MONOLITHIC POWER SYSTEMS INC
Form 10-K
February 16, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2009

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Commission file number: 000-51026

Monolithic Power Systems, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**77-0466789**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

6409 Guadalupe Mines Road, San Jose, CA 95120 (408) 826-0600

(Address of principal executive offices, including zip code and telephone number)

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

Title of each class	Name of each exchange on which registered
Common Stock, $0.001 Par Value	**The NASDAQ Global Select Market**

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933. ¨ Yes x No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934 (the Exchange Act). ¨ Yes x No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

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

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨ Smaller reporting company ¨

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

The number of shares of the registrant s stock outstanding as of June 30, 2009 was 34,256,923. The closing price of the registrant s common stock on the Nasdaq Global Select Market as of June 30, 2009 was $22.41. The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant based upon the closing price of the Common Stock on the Nasdaq Global Select Market on June 30, 2009 was $554,951,133.*

There were 35,235,634 shares of the registrant s common stock issued and outstanding as of February 2, 2010.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement for the registrant s 2010 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K to the extent stated herein. The Proxy Statement will be filed within 120 days of the registrant s fiscal year ended December 31, 2009.

* Excludes 9,493,374 shares of the registrant s common stock held by executive officers, directors and stockholders whose ownership exceeds 5% (affiliates) of the Common Stock outstanding at June 30, 2009. Exclusion of such shares should not be construed to indicate that any such person possesses the power, direct or indirect, to direct or cause the direction of the management or policies of the registrant or that such person is controlled by or under common control with the registrant.

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MONOLITHIC POWER SYSTEMS, INC.

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Except as the context otherwise requires, the terms Monolithic Power Systems , MPS , Registrant , Company , we , us , or our as used here references to Monolithic Power Systems, Inc. and its consolidated subsidiaries.

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FORWARD-LOOKING STATEMENTS

This annual report on Form 10-K and the documents incorporated herein by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that have been made pursuant to and in reliance on the provisions of the Private Securities Litigation Reform Act of 1995. These statements include among other things, statements concerning:

- the above-average industry growth of product and market areas that we have targeted,
- our plan to introduce additional new products within our existing product families as well as in new product categories and families,
- our belief that we will continue to incur significant legal expenses that vary with the level of activity in each of our legal proceedings,
- the impact of our outstanding litigation and changing market conditions on the revenue we derive from our CCFL product line,
- the effect of auction-rate securities on our liquidity and capital resources,
- the application of our products in the computer, consumer electronics, and communications markets continuing to account for a majority of our revenue,
- estimates of our future liquidity requirements,
- the cyclical nature of the semiconductor industry,
- protection of our proprietary technology,
- near term business outlook for 2010,
- the factors that we believe will impact our ability to achieve revenue growth,
- the percentage of our total revenue from various market segments, and
- the factors that differentiate us from our competitors.

In some cases, words such as would, could, may, should, predict, potential, targets, continue, anticipate, expect, intend, p estimate, project, forecast, will, the negative of these terms or other variations of such terms and similar expressions relating to the future identify forward-looking statements.

All forward-looking statements are based on our current outlook, expectations, estimates, projections, beliefs and plans or objectives about our business and our industry. These statements are not guarantees of future performance and are subject to risks and uncertainties. Actual results could differ materially from those predicted or implied in any such forward-looking statements.

Risks and uncertainties that could cause actual results to differ materially include those set forth throughout this annual report on Form 10-K and, in particular, in the section entitled Item 1A. Risk Factors .

We disclaim any duty to and undertake no obligation to update any forward-looking statements, whether as a result of new information relating to existing conditions, future events or otherwise or to release publicly the results of any future revisions we may make to forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Readers are cautioned not to place undue reliance on such statements, which speak only as of the date of this annual report on Form 10-K. Readers should carefully review future reports and documents that we file from time to time with the Securities and Exchange Commission, such as our quarterly reports on Form 10-Q and any current reports on Form 8-K.

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PART I

ITEM 1. BUSINESS

General

Monolithic Power Systems designs, develops and markets proprietary, advanced analog and mixed-signal semiconductors. We combine advanced process technology with our highly experienced analog designers to produce high-performance power management integrated circuits (ICs) for DC to DC converters, LED drivers, Cold Cathode Fluorescent Lamp (CCFL) backlight controllers, Class-D audio amplifiers, and other Linear ICs. Our products are used extensively in computing and network communications products, flat panel TVs, set top boxes and a wide variety of consumer and portable electronics products. We partner with world-class manufacturing organizations to deliver top quality, ultra-compact, high-performance solutions through productive, cost-efficient channels. Founded in 1997 and headquartered in San Jose, California, we have expanded our global presence with offices in Taiwan, China, Korea, Japan, and Europe, which operate under MPS International, Ltd.

Industry Overview

Semiconductors comprise the basic building blocks of electronic systems and equipment. Within the semiconductor industry, components can be classified either as discrete devices, such as individual transistors, or as ICs, in which a number of transistors and other elements are combined to form a more complicated electronic circuit. ICs can be further divided into three primary categories: digital, analog, and mixed-signal. Digital ICs, such as memory devices and microprocessors, can store or perform arithmetic functions on data that is represented by a series of ones and zeroes. Analog ICs, in contrast, handle real world signals such as temperature, pressure, light, sound, or speed. In addition, analog ICs also perform power management functions, such as regulating or converting voltages, for electronic devices. Mixed-signal ICs combine digital and analog functions onto a single chip and play an important role in bridging real world phenomena to digital systems.

Analog and Mixed-Signal Markets. We focus on the market for high performance analog and mixed-signal ICs. High performance products generally are differentiated by functionality and performance factors which include integration of higher levels of functionality onto a single chip, greater precision, higher speed and lower heat and noise. There are several key factors that distinguish analog and mixed-signal IC markets from digital IC markets and in particular the high performance portion of the analog and mixed signal IC market. These factors include longer product life cycles, numerous market segments, technology that is difficult to replicate, relative complexity of design and process technology, importance of experienced design engineers, lower capital requirements and diversity of end markets. We have, however, targeted product and market areas that we believe have the ability to offer above average industry growth over the long term.

Products and Applications

We currently have three primary product families that address multiple applications within the computing, consumer electronics, and communications markets. Our products are differentiated with respect to their high degree of integration and strong levels of accuracy and efficiency, making them cost-effective relative to many competing solutions. These product families include:

Direct Current (DC) to DC Converters. DC to DC converter ICs are used to convert and control voltages within a broad range of electronic systems, such as portable electronic devices, wireless LAN access points, computers, set top boxes, automobiles and medical equipment. We believe that our DC to DC converters are differentiated in the market, particularly with respect to their

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high degree of integration and rapid switching speeds. These features are important to our customers as they result in fewer components, a smaller form factor, more accurate regulation of voltages, and, ultimately, lower system cost and increased reliability through the elimination of many discrete components and power devices.

Lighting Control Products. Lighting control ICs are used in backlighting and general illumination products. Lighting control ICs for backlighting are used in systems that provide the light source for LCD panels typically found in notebook computers, LCD monitors, car navigational systems, and LCD televisions. Backlighting solutions are typically either cold cathode fluorescent lamps (CCFL) or WLED lighting sources. The CCFL ICs function by converting low-voltage direct current (DC) or battery voltage to high-voltage alternating current (AC). We believe our CCFL ICs were the first to utilize a full bridge resonant topology that allows for high efficiency, extended lifetimes for cold cathode fluorescent lamps (CCFLs), and lower signal interference with adjacent components. The full bridge topology is now the industry standard for these products. WLED lighting control ICs step-up or step-down a DC voltage and provide efficient precision power and protection to a LED string or to multiple LED strings.

Audio Amplifiers. Audio amplifier ICs are used to amplify sound produced by audio processors. We currently offer Class-D audio amplifiers, which are well-suited for applications that require both a small form factor and high power efficiency, such as plasma televisions, LCD televisions and DVD players. With today s systems becoming smaller and utilizing larger amounts of power, solution sizes and the management of heat dissipation are becoming increasingly important to the overall system design. The high degree of power efficiency and small form factor provided by our Class-D audio amplifiers allows system vendors to significantly reduce heat dissipation, eliminating the costly and sizable fans and heat sinks traditionally required by audio amplifier ICs. These features enable our customers to achieve their design and cost objectives without sacrificing sound quality.

We currently target our products at the consumer electronics, communications and computing markets, with the consumer market representing the largest portion of our revenue.

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The following is a brief summary of our product family solutions for various applications. For each of these applications, we are currently shipping product or have design wins, which are decisions by original equipment manufacturers, or OEMs, or original design manufacturers, or ODMs, to use our ICs:

Application	WLED Lighting Illumination (non-backlight)	LCD Backlight (Inverters or WLED)	DC to DC Converters (Buck & Boost)	µP Reset & Supervisory	Audio Amplifiers	Xenon Flash	Chargers (Switching & Linear)	Current Limit Switches
Computing								
Computers and PDA devices		X	X	X	X		X	X
LCD Monitors		X	X	X	X			
Disk Drives/Storage Networks			X					X
Consumer Electronics								
LCD TV Displays		X	X	X	X			X
Plasma TV Displays		X	X	X	X			X
Set Top Boxes			X	X	X			X
Blu-Ray & DVD Players		X	X	X	X			
Digital Still Cameras			X	X	X	X	X	
Commercial & Industrial Bulb & CFL Replacement	X							
GPS and Infotainment systems		X	X	X	X			X
Communications								
Cellular Handsets			X		X	X	X	
Networking Infrastructure			X	X				
VOIP			X	X				
Wireless Access Points			X	X				

We derive a majority of our revenue from the sales of our DC to DC converter IC product family to the computing, consumer electronics and communications markets. In the future, we will continue to introduce additional new products within our existing product families, such as high current, high voltage, small form factor switching voltage regulators, as well as expand our newer product families in battery chargers, voltage references and low dropout regulators. Our ability to achieve revenue growth will depend in part upon our ability to enter new market segments, gain market share, grow in regions outside of Greater China, expand our customer base and successfully secure manufacturing capacity.

Please refer to the table showing our revenue by product family in the section entitled Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Operations .

