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

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**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 April 3, 2005**

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: **000-22671**

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**QUICKLOGIC CORPORATION**

(Exact name of registrant as specified in its charter)

**DELAWARE**  
(State or other jurisdiction of  
incorporation or organization)

**77-0188504**  
(I.R.S. Employer Identification No.)

**1277 ORLEANS DRIVE SUNNYVALE, CA 94089**  
(Address of principal executive offices, including Zip Code)

**(408) 990-4000**  
(Registrant's telephone number, including area code)

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

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

As of May 5, 2005, 26,460,042 shares of the registrant's common stock were outstanding.

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**QUICKLOGIC CORPORATION  
FORM 10-Q  
MARCH 31, 2005**

**Part I. Financial Information**

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**PART I. Financial Information****Item 1. Financial Statements**

**QUICKLOGIC CORPORATION**  
**CONDENSED UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per share amounts)

	Three Months Ended March 31,	
	2005	2004
Revenue	\$ 12,527	\$ 10,368
Cost of revenue	4,888	4,555
Gross profit	7,639	5,813
Operating expenses:		
Research and development	2,454	3,248
Selling, general and administrative	4,298	3,909
Income (loss) from operations	887	(1,344)
Interest expense	(53)	(68)
Interest income and other, net	80	44
Income (loss) before income taxes	914	(1,368)
Provision for income taxes	50	—
Net income (loss)	\$ 864	\$ (1,368)
Net income (loss) per share:		
Basic	\$ 0.03	\$ (0.06)
Diluted	\$ 0.03	\$ (0.06)
Weighted average shares:		
Basic	26,385	24,846
Diluted	27,413	24,846

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

**QUICKLOGIC CORPORATION**  
**CONDENSED UNAUDITED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except par value amount)

	March 31, 2005	December 31, 2004
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 24,598	\$ 24,914
Short-term investment in Tower Semiconductor Ltd.	1,628	2,022
Accounts receivable, net of allowances for doubtful accounts of \$948 and \$1,088	5,859	4,786
Inventory	7,476	6,741
Other current assets	1,250	1,506
Total current assets	40,811	39,969
Property and equipment, net	5,138	5,403
Investment in Tower Semiconductor Ltd.	819	1,017
Other assets	4,458	4,552
<b>TOTAL ASSETS</b>	<b>\$ 51,226</b>	<b>\$ 50,941</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		

Trade payables	\$ 2,900	\$ 2,009
Accrued liabilities	2,534	2,511
Deferred income on shipments to distributors	1,813	1,667
Current portion of debt and capital lease obligations	1,853	2,286
Total current liabilities	<u>12,579</u>	<u>12,583</u>
Long-term liabilities:		
Debt and capital lease obligations, less current portion	697	1,036
Deferred royalty revenue	1,231	1,156
Total long-term liabilities	<u>1,928</u>	<u>2,192</u>
Total liabilities	<u>14,507</u>	<u>14,775</u>
Commitments and contingencies (see notes 10 and 11)		
Stockholders' equity:		
Common stock, \$0.001 par value; 100,000 shares authorized; 26,444 and 26,313 shares issued and outstanding, respectively	26	26
Additional paid-in capital	156,118	155,837
Accumulated other comprehensive loss	(592)	—
Accumulated deficit	(118,833)	(119,697)
Total stockholders' equity	<u>36,719</u>	<u>36,166</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 51,226</u>	<u>\$ 50,941</u>

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

**QUICKLOGIC CORPORATION**  
**CONDENSED UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	<u>Three Months Ended March 31,</u>	
	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Net income (loss)	\$ 864	\$ (1,368)
Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:		
Depreciation and amortization	665	1,163
Loss on disposal of property and equipment	7	20
Utilization of wafer credits from Tower Semiconductor Ltd.	94	52
Inventory write-down	205	130
Changes in assets and liabilities:		
Accounts receivable, net of allowances for doubtful accounts	(1,073)	(503)
Inventory	(940)	(883)
Other assets	256	381
Trade payables	260	69
Accrued liabilities	23	54
Deferred income and royalty revenue	221	519
Net cash provided by (used for) operating activities	<u>582</u>	<u>(366)</u>
Cash flows from investing activities:		
Capital expenditures for property and equipment	(407)	(415)
Net cash used for investing activities	<u>(407)</u>	<u>(415)</u>
Cash flows from financing activities:		
Payment of debt and capital lease obligations	(772)	(697)
Proceeds from issuance of common stock, net	281	106
Net cash used for financing activities	<u>(491)</u>	<u>(591)</u>
Net decrease in cash and cash equivalents	(316)	(1,372)
Cash and cash equivalents at beginning of period	24,914	26,443
Cash and cash equivalents at end of period	<u>\$ 24,598</u>	<u>\$ 25,071</u>
Supplemental schedule of non-cash activities:		
Capital lease obligation to finance capital expenditures and related maintenance	\$ —	\$ 1,482

**QUICKLOGIC CORPORATION**  
**CONDENSED UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(In thousands)

	Three Months Ended March 31,	
	2005	2004
Net income (loss)	\$ 864	\$ (1,368)
Other comprehensive gain (loss), net of tax:		
Unrealized gain (loss) on investments	(592)	3,688
Total comprehensive income	<u>\$ 272</u>	<u>\$ 2,320</u>

See accompanying Notes to Condensed Unaudited Consolidated Financial Statements.

**QUICKLOGIC CORPORATION**  
**NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1—The Company and Basis of Presentation**

QuickLogic Corporation (“QuickLogic” or the “Company”), founded in 1988, is a Delaware corporation. The Company operates in a single industry segment where it designs, develops, markets and supports advanced field programmable gate arrays (“FPGAs”), Embedded Standard Products (“ESPs”), associated software tools and programming hardware.

The accompanying interim financial statements are unaudited. In the opinion of management, these statements have been prepared in accordance with generally accepted accounting principles and include all adjustments, consisting only of normal recurring adjustments, necessary for the fair presentation of the results of the interim periods. The Company recommends that these financial statements be read in conjunction with the Company’s Form 10-K for the year ended December 31, 2004. Operating results for the three months ended March 31, 2005 are not necessarily indicative of the results that may be expected for the full year.

QuickLogic’s fiscal year ends on the Sunday closest to December 31. QuickLogic’s first fiscal quarter of 2005 ended Sunday, April 3, 2005. For presentation purposes, the financial statements and notes have been presented as ending on the last day of the nearest calendar month.

*Liquidity*

The Company anticipates that its existing cash resources will fund any operating losses, finance purchases of capital equipment and provide adequate working capital for the next twelve months. The Company’s liquidity is affected by many factors including, among others, the level of revenue and gross profit, market acceptance of existing and new products including Eclipse II and QuickPCI II parts, the expected decline in pASIC1 and pASIC2 revenue resulting from the end-of-life of these products, costs of securing access to adequate manufacturing capacity, inventory levels, wafer purchase commitments, customer credit terms, the amount and timing of research and development expenditures, the timing of new product introductions, production volumes, sales and marketing efforts, changes in operating assets and liabilities, the ability to obtain or renew debt financing and to remain in compliance with the terms of our credit facilities, the ability to raise funds from the sale of shares of Tower Semiconductor Ltd. (“Tower”) and equity in the Company, the exercise of employee stock options and participation in the Company’s employee stock purchase plan, and other factors related to the uncertainties of the industry and global economics. Accordingly, there can be no assurance that events in the future will not require the Company to seek additional capital or, if so required, that such capital will be available on terms acceptable to the Company.

*Principles of Consolidation*

The consolidated financial statements include the accounts of QuickLogic Corporation and its wholly owned subsidiaries, QuickLogic International, Inc., QuickLogic Canada Company, QuickLogic Kabushiki Kaisha, QuickLogic Software (India) Private Ltd., and QuickLogic GmbH. The Company uses the U.S. dollar as its functional currency. All significant intercompany accounts and transactions are eliminated in consolidation.

*Uses of Estimates*

The preparation of these financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosures of contingent assets and liabilities, and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates, particularly in relation to revenue recognition, the allowance for doubtful accounts, sales returns, valuation of investments, valuation of long-lived assets, inventory valuation including excess quantities and obsolescence, accounting for income taxes and estimating accrued

liabilities.

## Note 2—Significant Accounting Policies

### Revenue Recognition

The Company generally recognizes revenue as products are shipped if evidence of an arrangement exists, delivery has occurred, services, if any, have been rendered, the sales price is fixed or determinable, collection of the resulting receivable is reasonably assured, and product returns are reasonably estimable.

The Company sells products directly to original equipment manufacturers (“OEMs”) and through distributors. The

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## QUICKLOGIC CORPORATION

### NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Company ships programmed parts and unprogrammed parts. Distributors, third parties or the end customer may program unprogrammed parts. Revenue is recognized upon shipment to OEM customers. The Company sells to certain distributors under agreements, which, in the case of unprogrammed parts, provide for certain rights of return, and price adjustments on unsold inventory. These agreements generally permit the distributor to return unprogrammed parts with a value of up to 10% of the value of the total product purchases in the previous six months. Upon shipment of unprogrammed parts to a distributor, the Company records an account receivable from the distributor, relieves inventory by the cost of the product shipped, and records the deferred gross profit (revenue less cost of revenue) on the balance sheets as “deferred income on shipments to distributors” until the inventory is resold by the distributor. Revenue for programmed parts, for which there are no rights of return or price adjustments on unsold inventory, is recognized upon shipment to distributors. Reserves for estimated returns and allowances are provided against accounts receivable.

Software revenue from sales of design tool kits is recognized when persuasive evidence of an agreement exists, delivery of the software has occurred, no significant Company obligations with regard to implementation or integration remain, the fee is fixed or determinable and collection is probable. Software revenue amounts to less than 1% of revenue.

### Long-lived Assets

The Company reviews the recoverability of its long-lived assets, such as property and equipment and investments, annually and when events or changes in circumstances occur that indicate that the carrying value of the asset or asset group may not be recoverable. The assessment of possible impairment is based on the Company’s ability to recover the carrying value of the asset or asset group from the expected future pre-tax cash flows, undiscounted and without interest charges, of the related operations. If these cash flows are less than the carrying value of such asset, an impairment loss is recognized for the difference between estimated fair value and carrying value. The measurement of impairment requires management to estimate future cash flows and the fair value of long-lived assets.

### Comprehensive Income (Loss)

Comprehensive income (loss) includes all changes in equity (net assets) during a period from non-owner sources. Comprehensive income (loss) for the Company has included realized and unrealized holding gains or losses on Tower ordinary shares (see Note 4).

### Stock-Based Compensation

The Company has elected to measure employees’ stock-based compensation costs using the intrinsic value method prescribed by the Accounting Principles Board (“APB”) Opinion No. 25, “Accounting for Stock Issued to Employees” and to comply with the pro forma disclosure requirements of Statement of Financial Accounting Standards (“SFAS”) No. 123, “Accounting for Stock-Based Compensation.” Stock-based compensation to non-employees is based on the fair value of the option, estimated using the Black-Scholes Option-Pricing Model on the date of grant, and re-measured until vested. The related stock-based compensation expense is recognized over the vesting period.

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## QUICKLOGIC CORPORATION

### NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

The following table illustrates the effect on net income (loss) and net income (loss) per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation (in thousands except per share amounts):

	Three Months Ended March 31,	
	2005	2004
Net income (loss)—as reported	\$ 864	\$ (1,368)
Add: Stock-based employee compensation expense determined under APB No. 25, included in reported net income (loss), net of tax	—	—

Less: Stock-based employee compensation expense related to stock option plans	(870)	(1,294)
Net loss as adjusted	<u>\$ (6)</u>	<u>\$ (2,662)</u>
Net income (loss) per share — as reported:		
Basic	\$ 0.03	\$ (0.06)
Diluted	\$ 0.03	\$ (0.06)
Net loss per share — as adjusted:		
Basic	\$ 0.00	\$ (0.11)
Diluted	\$ 0.00	\$ (0.11)

#### Foreign Currency Transactions

All of the Company's sales and cost of manufacturing are transacted in U.S. dollars. The Company conducts research and development activities in Canada and India and has sales and marketing activities in various countries outside of the United States. Most of these costs are incurred in local currency. Foreign currency transaction gains and losses are included in other income and expense as they occur. The effect of foreign currency exchange rate fluctuations has not been significant to date. Operating expenses denominated in foreign currencies were approximately 26% and 23% of total operating expenses for the three months ended March 31, 2005 and 2004, respectively. The Company incurred a majority of these foreign currency expenses in Canada. The Company has not used derivative financial instruments to hedge its exposure to fluctuations in foreign currency.

