulations and accounting for income taxes; and (b) consultation with tax experts in a timely manner. During the second quarter of fiscal 2007, we hired a tax manager to increase our staffing level to support our review and reconciliation of tax provision calculation.

There were no changes in our internal control over the financial reporting that occurred during the third quarter of fiscal 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

Three actions seeking to assert derivative claims on behalf of MIPS have been filed in the United States District Court for the Northern District of California. The shareholder-plaintiffs in each of these actions seek to assert claims against current and former officers and directors related to our historic stock option grant practices. Each action alleges that the individual defendants breached their fiduciary duties and violated federal securities laws as a result of backdating stock option grants, insider trading and the dissemination of false financial statements. Each action asserts that the individual defendants' conduct injured MIPS and gives rise to numerous causes of action on behalf of MIPS under the federal securities laws and state law. Plaintiffs seek to recover, on behalf of MIPS, monetary damages, various equitable remedies, attorneys' fees and costs. The individual actions are:

- *Steger v. Bourgoin, et. al.*, No. C-06-06699, filed on October 27, 2006, and brought against John Bourgoin, Jack Browne, Kenneth L. Coleman, Sandy Creighton, Kevin C. Eichler, Fred M. Gibbons, Anthony B. Holbrook, William M. Kelly, Lavi Lev, and Derek Meyer as individual defendants and MIPS as nominal defendant;
- *Carco v. Holbrook, et. al.*, No. C-07-0661, filed on February 1, 2007, and brought against Anthony B. Holbrook, John E. Bourgoin, Mervin S. Kato, Kate Hunt Rundle, Brad Holtzinger, Mark Tyndall, Jack Browne, Sandy Creighton, Kevin C. Eichler, G. Michael Uhler, Robert R. Herb, Fred M. Gibbons, Benjamin A. Horowitz, Kenneth L. Coleman and William M. Kelly as individual defendants and MIPS as nominal defendant; and
- *Michaels v. Bourgoin, et. al.*, No. C-07-0771, filed on February 6, 2007, and brought against John E. Bourgoin, Sandy Creighton, Kevin C. Eichler, Lavi Lev, Derek Meyer, Kenneth L. Coleman, Fred M. Gibbons, Anthony B. Holbrook and William M. Kelly as individual defendants and MIPS as nominal defendant.

By order of the court dated April 12, 2007, the three actions were consolidated into a single action entitled *In re MIPS Technologies, Inc. Derivative Litigation*. Pursuant to the court's order, a consolidated complaint was due by May 29, 2007 and discovery in the consolidated action was stayed pending resolution of a motion to dismiss the consolidated complaint due to plaintiffs' lack of standing to sue on MIPS' behalf. On June 6, 2007, the parties jointly submitted to the court a stipulation and proposed order extending the time for lead plaintiff to file a consolidated complaint until July 16, 2007. It is not known when or on what basis these matters will be resolved.

On December 1, 2006, MIPS Technologies, Inc. filed a lawsuit in the United States District Court for the Northern District of California against Trident Microsystems, Inc. asserting patent and trademark infringement and unfair competition. This action sought various forms of relief including a permanent injunction from further infringement of the company's intellectual property, compensatory and enhanced damages, and attorneys' fees. In early April 2007, the parties entered into an agreement that settled the lawsuit and filed documentation with the Court stipulating to its dismissal. On April 9, 2007, we issued a press release reporting that the parties had reached agreement on the lawsuit, that the suit had been dismissed, and that Trident Microsystems had licensed the MIPS32 24KEc Pro Core.

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.

## ITEM 1A. RISK FACTORS

*Our success is subject to numerous risks and uncertainties, including those discussed below. These factors could hinder our growth, cause us to sustain losses or have other adverse effects on us, all of which could cause our stock price to decline.*

**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. Therefore, we believe that quarter-to-quarter comparisons of our revenue and operating results may not be a good indication of our future performance. It is possible that in some future periods our results of operations may be below the expectations of securities analysts and investors. In that event, the price of our common stock may fall.