Customers, Sales, and Marketing

We sell our products through third party distributors, value-added resellers and directly to OEMs, ODMs, and electronic manufacturing service (EMS) providers. Our third party distributors are subject to distribution agreements with us which allow the distributor to sell our products to end customers and other resellers. Distributors may distribute our products to end customers which include OEMs, ODMs or EMS providers. Our value-added resellers may second source our products and provide other services to customers. ODMs typically design and manufacture electronic products on behalf of OEMs, and EMS providers typically provide manufacturing services for OEMs and other electronic product suppliers. The following is a summary for the years ended December 31, 2009, 2008 and 2007 of those customers that accounted for more than 10% of our total revenue in one or more of these years:

	Revenue Year ended December 31,		
Customers	**2009**	**2008**	**2007**
A	13%	20%	18%
B	10%	10%	15%
C	10%	*	*

Current distribution agreements with several of our major distributors provide that each distributor shall have the non-exclusive right to sell and use its best efforts to promote and develop a market for our products in several countries in Asia. These agreements may be terminated by either us or the distributor on up to three months notice. These agreements provide that payment for purchases from us will generally occur within 30 to 45 days from the date of invoice. In addition, we allow for limited stock rotation in certain agreements.

We have sales offices located in the United States, Taiwan, China, Korea and Japan and have marketing representatives in Europe. Our products typically require a highly technical sales and applications engineering effort where we assist our customers in the design and use of our products in their application. We maintain a staff of applications engineers who work directly with our customers engineers in the development of their systems electronics containing our products.

Because our sales are billed and payable in United States dollars, our sales are not directly subject to fluctuating currency exchange rates. However, because 84% of our revenue in 2009 was attributable to direct or indirect sales to customers in Asia, changes in the relative value of the dollar may create pricing pressures for our products.

Our sales are made primarily pursuant to standard individual purchase orders. Our backlog consists of orders that we have received from customers which have not yet shipped. Our shippable backlog at December 31, 2009 was $27.8 million. We believe that backlog is not necessarily a good indicator of our future sales. Order lead times may vary, and, as is common within our industry, customers are allowed to reschedule or cancel orders on relatively short notice. Our quarterly revenue is also influenced by orders booked and shipped within that quarter which are not reflected as backlog at the end of any preceding quarter. Our manufacturing lead times are generally 4 to 12 weeks and we often build inventory in advance of customer orders based on our forecast of future customer orders. This subjects us to certain risks, most notably the possibility that sales will not meet our forecast, which could lead to inventories in excess of demand. If excess inventory exists, it may be necessary for us to sell it at a substantial discount or dispose of it altogether, either of which would negatively affect our profit margins.

We operate in the cyclical semiconductor industry where there is seasonal demand for certain of our products. While we are not and will not be immune from current and future industry downturns, we have targeted product and market areas that we believe have the ability to offer above average industry performance over the long term.

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Research and Development

We have assembled a qualified team of engineers in the United States, China and Europe with core competencies in analog and mixed-signal design. Through our research and development efforts, we have developed a collection of intellectual property and know-how that we are able to leverage across our products and markets. These include the development of high efficiency power devices, the design of precision analog circuits, expertise in mixed-signal integration and the development of proprietary semiconductor process technologies.

Our research and development efforts are generally targeted at three areas: systems architecture, circuit design and implementation, and process technology. In the area of systems architecture, we are exploring new ways of solving our customers system design challenges and are investing in the development of systems expertise in new markets and applications that align well with our core capabilities. In the area of circuit design and implementation, our initiatives include expanding our portfolio of products and adding new features to our products.

Please refer to the discussion of the amount spent on research and development during each of the last three fiscal years in the section entitled Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Operations Research and Development . In the area of process technology, we are investing research and development resources to provide leading-edge analog power processes for our next generation of integrated circuits. Process technology is a key strategic component to our future growth.

Patents and Intellectual Property Matters

We rely on our proprietary technologies, which include both our proprietary circuit designs for our products and our proprietary manufacturing process technologies. Our future success and competitive position depend in part upon our ability to obtain and maintain protection of our proprietary technologies.

In general, we have elected to pursue patent protection for aspects of our circuit designs that we believe are patentable and to protect our manufacturing process technologies by maintaining those process technologies as trade secrets. As of January 11, 2010 we had approximately 309 patents issued and pending, of which 55 have been issued in the United States. Our U.S. issued patents are scheduled to expire at various times through August 2027 and our other issued patents are scheduled to expire at various times through December 2027. Our patents are material to our business, but we do not rely on any one particular patent for our success. We also rely on a combination of nondisclosure agreements and other contractual provisions, as well as our employees commitment to confidentiality and loyalty, to protect our technology, know-how, and processes. We have entered into a patent license agreement with another integrated circuit company, pursuant to which we have granted this company a license (with certain limited sublicense rights) under certain of our patents to make, use, and sell certain of this company s own integrated circuit products for a period of two years ending in 2011, and for which this company is obligated to pay us royalties based on sales of those products. We also seek to register certain of our trademarks as we deem appropriate. We have not registered any of our copyrights and do not believe registration of copyrights is material to our business. Despite precautions that we take, it may be possible for unauthorized third parties to copy aspects of our current or future technology or products or to obtain and use information that we regard as proprietary. There can be no assurance that the steps we take will be adequate to protect our proprietary rights, that our patent applications will lead to issued patents, that others will not develop or patent similar or superior products or technologies, or that our patents will not be challenged, invalidated, or circumvented by others. Furthermore, the laws of the countries in which our products are or may be developed, manufactured or sold may not protect our products and intellectual property rights to the same extent as laws in the United States. Our failure to adequately protect our proprietary technologies could harm our business.

The semiconductor industry is characterized by frequent claims of infringement and litigation regarding patent and other intellectual property rights, such as our litigation with O2Micro International Limited (O2Micro) and Linear Technology Corporation (Linear). For a more complete description of our legal matters, please read the section entitled Item 3. Legal Proceedings and Note 10 to our consolidated financial statements. Patent infringement is an ongoing risk, in part because other companies in our industry could have patent rights that may not be identifiable when we initiate development efforts. Litigation may be necessary to enforce our intellectual property rights, and we may have to defend ourselves against infringement claims. Any such litigation could be very costly and may divert our management resources. Further, we have agreed to indemnify certain of our customers and a supplier in some circumstances against liability from infringement by our products. In the event any third party were to make an infringement claim against us or our customers, we could be enjoined from selling selected products or could be required to indemnify our customers or supplier or pay royalties or other damages to third parties. If any of our products is found to infringe and we are unable to obtain necessary licenses or other rights on acceptable terms, we would either have to change our product so that it does not infringe or stop making the infringing product, which could have a material adverse effect on our operating results, financial condition, and cash flows.

Manufacturing

We utilize a fabless business model, working with third parties to manufacture and assemble our integrated circuits. This fabless approach allows us to focus our engineering and design resources on our strengths and to reduce our fixed costs and capital expenditures. In contrast to many fabless semiconductor companies, who utilize standard process technologies and design rules established by their foundry partners, we have developed our own proprietary process technology and collaborate with our foundry partners to install our technology on their equipment in their facilities for use solely on our behalf. This close collaboration and control over the manufacturing process has historically resulted in favorable yields and product performance for our integrated circuits.

We currently contract with two suppliers to manufacture our wafers in foundries located in China. Once our silicon wafers have been produced, they are shipped to our facility in Chengdu, China for wafer sort. Our semiconductor products are then assembled and packaged by independent subcontractors in Malaysia and China. The assembled ICs are then sent for final testing at our Chengdu facility prior to shipping to our customers.

In September 2004, we signed an agreement with a Chinese local authority to construct a facility in Chengdu, China, initially for the testing of our ICs. Pursuant to this agreement, we agreed to contribute capital in the form of cash, in-kind assets, and/or intellectual property, of at least $5.0 million to our wholly-owned Chinese subsidiary as the registered capital for the subsidiary and have exercised the option to purchase land use rights for the facility for approximately $0.2 million. We also have the option to acquire the facility after a five-year lease term for the original construction cost less rents paid, which is currently estimated at $2.0 million, which option becomes exercisable in March 2011. We will likely enter into a purchase agreement for this facility at the end of the lease term. The facility has been fully operational since 2006 and we have benefitted from shorter manufacturing cycle times and lower labor and overhead costs. Furthermore, we are continuing to expand our product testing capabilities in our China facility and are able to take advantage of the rich pool of local engineering talent to expand our manufacturing support and engineering operations.

Key Personnel and Employees

Our performance is substantially dependent on the performance of our executive officers and key employees. Due to the relative complexity of the design of our analog and mixed-signal ICs, our engineers generally have more years of experience and greater circuit design aptitude than the more prevalent digital circuit design engineer. Analog engineers with advanced skills are limited in number

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and difficult to replace. The loss of the services of key officers, managers, engineers and other technical personnel would harm the business. Our future success will depend, in part, on our ability to attract, train, retain, and motivate highly qualified technical and managerial personnel. We may not be successful in attracting and retaining such personnel. Our employees are not represented by a collective bargaining organization, and we have never experienced a work stoppage or strike. Our management considers employee relations to be good. As of December 31, 2009, we employed 692 employees located in the United States, Taiwan, China, Japan, Korea and Europe.

Competition

The analog and mixed-signal semiconductor industry is highly competitive, and we expect competitive pressures to continue. Our ability to compete effectively and to expand our business will depend on our ability to continue to recruit both applications engineering and design engineering personnel, our ability to introduce new products, and our ability to maintain the rate at which we introduce these new products. Our industry is characterized by decreasing unit selling prices over the life of a product. We compete with domestic and international semiconductor companies, many of which have substantially greater financial and other resources with which to pursue engineering, manufacturing, marketing, and distribution of their products. We are in direct and active competition, with respect to one or more of our product lines, with at least 10 manufacturers of such products, of varying size and financial strength. The number of our competitors has grown due to expansion of the market segments in which we participate. We consider our primary competitors to include Fairchild Semiconductor International, Intersil Corporation, Linear Technology, Maxim Integrated Products, Micrel Inc., Microsemi Corporation, National Semiconductor Corporation, O2Micro International, Richtek Technology Corporation, Rohm Co., Ltd., Semtech Corporation, STMicroelectronics N.V., Texas Instruments Incorporated and Volterra.

We expect continued competition from existing competitors as well as competition from new entrants into the semiconductor market. We believe that we are competitive with respect to these factors, particularly because our ICs typically are smaller in size, are highly integrated, possess higher levels of power management functionalities and achieve high performance specifications at lower price points than most of our competition. However, we cannot assure you that our products will continue to compete favorably or that we will be successful in the face of increasing competition from new products and enhancements introduced by existing competitors or new companies entering this market.