#### Concentration of Credit Risk

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of cash and cash equivalents and accounts receivable. Cash and cash equivalents are maintained with high quality institutions. The Company's accounts receivable are denominated in U.S. dollars and are derived primarily from sales to customers located in North America, Europe, and Asia. The Company performs ongoing credit evaluations of its customers and generally does not require collateral.

Three distributors of the Company's products accounted for 20%, 18% and 15% of the Company's accounts receivable balance at March 31, 2005. Two distributors of the Company's products accounted for 24% and 22% of the Company's accounts receivable balance at December 31, 2004.

#### Warranty Costs

The Company generally warrants finished goods against defects in material and workmanship under normal use for 12 months from the date of shipment. The Company does not have significant product warranty related costs or liabilities. The one-time-programmable nature of QuickLogic's products minimizes warranty costs.

#### Recently Issued Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 153, "Exchanges of Nonmonetary Assets," which eliminates the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 will be effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The Company does not believe the adoption of SFAS No. 153 will have a material impact on

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## QUICKLOGIC CORPORATION

### NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

its financial statements.

On December 16, 2004, FASB issued SFAS No. 123(R), "Share-Based Payment," which is a revision of SFAS No. 123 and supersedes Accounting Principals Board ("APB") Opinion No. 25. SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be valued at fair value on the date of grant, and to be expensed over the applicable vesting period. Pro forma disclosure of the income statement effects of share-based payments is no longer an alternative. SFAS No. 123(R), as amended, is effective for all stock-based awards granted in fiscal years beginning after June 15, 2005. In addition, companies must also recognize compensation expense related to any awards that are not fully vested as of the effective date. Compensation expense for the unvested awards will be measured based on the fair value of the awards previously calculated in developing the pro forma disclosures in accordance with the provisions of SFAS No. 123. The Company is currently assessing the impact of adopting SFAS 123(R) and expects the impact upon adoption in fiscal year 2006 to be significant to its results of operations.

#### Note 3—Net Income (Loss) Per Share

Basic net income (loss) per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is computed using the weighted average number of common shares outstanding during the period plus potentially dilutive common shares outstanding during the period under the treasury stock method. In computing diluted net income (loss) per share, the average stock price for the period is used in determining the number of shares assumed to be purchased from the exercise of stock options. A reconciliation of the basic and diluted per share computations is as follows (in thousands, except per share amounts):

Three Months Ended March 31,

	2005			2004		
	Net Income	Shares	Per Share Amount	Net Loss	Shares	Per Share Amount
Basic	\$ 864	26,385	\$ 0.03	\$ (1,368)	24,846	\$ (0.06)
Effect of stock options	—	1,028	—	—	—	—
Diluted	\$ 864	27,413	\$ 0.03	\$ (1,368)	24,846	\$ (0.06)

For the three months ended March 31, 2004, potential common shares of 1.6 million were not included in the calculation of diluted net loss per share, as they were considered antidilutive due to the net loss the Company experienced in the period. For the three months ended March 31, 2005 and 2004, 5.0 million and 4.2 million, respectively, shares of common stock subject to outstanding options were antidilutive and, therefore, were not included in the calculation of diluted net income per share, as the per share exercise price for such options exceeded the average trading price of the Company's common stock during the respective period. While these potential common shares are currently antidilutive, they could be dilutive in the future.

**Note 4—Investment in Tower Semiconductor Ltd.**

The Company has entered into a Share Purchase Agreement (the "Agreement"), Foundry Agreement and other related agreements with Tower, as amended. Under the Agreement, the Company agreed to make a strategic investment in Tower as part of Tower's plan to build and equip a new wafer fabrication facility. The facility produces 200-mm wafers in geometries of 0.18 micron and below, using advanced complementary metal oxide semiconductor technology ("CMOS") acquired from Toshiba.

During 2001 and 2002, the Company paid a total of \$21.3 million to Tower to fulfill its entire investment requirements under the Agreement. In partial consideration for the investment, the Company received 1,757,368 Tower ordinary shares with an original cost of \$16.6 million. The Company wrote down the Tower shares by \$1.5 million, \$3.8 million and \$6.8 million in 2004, 2002 and 2001, respectively, due to an "other than temporary" decline in their market value. The carrying value of these shares following the 2004 write-down was \$2.26 per share, the market value of Tower ordinary shares on the last trading day of 2004.

During the year ended December 31, 2003, the Company sold 412,825 of the Tower ordinary shares for total proceeds of approximately \$2.1 million and recognized a gain of \$719,000 in the statements of operations. As of March 31, 2005, the Company held 1,344,543 available for sale Tower ordinary shares with an accumulated other comprehensive loss of

**QUICKLOGIC CORPORATION**

**NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

\$592,000, representing the difference between the \$2.26 carrying value per share and \$1.82 per share, the market value on the last trading day of the Company's first fiscal quarter of 2005.

The Company intends to hold 450,000 Tower ordinary shares in order to receive competitive product pricing under the Agreement and has recorded these shares as a long-term investment on the balance sheets. The remaining 894,543 shares are classified as a short-term investment on the balance sheets.

The Company also received \$4.7 million in prepaid wafer credits in consideration for the investment, \$4.4 million of which remained available as of March 31, 2005. These credits are recorded in other assets on the balance sheets and can be applied toward wafer purchases from Tower at 7.5% of the value of current purchases and at 15% of the value of purchases made after July 1, 2005.

**Note 5—Balance Sheet Components**

	March 31, 2005	December 31, 2004
(in thousands)		
<b>Inventory:</b>		
Raw materials	\$ 1,043	\$ 1,024
Work-in-process	5,506	4,908
Finished goods	927	809
	<u>\$ 7,476</u>	<u>\$ 6,741</u>
<b>Other current assets:</b>		
Prepaid expenses	\$ 1,078	\$ 1,278
Employee receivables	15	15
Other	157	213
	<u>\$ 1,250</u>	<u>\$ 1,506</u>
<b>Property and equipment:</b>		
Equipment	\$ 12,971	\$ 12,620
Software	8,690	8,647
Furniture and fixtures	840	851
Leasehold improvements	813	813

	23,314	22,931
Accumulated depreciation and amortization	(18,176)	(17,528)
	<u>\$ 5,138</u>	<u>\$ 5,403</u>
Other assets:		
Prepaid wafer credits	\$ 4,407	\$ 4,501
Other	51	51
	<u>\$ 4,458</u>	<u>\$ 4,552</u>
Accrued liabilities:		
Employee related accruals	\$ 1,978	\$ 1,400
Accrued adverse purchase commitments	—	70
Other	556	1,041
	<u>\$ 2,534</u>	<u>\$ 2,511</u>
Debt and capital lease obligations:		
Notes payable to bank	\$ 1,979	\$ 2,567
Capital lease	571	755
	<u>2,550</u>	<u>3,322</u>
Current portion	(1,853)	(2,286)
	<u>\$ 697</u>	<u>\$ 1,036</u>

**QUICKLOGIC CORPORATION**  
**NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

**Note 6—Obligations**

	March 31, 2005	December 31, 2004
	(in thousands)	
Revolving line of credit	\$ 2,000	\$ 2,000
Notes payable to bank	1,979	2,567
Deferred royalty revenue	1,231	1,156
Capital lease	571	755
	<u>5,781</u>	<u>6,478</u>
Current portion of long-term obligations	(3,853)	(4,286)
	<u>\$ 1,928</u>	<u>\$ 2,192</u>

*Revolving Line of Credit and Notes Payable to Bank*

Effective June 2004, the Company modified its Amended and Restated Loan and Security Agreement with Silicon Valley Bank. Terms of the modified agreement include an \$8.0 million revolving line of credit available through June 2005, and an additional \$2.0 million of borrowing capacity under the equipment line of credit that is available to be drawn against through June 2005. The revolving line of credit provides for formula advances based upon a percentage of eligible accounts receivable and for non-formula advances not to exceed \$4.0 million. Advances under the equipment line of credit must be repaid in either 30 or 36 equal monthly installments, depending upon the nature of the items financed. Terms of the various advances under the modified agreement are as follows (in thousands):

	Original Balance	Balance at March 31, 2005	Available Credit	Interest Rate	Maturity Date
<b>Revolving Line of Credit:</b>					
Formula advances	n/a	\$ 2,000	\$ 2,813	Prime + 1.00 %	June 27, 2005
Non-formula advances	n/a	—	3,187	Prime + 2.00 %	June 27, 2005
<b>Equipment Line of Credit:</b>					
Notes payable	\$ 2,332	191	n/a	Prime + 0.75 %	Multiple draws maturing on or before December 31, 2005
Notes payable	2,136	1,076	n/a	Prime + 2.00 %	Multiple draws maturing on or before December 1, 2006
Notes payable	859	712	n/a	Prime + 2.00 %	Multiple draws maturing on or before December 31, 2007 30 or 36 months from date of



Notes payable	n/a		1,141	Prime + 2.00 %	advance
Total		\$ 3,979			

The bank has a first priority security interest in the tangible and intangible assets of the Company to secure any outstanding amounts under the modified agreement. Under the terms and definitions of the modified agreement, the Company must maintain a minimum tangible net worth and adjusted quick ratio. The modified agreement also has certain restrictions on other indebtedness, the maintenance of depository accounts, and the payment of dividends. The Company was in compliance with the modified agreement as of March 31, 2005.

At March 31, 2005, the prime rate under the credit facility was 5.75%. As of March 31, 2005 and December 31, 2004, \$697,000 and \$1.0 million, respectively, of amounts outstanding under the equipment line of credit were classified as long-term liabilities.

#### *Capital Lease*

In January 2004, the Company leased design software and related maintenance under a two-year capital lease at an interest rate of 6.0% per annum. Terms of the agreement require the Company to make quarterly principal and interest

### **QUICKLOGIC CORPORATION** **NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

payments of approximately \$196,000 through October 2005. Accordingly, the Company recorded a capital asset for \$1.2 million that is being amortized over the term of the agreement, prepaid maintenance of \$280,000 that is being amortized over the term of the agreement and a capital lease obligation of \$1.5 million. As of March 31, 2005, the outstanding balance under the capital lease was \$571,000, all of which was classified as a short-term liability.

#### *Deferred Royalty Revenue*

In 2000, the Company entered into a technology license and wafer supply agreement with Aeroflex UTM ("Aeroflex"). Under the terms of the agreement, the Company received \$750,000 of prepaid royalties. In addition, Aeroflex receives prepaid royalty credit for a portion of the amounts paid for wafers purchased from the Company under the agreement. These prepaid royalties are recorded as a long-term liability and will be recognized as revenue when Aeroflex sells products incorporating the licensed technology. As of March 31, 2005 and December 31, 2004, the Company had recorded approximately \$1.2 million of deferred royalty revenue under this agreement. As of March 31, 2005, no royalty revenue had been earned under the agreement.

#### **Note 7 — Employee Stock Plans**

The Company has adopted the disclosure-only provisions of SFAS No. 123. If the Company had elected to recognize compensation expense under SFAS No. 123, net loss for the three months ended March 31, 2005 and 2004 would have been \$6,000 and \$2.7 million, respectively (see Note 2).

#### *1989 Stock Option Plan*

The 1989 Stock Option Plan (the "1989 Plan") provided for the issuance of incentive and nonqualified options for the purchase of up to approximately 4.6 million shares of common stock. Options granted under the 1989 Plan have a term of up to 10 years, and typically vest at a rate of 25% of the total grant per year over a four-year period. In September 1999, the Company adopted the 1999 Stock Plan and no further stock option grants were made under the 1989 Plan.