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

- our ability to identify attractive licensing opportunities and then enter into new licensing agreements on terms that are acceptable to us;
- our ability to successfully conclude licensing agreements of any significant value in a given quarter;
- the financial terms and delivery schedules of our contractual arrangements with our licensees, which may provide for significant up-front payments, payments based on the achievement of certain milestones or extended payment terms;
- the demand for products that incorporate our technology;
- our ability to develop, introduce and market new processor intellectual property;
- the establishment or loss of licensing relationships with semiconductor companies or digital consumer and 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 semiconductor companies and digital consumer and business product manufacturers; and
- uncertain economic and market conditions.

**The success of our business depends on maintaining and growing our contract revenue.** Contract revenue consists of technology license fees paid for access to our developed technology and engineering service fees related to technology under development. Our ability to secure the licenses from which our contract revenues are derived depends on our customers, including semiconductor companies, digital consumer and business product manufacturers, adopting our technology and using it in the products they sell. Our contract revenue increased by 5% in fiscal 2004 and increased 28% in fiscal 2005, but declined 12% in fiscal 2006. While we expect that we will continue to grant additional licenses to new licensees and develop new products to license to both new and existing licensees, we cannot predict whether we can maintain our current contract revenue levels or if contract revenue will grow. Our licensees are not obligated to license new or future generations of our products, so past contract revenue may not be indicative of the amount of such revenue in any future period. If we cannot maintain or grow our contract revenue or if our customers do not adopt our technology and obtain corresponding licenses, our results of operations will be adversely affected.

**Our ability to achieve design wins may be limited unless we are able to develop enhancements and new generations of our intellectual property.** Our future success will depend, in part, 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, core and related designs are not compatible

with the requirements of specific product applications, our ability to achieve design wins may be limited. Our failure to achieve a significant number of design wins would 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, or 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 in a potential product 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 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 sufficient to cover or in excess of the costs of development.

**We depend on royalties from the sale of products incorporating our technology, and we have limited visibility as to the timing and amount of such sales.** Our receipt of royalties from our licenses depends on our customers incorporating our technology into their products, their bringing these products to market, and the success of these products. In the case of our semiconductor customers, the amount of such sales is further dependent upon the sale of the products by their customers into which our customers' products are incorporated. Thus, our ability to achieve design wins and enter into licensing agreements does not assure us of future revenue. Any royalties that we are eligible to receive are based on the sales of products incorporating the semiconductors or other products of our licensees, and as a result we do not have direct access to information that will help us anticipate the timing and amount of future royalties. Factors that negatively affect our licensees and their customers could adversely affect our business. The success of our direct and indirect customers is subject to a number of factors, including:

- the competition these companies face and the market acceptance of their products;
- the engineering, marketing and management capabilities of these companies and technical challenges unrelated to our technology that they face in developing their products; and
- their financial and other resources.

Because we do not control the business practices of our licensees and their customers, we have little influence on the degree to which our licensees promote our technology and do not set the prices at which products incorporating our technology are sold.

We rely on our customers to correctly report to us the number or dollar value of products incorporating our technology that they have sold, as these sales are the basis for the royalty payments that they make to us. We have the right under our licensing agreements to perform a royalty audit of the customer's sales so that we can verify the accuracy of their reporting, and if we determine that there has been an over-reported or under-reported amount of royalty, we account for the results when they are identified. By way of an example, we determined in the second quarter of fiscal 2005, as a result of an audit, that one of our customers had inadvertently reported a higher level of royalty than had actually occurred, and we accrued for this event as an offset against revenue in the quarter.