Geographical and Segment Information

Please refer to the geographical and segment information for each of the last three fiscal years in Note 13 to our consolidated financial statements.

Please refer to the discussion of risks attendant to our foreign operations in the section entitled Item 1A: Risk Factors .

Available Information

We were incorporated in California in 1997 and reincorporated in Delaware in November 2004. Our executive offices are located at 6409 Guadalupe Mines Road, San Jose, CA 95120. Our telephone number is (408) 826-0600. Our e-mail address is investors@monolithicpower.com, and our website is www.monolithicpower.com. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those filed or furnished pursuant to Sections 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, are available free of charge. These may be obtained from our website, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission, or at the SEC website at www.sec.gov. Information contained on our website is not a part of this Form 10-K.

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Executive Officers of the Registrant

The executive officers of the Company, and their ages as of February 1, 2010 are as follows:

Name	Age	Position
Michael R. Hsing	50	President, Chief Executive Officer, and Director
Rick Neely	55	CFO, Senior Vice President of Finance and Principal Financial and Accounting Officer
Deming Xiao	47	President of MPS Asia Operations
Maurice Sciammas	50	Senior Vice President of Worldwide Sales and Marketing
Paul Ueunten	55	Senior Vice President of Engineering

Michael R. Hsing has served on our board of directors and has served as our President and Chief Executive Officer since founding Monolithic Power Systems in August 1997. Before founding our company, Mr. Hsing held senior technical positions at companies such as Supertex, Inc. and Micrel, Inc. Mr. Hsing is an inventor on numerous patents related to the process development of bipolar mixed-signal semiconductor manufacturing. Mr. Hsing holds a B.S.E.E. from the University of Florida.

Rick Neely joined us in September 2005. He currently serves as our Senior Vice President of Finance and Chief Financial Officer. From November 2002 to September 2005, he served as Chief Financial Officer of NuCORE Technology, a fabless semiconductor company. Prior to that, he was the principal of his own consulting practice from May 2001 to November 2002. He also served as Chief Financial Officer of Alventive Inc. from May 2000 to May 2001. Prior to that he served as Chief Financial Officer and Interim Chief Executive Officer of Beyond.com, Vice President of Finance and Operations at Synopsys, and Vice President and Corporate Controller of Heartport. Mr. Neely spent 16 years, from 1980 to 1996, with Advanced Micro Devices (AMD) in a variety of senior financial management positions worldwide. Mr. Neely holds a MBA from the University of Chicago and an undergraduate degree in Economics from Whitman College.

Maurice Sciammas currently serves as our Senior Vice President of Worldwide Sales and Marketing. Mr. Sciammas joined the Company in July 1999 and served as Vice President of Products and Vice President of Sales (excluding greater China) until he was appointed to his current position. Before joining the Company, he was Director of IC Products at Supertex from 1990 to 1999. He has also held positions at Micrel, Inc. He holds a B.S.E.E. degree from San Jose State University.

Deming Xiao has served as our President of our Asia Operations since January 2008. Since joining us in May 2001, Mr. Xiao has held several executive positions, including Foundry Manager and Senior Vice President of Operations. Before joining us, from June 2000 to May 2001, Mr. Xiao was Engineering Account Manager at Chartered Semiconductor Manufacturing, Inc. Prior to that, Mr. Xiao spent 6 years as the Manager of Process Integration Engineering at Fairchild Imaging Sensors. Mr. Xiao holds a B.S. in Semiconductor Physics from Sichuan University, Chengdu, China and a M.S.E.E. from Wayne State University.

Paul Ueunten has served as our Senior Vice President of Design Engineering since October 2007. Mr. Ueunten joined us in May 1998 and held several senior level positions, including Vice President of Design Engineering. Before joining us, Mr. Ueunten held positions at National Semiconductor, Signetics Corporation and Sperry Flight Systems. Mr. Ueunten holds a MS in Electrical Engineering from the University of Santa Clara, a BS in Electrical Engineering from the University of Washington and a BS in Engineering-Physics from Pacific Lutheran University. Mr. Ueunten is credited with a number of patents and is a Member of the Institute of Electrical and Electronics Engineers.

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ITEM 1A. RISK FACTORS

Our business involves risks and uncertainties. You should carefully consider the risks described below, together with all of the other information in this annual report on Form 10-K and other filings with the Securities and Exchange Commission in evaluating our business. If any of the following risks actually occur, our business, financial condition, operating results, and growth prospects would likely be adversely affected. In such an event, the trading price of our common stock could decline, and you could lose all or part of your investment in our common stock. Our past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods. These risks involve forward-looking statements and our actual results may differ substantially from those discussed in these forward-looking statements.

If we are unsuccessful in any of the legal proceedings involving us and O2Micro, we could be prevented from selling many of our products and/or be required to pay substantial damages. An unfavorable outcome or an additional award of damages, attorneys fees or an injunction could cause our revenue to decline significantly and could severely harm our business and operating results.

We are engaged in legal proceedings with O2Micro. These proceedings involve various claims and counterclaims alleging, among other things, patent infringement. O2Micro has also in the past taken legal action against certain of our customers, which we were obligated to indemnify. Other new or existing customers may request similar indemnity from us because of continued legal actions between us and O2Micro. See the section entitled Item 3. Legal Proceedings of this annual report on Form 10-K for more information.

If we are not ultimately successful in any of these proceedings or other litigation that could be brought against us or our customer, or if any of the decisions in our favor are reversed on appeal, we could be ordered to pay monetary fines and/or damages. If we are found liable for willful patent infringement, damages could be doubled or tripled. We and/or our customers could also be prevented from selling some or all of our products. Moreover, our customers and end-users could decide not to use our products or our products or our customers accounts payable to us could be seized. Finally, interim developments in these proceedings could increase the volatility in our stock price as the market assesses the impact of such developments on the likelihood that we will or will not ultimately prevail in these proceedings.

Given our inability to control the timing and nature of significant events in our legal proceedings, our legal expenses are difficult to forecast and may vary substantially from our publicly-disclosed forecasts with respect to any given quarter, which could contribute to increased volatility in our stock price and business.

Until our legal proceedings with O2Micro and Linear are resolved, we will continue to incur significant legal expenses that vary with the level of activity in each of these proceedings. This level of activity is not entirely within our control as we may need to respond to legal actions by the opposing parties or scheduling decisions by the judges. Consequently, it is difficult for us to forecast our legal expenses for any given quarter, which adversely affects our ability to forecast our expected results of operations in general. If we fail to meet the expectations of securities or industry analysts as a result of unexpected changes in our legal expenses, our stock price could be impacted.

Our ongoing legal proceedings and the potential for additional legal proceedings have diverted, and may continue to divert, financial and management resources.

The semiconductor industry is characterized by frequent claims of infringement and litigation regarding patent and other intellectual property rights, such as our litigation matters with O2Micro and

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Linear. Patent infringement is an ongoing risk, in part because other companies in our industry could have patent rights that may not be identifiable when we initiate development efforts. Litigation may be necessary to enforce our intellectual property rights, and we may have to defend ourselves against additional infringement claims. Such litigation is very costly. In the event any third party makes a new infringement claim against us or our customers, we could incur additional ongoing legal expenses. Our management team may also be required to devote a great deal of time, effort and energy to these legal proceedings, which could adversely affect our business.

We expect our operating results to fluctuate from quarter to quarter and year to year, which may make it difficult to predict our future performance and could cause our stock price to decline.

Our revenue, expenses, and results of operations are difficult to predict, have varied significantly in the past and will continue to fluctuate significantly in the future due to a number of factors, many of which are beyond our control. We expect fluctuations to continue for a number of reasons, including:

- a deterioration in general demand for electronic products as a result of worldwide financial crises and associated macro-economic slowdowns;
- a deterioration in business conditions at our distributors, value-added resellers and/or end-customers;
- adverse general economic conditions in the countries where our products are sold or used;
- the timing of developments and related expenses in our litigation matters with O2Micro and Linear and any future litigation;
- the possibility of additional lost business as a result of customer and prospective customer concerns about adverse outcomes in our litigations or about being litigation targets;
- continued dependence on our turns business (orders received and shipped within the same fiscal quarter);
- increases in assembly costs due to commodity price increases, such as the price of gold;
- the timing of new product introductions by us and our competitors;
- the acceptance of our new products in the marketplace;
- our ability to develop new process technologies and achieve volume production;
- the scheduling, rescheduling, or cancellation of orders by our customers;

- the cyclical nature of demand for our customers products;
- inventory levels and product obsolescence;
- seasonality and variability in the computer, consumer electronics, and communications markets;
- the availability of adequate manufacturing capacity from our outside suppliers;
- changes in manufacturing yields; and
- movements in exchange rates, interest rates or tax rates.

Due to the factors noted above and other risks described in this section, many of which are beyond our control, you should not rely on quarter-to-quarter or year-over-year comparisons to predict our future financial performance. Unfavorable changes in any of the above factors may seriously harm our business and cause our stock price to decline.

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The market for government-backed student loan auction-rate securities has suffered a decline in liquidity which may impact the liquidity and potential value of our investment portfolio.

The market for government-backed student loan auction-rate securities with interest rates that reset through a Dutch auction every 7 to 35 days, became illiquid in 2008. As of December 31, 2009, the Company s investment portfolio included $35.6 million, net of impairment charges of $1.8 million, in government-backed student loan auction-rate securities. As of that date, $37.4 million, the face value of our auction-rate security investments, have failed to reset through successful auctions and it is unclear as to when these investments will regain their liquidity. The underlying maturity of these auction-rate securities is up to 38 years.

Based on certain assumptions described in Note 2 to our consolidated financial statements and the Liquidity and Capital Resources section of Part II, Item 7 of this annual report on Form 10-K, we recorded temporary and other-than-temporary impairment charges on these investments. The valuation is subject to fluctuations in the future, which will depend on many factors, including the collateral quality, potential to be called or restructured, underlying final maturity, insurance guaranty, liquidity and market conditions, among others. We experienced our first failed auction in mid-February 2008. Although we accepted an offer to participate in an auction-rate securities rights offering from UBS in October 2008 to sell up to $16.9 million in eligible auction-rate securities held by us at par to UBS commencing in June 2010, if UBS does not follow through on its commitment to purchase the auction-rate securities at par or the auctions continue to fail, the liquidity of our investment portfolio may be negatively impacted and the value of our investment portfolio could decline.