#### *1999 Stock Plan*

The 1999 Stock Plan (the "1999 Plan") was adopted by the board of directors in August 1999 and was approved by the Company's stockholders in September 1999. As of March 31, 2005, approximately 13.1 million shares were reserved for issuance under the 1999 Plan. In addition, each January an annual increase is added to the 1999 Plan equal to the lesser of (i) 5,000,000 shares, (ii) 5% of the Company's outstanding shares on such date, or (iii) a lesser amount determined by the board of directors. Options that are cancelled under the 1989 Plan also become available for grant under the 1999 Plan. Options granted under the 1999 Plan have a term of up to 10 years. Options typically vest at a rate of 25% of the total grant one year after the vesting commencement date, and one forty-eighth for each month of service thereafter. However, the Company has implemented a different vesting schedule in the past and may implement different vesting schedules in the future with respect to any new stock option grant.

The weighted average estimated fair value, as defined by SFAS No. 123, for options granted during the three months ended March 31, 2005 and 2004 was \$1.91 and \$2.39 per option, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The Black-Scholes model, as well as other currently accepted option valuation models, was developed to estimate the fair value of freely tradable, fully transferable options without restrictions. These assumptions differ significantly from the characteristics of the Company's stock option grants.

The following weighted average assumptions are included in the estimated fair value calculations for stock option grants:

<b>Three Months Ended March 31,</b>	
<b>2005</b>	<b>2004</b>

Expected life (years)	3.50%	3.53%
Risk-free interest rate	—	—
Volatility	88%	73%
Dividend yield	—	—

**QUICKLOGIC CORPORATION**  
**NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

*Employee Stock Purchase Plan*

The 1999 Employee Stock Purchase Plan (“ESPP”) was adopted by the board of directors in August 1999 and was approved by the Company’s stockholders in September 1999. As of March 31, 2005, approximately 3.9 million shares were reserved for issuance under the ESPP. In addition, each August an annual increase is added to the ESPP equal to the lesser of (i) 1,500,000 shares, (ii) 4% of the Company’s outstanding shares on such date, or (iii) a lesser amount determined by the board of directors. The ESPP contains consecutive, overlapping, twenty-four month offering periods. Each offering period includes four six-month purchase periods. The ESPP permits participants to purchase shares through payroll deductions of up to 20% of an employee’s total compensation (maximum of 20,000 shares per purchase period) at 85% of the lower of the fair market value of the common stock at the beginning of an offering period or the end of a purchase period. There were no purchases pursuant to the Company’s ESPP during the three months ended March 31, 2005 and 2004.

*Rights Plan*

In 2001, the board of directors adopted a Rights Agreement, which provides for a dividend of one Preferred Stock Purchase Right (each a “Right” and collectively, the “Rights”) for each share of common stock to stockholders of record on December 12, 2001. Each Right will entitle stockholders to buy one ten-thousandth of a share of Series A Junior Participating Preferred Stock of QuickLogic at an exercise price of \$32.50, subject to adjustment. The Rights will become exercisable only if a person or group becomes the beneficial owner of 15% or more of the common stock, or commences a tender or exchange offer which would result in the offer or beneficially owning 15% or more of the common stock, without the approval of the board of directors. The Company is entitled to redeem the Rights at \$0.001 per Right up to ten days after the public announcement of a 15% holder. If not earlier terminated or redeemed, the Rights will expire on November 27, 2011.

**Note 8—Income Taxes**

In the first quarter of 2005, the Company recorded income tax expense of approximately \$50,000, which consisted of income taxes on foreign operations of \$30,000 and federal alternative minimum income taxes of \$20,000.

Due to the uncertainties surrounding the realization of the deferred tax assets resulting from the Company’s accumulated deficit and net tax losses in prior years, the Company has provided a full valuation allowance against the associated deferred tax assets. The Company will continue to assess the realizability of the deferred tax assets in future periods.

At December 31, 2004, the Company had net operating loss carryforwards for federal and state income tax purposes of approximately \$79 million and \$14 million, respectively. These carryforwards, if not utilized to offset future taxable income and income taxes payable, will expire beginning in 2006 for federal purposes and 2005 for state purposes.

Under the Tax Reform Act of 1986, the amount of and the benefit from net operating losses that can be carried forward may be impaired in certain circumstances. Events which may cause changes in the Company’s tax carryovers include, but are not limited to, a cumulative ownership change of more than 50% over a three-year period. Since inception, the Company believes cumulative changes in ownership may have triggered the loss carryforward deduction limitation under IRC Section 382. However, the Company believes that such limitations will not have a material effect on the future utilization of the losses.

**QUICKLOGIC CORPORATION**  
**NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

**Note 9—Information Concerning Geographic Information and Major Customers**

The following is a breakdown of revenue by shipment destination (in thousands):

	Three Months Ended March 31,	
	2005	2004
Revenue by geography:		
United States	\$ 5,881	\$ 4,960
Japan	2,083	2,437
Europe	3,137	1,805
China	141	90

Rest of North America	374	365
Total revenue	\$ 12,527	\$ 10,368

Three distributors of the Company's products accounted for approximately 24%, 16% and 13% of revenue in the three months ended March 31, 2005. The same three distributors of the Company's products accounted for approximately 18%, 17%, and 16% of revenue in the three months ended March 31, 2004. For the three months ended March 31, 2005, one domestic systems manufacturer accounted for 11% of revenue. One Japanese systems manufacturer, purchasing our products through a distributor, accounted for 14% of revenue in the three months ended March 31, 2004.

As of March 31, 2005 less than 10% of the Company's long-lived assets, including property and equipment and other assets, were located outside the United States.

#### Note 10—Commitments

Certain of the Company's wafer manufacturers require the Company to forecast wafer starts several months in advance. The Company is committed to take delivery of and pay for a portion of forecasted wafer volume. As of March 31, 2005 and December 31, 2004, the Company had \$4.9 million and \$6.4 million, respectively, of outstanding commitments for the purchase of wafers.

The Company leases, with an option to renew, its primary facility under a non-cancelable operating lease that expires in 2009. In addition, the Company rents development facilities in Canada and India and sales offices in Europe and Asia. Total rent expense, net of sublease income, for the three months ended March 31, 2005 and 2004 was approximately \$260,000 and \$230,000, respectively.

#### Note 11—Litigation

On October 26, 2001, a putative securities class action was filed in the U.S. District Court for the Southern District of New York against certain investment banks that underwrote QuickLogic's initial public offering, QuickLogic and some of QuickLogic's officers and directors. The complaint alleges excessive and undisclosed commissions in connection with the allocation of shares of common stock in QuickLogic's initial and secondary public offerings and artificially high prices through "tie-in" arrangements which required the underwriters' customers to buy shares in the aftermarket at pre-determined prices in violation of the federal securities laws. Plaintiffs seek an unspecified amount of damages on behalf of persons who purchased QuickLogic's stock pursuant to the registration statements between October 14, 1999, and December 6, 2000. Various plaintiffs have filed similar actions asserting virtually identical allegations against over 300 other public companies, their underwriters, and their officers and directors arising out of each company's public offering. These actions, including the action against QuickLogic, have been coordinated for pretrial purposes and captioned *In re Initial Public Offering Securities Litigation*, 21 MC 92. A stipulation of settlement for the claims against the issuer defendants, including the Company, has been signed and was submitted to the court. Under the stipulation of settlement, the plaintiffs will dismiss and release all claims against participating defendants in exchange for a contingent payment guaranty by the insurance companies collectively responsible for insuring the issuers in all the related cases, and the assignment or surrender to the plaintiffs of certain claims the issuer defendants may have against the underwriters. Under the guaranty, the insurers will be required to pay the amount, if any, by which \$1.0 billion exceeds the aggregate amount ultimately collected by the plaintiffs from the underwriter defendants in all the cases. On February 15, 2005, the court preliminarily approved the settlement contingent on specified modifications. The settlement is still subject to court approval and a number of other conditions. There is no guarantee that the settlement will become effective.

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### QUICKLOGIC CORPORATION

#### NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

On July 3, 2003, a putative securities class action was filed in the U.S. District Court for the Southern District of New York by shareholders of Tower Semiconductor Ltd. against Tower, several of its directors, and several of its investors, including QuickLogic. QuickLogic was named solely as an alleged control person. On August 19, 2004, the court dismissed the claims against all defendants, including QuickLogic, with prejudice. On September 29, 2004 one of the plaintiffs filed a notice of appeal from the judgment.

No estimate can be made of the possible loss or possible range of loss associated with the resolution of these contingencies and, accordingly, the Company has not recorded a liability.

From time to time, the Company is involved in legal actions arising in the ordinary course of business, including but not limited to intellectual property infringement and collection matters. Absolute assurance cannot be given that third party assertions will be resolved without costly litigation in a manner that is not adverse to the Company or without requiring future royalty payments.

#### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*The following Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as information contained in "Risk Factors" below and elsewhere in this Quarterly Report on Form 10-Q, contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. We intend that these forward-looking statements be subject to the safe harbors created by those provisions. Forward-looking statements are generally written in the future tense and/or are preceded by words such as "will," "may," "should," "forecast," "could," "expect," "suggest," "believe,"*

“anticipate,” “intend,” “plan,” or other similar words. Forward-looking statements include statements regarding (1) our revenue levels, (2) our gross profit and factors that affect gross profit, (3) our level of operating expenses, (4) our research and development efforts, (5) our liquidity, (6) our partners and suppliers, and (7) the commercial success of our products. The following discussion should be read in conjunction with the attached condensed unaudited consolidated financial statements and notes thereto, and with our audited financial statements and notes thereto for the fiscal year ended December 31, 2004, found in our Annual Report on Form 10-K filed on March 17, 2005.

The forward-looking statements contained in this Quarterly Report involve a number of risks and uncertainties, many of which are outside of our control. Factors that could cause actual results to differ materially from projected results include, but are not limited to, risks associated with (1) limited visibility into demand for our products, including demand from significant customers or for new products such as Eclipse II or QuickPCI II, (2) the expected decline in revenue from our pASIC1 and pASIC2 products, (3) the commercial and technical success of our new products, (4) our relationship with and the manufacturing of our products by Tower Semiconductor Ltd., and (5) the liquidity required to support our future operating and capital requirements. Although we believe that the assumptions underlying the forward-looking statements contained in this Quarterly Report are reasonable, any of the assumptions could be inaccurate, and therefore there can be no assurance that such statements will be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that the results or conditions described in such statements or our objectives and plans will be achieved. Furthermore, past performance in operations and share price is not necessarily indicative of future performance. QuickLogic disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

## Overview

We operate in a single industry segment where we design and sell field programmable gate arrays, embedded standard products, associated software and programming hardware. In 1991, we introduced our first line of field programmable gate array products, or FPGAs, based upon our ViaLink technology. Our Mature product family consists of our three FPGA product families: pASIC1, pASIC2 and pASIC3. Our newer FPGA product families generally contain greater logic capacity, but do not necessarily replace sales of older generation products.

In September 1998, we introduced our first line of Embedded Standard Products, or ESPs, to address the design community’s demand for an alternative to existing options: Application Specific Integrated Circuits, or ASICs, and system-on-a-chip products. ESP products embed standard functions on programmable logic devices. These products provide engineers with the ease-of-use, guaranteed functionality, high performance, low non-recurring engineering charges and immediate availability of application specific standard products, or ASSPs, combined with the flexibility and time-to-market advantages of programmable logic. Our ESP product family includes QuickRAM, QuickPCI, and V3 products. Our Advanced ESP product family includes QuickMIPS, Eclipse, Eclipse II and QuickPCI II products. We also license our QuickWorks and QuickTools design software and sell our programming hardware and include these sales as Advanced ESP revenue.

Our newest products target low-power, high-performance applications where system designers want to add features to or improve the performance of a system through the use of FPGA devices. Our products generally target complex, high-performance embedded systems in rapidly changing markets where system manufacturers seek to minimize time-to-market and maximize product differentiation and functionality. Our product offering includes the lowest-power FPGAs available in the industry today, enabling designers to utilize the high performance of our FPGA architecture in low-power embedded systems. Compared to our competitors’ SRAM-based FPGAs, our devices provide a higher level of intellectual property security since it is extremely difficult to clone or reverse engineer intellectual property that is implemented using our one-time-programmable ViaLink technology. We compete in various markets, including: instrumentation and test; data communications and telecommunications; consumer applications; video, audio and graphics imaging; high-performance computing; and military and aerospace systems. Based on current customer design activity, we expect that consumer applications will represent a higher proportion of our revenue in the future.