**If we do not compete effectively in the market for embedded processors, our business will be adversely affected.** Competition in the market for embedded processors is intense. Our products compete with those of other designers and developers of processors and cores, as well as those of 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 other technology designs. The market for embedded processors has recently faced

downward pricing pressures on products. We cannot assure you that we will be able to compete successfully or that competitive pressure will not materially and adversely affect our business, results of operations and financial condition.

In order to be successful in marketing our products to semiconductor companies, we must differentiate our processors, cores and related designs from those available or under development by the internal design groups of these companies, including some of our current and prospective licensees. Many of these internal design groups have substantial engineering and design resources and are part of larger organizations with substantial financial and marketing resources. These internal design groups may develop products that compete with ours.

Some 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 encounter difficulties with future acquisitions, which could harm our business.** As part of our business strategy, in the future we may seek to acquire or invest in businesses or technologies that we believe can complement or expand our business, enhance our technical capabilities or that may otherwise offer growth opportunities. Any future acquisitions may require debt or equity financing, or the issuance of shares in the transaction, any of which could increase our leverage or be dilutive to our existing stockholders. We may not be able to complete acquisitions or strategic customer transactions on terms that are acceptable to us, or at all. We may incur charges related to acquisitions or investments that are completed. For instance, we recorded an in-process research and development charge in the first quarter of fiscal 2006 as a result of our acquisition of First Silicon Solutions, Inc. We will also face challenges integrating acquired businesses and operations and assimilating and managing the personnel of the acquired operations. Geographic distances may further complicate the difficulties of this integration. The integration of acquired businesses, an area in which we have limited experience, may not be successful and could result in disruption to other parts of our business. Acquisitions involve a number of other risks and challenges, including:

- diversion of management's attention;
- potential loss of key employees and customers of the acquired companies;
- exposure to unanticipated contingent liabilities of acquired companies; and
- use of substantial portions of our available cash to consummate the acquisition and/or operate the acquired business.

Any of these and other factors could harm our ability to realize the anticipated benefits of an acquisition.

**We depend on our key personnel to succeed.** Our 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 cannot assure that we will retain our key officers and employees. Competition for qualified personnel, particularly those with significant experience in the semiconductor and processor design industries, remains 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 make it difficult to meet key objectives, such as timely and effective project milestones and product introductions which could adversely affect our business, results of operations and financial condition.

**Changes in effective tax rates or adverse outcomes from examination of our income tax returns could adversely affect our results.** Our future effective tax rates could be adversely affected by earnings being lower than anticipated in countries with low statutory tax rates, by changes in the valuation of our deferred tax assets and liabilities, or by changes in tax laws or the interpretation of tax laws. In addition, the Internal Revenue Service has completed its examination of our federal income tax return for fiscal year 2002 and has issued a notice of proposed adjustment. A settlement was reached in May 2006 in which adequate amounts had been provided in prior periods. The assessment was recorded in the fourth fiscal quarter of 2006. We operate in countries other than the United States and occasionally face inquiries and examinations regarding tax matters in these countries. There can be no assurance that the outcomes from our current examination or any other examinations will not have an adverse effect on our operating results and financial condition.

**We may be subject to litigation and other legal claims that could adversely affect our financial results.** From time to time, we are subject to litigation and other legal claims incidental to our business. In addition, it is standard practice for

us to include some form of indemnification of our licensees in our core and architecture license agreements, and from time to time we are engaged in claims by our licensees with respect to these obligations. It is possible that we could suffer unfavorable outcomes from litigation or other legal claims, including those made with respect to indemnification obligations, that are currently pending or that may arise in the future. Any such unfavorable outcome could materially adversely affect our financial condition or results of operations.

**We may be subject to claims of infringement.** We cannot assure you that any of the patents or other intellectual property rights that we own or use 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. As we grow our business and expand into new markets that other companies are developing in, the risk that our technology may infringe upon the intellectual property rights of others increases. We cannot be certain that third parties will not make a claim of infringement against us, our licensees, or our licensees' customers in connection with use of our technology. For example, Technology Properties Limited, Inc. filed a lawsuit in November 2005 against some of our licensees based upon the alleged infringement of certain microprocessor-related patents. 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 on acceptable terms to us 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.