Should there be further deterioration in the market for auction-rate securities or if the accounting rules for these securities change, the value of our portfolio may decline, which may have an adverse impact on our cash position and our earnings.

We may be unsuccessful in developing and selling new products or in penetrating new markets required to maintain or expand our business.

Our competitiveness and future success depend on our ability to design, develop, manufacture, assemble, test, market, and support new products and enhancements on a timely and cost-effective basis. A fundamental shift in technologies in any of our product markets could have a material adverse effect on our competitive position within these markets. Our failure to timely develop new technologies or to react quickly to changes in existing technologies could materially delay our development of new products, which could result in product obsolescence, decreased revenue, and/or a loss of market share to competitors.

As we develop new product lines, we must adapt to market conditions that are unfamiliar to us, such as competitors and distribution channels that are different from those we have known in the past. Some of our new product lines require us to re-equip our labs to test parameters we have not tested in the past. If we are unable to adapt rapidly to these new and additional conditions, we may not be able to successfully penetrate new markets.

The success of a new product depends on accurate forecasts of long-term market demand and future technological developments, as well as on a variety of specific implementation factors, including:

- timely and efficient completion of process design and device structure improvements;

timely and efficient implementation of manufacturing, assembly, and test processes;

the ability to secure and effectively utilize fabrication capacity in different geometries;

product performance;

- the quality and reliability of the product; and
- effective marketing, sales and service.

To the extent that we fail to timely introduce new products or to quickly penetrate new markets, our revenue and financial condition could be materially adversely affected.

We may be unsuccessful in developing and selling new products with margins similar to or better than what we have experienced in the past, which would impact our overall gross margin and financial performance.

Our success depends on products that are differentiated in the market, which result in gross margins that have historically been above the industry averages. Should we fail to develop and introduce sufficiently differentiated products that result in higher gross margins than industry averages, our financial condition could be materially adversely affected.

If demand for our products declines in the major end markets that we serve, our revenue will decrease.

We believe that the application of our products in the computer, consumer electronics and communications markets will continue to account for the majority of our revenue. If the demand for our products declines in the major end markets that we serve, our revenue will decrease. In addition, as technology evolves, the ability to integrate the functionalities of various components, including our discrete semiconductor products, onto a single chip and/or onto other components of systems containing our products increases. Should our customers require integrated solutions that we do not offer, demand for our products could decrease, and our business and results of operations could be adversely affected.

Certain of our products go into tubes that contain mercury, which is the subject of environmental concerns.

Our CCFL products go into tubes that contain mercury, which is the subject of environmental concerns, particularly in Europe. Should environmental issues impair the widespread use of our CCFL-based products, and should we be unable to produce replacement products based on LED lighting fast enough to compensate for the loss of our CCFL-related business, our business and results of operations could be adversely affected.

We may not experience growth rates comparable to past years.

In the past, our revenues increased significantly in certain years due to increased sales of certain of our products. Due to increased competition, reduced global electronics demand, end-customer market downturn, market acceptance and penetration of our current and future products and ongoing litigation, we may not experience growth rates comparable to past periods, which could affect our stock price and results of operations.

We may not be profitable on a quarterly or annual basis.

Our profitability is dependent on many factors, including:

- our sales, which because of our turns business (i.e., orders received and shipped within the same fiscal quarter), is difficult to accurately forecast;
- consumer electronic sales, which has experienced and may continue to experience a downturn as a result of the worldwide economic crisis;

our competition, which could adversely impact our selling prices and our potential sales;

our manufacturing costs, including our ability to negotiate with our vendors and our ability to efficiently run our test facility in China; and

our operating expenses, including general and administrative expenses, selling and marketing expenses, stock-based compensation expenses, litigation expenses, which we expect to be significant due to the litigation in which we are involved, and research and development expenses relating to products that will not be introduced and will not generate revenue until later periods, if at all.

We may not achieve profitability on a quarterly or annual basis in the future. Unfavorable changes in any of the factors noted above may have a material adverse effect on our quarterly or annual profitability.

The future trading price of our common stock could be subject to wide fluctuations in response to a variety of factors.

The future trading price of our common stock is likely to be highly volatile and could be subject to wide fluctuations in price in response to various factors, many of which are beyond our control, including:

our results of operations and financial performance;

general economic, industry and global market conditions;

the depth and liquidity of the market for our common stock;

developments generally affecting the semiconductor industry;

commencement of or developments relating to our involvement in litigation, including the O2Micro and Linear matters;

investor perceptions of us and our business;

changes in securities analysts expectations or our failure to meet those expectations;

actions by institutional or other large stockholders;

terrorist acts or acts of war;

actual or anticipated fluctuations in our results of operations;

- developments with respect to intellectual property rights;
- announcements of technological innovations or significant contracts by us or our competitors;
- introduction of new products by us or our competitors;
- our sale of common stock or other securities in the future;
- conditions and trends in technology industries;
- changes in market valuation or earnings of our competitors; and
- changes in the estimation of the future size and growth rate of our markets.

In addition, the stock market in general often experiences substantial volatility that is seemingly unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the trading price of our common stock.

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The highly cyclical nature of the semiconductor industry, which has produced significant and sometimes prolonged downturns, could materially adversely affect our operating results, financial condition and cash flows.

Historically, the semiconductor industry has been highly cyclical and, at various times, has experienced significant downturns and wide fluctuations in supply and demand. These conditions have caused significant variances in product demand and production capacity, as well as rapid erosion of average selling prices. The industry may experience severe or prolonged downturns in the future, which could result in downward pressure on the price of our products as well as lower demand for our products. Because significant portions of our expenses are fixed in the short term or incurred in advance of anticipated sales, we may not be able to decrease our expenses in a timely manner to offset any sales shortfall. These conditions could have a material adverse effect on our operating results, financial condition and cash flows.

The complexity of calculating our tax provision may result in errors that could result in restatements of our financial statements.

Due to the complexity associated with the calculation of our tax provision, we have hired independent tax advisors to assist us in the calculation. If we or our independent tax advisors fail to resolve or fully understand certain issues, we could be subject to errors, which would result in us having to restate our financial statements. Restatements are generally costly and could adversely impact our results of operations and/or have a negative impact on the trading price of our common stock.

We face risks in connection with our internal control over financial reporting related to income taxes.

Because of the complexity of our tax structure, we have had errors in our financial statements in the calculation of our tax provision that previously resulted in restatements of our prior year financial results. Although we believe that we have implemented appropriate internal control over financial reporting related to the computation of our income tax provision, we cannot be certain that any measures we have taken or may take in the future will ensure that we implement and maintain adequate internal control over financial reporting and that we will avoid any material weakness in the future. In addition, we cannot assure you that we will not in the future identify further material weaknesses in our internal control over financial reporting related to the calculation of our income tax provision that we have not discovered to date, which may impact the reliability of our financial reporting and financial statements.

Changes in effective tax rates or adverse outcomes resulting from examination of our income tax returns could adversely affect our results

Our future effective tax rates could be adversely affected by earnings being lower than anticipated in countries where we have lower statutory rates and higher than anticipated in countries where we have higher statutory rates, by changes in the valuation of our deferred tax assets and liabilities, or by changes in tax laws, regulations, accounting principles or interpretations thereof. In addition, we are subject to the continuous examination of our income tax returns by the Internal Revenue Service and other tax authorities. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from these continuous examinations will not have an adverse effect on our operating results and financial condition.

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We receive a significant portion of our revenue from our distribution channel, and the loss of any one of these distributors or value-added resellers or failure to collect a receivable from them could adversely affect our operations and financial position.

We market our products through distribution arrangements and value-added resellers and through our direct sales and applications support organization to customers that include OEMs, ODMs and electronic manufacturing service providers. Receivables from our customers are generally not secured by any type of collateral and are subject to the risk of being uncollectible. For the year ended December 31, 2009, sales to our three largest distributors and/or customers accounted for approximately 34% of our total revenue. Significant deterioration in the liquidity or financial condition of any of our major customers or any group of our customers could have a material adverse impact on the collectibility of our accounts receivable and our future operating results. We primarily conduct our sales on a purchase order basis, and we do not have any long-term supply contracts.

Moreover, we believe a high percentage of our products are eventually sold to a number of OEMs. Although we communicate with OEMs in an attempt to achieve design wins, which are decisions by OEMs and/or ODMs to incorporate our products, we do not have purchase commitments from these end users. Therefore, there can be no assurance that the OEMs and/or ODMs will continue to incorporate our ICs into their products. OEM technical specifications and requirements can change rapidly, and we may not have products that fit new specifications from an end-customer for whom we have had previous design wins. We cannot be certain that we will continue to achieve design wins from large OEMs, that our direct customers will continue to be successful in selling to the OEMs, or that the OEMs will be successful in selling products which incorporate our ICs. The loss of any significant customer, any material reduction in orders by any of our significant customers or by their OEM customers, the cancellation of a significant customer order, or the cancellation or delay of a customer s or OEM s significant program or product could reduce our revenue and adversely affect our operations and financial condition.

Failure to protect our proprietary technologies or maintain the right to certain technologies may negatively affect our ability to compete.

We rely heavily on our proprietary technologies. Our future success and competitive position depend in part upon our ability to obtain and maintain protection of certain proprietary technologies used in our products. We pursue patents for some of our new products and unique technologies, and we also rely on a combination of nondisclosure agreements and other contractual provisions, as well as our employees commitment to confidentiality and loyalty, to protect our technology, know-how, and processes. Despite the precautions we take, it may be possible for unauthorized third parties to copy aspects of our current or future technology or products or to obtain and use information that we regard as proprietary. We intend to continue to protect our proprietary technology, including through patents. However, there can be no assurance that the steps we take will be adequate to protect our proprietary rights, that our patent applications will lead to issued patents, that others will not develop or patent similar or superior products or technologies, or that our patents will not be challenged, invalidated, or circumvented by others. Furthermore, the laws of the countries in which our products are or may be developed, manufactured, or sold may not protect our products and intellectual property rights to the same extent as laws in the United States. Our failure to adequately protect our proprietary technologies could harm our business.

Our products must meet exacting specifications, and undetected defects and failures may occur, which may cause customers to return or stop buying our products and may expose us to product liability risk.