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Our proprietary ViaLink programmable metal-to-metal technology is the core of our FPGA products and the foundation of our ESP products. Our ViaLink technology allows us to create devices smaller than competitors’ comparable products, thereby minimizing silicon area and cost. In addition, our ViaLink technology has lower electrical resistance and capacitance than other programmable technologies and, consequently, supports higher signal-speed and low power consumption. Our user-programmable platform and design software facilitates full utilization of a device’s logic cells, clocks and input/output pins. These logic cells have been optimized to efficiently implement a wide range of logic functions at high speed, thereby enabling greater usable device density and design flexibility. Our architecture uses our ViaLink technology to maximize interconnects at every routing wire intersection, which allows more paths between logic cells. As a consequence, system designers are able to use our devices with smaller gate counts to implement their designs than if they had used competing FPGAs. The abundance of interconnect resources also provides a dense connection between the ASSP and the FPGA portions of Embedded Standard Products.

We believe that important industry trends in our target markets include lower power consumption, higher performance, shorter time to market, increased intellectual property security, higher development expenses and increased product development risks. We believe our products are designed to address many of these trends.

The market for programmable logic devices is expected to grow more quickly than the semiconductor industry, and we believe the FPGA programmable logic market will grow more quickly than the market for complex programmable logic devices. One factor fueling this high growth is the migration from ASIC circuit designs to programmable logic circuit designs. System designers often choose programmable logic solutions over ASIC solutions, due to the relatively low development cost, low development risk, quick time to market and high adaptability or flexibility of programmable logic devices, and due to the ability of programmable logic suppliers to reduce

the unit costs of their products over time.

Technology developed for personal computer applications, such as (micro) hard disk drives and Wi-Fi communication modules, is being designed into embedded applications, as embedded system designers seek to improve the value of their systems by incorporating these features. This adoption of new features by embedded system designers is increasing the use of programmable logic, since embedded processors often do not have the native ability to interface to components such as Wi-Fi modules or micro hard disk drives, which were designed to work in a personal computer environment. Our Eclipse II and QuickPCI II devices have compelling advantages in these programmable interconnect applications, where customers benefit from their low power consumption, small form factor and high bandwidth.

We believe that the market for low-power embedded applications will be a relatively high-growth market, as OEMs serving the consumer or professional portable markets accelerate the offering of devices such as PDAs incorporating Wi-Fi capability, wireless VoIP telephones, or consumer products utilizing a micro hard drive.

We believe our products offer bulletproof intellectual property security compared to SRAM-based FPGA or ASIC solutions. We believe intellectual property security will be important to system designers who choose to implement proprietary algorithms or features in programmable logic rather than ASIC devices.

In 2000, we entered into a Share Purchase Agreement, Foundry Agreement and other related agreements, as amended, with Tower Semiconductor Ltd., or Tower. Under the terms of the agreements, we agreed to make a strategic investment in Tower as part of Tower's plan to build and equip a new wafer fabrication facility. The facility produces 200-mm wafers in geometries of 0.18 micron, using advanced complementary metal oxide semiconductor, or CMOS, technology acquired from Toshiba.

During 2001 and 2002, we paid Tower a total of \$21.3 million to fulfill our entire investment requirements under the terms of the agreement. In partial consideration for the investment, we received 1,757,368 Tower ordinary shares with an original cost of \$16.6 million. We wrote down the Tower shares due to an "other than temporary" decline in their market value by \$1.5 million, \$3.8 million and \$6.8 million in fiscal 2004, 2002 and 2001, respectively. During 2003, we sold 412,825 of the available for sale Tower ordinary shares for total proceeds of approximately \$2.1 million and recognized a gain in the amount of \$719,000. As of March 31, 2005, we held 1,344,543 available for sale Tower ordinary shares valued at \$1.82 per share, the market value of these shares at the end of our first fiscal quarter of 2005. We intend to continue to hold 450,000 Tower ordinary shares in order to receive competitive product pricing and, accordingly, have classified these shares as a long-term investment on our balance sheets. The remaining 894,543 shares are recorded as a short-term investment on our balance sheets. The carrying value of these shares is \$2.26 per share. If the fair value of our Tower investment remains below \$2.26 per share at the end of our second fiscal quarter, we will incur a charge for the write down of these marketable

securities.

We also received \$4.7 million in prepaid wafer credits in partial consideration for the investment. These credits can be applied toward wafer purchases from Tower at 7.5% of the value of current purchases and at 15% of the value of purchases made after July 1, 2005. As of March 31, 2005 and December 31, 2004 we had \$4.4 million and \$4.5 million, respectively, of prepaid wafer credits classified as other long-term assets on our balance sheets.

We sell programmed and unprogrammed products through distributors and directly to original equipment manufacturers. However, we sell the majority of our products through point-of-sale distributors. The percentage of sales derived through distributors was 70% and 71% in the three months ended March 31, 2005 and 2004, respectively. For the three months ended March 31, 2005 and 2004, approximately 68% and 70%, respectively, of the units shipped to our point-of-sale distributors were programmed by us.

Three distributors of the Company's products accounted for 24%, 16% and 13% of revenue in the three months ended March 31, 2005. Three distributors of the Company's products accounted for 18%, 17% and 16% of revenue in the three months ended March 31, 2004. For the three months ended March 31, 2005, one domestic manufacturer accounted for 11% of revenue. One Japanese systems manufacturer, purchasing our products through a distributor, accounted for 14% of revenue in the three months ended March 31, 2004. We anticipate that a limited number of distributors will continue to account for a significant portion of our total sales and that individual distributors could account for a larger portion of our revenue.

Our international sales were 53% and 52% of revenue in the three months ended March 31, 2005 and 2004, respectively. Revenue from sales to international customers is expected to continue to represent a significant portion of our revenue. All of our sales originate in the United States and are denominated in U.S. dollars.

We outsource the wafer manufacturing, assembly and testing of all of our products. We currently rely upon Taiwan Semiconductor Manufacturing Company Ltd., or TSMC, Cypress Semiconductor Corporation, Tower and Samsung Semiconductor, Inc. to manufacture our products, and we rely primarily upon Amkor Technology, Inc. and Advanced Semiconductor Engineering Inc., or ASE, to assemble, test and program our products. Our wafer suppliers' lead times are often as long as three months and sometimes longer. In addition, Cypress and Tower require us to provide them with a monthly wafer start forecast. Under the terms of our agreements with them, we are limited in the quantity that we can increase or decrease our wafer forecast and we are committed to take delivery of and pay for a minimum portion of the forecasted wafer volume. Our long manufacturing cycle times are at odds with our customers' desire for short delivery lead times and, as a result, we typically purchase wafers based on our internal forecasts of customer demand.

## **Critical Accounting Policies and Estimates**

The methods, estimates and judgments we use in applying our most critical accounting policies have a significant impact on the results we report in our financial statements. The U.S. Securities and Exchange Commission, or SEC, has defined critical accounting policies as those that are most important to the portrayal of our financial condition and results of operations and require us to make our most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, our critical policies include revenue recognition including sales returns and allowances, inventory valuation including excess quantities and product obsolescence, allowance for doubtful accounts, valuation of investments, valuation of long-lived assets, accounting for income taxes, and estimating accrued liabilities. We believe that we apply judgments and estimates in a consistent manner and that such consistent application results in financial statements and accompanying notes that fairly represent all periods presented. However, any factual errors or errors in these judgments and estimates may have a material impact on our statement of operations and financial condition. For a discussion of our significant accounting policies, please see Note 2 to the Condensed Unaudited Consolidated Financial Statements in this Quarterly Report on Form 10-Q. For a discussion of critical accounting policies and estimates, please see Item 7 in our Annual Report on Form 10-K for the fiscal year ended December 31, 2004 filed on March 17, 2005.

## Results of Operations

The following table sets forth the percentage of revenue for certain items in our statements of operations for the periods indicated:

	Three Months Ended March 31,	
	2005	2004
Revenue	100.0 %	100.0 %
Cost of revenue	39.0	43.9
Gross profit	61.0	56.1
Operating expenses:		
Research and development	19.6	31.3
Selling, general and administrative	34.3	37.7
Income (loss) from operations	7.1	(12.9)
Interest expense	(0.4)	(0.7)
Interest income and other, net	0.6	0.4
Income (loss) before income taxes	7.3	(13.2)
Provision for income taxes	0.4	—
Net income (loss)	6.9 %	(13.2) %

### Three Months Ended March 31, 2005 and 2004

*Revenue.* Our revenue for the three months ended March 31, 2005 was \$12.5 million, representing a growth of \$2.2 million, or 20.8%, from revenue of \$10.4 million in the three months ended March 31, 2004. This revenue increase was due to a \$3.3 million increase in our Mature product revenue primarily related to higher customer demand and end-of-life purchases of our pASIC1 and pASIC2 products. This increase was partially offset by a decline in our Advanced ESP product revenue of \$490,000, primarily due to a decrease in revenue from a Japanese systems manufacturer purchasing product through a distributor, and a decline in our ESP product revenue of \$630,000.

Our revenue for the three months ended March 31, 2005 was 13.1% higher sequentially, increasing to \$12.5 million from \$11.1 million in the three months ended December 31, 2004. This increase primarily resulted from a \$1.4 million increase in sales of our Mature products due primarily to higher revenue from our pASIC1 products.

Our foundry agreement with the supplier that fabricates our pASIC1 and pASIC2 products expires at the end of 2005. We have announced an end-of-life for these products and have asked our customers to take delivery of lifetime buy orders before the end of 2005. These product families contributed \$6.4 million and \$3.3 million of our revenue in the three months ended March 31, 2005 and 2004, respectively. While we may have limited production capacity for these products beyond 2005, we expect to experience a significant reduction in pASIC1 and pASIC2 revenue near the end of 2005. We currently believe that a majority of our customers that use pASIC1 and pASIC2 products will purchase enough product to satisfy their demand throughout the expected life of their products rather than migrate to other QuickLogic products, and that pASIC1 and pASIC2 products will contribute less than 10% of our revenue by the first quarter of 2006 and no revenue by the end of 2006. As a result, we could experience fluctuations in demand as customers build inventory of these products, design systems using devices supplied by others or reduce purchases of our products.

In order to maintain or grow our revenue from its current level after the end-of-life period in 2005 for our pASIC1 and pASIC2 products, we are dependent upon increased revenue from our existing products, especially our new Eclipse II and QuickPCI II products, and the development of additional commercially successful new products.

We continue to seek to expand our revenue, including the pursuit of high volume sales opportunities. Our industry is characterized by intense price competition and by lower prices as order volumes increase. While winning large volume sales opportunities will increase our revenue, we believe these opportunities may decrease our average selling price and gross profit as a percentage of revenue.

*Gross Profit.* Gross profit was \$7.6 million and \$5.8 million in the three months ended March 31, 2005 and 2004, respectively, which was 61.0% and 56.1% of revenue for those periods, respectively. The \$1.8 million improvement in gross profit was primarily due to higher revenue and changes in product mix, which contributed \$1.6 million of this improvement, and lower production variances, which accounted for the remainder of the gross profit improvement. Our absorbed overhead

variances improved by approximately \$290,000 during this period, due largely to lower depreciation and amortization as a result of the impairment of long-lived assets recorded in the fourth quarter of 2004.

*Research and Development Expense.* Research and development expense was \$2.5 million and \$3.2 million in the three months ended March 31, 2005 and 2004, respectively, which was 19.6% and 31.3% of revenue for those periods. The decrease of approximately \$790,000 was primarily due to lower charges for pre-production material and other expenses associated with the development of our 0.18 micron products which were released for production in late 2004. We believe that continued investments in product development and process technology are essential for us to remain competitive in the markets we serve. We expect that these development efforts will allow us to expand our product offering and provide additional value to our customers and stockholders.

*Selling, General and Administrative Expense.* Selling, general and administrative expense was \$4.3 million and \$3.9 million for the three months ended March 31, 2005 and 2004, respectively, which was 34.3% and 37.7% of revenue for those periods. The \$390,000 increase in selling, general and administrative expense was primarily the result of \$550,000 in higher outside services associated with compliance related matters, legal expenses, commissions and promotional expenses, partially offset by lower bad debt expense of \$140,000 as a result of collecting previously reserved accounts receivable.