**Our intellectual property may be misappropriated or expire, and we may be unable to obtain or enforce intellectual property rights.** 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. As part of our business strategy, we license our technology in multiple geographies including in countries whose laws do not provide as much protection for our intellectual property as the laws of the United States and where we may not be able to enforce our rights. In addition, intellectual property rights which we have obtained in particular geographies may expire from time to time. As a result, we cannot be certain that we will be able to prevent other parties from designing and marketing unauthorized MIPS compatible products, that others will not independently develop or otherwise acquire the same or substantially equivalent technologies as ours, or that others will not use information contained in our expired patents to successfully compete against us. 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 also cannot assure you that any of our patent applications to protect our intellectual property will be approved, and patents that have issued do expire over time. Recent judicial decisions and proposed legislation in the U.S. may increase the cost of obtaining patents, limit the ability to adequately protect our proprietary technology, and have a negative impact on the enforceability of our patents. In addition, effective trade secret protection may be unavailable or limited in certain countries. If we are unable to protect, maintain or enforce our intellectual property rights, our technology may be used without the payment of license fees and royalties, which could weaken our competitive position, reduce our operating results and increase the likelihood of costly litigation.

**We have recorded long-lived assets, and our results of operations would be adversely affected if their value becomes impaired.** In the first quarter of fiscal 2006, we acquired certain core and developed technologies and customer relationships and a tradename, and the purchase price of these long-lived assets is being amortized over schedules based on their useful lives. If we complete additional acquisitions in the future, our purchased intangible assets amortization charge could increase, and we may be required to record substantial amounts of goodwill. We evaluate our long-lived assets, including purchased assets, for impairment on an annual basis or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable from its estimated future cash flows.

In the future, if we determine that our long-lived assets are impaired, we will have to recognize additional charges for this impairment. We cannot be sure that we will not be required to record additional long-lived asset impairment charges in the future.

**The matters relating to the investigation by the Special Committee of the Board of Directors and the restatement of our consolidated financial statements may result in additional litigation and government enforcement actions.** On August 30, 2006, we announced that our board of directors had formed a Special Committee consisting of independent directors and the Special Committee had hired independent counsel to conduct a full investigation of our historical option grant practices from the time of our initial public offering in July 1998 through June 2006. As described in Item 7, "Management's

Discussion and Analysis of Financial Condition and Results of Operations” and in Note 3, “Restatement of Consolidated Financial Statements” in Notes to Consolidated Financial Statements in our 2006 Annual Report on Form 10-K, as a result of the independent investigation, as well as our internal review, our management has concluded, and the Audit and Corporate Governance Committee of the Board of Directors agrees, that incorrect measurement dates were used for financial accounting purposes for certain stock option grants made in prior periods. As a result, we have recorded net additional non-cash stock-based compensation expense and related tax effects with regard to certain past stock option grants, and we have restated certain previously filed financial statements.

The Special Committee investigation, our internal review, and related activities have resulted in our incurring substantial expenses for legal, accounting, tax and other professional services.

While our management believes that we have made appropriate judgments in determining the correct measurement dates for the stock option grants, the Securities and Exchange Commission (“SEC”) may disagree with the manner in which we have accounted for and reported, or not reported, the financial impact of past incorrect measurement dates. Accordingly, there is a risk that we may have to further restate our prior financial statements, amend prior filings with the SEC, or otherwise take other actions not currently contemplated.