Our customers generally establish demanding specifications for quality, performance, and reliability that our products must meet. Integrated circuits as complex as ours often encounter

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development delays and may contain undetected defects or failures when first introduced or after commencement of commercial shipments, which might require product replacement or recall. Further, our third-party manufacturing processes or changes thereof, or raw material used in the manufacturing processes may cause our products to fail. We have from time to time in the past experienced product quality, performance or reliability problems. Our standard warranty period is one year, which exposes the company to significant risks of claims for defects and failures. If defects and failures occur in our products, we could experience lost revenue, increased costs, including warranty expense and costs associated with customer support, delays in, cancellations or rescheduling of orders or shipments, and product returns or discounts, any of which would harm our operating results.

In addition, product liability claims may be asserted with respect to our technology or products. Although we currently have insurance, there can be no assurance that we have obtained a sufficient amount of insurance coverage, that asserted claims will be within the scope of coverage of the insurance, or that we will have sufficient resources to satisfy any asserted claims.

We currently depend on two third-party suppliers to provide us with wafers for our products. If any of our wafer suppliers become insolvent and are unable and/or fail to provide us sufficient wafers at acceptable yields and at anticipated costs, our revenue and gross margin may decline or we may not be able to fulfill our customer orders.

We have a supply arrangement with two suppliers for the production of wafers. Should any of our suppliers become insolvent, we many not be able to fulfill our customer orders, which would likely cause a decline in our revenue. In the recent past, as a result of the global economic crisis, many wafer foundries in the semiconductor industry were operating well below normal capacity, including the two suppliers to MPS, potentially impairing our suppliers ability to meet their financial obligations.

While certain aspects of our relationship with these suppliers are contractual, many important aspects of this relationship depend on our suppliers continued cooperation and our management relationships. In addition, the fabrication of ICs is a highly complex and precise process. Problems in the fabrication process can cause a substantial percentage of wafers to be rejected or numerous ICs on each wafer to be non-functional. This could potentially reduce yields. The failure of our suppliers to supply us wafers at acceptable yields could prevent us from fulfilling our customer orders for our products and would likely cause a decline in our revenue.

Although we provide our suppliers with rolling forecasts of our production requirements, their ability to provide wafers to us is limited by the available capacity, particularly capacity in the geometries we require, at the facilities in which they manufacture wafers for us. An increased need for capacity to meet internal demands or demands of other customers could cause our suppliers to reduce capacity available to us. Our suppliers may also require us to pay amounts in excess of contracted or anticipated amounts for wafer deliveries or require us to make other concessions in order to acquire the wafer supply necessary to meet our customer requirements. If our suppliers extend lead times, limit supplies or the types of capacity we require, or increase prices due to capacity constraints or other factors, our revenue and gross margin may decline.

Further, as is common in the semiconductor industry, our customers may reschedule or cancel orders on relatively short notice. Under our agreement with our suppliers, we have an option to order wafers based on a committed forecast that can cover a period of one to six months. If our customers cancel orders after we submit a committed forecast to our suppliers for the corresponding wafers, we may be required to purchase wafers that we may not be able to resell, which would adversely affect our operating results, financial condition, and cash flows.

We might not be able to deliver our products on a timely basis if our relationships with our assembly and test subcontractors are disrupted or terminated.

All of our products are assembled by third-party subcontractors and a portion of our testing is currently performed by third-party subcontractors. We do not have any long-term agreements with these subcontractors. As a result, we may not have direct control over product delivery schedules or product quality. Also, due to the amount of time typically required to qualify assembly and test subcontractors, we could experience delays in the shipment of our products if we were forced to find alternate third parties to assemble or test our products. In addition, the current global economic crisis may materially impact our assembly supplier s ability to operate. Any future product delivery delays or disruptions in our relationships with our subcontractors could have a material adverse effect on our operating results, financial condition, and cash flows.

We derive most of our revenue from direct or indirect sales to customers in Asia and have significant operations in Asia, which may expose us to political, cultural, regulatory, economic, foreign exchange, and operational risks.

We derive most of our revenue from customers located in Asia through direct or indirect sales through distribution arrangements with parties located in Asia. As a result, we are subject to increased risks due to this geographic concentration of business and operations. For the year ended December 31, 2009, approximately 84% of our revenue was from customers in Asia. There are risks inherent in doing business in Asia, and internationally in general, including:

- changes in, or impositions of, legislative or regulatory requirements, including tax laws in the United States and in the countries in which we manufacture or sell our products;
- trade restrictions, including restrictions imposed by the United States government on trading with parties in foreign countries;
- currency exchange rate fluctuations impacting intra-company transactions;
- transportation delays;
- changes in tax regulations in China that may impact our tax status in Chengdu;
- multi-tiered distribution channels that lack visibility to end customer pricing and purchase patterns;
- international political relationships and threats of war;
- terrorism and threats of terrorism;
- epidemics and illnesses;

work stoppages and infrastructure problems due to adverse weather conditions or natural disasters;

economic and political instability;

changes in import/export regulations, tariffs, and freight rates;

longer accounts receivable collection cycles and difficulties in collecting accounts receivables;

enforcing contracts generally; and

less effective protection of intellectual property and contractual arrangements.

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The price and availability of commodities (e.g., gold, platinum, copper and silicon) may adversely impact our ability to deliver our products in a timely and cost-effective manner and may affect our business and results of operations.

Our products incorporate commodities such as gold, platinum, copper and silicon. The price and availability of these commodities and other like commodities that we use could negatively impact our business and results of operations.

Devaluation of the U.S. Dollar relative to other foreign currencies, including the Chinese Yuan, may adversely affect results of operations.

Our manufacturing and packaging suppliers are and will continue to be primarily located in China for the foreseeable future. Should the value of the Chinese Yuan continue to rise against the U.S. Dollar, there could be an increase in our manufacturing costs relative to competitors who have manufacturing facilities located in the U.S., which could adversely affect our operations. In addition, because we collect payments from all customers in U.S. dollars, fluctuations in the value of foreign currencies could have an adverse impact on our customers business, which could negatively impact our business and results of operations.

We and our manufacturing partners are or will be subject to extensive Chinese government regulation, and the benefit of various incentives from Chinese governments that we and our manufacturing partners receive may be reduced or eliminated, which could increase our costs or limit our ability to sell products and conduct activities in China.

Most of our manufacturing partners are located in China. In addition, we have established a facility in China, initially for the testing of our ICs. The Chinese government has broad discretion and authority to regulate the technology industry in China. China s government has implemented policies from time to time to regulate economic expansion in China. It also exercises significant control over China s economic growth through the allocation of resources, controlling payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. New regulations or the readjustment of previously implemented regulations could require us and our manufacturing partners to change our business plans, increase our costs, or limit our ability to sell products and conduct activities in China, which could adversely affect our business and operating results.

In addition, the Chinese government and provincial and local governments have provided, and continue to provide, various incentives to encourage the development of the semiconductor industry in China. Such incentives include tax rebates, reduced tax rates, favorable lending policies, and other measures, some or all of which may be available to our manufacturing partners and to us with respect to our facility in China. Any of these incentives could be reduced or eliminated by governmental authorities at any time. Any such reduction or elimination of incentives currently provided to our manufacturing partners could adversely affect our business and operating results.

There are inherent risks associated with the operation of our testing facility in China, which could increase product costs or cause a delay in product shipments.

We have a testing facility in China that began operations in 2006. In addition to the risks discussed elsewhere in this annual report, we face the following risks, among others:

- inability to maintain appropriate and acceptable manufacturing controls; and

- higher than anticipated overhead and other costs of operation.

If we are unable to continue a fully operational status with appropriate controls, we may incur higher costs than our current expense levels, which would affect our gross margins. In addition, if capacity restraints result in significant delays in product shipments, our business and results of operations would be adversely affected.

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Due to the nature of our business as a component supplier, we may have difficulty both in accurately predicting our future revenue and appropriately budgeting our expenses.

Because we provide components for end products and systems, demand for our products is influenced by our customers end product demand. As a result, we may have difficulty in accurately forecasting our revenue and expenses. Our revenue depends on the timing, size, and speed of commercial introductions of end products and systems that incorporate our products, all of which are inherently difficult to forecast, as well as the ongoing demand for previously introduced end products and systems. In addition, demand for our products is influenced by our customers ability to manage their inventory. Our sales to distributors are subject to higher volatility because they service demand from multiple levels of the supply chain which, in itself, is inherently difficult to forecast. If our customers, including distributors, do not manage their inventory correctly or misjudge their customers demand, our shipments to and orders from our customers may vary significantly on a quarterly basis.

The average selling prices of products in our markets have historically decreased over time and will likely do so in the future, which could harm our revenues and gross profits.

Average selling prices of semiconductor products in the markets we serve have historically decreased over time. Our gross profits and financial results will suffer if we are unable to offset any reductions in our average selling prices by reducing our costs, developing new or enhanced products on a timely basis with higher selling prices or gross profits, or increasing our sales volumes. Additionally, because we do not operate our own manufacturing or assembly facilities, we may not be able to reduce our costs as rapidly as companies that operate their own facilities, and our costs may even increase, which could also reduce our margins.

We purchase inventory in advance based on expected demand for our products, and if demand is not as expected, we may have insufficient or excess inventory, which could adversely impact our financial position.

As a fabless semiconductor company, we purchase our inventory from a third party manufacturer in advance of selling our product. We place orders with our manufacturer based on existing and expected orders from our customers for particular products. While our contracts with our customers and distributors include lead time requirements and cancellation penalties that are designed to protect us from misalignment between customer orders and inventory levels, we must nonetheless make some predictions when we place orders with our manufacturer. In the event that our predictions are inaccurate due to unexpected increases in orders or unavailability of product within the time frame that is required, we may have insufficient inventory to meet our customer demands. In the event that we order products that we are unable to sell due to a decrease in orders, unexpected order cancellations, injunctions due to patent litigations, or product returns, we may have excess inventory which, if not sold, may need to be disposed of. If any of these situations were to arise, it could have a material impact on our business and financial position.

Because of the lengthy sales cycles for our products and the fixed nature of a significant portion of our expenses, we may incur substantial expenses before we earn associated revenue and may not ultimately achieve our forecasted sales for our products.

The introduction of new products presents significant business challenges because product development plans and expenditures must be made up to two years or more in advance of any sales. It takes us up to 12 months or more to design and manufacture a new product prototype. Only after we have a prototype do we introduce the product to the market and begin selling efforts in an attempt to achieve design wins. This sales process, which averages six to twelve months, requires us to expend significant sales and marketing resources without any assurance of success. Volume production of

products that use our ICs, if any, may not be achieved for an additional three to six months after an initial sale. Sales cycles for our products are lengthy for a number of reasons:

- our customers usually complete an in-depth technical evaluation of our products before they place a purchase order;
- the commercial adoption of our products by OEMs and ODMs is typically limited during the initial release of their product to evaluate product performance and consumer demand;
- our products must be designed into a customer s product or system; and
- the development and commercial introduction of our customers products incorporating new technologies frequently are delayed.