*Interest Expense.* Interest expense was \$53,000 for the three months ended March 31, 2005 compared to \$68,000 for the three months ended March 31, 2004. This decrease was primarily due to lower average outstanding balances, partially offset by higher interest rates.

*Interest and Other Income, Net.* Interest and other income, net was \$80,000 of income for the three months ended March 31, 2005 as compared to \$44,000 of income for the three months ended March 31, 2004. The \$36,000 increase in interest and other income, net is primarily due to increased interest income received as a result of higher invested cash balances and higher interest rates.

*Provision for Income Taxes.* We recorded a provision for income taxes of \$50,000 for the three months ended March 31, 2005, which consisted of income taxes on foreign operations of \$30,000 and federal alternative minimum income taxes of \$20,000. We incurred a tax loss in the three months ended March 31, 2004. Our ability to utilize our income tax loss carryforwards in future periods is uncertain and, accordingly, we recorded a full valuation allowance against the related tax benefit. We will continue to assess the realizability of the deferred tax assets in future periods.

## **Liquidity and Capital Resources**

We have financed our operating losses and capital investments through sales of common stock, private equity investments, capital and operating leases, bank lines of credit and cash flow from operations. As of March 31, 2005, our principal sources of liquidity consisted of our cash and cash equivalents of \$24.6 million, available credit under our revolving line of credit with Silicon Valley Bank of approximately \$6.0 million, available credit under our equipment line of credit of approximately \$1.1 million, and our short-term investment in Tower with a market value of approximately \$1.6 million.

As of March 31, 2005, our interest-bearing debt consisted of \$4.0 million outstanding from Silicon Valley Bank and \$571,000 outstanding under a capital lease. As of March 31, 2005, our accumulated deficit was \$118.8 million. Capital expenditures, which are largely driven by the development of new products and manufacturing levels, could be up to \$5.0 million in the next twelve months.

In June 2004, we modified our Amended and Restated Loan and Security Agreement with Silicon Valley Bank. Terms of the modified agreement include an \$8.0 million revolving line of credit available through June 2005 and an additional \$2.0 million of borrowing capacity under an equipment financing line of credit that is available to be drawn against through June 2005. The revolving line of credit provides for formula advances based upon a percentage of eligible accounts receivable and for non-formula advances not to exceed \$4.0 million. As of March 31, 2005 under the revolving line of credit, we had borrowed \$2.0 million and had available formula and non-formula advances totaling \$6.0 million. As of March 31, 2005, we had \$2.0 million outstanding under the existing and previous equipment lines of credit, with \$1.1 million available to be drawn against future equipment purchases. Advances under the equipment line of credit must be repaid in either 30 or 36 equal monthly installments, depending upon the nature of the items financed. The bank has a first priority security interest in our tangible and intangible assets to secure any outstanding amounts under the modified agreement. Under the terms and definitions of the modified agreement, we must maintain a minimum tangible net worth and adjusted quick ratio. The modified agreement also has certain restrictions on other indebtedness, the maintenance of depository accounts and the

payment of dividends. We were in compliance with all loan covenants as of March 31, 2005. We are currently negotiating the renewal of this credit facility. If we do not renew this credit facility, we will be required to repay the outstanding balance of the revolving line of credit on or before the June 27, 2005 expiration date.

As of March 31, 2005, we also had \$571,000 outstanding under a capital lease obligation. The capital lease obligation bears interest at 6.0% per annum and is being repaid in quarterly amounts of \$196,000 through October 2005.

*Net cash from operating activities*

Net cash provided by operating activities was \$582,000 in the three months ended March 31, 2005. The cash provided resulted primarily from net income of \$864,000, adjusted for \$971,000 of non-cash charges including depreciation and amortization of \$665,000 and reserves for excess inventory of \$205,000. In addition, changes in working capital accounts used cash in the amount of \$1.3 million primarily as a result of an increase of \$1.1 million in accounts receivable, net of allowances for doubtful accounts, and a \$940,000 increase in work-in-process and finished goods inventory in anticipation of increased future sales, partially offset by a \$260,000 increase in trade payables related to the increase in inventory, a \$256,000 reduction in other current assets due to the amortization of prepaid expenses and a \$221,000 increase in deferred income and royalty revenue due primarily to higher inventories at distributors on which revenue is deferred.

Net cash used by operating activities was \$366,000 in the first quarter of 2004. The cash used resulted primarily from the net loss of \$1.4 million, adjusted for non-cash charges and other items including depreciation and amortization of \$1.2 million and reserves for excess inventories of \$130,000. In addition, changes in working capital accounts used cash in the amount of \$363,000 primarily as a result of higher inventories of \$883,000 due to the build up of wafers, programming hardware for sale to customers and finished goods that are scheduled to ship early in the next quarter and a higher receivables balance of \$503,000 due primarily to the timing of sales in the quarter. These increases were partially offset by a \$519,000 increase in deferred income and royalty revenue primarily as a result of higher inventories at distributors on which revenue is deferred and a decrease in other assets of \$381,000 primarily due to the amortization of prepaid expenses.

#### *Net cash from investing activities*

Net cash used for investing activities for the three months ended March 31, 2005 was \$407,000 as a result of capital expenditures made primarily to acquire equipment and software used in the development and production of our products. Net cash used for investing activities was \$415,000 for the three months ended March 31, 2004. This amount was invested primarily to acquire equipment and software used in the development and production of our products. Also, in the three months ended March 31, 2004, we entered into a capital lease obligation to acquire design software and related maintenance. As a result of this agreement, we recorded a capital lease obligation for \$1.5 million, property and equipment of \$1.2 million and prepaid maintenance of \$280,000 on the balance sheet. This transaction was treated as a non-cash transaction in our statement of cash flows for the three months ended March 31, 2004.

#### *Net cash from financing activities*

Net cash used for financing activities was \$491,000 for the three months ended March 31, 2005. The use of funds was due to scheduled repayments of \$772,000 under the terms of our long-term obligations, partially offset by \$281,000 of proceeds related to the issuance of common shares upon the exercise of stock options by employees. Net cash used for financing activities was \$591,000 for the three months ended March 31, 2004. The use of funds was due to scheduled repayments of \$697,000 under the terms of our long-term obligations, partially offset by \$106,000 of proceeds related to the issuance of common stock upon the exercise of stock options by employees.

We require substantial working capital to fund our business, particularly to finance our operations, the acquisition of property and equipment, working capital and the repayment of debt. Our future liquidity will depend on many factors such as these, as well as our level of revenue and gross profit, market acceptance of our existing and new products including our Eclipse II and QuickPCI II parts, the expected decline in pASIC1 and pASIC2 revenue resulting from the end-of-life of these products, costs of securing access to adequate manufacturing capacity, inventory levels, wafer purchase commitments, customer credit terms, the amount and timing of research and development expenditures, the timing of new product introductions, production volumes, the quality of our products, sales and marketing efforts, changes in operating assets and liabilities, our ability to obtain or renew debt financing and to remain in compliance with the terms of our credit facilities, our ability to raise funds from the sale of Tower shares and equity in the Company, the exercise of employee stock options and participation in our employee stock purchase plan, and other factors related to the uncertainties of the industry and global economics. However, we believe that our existing cash resources will be sufficient to fund any operating losses, capital

expenditures of up to \$5.0 million, and provide adequate working capital for at least the next twelve months. As our liquidity is affected by many factors as mentioned above and as discussed in our "Risk Factors," there can be no assurance that we will not seek additional capital during the next twelve months or that such capital will be available on terms acceptable to us.

#### **Contractual Obligations and Commercial Commitments**

The following table summarizes our contractual obligations and commercial commitments as of March 31, 2005 and the effect such obligations and commitments are expected to have on our liquidity and cash flows in future periods (in thousands):

	Payments Due by Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
<i>Contractual cash obligations:</i>					
Operating leases	\$ 2,967	\$ 702	\$ 1,402	\$ 863	\$ —
Wafer purchases (1)	4,938	4,938	—	—	—
Other purchase commitments	1,572	1,572	—	—	—
<b>Total contractual cash obligations</b>	<b>9,477</b>	<b>7,212</b>	<b>1,402</b>	<b>863</b>	<b>—</b>
<i>Other commercial commitments (2):</i>					
Revolving line of credit	2,000	2,000	—	—	—



Notes payable to bank	1,979	1,387	697	=	=
Capital lease obligations	—	—	—	—	—
<b>Total commercial commitments</b>	<b>4,550</b>	<b>3,853</b>	<b>697</b>	<b>—</b>	<b>—</b>
Total contractual obligations and commercial commitments	\$ 14,027	\$ 11,065	\$ 2,099	\$ 863	\$ —

(1) Certain of our wafer manufacturers require us to forecast wafer starts several months in advance. We are committed to take delivery of and pay for a portion of forecasted wafer volume. Wafer purchase commitments of \$4.9 million include both firm purchase commitments and a portion of our forecasted wafer starts as of March 31, 2005.

(2) Other commercial commitments are included as liabilities on our balance sheet as of March 31, 2005.

### Inflation

The impact of inflation on our business has not been material for the periods presented.

### Off-Balance Sheet Arrangements

We do not maintain any off-balance sheet partnerships, arrangements or other relationships with unconsolidated entities or others, often referred to as structured finance or special purpose entities, which are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

### Recently Issued Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards, or SFAS, No. 153, "Exchanges of Nonmonetary Assets," which eliminates the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 will be effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. We do not believe the adoption of SFAS No. 153 will have a material impact on our financial statements.

On December 16, 2004, FASB issued SFAS No. 123(R), "Share-Based Payment," which is a revision of SFAS No. 123 and supersedes Accounting Principals Board, or APB, Opinion No. 25. SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be valued at fair value on the date of grant, and to be expensed over the applicable vesting period. Pro forma disclosure of the income statement effects of share-based payments is no longer an alternative. SFAS No. 123(R), as amended, is effective for all stock-based awards granted in fiscal years beginning after December 15, 2005. In addition, companies must also recognize compensation expense related to any awards that are not fully vested as of the effective date. Compensation expense for the unvested awards will be measured based on the fair value of the awards previously calculated in developing the pro forma disclosures in accordance with the provisions

of SFAS No. 123. See Notes 2 and 7 to our Condensed Unaudited Consolidated Financial Statements for information related to the pro forma effects on our reported net income (loss) and net income (loss) per share of applying the fair value recognition provisions of the previous SFAS No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation. We are currently assessing the impact of adopting SFAS 123(R) and expect the impact upon adoption in fiscal year 2006 to be significant to our results of operations.

### Risk Factors

*We may be unable to accurately estimate quarterly revenue, which could adversely affect the trading price of our stock*

We offer our customers a short delivery lead-time and a majority of our shipments during a quarter are ordered by the customer in that quarter. As a result, we often have low visibility to the current quarter's revenue, and our revenue levels can change significantly in a short period of time. Furthermore, our ability to respond to increased demand is limited to inventory on hand or on order and the capacity available at our contract manufacturers. In addition, a significant portion of our revenue is deferred until our distributors ship unprogrammed parts to end customers since the price is not fixed or determinable until that time. Therefore, we are highly dependent on the accuracy and timeliness of resale and inventory reports from our distributors. Inaccurate distributor resale or inventory reports, as well as unanticipated changes in distributor inventory levels, could contribute to our difficulty in predicting and reporting our quarterly revenue and results of operations. If we fail to accurately estimate customer demand, record revenue, or if our available capacity is less than needed to meet customer demand, our results of operations could be harmed and our stock price could materially fluctuate.

*We expect the announced end-of-life of our pASIC1 and pASIC2 products will result in fluctuations and a decline in our revenue*

Our foundry agreement with the supplier that fabricates our pASIC1 and pASIC2 products expires on December 31, 2005. We have announced an end-of-life for these products and have asked our customers to take delivery of lifetime buy orders before the end of 2005. While we may have limited capacity beyond 2005, we currently expect that these products will contribute less than 10% of our revenue by the first quarter of 2006 and no revenue by the end of 2006. Revenue from these products was \$6.4 million in the quarter ended March 31, 2005. Revenue from these products was \$5.1 million, \$5.2 million, \$4.3 million and \$3.3 million in the quarters ended December 31, September 30, June 30 and March 31, 2004, respectively. We currently expect that a majority of our customers that use pASIC1 and pASIC2 products will purchase enough product to satisfy their demand throughout the expected life of their products rather than migrate to other QuickLogic products. As a result, we expect to experience fluctuations in demand as these customers build

inventory of these products, design systems using devices supplied by others or reduce purchases of our products. If we are unable to: migrate customers to other products; develop customer demand for our Eclipse II and QuickPCI II products, which have strong customer design-in activity but have not contributed significant revenue or gross profit to date; increase revenue and gross profit from our other products; or obtain adequate production capacity; our revenue and gross profit may decline and our operating results and liquidity would be adversely affected.