As described in Part I, Item 3, “Legal Proceedings”, derivative complaints have been filed in federal courts against current and former officers and directors pertaining to allegations relating to stock option grants. Additional litigation based on similar allegations may also be filed. We have provided the results of our independent investigation to the SEC and we have responded to informal requests for documents and additional information. We intend to continue to provide the SEC with our full cooperation. No assurance can be given regarding the outcomes from litigation, regulatory proceedings or government enforcement actions relating to our past stock option practices. The resolution of these matters will be time consuming, expensive, and will distract our management from the conduct our business. Furthermore, if we are subject to adverse findings in litigation, regulatory proceedings or government enforcement actions, we could be required to pay damages or penalties or have other remedies imposed, which could harm our results of operations and financial condition.

Since September 2006, we have received several Nasdaq Staff Determination notices stating that the we were not in compliance with the requirements for continued listing due to the delayed filings of our SEC reports. With the filing of our 2006 Annual Report on Form 10-K for the fiscal year ended June 30, 2006 and the concurrent filing of our Quarterly Reports on Form 10-Q for the quarters ended September 30, 2006, December 31, 2006 and March 31, 2007, we believe that we have remedied our non-compliance, subject to Nasdaq’s affirmative completion of our compliance protocols and its notification to us accordingly. However, if the SEC disagrees with the manner in which we have accounted for and reported, or not reported, the financial impact of past stock option grants, there could be further delays in filing our subsequent SEC reports that might result in delisting of our common stock from the Nasdaq Global Market.

## **ITEM 6. EXHIBITS**

### (a) Exhibits

- 31.1 [Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 31.2 [Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 32.1 [Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \\*](#)
- 32.2 [Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \\*](#)

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\* As contemplated by SEC Release No. 33-8212, these exhibits are furnished with this Quarterly Report on Form 10-Q and are not deemed filed with the Securities and Exchange commission and are not incorporated by reference in any filing of MIPS Technologies, Inc. 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 in any such filings.

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



## FORM 10-Q CERTIFICATION

I, John E. Bourgoïn, certify that:

1. I have reviewed this quarterly report on Form 10-Q of MIPS Technologies, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15d-15(f)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under such supervision, 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;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusion about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's third fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: June 28, 2007

By: /s/ JOHN E. BOURGOIN

*John E. Bourgoïn*  
*President and Chief Executive Officer,*  
*MIPS Technologies, Inc.*

## FORM 10-Q CERTIFICATION

I, Mervin S. Kato, certify that:

1. I have reviewed this quarterly report on Form 10-Q of MIPS Technologies, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15d-15(f)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under such supervision, 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;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusion about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's third fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: June 28, 2007

By: /s/ MERVIN S. KATO

*Mervin S. Kato*

*Vice President and Chief Financial Officer,  
MIPS Technologies, Inc.*

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, John E. Bourgoïn, certify, that to my knowledge, the Quarterly Report on Form 10-Q of MIPS Technologies, Inc. for the three months ended March 31, 2007 (the "*Form 10-Q*"), to which this certificate is an exhibit fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934, as amended, and that information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of MIPS Technologies, Inc. for the three month period covered by the Form 10-Q.

Date: June 28, 2007

By: /s/ JOHN E. BOURGOIN

*John E. Bourgoïn*  
*President and Chief Executive Officer,*  
*MIPS Technologies, Inc.*

A signed original of this written statement required by Section 906 has been provided by MIPS Technologies and will be retained by it and furnished to the Securities Exchange Commission or its staff upon request.

**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, Mervin S. Kato, certify, that to my knowledge, the Quarterly Report on Form 10-Q of MIPS Technologies, Inc. for the three months ended March 31, 2007 (the "*Form 10-Q*"), to which this certificate is an exhibit fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934, as amended, and that information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of MIPS Technologies, Inc. for the three month period covered by the Form 10-Q.

Date: June 28, 2007

By: /s/ MERVIN S. KATO

*Mervin S. Kato*

*Vice President and Chief Financial Officer,  
MIPS Technologies, Inc*

A signed original of this written statement required by Section 906 has been provided by MIPS Technologies and will be retained by it and furnished to the Securities Exchange Commission or its staff upon request.