As a result of our lengthy sales cycles, we may incur substantial expenses before we earn associated revenue because a significant portion of our operating expenses is relatively fixed and based on expected revenue. The lengthy sales cycles of our products also make forecasting the volume and timing of orders difficult. In addition, the delays inherent in lengthy sales cycles raise additional risks that customers may cancel or change their orders. Our sales are made by purchase orders. Because industry practice allows customers to reschedule or cancel orders on relatively short notice, backlog is not always a good indicator of our future sales. If customer cancellations or product changes occur, we could lose anticipated sales and not have sufficient time to reduce our inventory and operating expenses.

The loss of any of our key personnel or the failure to attract or retain specialized technical and management personnel could impair our ability to grow our business.

Our future success depends upon our ability to attract and retain highly qualified technical and managerial personnel. We are particularly dependent on the continued services of our key executives, including Michael Hsing, our President and Chief Executive Officer, who founded our company and developed our proprietary process technology. In addition, personnel with highly skilled analog and mixed-signal design engineering expertise are scarce and competition for personnel with these skills is intense. There can be no assurance that we will be able to retain existing key employees or that we will be successful in attracting, integrating or retaining other highly qualified personnel with critical capabilities in the future. If we are unable to retain the services of existing key employees or are unsuccessful in attracting new highly qualified employees quickly enough to meet the demands or our business, including design cycles, our business could be harmed.

If we fail to retain key employees in sales, applications, finance and legal or to make continued improvements to our internal systems, particularly in the accounting and finance area, our business may suffer.

Since 2006, we significantly increased the quantity and quality of our sales, applications, financial and legal staff. However, if we fail to continue to adequately staff these areas, maintain or upgrade our business systems and maintain internal controls that meet the demands of our business, our ability to operate effectively will suffer. The operation of our business also depends upon our ability to retain these employees, as these employees hold a significant amount of institutional knowledge about us and our products, and, if they were to terminate their employment, our sales and internal control over financial reporting could be adversely affected.

We intend to continue to expand our operations, which may strain our resources and increase our operating expenses.

We plan to continue to expand our domestic and foreign operations through internal growth, strategic relationships, and/or acquisitions. We expect that any such expansion will strain our systems and operational and financial controls. In addition, we are likely to incur significantly higher operating costs. To manage our growth effectively, we must continue to improve and expand our systems and controls, as well as hire experienced administrative and financial personnel. If we fail to do so, our growth will be limited. If we fail to effectively manage our planned expansion of operations, our business and operating results may be harmed.

We may engage in future acquisitions that dilute the ownership interests of our stockholders and cause us to incur debt or to assume contingent liabilities, and we may be unable to successfully integrate these companies into our operations, which would adversely affect our business.

As a part of our business strategy, from time to time we review acquisition prospects that would complement our current product offerings, enhance our design capability or offer other competitive opportunities. In the event of future acquisitions, we could use a significant portion of our available cash, cash equivalents and short-term investments, issue equity securities which would dilute current stockholders percentage ownership, and/or incur substantial debt or contingent liabilities. Such actions by us could impact our operating results and/or the price of our common stock. In addition, if we are unsuccessful in integrating any acquired company into our operations or if integration is more difficult than anticipated, we may experience disruptions that could harm our business.

We compete against many companies with substantially greater financing and other resources, and our market share may be reduced if we are unable to respond to our competitors effectively.

The analog and mixed-signal semiconductor industry is highly competitive, and we expect competitive pressures to continue. Our ability to compete effectively and to expand our business will depend on our ability to continue to recruit applications and design talent, our ability to introduce new products, and our ability to maintain the rate at which we introduce these new products. We compete with domestic and non-domestic semiconductor companies, many of which have substantially greater financial and other resources with which to pursue engineering, manufacturing, marketing, and distribution of their products. We are in direct and active competition, with respect to one or more of our product lines, with at least 10 manufacturers of such products, of varying size and financial strength. The number of our competitors has grown due to the expansion of the market segments in which we participate. We consider our competitors to include, but not be limited to: Fairchild Semiconductor, Intersil, Linear, Maxim Integrated Products, Micrel, Microsemi, National Semiconductor, O2Micro, RichTek, Rohm, Semtech, STMicroelectronic, Texas Instruments and Volterra. We expect continued competition from existing competitors as well as competition from new entrants in the semiconductor market.

We cannot assure you that our products will continue to compete favorably or that we will be successful in the face of increasing competition from new products and enhancements introduced by existing competitors or new companies entering this market, which would materially and adversely affect our results of operations and our financial condition.

If securities or industry analysts downgrade our stock or do not continue to publish research or reports about our business, our stock price and trading volume could decline.

The trading market for our common stock will depend on the research and reports that industry or securities analysts publish about us or our business. We do not have any control over these analysts. If one or more of the analysts who cover us downgrade our stock, our stock price would likely decline. If one or more of these analysts cease coverage of us or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

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Because of their significant stock ownership, our officers and directors will be able to exert significant influence over our future direction.

Executive officers, directors, and affiliated entities beneficially owned in aggregate, approximately 14% of our outstanding common stock as of December 31, 2009. These stockholders, if acting together, would be able to significantly influence all matters requiring approval by our stockholders, including the election of directors and the approval of mergers or other business combination transactions.

Major earthquakes or other natural disasters and resulting systems outages may cause us significant losses.

Our corporate headquarters, the production facilities of our third-party wafer supplier, our IC testing facility, a portion of our assembly and research and development activities, and certain other critical business operations are located in or near seismically active regions and are subject to periodic earthquakes. We do not maintain earthquake insurance and could be materially and adversely affected in the event of a major earthquake. Much of our revenue, as well as our manufacturers and assemblers, are concentrated in Asia. Such concentration increases the risk that other natural disasters, labor strikes, terrorism, war, political unrest, epidemics, and/or health advisories could disrupt our operations. In addition, we rely heavily on our internal information and communications systems and on systems or support services from third parties to manage our operations efficiently and effectively. Any of these are subject to failure due to a natural disaster or other disruption. System-wide or local failures that affect our information processing could have material adverse effects on our business, financial condition, operating results, and cash flows.

Our facilities in Chengdu, China are located in a seismically active area, as evidenced by the May 2008 earthquake that was centered in the Sichuan Province of China. Although there was no damage to our facilities as a result of that earthquake, should there be additional earthquakes in the area, we may incur losses and our business, financial condition and/or operating results may suffer.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our primary operating locations are currently in San Jose, California and Chengdu, Sichuan, China. We currently lease approximately 55,110 square feet in San Jose which serves as our corporate headquarters, sales and research and development center. Certain test procedures and manufacturing also take place in our San Jose facility. We lease approximately 56,000 square feet in Chengdu which serves as our test facility and manufacturing hub and we are currently in the process of constructing a 140,000 square foot research and development facility in Chengdu, which will be operational in mid-2010. We also lease sales offices in Japan, China, Taiwan and Korea. We believe that our existing facilities are adequate for our current operations.

ITEM 3. LEGAL PROCEEDINGS

Chip Advanced Technology Inc.

On December 12, 2007, we filed a patent infringement lawsuit in the U.S. District Court for the Central District of California against Chip Advanced Technology Inc. (CAT), asserting that CAT willfully infringed a MPS patent that enables efficient low voltage, low current power conversions, such as DC-DC step down converters. CAT was subsequently acquired by ITE Technology (ITE), which became a successor in interest to CAT. On July 28, 2009, we entered into a license agreement and a settlement agreement with ITE in which the parties agreed to mutually release and dismiss the complaints.

O2Micro, Inc.

We have been engaged in a number of legal proceedings involving patent infringement claims with O2Micro, Inc. and its parent corporation, O2Micro. Currently, there are two proceedings pending, both involving O2 Micro s U.S. Patent No. 7,417,382 (382 patent). One proceeding is pending in the International Trade Commission. The other is pending in the United States District Court for the Northern District of California. O2 Micro alleges that certain of our CCFL backlight inverter products infringe its patents. We allege that we do not infringe and the patent is invalid. The ITC Investigation was held on October 19, 2009. Trial in the Northern District of California case is scheduled for August 2, 2010. We are not able to reasonably estimate the probability of loss or the range of possible loss in this case.

Taiwan Sumida Electronics

During the quarter ended September 30, 2009, we completed the litigation process with respect to a lawsuit related to Taiwan Sumida Electronics (TSE), a customer. In connection with the completion of this lawsuit, we also jointly terminated an escrow agreement with TSE and retrieved the deposit of $7.4 million. The escrow termination resulted in recording a reversal of a litigation provision of approximately $7.4 million during the quarter ended September 30, 2009. This provision was recorded as a litigation provision in the second quarter of 2007 and the reversal of this provision in the quarter ended September 30, 2009 is reflected in the Patent Litigation Provision Reversal, net item in the Consolidated Statement of Operations.

Linear Technology Corporation

On July 1, 2008, the United States District Court for the District of Delaware held as a matter of law that we did not breach our October 1, 2005 Settlement and License Agreement with Linear Technology Corporation (Linear). Based upon that ruling, we anticipate filing a motion to seek recovery of its attorney fees when the final judgment is entered. The court has not issued its final judgment concerning the patent validity and enforceability issues.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

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PART II

ITEM 5. MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDERS MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES.

Market Price of Our Common Stock

Our common stock is traded on the Nasdaq Global Select Market under the symbol MPWR . The following table sets forth, for the periods indicated, the high and low sales price per share of our common stock on the Nasdaq Global Select Market. These prices represent quotations among dealers without adjustments for retail mark-ups, markdowns or commissions, and may not represent prices of actual transactions.