*If we fail to successfully develop, introduce and sell new products, we may be unable to compete effectively in the future*

We operate in a highly competitive, quickly changing environment marked by rapid obsolescence of existing products. To compete successfully, we must obtain access to advanced fabrication capacity and dedicate significant resources to specify, design, develop, manufacture and sell new or enhanced products that provide increasingly higher levels of performance, low power consumption, new features, reliability and/or cost savings to our customers. For example, our new Eclipse II, QuickPCI II and QuickMIPS products are produced at Tower's new advanced fabrication facility. We experience a long delay between the time when we expend these development resources and invest in related long-lived assets, and the time when we begin to generate revenue, if any, from these expenditures. For example, in the fourth quarter of 2004 we recorded a \$3.2 million long-lived asset impairment charge related to our QuickMIPS products. If we are unable to design, produce and sell new products that meet design specifications, address customer requirements, and generate sufficient revenue and gross profit, if market demand for our products fails to materialize, or if our customers do not successfully introduce products incorporating our devices, our business will be materially harmed and we may be required to write-off related inventory and long-lived assets.

*Our future results depend on our relationship with Tower*

We have invested approximately \$21.3 million in Tower. In return for our investment, we have received equity, prepaid wafer credits and committed production capacity in Tower's foundry facility. We believe that Tower's long-term operation of this fabrication facility depends on its ability to attract sufficient customer demand, to obtain additional

financing, the release of grants and approvals for changes in grant programs from the Israeli government's Investment Center, and its ability to remain in compliance with the terms of its grant and credit agreements. The current political uncertainty and security situation in the Middle East where Tower's fabrication facility is located, the cyclical nature of the market for foundry manufacturing services, the early stage of operation of Tower's fabrication facility, Tower's financial condition, the recent turnover of Tower's Chairman and CEO, or other factors may adversely impact Tower's business prospects and may discourage future investments in Tower from outside sources. If Tower is unable to obtain adequate financing and increase production output in a timely manner, the value of our investment in Tower may decline significantly or possibly become worthless, our wafer credit from Tower may decline in value or possibly become worthless, and we would have to identify and qualify a substitute supplier to manufacture our products. This could require significant development time, cause product shipment delays, impair long-lived assets, damage our liquidity and severely harm our business.

The value of our investment in Tower and its corresponding wafer credits may also be adversely affected by a deterioration of conditions in the market for foundry manufacturing services and the market for semiconductor products generally. If the fair value of our Tower investment remains below \$2.26 per share for a period of time or our wafer credits are deemed to be impaired, we will record additional losses. At March 31, 2005, the aggregated value of our Tower investment and wafer credits recorded on our balance sheets was \$6.9 million.

In addition, Tower solely manufactures our Eclipse II, and certain QuickPCI II and QuickMIPS products, and we have made significant purchases and purchase commitments to Tower for these devices. As these are new products being manufactured in a new facility, there are significant manufacturing and engineering risks associated with these quantities of product. We expect these devices to be a source of significant long-term revenue. If Tower is unable to produce these devices, demand for these products does not meet our expectations or if we are unable to achieve product performance or cost targets, our revenue, gross margin, research and development expenses and liquidity will be affected and we may record additional losses against inventory, purchase commitments and long-lived assets.

*We depend upon third parties to fabricate, assemble, test and program our products, and they may discontinue manufacturing our products, fail to give our products priority, be unable to successfully manufacture our products to meet performance, volume or cost targets, or inaccurately report inventory to us*

We contract with third parties to fabricate, assemble, test and program our devices. Our devices are generally fabricated and assembled by single suppliers, and the loss of a supplier, expiration of a supply agreement or the inability of our suppliers to manufacture our products to meet volume, performance and cost targets could have a material adverse effect on our business. For instance, a single supplier fabricates our pASIC1 and pASIC2 products under an agreement that expires in December 2005. While we may be able to purchase wafers after 2005, we do not have a firm capacity commitment from the supplier. If for any reason this or any other supplier becomes unable or unwilling to continue to provide services of acceptable quality, at acceptable costs and in a timely manner, our ability to deliver our products to our customers could be severely impaired. We would have to identify and qualify substitute suppliers, which could be time consuming and difficult and could result in unforeseen operational problems, or we could announce an end-of-life program for these products. Alternate suppliers might not be available to fabricate, assemble, test and program our devices or, if available, might be unwilling or unable to offer services on acceptable terms.

In addition, if competition for wafer manufacturing capacity increases, or if we need to migrate to more advanced wafer manufacturing technology, we may be required to pay or invest significant amounts to secure access to this capacity. The number of companies that provide these services is limited and some of them have limited operating histories and financial resources. In the event

our current suppliers refuse or are unable to continue to provide these services to us, we may be unable to procure services from alternate suppliers in a timely manner, if at all. Furthermore, if customer demand for our products increases, we may be unable to secure sufficient additional capacity from our current suppliers on commercially reasonable terms, if at all. Moreover, our reliance on a limited number of suppliers subjects us to reduced control over delivery schedules, quality assurance and costs. This lack of control may cause unforeseen product shortages or may increase our cost to manufacture, assemble or test testing our products, which would adversely affect our operating results and cash flows.

We record a majority of our inventory transactions based on information from our subcontractors. If we do not receive prompt and accurate information from our vendors, we could misstate inventory levels, incorrectly record gross profit, be unable to meet our delivery commitments to customers or commit to manufacturing inventory that is not required to meet customer delivery commitments, which could materially harm our business.

*Fluctuations in our manufacturing processes and product yields and quality, especially for new products, may increase our costs*

Difficulties encountered during the complex semiconductor manufacturing process can render a substantial percentage of semiconductor wafers nonfunctional, and manufacturing fluctuations may change the performance distribution of manufactured products. We have, in the recent past, experienced manufacturing runs that have contained substantially reduced or no functioning devices, or that generated devices with below normal performance. In addition, yield problems may take a significant period of time to analyze and correct. Our reliance on third party suppliers may extend the period of time required to analyze and correct these problems. As a result, we may incur substantially higher manufacturing costs and inventory shortages.

Yield fluctuations frequently occur in connection with the manufacture of newly introduced products, with manufacturing at new facilities or on new manufacturing processes. Newly introduced products and products that incorporate new intellectual property, such as our QuickMIPS, QuickPCI II and Eclipse II products, are often more complex and more difficult to produce, increasing the risk of manufacturing-related defects. New manufacturing facilities or processes, such as at Tower, are often more complex and take a period of time to achieve expected quality levels and product costs. While we test our products, they may still contain errors or defects that are found after we have commenced commercial production, that occur due to manufacturing variations or as new intellectual property is incorporated into our products. If our products contain undetected or unresolved defects, we may lose market share, experience delays in or loss of market acceptance, reserve or scrap inventory, or be required to issue a product recall. In addition, we would be at risk of product liability litigation if defects in our products are discovered. Although we attempt to limit our liability to end users through disclaimers of special, consequential and indirect damages and similar provisions, we cannot assure you that such limitations of liability will be legally enforceable.

*We have significant customers and limited visibility into the long-term demand for our products from these customers*

A few of our end customers can represent a significant portion of our total revenue in a given reporting period. As in the past, future demand from these customers may fluctuate significantly. These customers typically order products with short requested delivery lead times, and do not provide a firm commitment to purchase product past the period covered by purchase orders. In addition, our manufacturing lead times are longer than the delivery lead times requested by these customers, and we make significant inventory purchases in anticipation of future demand. For example, a Chinese customer, purchasing product through a distributor, represented 14% of our total revenue in 2003, but only 3% of revenue in 2004. If revenue from any significant customer were to decline substantially, we may be unable to offset this decline with increased revenue from other customers and we may purchase excess inventory. These factors could severely harm our business.

In addition, we may have made a significant investment in long-lived assets for the production of our products based upon historical and expected demand. If demand for or gross margin generated from our products does not meet our expectations, we may be required to write-off inventory or incur charges against long-lived assets, which would materially harm our business.

*We will be unable to compete effectively if we fail to anticipate product opportunities based upon emerging technologies and standards and fail to develop products that incorporate these technologies and standards*

We may spend significant time and money to design and develop products around an industry standard or emerging technology. To date, we have introduced products, such as QuickPCI, that are designed to support a specific industry standard. Additionally, customers may shift their demand to environmentally friendly products, such as products manufactured with lead-free assembly components, that we may not have developed. If an industry standard or emerging technology that we have targeted fails to achieve broad market acceptance, or if we are unable to bring the technology to market in a timely manner, we may be unable to generate significant revenue from our research and development efforts. As a result, our business would be materially harmed and we may be required to write-off related inventory and long-lived assets.

We have the capability and capacity to design and develop only a limited number of products that support specific industry standards. If systems manufacturers move away from the use of industry standards that we support with our products and adopt alternative standards, we may be unable to design and develop new products that conform to these new standards. Typically, the expertise required is unique to each industry standard, and we would likely have to either hire individuals with the required expertise or acquire such expertise through a licensing arrangement. The demand for individuals with the

necessary expertise to develop a product relating to a particular industry standard is generally high, and we may not be able to hire such individuals. The cost to acquire such expertise through licensing or other means may be high and such arrangements may not be possible in a timely manner, if at all.

*We may not have the liquidity to support our future operations and capital requirements*

Our cash balance at March 31, 2005 was \$24.6 million. At March 31, 2005, our interest-bearing debt consisted of \$4.0 million outstanding from Silicon Valley Bank and \$571,000 outstanding under a capital lease. At March 31, 2005, we had approximately \$6.0 million available to borrow under our revolving credit facility and approximately \$1.1 million available to borrow under our equipment line of credit. We are currently negotiating a renewal of our credit facility with Silicon Valley Bank which expires on June 27, 2005. If these negotiations do not result in a renewal of our credit facility, we would be required to pay any outstanding balances on the revolving credit facility. We held 1,344,543 Tower Ordinary Shares available for sale worth approximately \$2.4 million based upon the market closing price of \$1.82 per share at the end of our reporting period. However, our ability to obtain competitive pricing from Tower is tied to our ownership of at least 450,000 of these Tower shares.

Capital expenditures, which are largely driven by the introduction and initial manufacturing of new products, could be up to \$5.0 million in the next twelve months. As of March 31, 2005, we had commitments to purchase \$4.9 million of wafer inventory.

As a result of these potential investments, as well as research and development, selling, marketing and administrative expenses, changes in working capital and interest and debt payments, we will need to generate higher revenue and gross profit, especially from our Eclipse II and QuickPCI II products, to achieve positive cash flow. Whether we can achieve cash flow levels sufficient to support our operations cannot be accurately predicted. Unless such cash flow levels are achieved, we may borrow additional funds or sell debt or equity securities, or some combination thereof, to provide funding for our operations. If adequate funds are not available when needed, our financial condition and operating results would be materially adversely affected and we may not be able to operate our business without significant changes in our operations, or at all.

*We have a history of losses and cannot assure you that we will remain profitable in the future*

We incurred significant losses in 2004, 2003 and 2002. Our accumulated deficit as of March 31, 2005 was \$118.8 million. Although we recorded net income of \$864,000 for the three months ended March 31, 2005, we may not remain profitable in any future periods. Our recent revenue growth, net income for the three months ended March 31, 2005 and our profitability in certain years prior to 2001 cannot be relied upon as any indication of the Company's future operating results or prospects.

*If we fail to adequately forecast demand for our products, we may incur product shortages or excess product inventory*

Our agreements with third-party manufacturers require us to provide forecasts of our anticipated manufacturing orders, and place binding manufacturing commitments in advance of receiving purchase orders from our customers. This may result in product shortages or excess product inventory because we are limited in our ability to increase or decrease our forecasts under such agreements. Obtaining additional supply in the face of product shortages may be costly, or not possible, especially in the short term since most of our products have only a single fabrication and assembly source. Our failure to adequately forecast demand for our products could materially harm our business.