	High	Low
2009		
Fourth Quarter ended December 31, 2009	$ 24.75	$ 18.93
Third Quarter ended September 30, 2009	$ 25.26	$ 20.80
Second Quarter ended June 30, 2009	$ 23.40	$ 14.92
First Quarter ended March 31, 2009	$ 16.90	$ 10.67
2008		
Fourth Quarter ended December 31, 2008	$ 17.37	$ 6.96
Third Quarter ended September 30, 2008	$ 29.07	$ 15.98
Second Quarter ended June 30, 2008	$ 27.50	$ 17.88
First Quarter ended March 31, 2008	$ 22.36	$ 14.64

Holders of Our Common Stock

As of January 27, 2010, we had approximately 22 stockholders of record and the closing price of common stock was $21.66 per share as reported by The Nasdaq Global Select Market. Many of our shares of common stock are held by brokers and other institutions on behalf of stockholders. Based on several factors, including our proxy mailing from 2009, we estimate the total number of stockholders represented by these record holders to be at least 1,852.

Dividend Policy

We have not paid cash dividends on our common stock since our inception. We currently expect to retain earnings for use in the operation and expansion of our business, and therefore do not anticipate paying any cash dividends for the next several years.

Performance of Our Common Stock

The following graph compares the cumulative 60-month total return provided shareholders on our common stock relative to the cumulative total returns of the Nasdaq Composite Index, the S & P 500 Index and the Philadelphia Semiconductor Index. An investment of $100 (with reinvestment of all dividends) is assumed to have been made in our common stock on 11/19/2004 and its relative performance is tracked through 12/31/2009.

The information contained in the Stock Performance Graph section shall not be deemed to be soliciting material or filed or incorporated by reference in future filings with the SEC, or subject to the liabilities of Section 18 of the Exchange Act, except to the extent that the Company specifically incorporates it by reference into a document filed under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.

Recent Sales of Unregistered Securities

There were no sales of unregistered securities during the year ended December 31, 2009.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

There were no purchases of the issuer s equity securities by the issuer and affiliated purchasers during the year ended December 31, 2009.

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ITEM 6. SELECTED FINANCIAL DATA

The following financial data is derived from our audited annual consolidated financial statements as of and for the years ended December 31, 2009, 2008, 2007, 2006 and 2005. You should read the following table in conjunction with the consolidated financial statements and the related notes contained elsewhere in this report on Form 10-K. Operating results for any year are not necessarily indicative of results to be expected for any future periods.

Consolidated Statement of Operations Data:

	Year ended December 31,				
	2009	2008	2007	2006	2005
	(in thousands, except per share amounts)				
Revenue	$ 165,008	$ 160,511	$ 134,004	$ 105,015	$ 99,131
Cost of revenue, including stock-based compensation*	67,330	61,184	48,781	38,107	36,003
Gross profit	97,678	99,327	85,223	66,908	63,128
Operating expenses:					
Research and development, including stock-based compensation*	38,295	34,850	27,342	22,301	14,826
Selling, general and administrative, including stock-based compensation*	36,752	35,256	29,537	27,594	18,434
Lease abandonment			(496)	1,218	
Litigation expense	9,457	6,714	9,370	11,560	18,367
Patent litigation settlement (provision reversal)	(6,356)		9,800	3,000	5,037
Total operating expenses	78,148	76,820	75,553	65,673	56,664
Income from operations	19,530	22,507	9,670	1,235	6,464
Other income (expense):					
Interest and other income	1,047	3,587	4,741	2,637	1,703
Other expense	(429)	(652)	(139)	(273)	(111)
Total other income, net	618	2,935	4,602	2,364	1,592
Income before income taxes	20,148	25,442	14,272	3,599	8,056
Income tax provision	474	1,216	2,692	6,024	2,949
Net income (loss)	19,674	24,226	11,580	(2,425)	5,107
Basic income (loss) per share	$ 0.57	$ 0.72	$ 0.37	$ (0.08)	$ 0.18
Diluted income (loss) per share	$ 0.54	$ 0.67	$ 0.33	$ (0.08)	$ 0.17
Weighted-average common shares outstanding	34,310	33,509	31,703	29,502	27,998
Stock options, restricted stock and warrants	2,324	2,611	3,387		2,873
Diluted weighted-average common equivalent shares outstanding	36,634	36,120	35,090	29,502	30,871

* Stock-based compensation has been included in the following line items:					
Cost of revenue	$ 246	$ 344	$ 539	$ 539	$ 366
Research and development	6,408	5,821	4,625	5,236	2,611
Selling, general and administrative	7,957	6,993	6,064	5,749	2,408
Total	$ 14,611	$ 13,158	$ 11,228	$ 11,524	$ 5,385

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Consolidated Balance Sheet Data:

	As of December 31,				
	2009	2008	2007	2006	2005
			(in thousands)		
Cash and cash equivalents	$ 46,717	$ 83,266	$ 83,114	$ 50,816	$ 25,091
Short-term investments	118,914	21,922	27,765	27,674	38,814
Long-term investments	19,445	37,425			
Restricted cash		7,360	7,350		2,938
Working capital	179,577	117,365	119,348	77,111	65,450
Restricted assets		7	8,340	8,309	6,433
Total assets	241,821	195,299	172,590	117,327	100,775
Common stock	175,518	147,298	143,890	113,168	98,342
Total stockholders equity	212,957	164,645	137,537	95,025	78,168

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the consolidated financial statements and related notes which appear elsewhere in this report on Form 10-K.

Overview

We are a fabless semiconductor company that designs, develops, and markets proprietary, advanced analog and mixed-signal semiconductors. We currently offer products that serve multiple markets, including flat panel televisions, wireless communications, telecommunications equipment, general consumer products, notebook computers, cellular handsets, and set top boxes, among others. We believe that we differentiate ourselves by offering solutions that are more highly integrated, smaller in size, more energy efficient, more accurate with respect to performance specifications and, consequently, more cost-effective than many competing solutions. We plan to continue to introduce additional new products within our existing product families, as well as in new product categories.

We operate in the cyclical semiconductor industry where there is seasonal demand for certain of our products. We are not and will not be immune from current and future industry downturns, but we have targeted product and market areas that we believe have the ability to offer above average industry performance over the long term.

We work with third parties to manufacture and assemble our integrated circuits (ICs). This has enabled us to limit our capital expenditures and fixed costs, while focusing our engineering and design resources on our core strengths.

Following the introduction of a product, our sales cycle generally takes six to twelve months to achieve revenue. Volume production is usually achieved in three to six months after we receive an initial customer order for a new product. Typical lead times for orders are fewer than 90 days. These factors, combined with the fact that orders in the semiconductor industry can typically be cancelled or rescheduled without significant penalty to the customer, make the forecasting of our orders and revenue difficult.

We derive most of our revenue from sales through distribution arrangements or direct sales to customers in Asia, where the components we produce are incorporated into an end-user product. 84% of our revenue for the year ended December 31, 2009 and 89% of our revenue for the year ended December 31, 2008 was attributable to direct or indirect sales to customers in Asia. We derive a majority of our revenue from the sales of our DC to DC converter product family which services the consumer electronics, communications and computing markets. We believe our ability to achieve revenue growth will depend, in part, on our ability to develop new products, enter new market segments, gain market share, manage litigation risk, diversify our customer base and successfully secure manufacturing capacity.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles in the U.S. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. We evaluate our estimates on an on-going basis, including those related to revenue recognition, stock-based compensation, long-term investments, short-term investments, inventories, income taxes, warranty obligations and contingencies. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making the judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Estimates and judgments used in the preparation of our financial statements are, by their nature, uncertain and unpredictable, and depend upon, among other things, many factors outside of our control, such as demand for our products and economic conditions. Accordingly, our estimates and judgments may prove to be incorrect and actual results may differ, perhaps significantly, from these estimates.

We believe the following critical accounting policies reflect our more significant judgments used in the preparation of our consolidated financial statements.

Revenue Recognition. We recognize revenue in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 605-10-S25 *Revenue Recognition Overall Recognition*. ASC 605-10-S25 requires that four basic criteria must be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the fee is fixed and determinable; and (4) collectibility is reasonably assured. Determination of criteria (3) and (4) are based on management s judgment regarding the fixed nature of the fee charged for products delivered and the collectibility of those fees. The application of these criteria has resulted in our generally recognizing revenue upon shipment (when title passes) to customers. Should changes in conditions cause management to determine these criteria are not met for certain future transactions, revenue recognized for any reporting period could be adversely impacted.

Approximately 80% of our distributor sales are made through distribution arrangements with third parties. These arrangements do not include any special payment terms (our normal payment terms are 30-45 days), price protection or exchange rights. Returns are limited to our standard product warranty. Certain of our large distributors have contracts that include limited stock rotation rights that permit the return of a small percentage of the previous six months purchases in return for a compensating new order of equal or greater dollar value.

We maintain a sales reserve for stock rotation rights, which is based on historical experience of actual stock rotation returns on a per distributor basis, where available, and information related to products in the distribution channel. This reserve is recorded at the time of sale. In the future, if we are unable to estimate our stock rotation returns accurately, we may not be able to recognize revenue from sales to our distributors based on when we sell inventory to our distributors. Instead, we may have to recognize revenue when the distributor sells through such inventory to an end-customer.

We generally recognize revenue upon shipment of products to the distributor for the following reasons (based on ASC 605-15-25-1 *Revenue Recognition Products Recognition Sales of Products When Right of Return Exists*):

(1) Our price is fixed and determinable at the date of sale. We do not offer special payment terms, price protection or price adjustments to distributors where we recognize revenue upon shipment

(2) Our distributors are obligated to pay us and this obligation is not contingent on the resale of our products

(3) The distributor s obligation is unchanged in the event of theft or physical destruction or damage to the products

(4) Our distributors have stand-alone economic substance apart from our relationship

(5) We do not have any obligations for future performance to directly bring about the resale of our products by the distributor

(6) The amount of future returns can be reasonably estimated. We have the ability and the information necessary to track inventory sold to and held at our distributors. We maintain a history of returns and have the ability to estimate the stock rotation returns on a quarterly basis.

If we enter into arrangements that have rights of return that are not estimable, we recognize revenue under such arrangements only after the distributor has sold our products to an end customer.

Approximately 20% of our distributor sales are made through small distributors based on purchase orders rather than formal distribution arrangements. These distributors do not receive any stock rotation rights. We do not have a history of accepting returns from these distributors.

The terms in a majority of our distribution agreements include the non-exclusive right to sell, and the agreement to use best efforts to promote and develop a market for, our products in certain regions of the world and the ability to terminate the distribution agreement by either party with up to three months notice. We provide a one year warranty against defects in materials and workmanship. Under this warranty, we will repair the goods, provide replacements at no charge, or, under certain circumstances, provide a refund to the customer for defective products. Estimated warranty returns and warranty costs are based on historical experience and are recorded at the time product revenue is recognized.