*We depend upon third party distributors to market and sell our products, and they may discontinue sale of our products, fail to give our products priority or be unable to successfully market, sell and support our products*

We contract with third-party distributors to market and sell a significant portion of our products. We typically have only a few distributors serving each geographic market, and, in the future, we may have a single distributor covering a geographic market. Although we have contracts with our distributors, our agreements with them may be terminated on short notice by either party and, if terminated, we may be unable to recruit additional or replacement distributors. As a result, our future performance will depend in part on our ability to retain our existing distributors and attract new distributors that will be able to effectively market, sell and support our products. The loss of one or more of our principal distributors, or our inability to attract new distributors, could materially harm our business.

Many of our distributors, including our principal distributors, market and sell products for other companies, and many of these products may compete directly or indirectly with our products. We generally are not one of the principal suppliers of products to our distributors. If our distributors give higher priority or greater attention to the products of other companies,

including products that compete with our products, our business would be materially harmed.

Individual distributors and OEM customers often represent a significant portion of our accounts receivable. If we are unable to collect funds due from these distributors and customers, our financial results may be materially harmed.

*Our future operating results are likely to fluctuate and therefore may fail to meet expectations, which could cause our stock price to decline*

Our operating results have varied widely in the past and are likely to do so in the future. In addition, our past operating results may not be an indicator of future operating results. Our future operating results will depend on many factors and may fail to meet our expectations for a number of reasons, including those set forth in these risk factors. Any failure to meet expectations could cause our stock

price to significantly fluctuate or decline.

Factors that could cause our operating results to fluctuate include:

- a significant change in sales to our largest customers;
- successful development and market acceptance of our products;
- our ability to accurately forecast product volumes and mix, and to respond to rapid changes in customer demand;
- the effect of end-of-life programs;
- changes in product mix or production variances that affect gross profit;
- our ability to adjust our manufacturing capacity and costs in response to economic and competitive pressures;
- our reliance on subcontract manufacturers for product capacity, yield and quality;
- our competitors' product portfolio and product pricing policies;
- timely implementation of efficient manufacturing technologies;
- changes in accounting and corporate governance rules;
- impact of import and export laws and regulations;
- the cyclical nature of the semiconductor industry and general economic, market, political and social conditions in the countries where we sell our products and the related effect on our customers, distributors and suppliers; and
- our ability to obtain capital, debt financing and insurance on commercially reasonable terms.

Although certain of these factors are out of our immediate control, unless we can anticipate and be prepared with contingency plans that respond to these factors, our business may be materially harmed.

*Our customers may cancel or change their product plans after we have expended substantial time and resources in the design of their products*

If one of our potential customers cancels, reduces or delays product orders from us or chooses not to release equipment that incorporates our products after we have spent substantial time and resources in assisting them with their product design, our business could be materially harmed. Our customers often evaluate our products for six months or more before designing them into their systems, and they may not commence volume shipments for up to an additional six to twelve months, if at all. During this lengthy sales cycle, our potential customers may also cancel or change their product plans. Even when customers incorporate one or more of our products into their systems, they may discontinue production. Customers whose products achieve high volume production may choose to replace our products with lower cost semiconductors.

*We may encounter periods of industry-wide semiconductor oversupply, resulting in pricing pressure, as well as undersupply, resulting in a risk that we could be unable to fulfill our customers' requirements*

The semiconductor industry has historically been characterized by wide fluctuations in the demand for, and supply of, its products. These fluctuations have resulted in circumstances when supply of and demand for semiconductors have been widely out of balance. An industry-wide semiconductor oversupply could result in severe downward pricing pressure from customers. In a market with undersupply of manufacturing capacity, we would have to compete with larger foundry customers for limited manufacturing resources. In such an environment, we may be unable to have our products manufactured in a timely manner, at a cost that generates adequate gross profit, or in sufficient quantities. Since we outsource

all of our manufacturing and have only a single-source of wafer supply, test and assembly for most of our products, we are particularly vulnerable to such supply shortages and capacity limitations. As a result, we may be unable to fulfill orders and may lose customers. Any future industry-wide oversupply or undersupply of semiconductors could materially harm our business.

*Customers may cancel or defer significant purchase orders or our distributors may return our products, which would cause our inventory levels to increase and our revenue to decline*

Our distributors or customers may cancel purchase orders at any time with little or no penalty. Contractually, our distributors are generally permitted to return unprogrammed products worth up to 10%, by value, of the products they purchase from us. If our distributors or customers cancel or defer significant purchase orders or return our products, our accounts receivable collections would decrease and inventories would increase, which would materially harm our business.

*Problems associated with international business operations could affect our ability to manufacture and sell our products*

Most of our products are manufactured outside of the United States at manufacturing facilities operated by our suppliers in Taiwan, South Korea, the Philippines, Israel and Malaysia. We expect to manufacture a majority of the products that we currently have under development in Israel and to assemble these products in South Korea, the Philippines or Malaysia. As a result, these manufacturing

operations and new product introductions are subject to risks of political instability, including the risk of conflict between Taiwan and the People's Republic of China, between South Korea and North Korea, and conflicts involving Israel or Malaysia.

A significant portion of our total revenue comes from sales to customers located outside the United States. We anticipate that sales to customers located outside the United States will continue to represent a significant portion of our total revenue in future periods. In addition, most of our domestic customers sell their products outside of North America, thereby indirectly exposing us to risks associated with foreign commerce and economic instability. In addition to overseas sales offices, we have significant research and development activities in Canada and India. Accordingly, our operations and revenue are subject to a number of risks associated with foreign commerce, including the following:

- managing foreign distributors;
- staffing and managing foreign offices;
- political and economic instability;
- foreign currency exchange fluctuations;
- changes in tax laws, import and export regulations, tariffs and freight rates;
- timing and availability of export licenses;
- supplying products that meet local environmental regulations;
- inadequate protection of intellectual property rights; and
- obtaining governmental approvals for certain products.

In the past, we have denominated sales of our products to foreign countries exclusively in U.S. dollars. As a result, any increase in the value of the U.S. dollar relative to the local currency of a foreign country will increase the price of our products in that country so that our products become relatively more expensive to customers in the local currency of that foreign country. As a result, sales of our products in that foreign country may decline. To the extent any such risks materialize, our business could be materially harmed.

In addition, we incur costs in foreign countries that may be difficult to reduce quickly because of employee-related laws and practices in those foreign countries.

*Many systems manufacturers may be unwilling to switch to our products because of their familiarity with the products offered by our direct competitors, such as Xilinx and Altera, which dominate the programmable logic market*

The semiconductor industry is intensely competitive and characterized by:

- erosion of selling prices over product lives;
- rapid technological change;

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- short product life cycles; and
- strong domestic and foreign competition.

If we are not able to compete successfully in this environment, our business will be materially harmed.

Many of our competitors have substantially greater financial, technical, manufacturing, marketing, sales, distribution, name recognition and other resources than we do. In addition, many of our competitors have well-established relationships with our current and potential customers and have extensive knowledge of system applications. In the past, we have lost potential customers to competitors for various reasons, including, but not limited to, re-programmability and lower price. Our current direct competitors include suppliers of complex programmable logic devices and field programmable gate arrays, such as Xilinx, Inc., Altera Corporation, Actel Corporation, and Lattice Semiconductor Corporation. Xilinx and Altera together have a majority share of the programmable logic market. Many systems manufacturers may be unwilling or unable to switch to our products due to their familiarity with competitors' products or other inhibiting factors.

We also face competition from companies that offer ASICs, which may be purchased for a lower price at higher volumes and typically have greater logic capacity, additional features and higher performance than those of our products. We may also face competition from suppliers of embedded microprocessors, such as Freescale Semiconductor, Inc. (formerly Motorola), or from suppliers of products based on new or emerging technologies. Our inability to successfully compete in any of the following areas could materially harm our business:

- the development of new products and advanced manufacturing technologies;
- the quality, performance characteristics, price and availability of devices, programming hardware and software development tools;
- the ability to engage with companies that provide synergistic products and services;

- the incorporation of industry standards in our products;
- the diversity of product offerings available to customers; or
- the quality and cost effectiveness of design, development, manufacturing and marketing efforts.

*We may be unable to successfully grow our business if we fail to compete effectively with others to attract and retain key personnel*

We believe our future success will depend upon our ability to attract and retain engineers and other highly competent personnel. Our employees are at-will and not subject to employment contracts. Hiring and retaining qualified sales and technical personnel is difficult due to the limited number of qualified professionals. Competition for these types of employees is intense. In addition, new hires frequently require extensive training before they achieve desired levels of productivity. We have in the past experienced difficulty in recruiting and retaining qualified senior management, sales and technical personnel. Failure to attract, hire, train and retain personnel could materially harm our business.

*We may be unable to adequately protect our intellectual property rights, and may face significant expenses as a result of future litigation*

Protection of intellectual property rights is crucial to our business, since that is how we keep others from copying the innovations that are central to our existing and future products. From time to time, we receive letters alleging patent infringement or inviting us to license other parties' patents. We evaluate these requests on a case-by-case basis. These situations may lead to litigation if we reject the offer to obtain the license.

We have in the past and are currently involved in litigation relating to alleged infringement by us of others' patents or other intellectual property rights. This kind of litigation is expensive and consumes large amounts of management's time and attention. Additionally, matters that we initially consider not material to our business could become costly. For example, we incurred substantial costs associated with the litigation and settlement of our dispute with Actel, which materially harmed our business. In addition, if the letters we sometimes receive alleging patent infringement or other similar matters result in litigation that we lose, a court could order us to pay substantial damages and/or royalties, and prohibit us from making, using, selling or importing essential technologies. For these and other reasons, this kind of litigation could materially harm our business.

Also, although we may seek to obtain a license under a third party's intellectual property rights in order to bring an

end to certain claims or actions asserted against us, we may not be able to obtain such a license on reasonable terms, or at all. We have entered into technology license agreements with third parties which give those parties the right to use patents and other technology developed by us, and which give us the right to use patents and other technology developed by them. We anticipate that we will continue to enter into these kinds of licensing arrangements in the future; however, it is possible that desirable licenses will not be available to us on commercially reasonable terms. If we lose existing licenses to key technology, or are unable to enter into new licenses that we deem important, it could materially harm our business.

Because it is critical to our success that we continue to prevent competitors from copying our innovations, we intend to continue to seek patent and trade secret protection for our products. The process of seeking patent protection can be long and expensive, and we cannot be certain that any currently pending or future applications will actually result in issued patents, or that, even if patents are issued, they will be of sufficient scope or strength to provide meaningful protection or any commercial advantage to us. Furthermore, others may develop technologies that are similar or superior to our technology or design around the patents we own. We also rely on trade secret protection for our technology, in part through confidentiality agreements with our employees, consultants and other third parties. However, employees may breach these agreements, and we may not have adequate remedies for any breach. In any case, others may come to know about or determine our trade secrets through a variety of methods. In addition, the laws of certain territories in which we develop, manufacture or sell our products may not protect our intellectual property rights to the same extent as the laws of the United States.

*We may engage in manufacturing, distribution or technology agreements that involve numerous risks, including the use of cash, diversion of resources and significant write-offs*

We have entered into and, in the future, intend to enter into agreements that have involved numerous risks, including the use of significant amounts of our cash; diversion from other development projects or market opportunities; our ability to incorporate licensed technology in our products; our ability to introduce related products in a cost-effective and timely manner; our ability to collect amounts due under these contracts; and market acceptance of related products. For instance, we have licensed certain microprocessor technology from MIPS Technologies and obtained other elements of our products from other third-party companies. In the fourth quarter of 2004, we determined that the expected revenue and gross profit from the products incorporating the third party elements would not be sufficient to recover the carrying value of the related third party elements and other long-lived assets, and we recorded a \$3.2 million long-lived asset impairment charge. If we fail to recover the cost of these or other assets from the cash flow generated by the related products, our assets will become impaired and our financial results would be harmed.

*Our business is subject to the risks of earthquakes, other catastrophic events and business interruptions for which we may maintain limited insurance*

Our operations and the operations of our suppliers are vulnerable to interruption by fire, earthquake, power loss, flood, terrorist acts and other catastrophic events beyond our control. In particular, our headquarters is located near earthquake fault lines in the San Francisco Bay area. In addition, we rely on sole suppliers to manufacture our products and would not be able to qualify an alternate

supplier of our products for several quarters. Our suppliers often hold significant quantities of our inventory which, in the event of a disaster, could be destroyed. In addition, our business processes and systems are vulnerable to computer viruses, break-ins, and similar disruptions from unauthorized tampering. Any catastrophic event, such as an earthquake or other natural disaster, the failure of our computer systems, war or acts of terrorism, could significantly impair our ability to maintain our records, pay our suppliers, or design, manufacture or ship our products. The occurrence of any of these events could also affect our customers, distributors and suppliers and produce similar disruptive effects upon their business. If there is an earthquake or other catastrophic event near our headquarters, our customers' facilities, our distributors' facilities or our suppliers' facilities, our business could be seriously harmed.

We do not have a detailed disaster recovery plan. In addition, we do not maintain sufficient business interruption and other insurance policies to compensate us for all losses that may occur. Any losses or damages incurred by us as a result of a catastrophic event or any other significant uninsured loss could have a material adverse effect on our business.

*Our principal stockholders have significant voting power and may vote for actions that may not be in the best interests of our other stockholders*

Our officers, directors and principal stockholders together control a significant portion of our outstanding common stock. As a result, these stockholders, if they act together, will be able to significantly influence our operations, affairs and all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions. This concentration of ownership may have the effect of delaying or preventing a change in control and might affect the

market price of our common stock. This concentration of ownership may not be in the best interest of our other stockholders.

*Our Shareholder Rights Plan, certificate of incorporation, bylaws and Delaware law contain provisions that could discourage a takeover that is beneficial to stockholders*

Our Shareholder Rights Plan as well as provisions of our certificate of incorporation, our bylaws and Delaware law could make it difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders.

*The market price of our common stock may fluctuate significantly and could lead to securities litigation*

Stock prices for many companies in the technology and emerging growth sectors have experienced wide fluctuations that have often been unrelated to the operating performance of such companies. In the past, securities class action litigation has often been brought against a company following periods of volatility in the market price of its securities. In the future, we may be the target of similar litigation. Securities litigation could result in substantial costs and divert management's attention and resources.

*Changes to existing accounting pronouncements or taxation rules or practices may cause adverse revenue fluctuations, affect our reported results of operations or how we conduct our business*

FASB has issued Statement 123R, "Share-Based Payment," which will require us to measure compensation costs for all stock based compensation (including stock options and our employee stock purchase plan, as currently constructed) at fair value and take a compensation charge equal to that value. If this accounting pronouncement had been in effect during the current period, we estimate that we would have reported a significantly lower net income or even a net loss.

New accounting pronouncements or taxation rules and varying interpretations of accounting pronouncements or taxation practice have occurred and may occur in the future. Any future changes in accounting pronouncements or taxation rules or practices may have a significant effect on how we report our results and may even affect our reporting of transactions completed before the change is effective. This change to existing rules, future changes, if any, or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business.

*Compliance with changing regulation of corporate governance and public disclosure may result in additional expenses*

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations and The Nasdaq National Market rules, are creating uncertainty for companies such as ours. These new or changed laws, regulations and standards are subject to varying interpretations in many cases due to their lack of specificity, and as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies, which could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices. We are committed to maintaining high standards of corporate governance and public disclosure. As a result, we intend to invest resources to comply with evolving laws, regulations and standards, and this investment may result in increased general and administrative expenses and a diversion of management time and attention from profit-generating activities to compliance activities. If our efforts to comply with new or changed laws, regulations and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to practice, our reputation may be harmed.

*While we believe that we currently have adequate internal control procedures in place, we are still exposed to potential risks from recent legislation requiring companies to evaluate controls under Section 404 of the Sarbanes-Oxley Act of 2002*

As of December 2004, we have evaluated our internal control systems in order to allow management to report on, and our independent registered public accounting firm to attest to, our internal controls, as required by Section 404 of the Sarbanes-Oxley Act. We performed the system and process evaluation and testing required in an effort to comply with the management certification and auditor



attestation requirements of Section 404. As a result, we are incurred additional expenses and a diversion of management's time. While we believe that our internal control procedures are adequate and we intend to continue to fully comply with the requirements relating to internal controls and all other aspects of Section 404, we cannot be certain as to the outcome of future evaluations, testing and remediation actions or the impact of the same on our operations. If we are not able to remain in compliance with the requirements of Section 404, we might be subject to sanctions or investigation by regulatory authorities, such as the SEC or The Nasdaq National Market. Any such action could adversely affect our financial results and the market price of our common stock.

*We have implemented import and export control procedures to comply with United States regulations but we are still exposed to potential risks from import and export activity*

Our products, technology and software are subject to U.S. import and export control laws and regulations which, in some instances, may impose restrictions on business activities, or otherwise require licenses or other authorizations from agencies such as the U.S. Department of State, U.S. Department of Commerce and U.S. Department of the Treasury. We have import and export licensing and compliance procedures in place for purposes of conducting our business consistent with U.S. laws and regulations, and we periodically review these procedures to maintain compliance with the requirements relating to import and export regulations. If we are not able to remain in compliance with import and export regulations, we might be subject to investigation, sanctions or penalties by regulatory authorities. Such penalties can include civil, criminal or administrative remedies (such as loss of export privileges). We cannot be certain as to the outcome of an evaluation, investigation, inquiry or other action or the impact of these items on our operations. Any such action could adversely affect our financial results and the market price of our common stock.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

#### **Interest Rate Risk**

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio and variable rate debt. We do not use derivative financial instruments to manage our interest rate risk. We are adverse to principal loss and ensure the safety and preservation of invested funds by limiting default, market and reinvestment risk. Our investment portfolio is generally comprised of investments that meet high credit quality standards. Since these securities are subject to interest rate risk, they could decline in value if interest rates fluctuate. Due to the short duration and conservative nature of our investment portfolio, we do not anticipate any material loss with respect to our investment portfolio. A 10% move in interest rates as of March 31, 2005 would have an immaterial effect on our financial position, results of operations and cash flows.

#### **Foreign Currency Exchange Rate Risk**

All of our sales and cost of manufacturing are transacted in U.S. dollars. We conducted a portion of our research and development activities in Canada and India and have sales and marketing offices in several locations outside of the United States. Most of the costs incurred at these international locations are in local currency. If these local currencies strengthen against the dollar, our payroll and other local expenses will be higher than we currently anticipate. Since our sales are transacted in U.S. dollars, this negative impact on expenses would not be offset by any positive effect on revenue. Operating expenses denominated in foreign currencies were approximately 26% and 23% of total operating expenses for the three months ended March 31, 2005 and 2004, respectively. A majority of these foreign expenses were incurred in Canada. A currency exchange rate fluctuation of 10% would have caused our operating expenses to change by approximately \$200,000 in the three months ended March 31, 2005.

### **Item 4. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934, as amended, is (i) recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, while no cost-effective control system will preclude all errors and irregularities, our current disclosure controls and procedures are effective to provide reasonable assurance that the financial statements and other disclosures in our SEC reports are reliable.

#### **Changes in Internal Controls Over Financial Reporting**

There were no changes in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## Part II. Other Information

### Item 1. Legal Proceedings

On October 26, 2001, a putative securities class action was filed in the U.S. District Court for the Southern District of New York against certain investment banks that underwrote QuickLogic's initial public offering, QuickLogic and some of QuickLogic's officers and directors. The complaint alleges excessive and undisclosed commissions in connection with the allocation of shares of common stock in QuickLogic's initial and secondary public offerings and artificially high prices through "tie-in" arrangements which required the underwriters' customers to buy shares in the aftermarket at pre-determined prices in violation of the federal securities laws. Plaintiffs seek an unspecified amount of damages on behalf of persons who purchased QuickLogic's stock pursuant to the registration statements between October 14, 1999 and December 6, 2000. Various plaintiffs have filed similar actions asserting virtually identical allegations against over 300 other public companies, their underwriters, and their officers and directors arising out of each company's public offering. These actions, including the action against QuickLogic, have been coordinated for pretrial purposes and captioned *In re Initial Public Offering Securities Litigation, 21 MC 92*. A stipulation of settlement for the claims against the issuer defendants, including the Company, has been signed and was submitted to the court. Under the stipulation of settlement, the plaintiffs will dismiss and release all claims against participating defendants in exchange for a contingent payment guaranty by the insurance companies collectively responsible for insuring the issuers in all the related cases, and the assignment or surrender to the plaintiffs of certain claims the issuer defendants may have against the underwriters. Under the guaranty, the insurers will be required to pay the amount, if any, by which \$1.0 billion exceeds the aggregate amount ultimately collected by the plaintiffs from the underwriter defendants in all the cases. On February 15, 2005, the court preliminarily approved the settlement contingent on specified modifications. The settlement is still subject to court approval and a number of other conditions. There is no guarantee that the settlement will become effective.

On July 3, 2003, a putative securities class action was filed in the U.S. District Court for the Southern District of New York by shareholders of Tower Semiconductor Ltd. against Tower, several of its directors, and several of its investors, including QuickLogic. QuickLogic was named solely as an alleged control person. On August 19, 2004, the court dismissed the claims against all defendants, including QuickLogic, with prejudice. On September 29, 2004, one of the plaintiffs filed a notice of appeal from the judgment.

### Item 6. Exhibits

#### a. Exhibits

The following Exhibits are filed with this report:

Exhibit Number	Description
3.2 (1)	Amended and Restated Bylaws of the Registrant.
10.19 (2)	2005 Executive Bonus Plan.
31.1	CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	CEO and CFO Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(1) Incorporated by reference to QuickLogic's Current Report on Form 8-K (Item 5.03) filed on May 2, 2005.

(2) Incorporated by reference to QuickLogic's Current Report on Form 8-K (Item 1.01) filed on May 2, 2005.

### Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

#### QUICKLOGIC CORPORATION

/s/ CARL M. MILLS

Carl M. Mills

*Vice President, Finance and Chief Financial Officer (as Principal Accounting and Financial Officer and on behalf of Registrant)*

Date: May 12, 2005

<b>Exhibit Number</b>	<b>Description</b>
3.2 (1)	Amended and Restated Bylaws of the Registrant.
10.19 (2)	2005 Executive Bonus Plan.
31.1	CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
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- (1) Incorporated by reference to QuickLogic's Current Report on Form 8-K (Item 5.03) filed on May 2, 2005.  
(2) Incorporated by reference to QuickLogic's Current Report on Form 8-K (Item 1.01) filed on May 2, 2005.

## CERTIFICATIONS

I, E. Thomas Hart, certify that:

1. I have reviewed this quarterly report on Form 10-Q of QuickLogic Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state 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 Rules 13a-15(f) and 15d-15(f)) for the registrant and 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 report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our 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 conclusions 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 most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) 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 the registrant's board of directors (or persons performing the equivalent functions):
  - (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 control over financial reporting.

Date: May 12, 2005

/s/ E. Thomas Hart

E. Thomas Hart

*Chief Executive Officer*

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I, Carl M. Mills, certify that:

1. I have reviewed this quarterly report on Form 10-Q of QuickLogic Corporation;
2. Based on my knowledge, this 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 Rules 13a-15(f) and 15d-15(f)) for the registrant and 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 report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our 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 conclusions 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 most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) 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 the registrant's board of directors (or persons performing the equivalent functions):
  - (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 control over financial reporting.

Date: May 12, 2005

/s/ Carl M. Mills  
Carl M. Mills  
*Chief Financial Officer*

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**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND 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, E. Thomas Hart, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of QuickLogic Corporation on Form 10-Q for the quarter ended April 3, 2005, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of QuickLogic Corporation.

By: /s/ E. Thomas Hart  
Date: May 12, 2005  
Name: E. Thomas Hart  
Title: *Chief Executive Officer*

I, Carl M. Mills, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of QuickLogic Corporation on Form 10-Q for the quarter ended April 3, 2005, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of QuickLogic Corporation.

By: /s/ Carl M. Mills  
Date: May 12, 2005  
Name: Carl M. Mills  
Title: *Chief Financial Officer*

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