In 2006, we signed a distribution agreement with a U.S. distributor. Revenue from this distributor is recognized upon sale by the distributor to the end customer because the distributor has certain rights of return which management believes are not estimable. The deferred revenue balance from this distributor as of December 31, 2009 and 2008 was $0.9 million and $0.5 million, respectively.

Inventory Valuation. We value our inventory at the lower of the standard cost (which approximates actual cost on a first-in, first-out basis) or its current estimated market value. We write down inventory for obsolescence or lack of demand, based on assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required. On the contrary, if market conditions are more favorable, we may be able to sell inventory that was previously reserved.

Accounting for Income Taxes.   ASC 740-10 *Income Taxes Overall* prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. In accordance with ASC 740-10, we recognize federal, state and foreign current tax liabilities or assets based on our estimate of taxes payable or refundable in the current fiscal year by tax jurisdiction. We also recognize federal, state and foreign deferred tax assets or liabilities for our estimate of future tax effects attributable to temporary differences and carryforwards. We record a valuation allowance to reduce any deferred tax assets by the amount of any tax benefits that, based on available evidence and judgment, are not expected to be realized.

Our calculation of current and deferred tax assets and liabilities is based on certain estimates and judgments and involves dealing with uncertainties in the application of complex tax laws. Our estimates of current and deferred tax assets and liabilities may change based, in part, on added certainty or finality or uncertainty to an anticipated outcome, changes in accounting or tax laws in the U.S., or foreign jurisdictions where we operate, or changes in other facts or circumstances. In addition, we recognize liabilities for potential U.S. and foreign income tax for uncertain income tax positions taken on our tax returns if it has less than a 50% likelihood of being sustained. If we determine that payment of these amounts is unnecessary or if the recorded tax liability is less than our current assessment, we may be required to recognize an income tax benefit or additional income tax expense in our financial statements in the period such determination is made. We have calculated our uncertain tax positions which were attributable to certain estimates and judgments primarily related to transfer pricing, cost sharing and our international tax structure exposure.

As of December 31, 2009, 2008 and 2007, we had a valuation allowance of $14.6 million, $14.4 million and $11.9 million, respectively, attributable to management s determination that none of the deferred tax assets will be realized, except for certain deferred tax assets related to uncertain income tax positions. Should it be determined that all or part of the net deferred tax asset will not be realized in the future, an adjustment to increase the deferred tax asset valuation allowance will be charged to income in the period such determination is made. Likewise, in the event we were to determine that we would be able to realize our deferred tax assets in the future in excess of our net recorded amount, an adjustment to the valuation allowance for the deferred tax asset would increase income in the period such determination was made.

Contingencies. We are engaged in legal proceedings resulting from several patent infringement actions against us. In addition, from time to time, we become aware that we are subject to other contingent liabilities. When this occurs, we will evaluate the appropriate accounting for the potential contingent liabilities using ASC 450-20-25-2 *Contingencies Loss Contingencies Recognition* to determine whether a contingent liability should be recorded. In making this determination, management may, depending on the nature of the matter, consult with internal and external legal counsel and technical experts. Based on the facts and circumstances in each matter, we use our judgment to determine whether it is probable that a contingent loss has occurred and whether the amount of such loss can be estimated. If we determine a loss is probable and estimable, we record a contingent loss in accordance with ASC 450-20-25-2. In determining the amount of a contingent loss, we take into account advice received from experts for each specific matter regarding the status of legal proceedings, settlement negotiations (which may be ongoing), prior case history and other factors. Should the judgments and estimates made by management need to be adjusted as additional information becomes available, we may need to record additional contingent losses that could materially and adversely impact our results of operations. Alternatively, if the judgments and estimates made by management are adjusted, for example, if a particular contingent loss does not occur, the contingent loss recorded would be reversed which could result in a favorable impact on our results of operations.

Accounting for Stock-Based Compensation. We have adopted the provisions of ASC 718-10-30 *Compensation Stock Compensation Overall Initial Measurement*, under the modified prospective method. ASC 718-10-30 eliminates the alternative of applying the intrinsic value measurement to stock compensation awards issued to employees. Rather, the standard requires us to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide services in exchange for the award, known as the requisite service period (usually the vesting period). We currently use the Black-Scholes option-pricing model to estimate the fair value of our share-based payments. The Black-Scholes option-pricing model is based on a number of assumptions, including historical volatility, expected life, risk-free interest rate and expected dividends. If these assumptions change, stock-based compensation may differ significantly from what we have recorded in the past. The amount of stock-based compensation that we recognize is also based on an expected forfeiture rate. If there is a difference between the forfeiture assumptions used in determining stock-based compensation costs and the actual forfeitures which become known over time, we may change the forfeiture rate, which could have a significant impact on our stock-based compensation expense.

Warranty Reserves. We currently provide a 12-month warranty against defects in materials and workmanship and will either repair the goods or provide replacement products at no charge to the customer for defective products. We record estimated warranty costs by product, which are based on historical experience over the preceding 12 months, at the time we recognize product revenue. Reserve requirements are recorded in the period of sale and are based on an assessment of the products sold with warranty and historical warranty costs incurred. As the complexity of our products increases, we could experience higher warranty claims relative to sales than we have previously experienced, and we may need to increase these estimated warranty reserves.

Fair Value of Financial Instruments. We adopted the provisions of ASC 820-10 *Fair Value Measurements and Disclosures Overall,* effective January 1, 2008. This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles in the United States of America, and requires that assets and liabilities carried at fair value be classified and disclosed in one of the three categories, as follows:

Level 1: Quoted prices in active markets for identical assets;

Level 2: Significant other observable inputs; and

Level 3: Significant unobservable inputs.

We also adopted the provisions of ASC 820-10-35-51 *Fair Value Measurement and Disclosure Overall Subsequent Measurement Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, effective April 1, 2009. This FSP provides additional guidance for estimating fair value in accordance with ASC 820-10 *Fair Value Measurements and Disclosures Overall*, when the volume and level of activity for the asset or liability have significantly decreased.

Our financial instruments include cash and cash equivalents and short-term and long-term investments. Cash equivalents are stated at cost, which approximates fair market value based on quoted market prices. Short-term and long-term investments are stated at their fair market value.

The face value of our holdings in auction rate securities is $37.4 million, of which $20.5 million is currently classified as long-term available-for-sale investments and $16.9 million is classified as short-term trading investments. The securities that are classified as short-term trading securities have been classified as such because the Company intends to exercise its put option to sell these securities to UBS in June of 2010. These investments are accounted for in accordance with ASC 320-10, *Investments Debt and Equity Securities Overall.* Investments in available-for-sale securities are recorded at fair value, and unrealized gains or losses (that are deemed to be temporary) are

recognized through shareholders equity, as a component of accumulated other comprehensive income in our consolidated balance sheet. We record an impairment charge to earnings when an available-for-sale investment has experienced a decline in value that is deemed to be other-than-temporary. Investments in trading securities are recorded at fair value and unrealized gains and losses are recognized in other income (expense) in our consolidated statement of operations.

We adopted the provisions of ASC 320-10-35 *Investments Debt and Equity Securities Overall Subsequent Measurement* and ASC 320-10-50 *Investments Debt and Equity Securities Overall Disclosure,* effective April 1, 2009 and used the guidelines therein to determine whether the impairment is temporary or other-than temporary. Other-than-temporary impairment charges exists when the entity has the intent to sell the security or it will more likely than not be required to sell the security before anticipated recovery. During the year ended December 31, 2009, we recognized a credit loss of $70,000, which was deemed to be other-than-temporary in other income (expense) in our Consolidated Statement of Operations.

The UBS put right is accounted for in accordance with ASC 820-10-35 *Fair Value Measurement and Disclosures Overall Subsequent Measurement.* We value the UBS put right at fair value, which is estimated to be equal to the par value of the auction-rate securities less their fair value as determined by management. Refer to Note 2 to our consolidated financial statements for further information.

Based on certain assumptions described in Note 2 to our consolidated financial statements and the Liquidity and Capital Resources section of Part II, Item 7 of this annual report on Form 10-K, we recorded impairment charges on our holdings in auction-rate securities. The valuation of these securities is subject to fluctuations in the future, which will depend on many factors, including the collateral quality, potential to be called or restructured, underlying final maturity, insurance guaranty, liquidity and market conditions, among others.

Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2009-13, Multiple-Deliverable Revenue Arrangements (ASU 2009-13). The new standard changes the requirements for establishing separate units of accounting in a multiple element arrangement and requires the allocation of arrangement consideration to each deliverable to be based on the relative selling price. ASU 2009-13 is effective for fiscal years beginning on or after June 15, 2010. The Company is currently evaluating ASU 2009-13 and the impact, if any, that it may have on its results of operations or financial position.

In April 2009, the FASB issued transition guidance Accounting Standards Codification (ASC) 820-10-65-4 *Fair Value Measurements and Disclosures Overall Transition Guidance,* the provisions of which have been incorporated in ASC 820-10-50-2 *Fair Value Measurements and Disclosures Overall Disclosures.* ASC 820-10-50-2 requires disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. This guidance is effective for interim and annual periods ending after June 15, 2009. The Company adopted this standard effective April 1, 2009, the results of which are disclosed in Note 2 Fair Value Measurements.

In April 2009, the FASB issued transition guidance ASC 320-10-65-1 *Transition Related to FASB Staff Position* (FSP) *SFAS No. 115-2 and SFAS No. 124-2, Recognition and Presentation of Other-Than-Temporary Impairments,* the provisions of which have been incorporated in ASC 320-10-35 *Investments Debt and Equity Securities Overall Subsequent Measurement* and ASC 320-10-50 *Investments Debt and Equity Securities Overall Disclosure*. The objective of an other-than-temporary impairment analysis under existing U.S. generally accepted accounting principles (GAAP) is

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to determine whether the holder of an investment in a debt or equity security for which changes in fair value are not regularly recognized in earnings (such as securities classified as held-to-maturity or available-for-sale) should recognize a loss in earnings when the investment is impaired. An investment is impaired if the fair value of the investment is less than its amortized cost basis. ASC 320-10-35 and ASC 320-10-50 amend the other-than-temporary impairment guidance in U.S. GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. ASC 320-10-35 and ASC 320-10-50 do not amend existing recognition and measurement guidance related to other-than-temporary impairments of equity securities. This guidance is effective for interim and annual periods ending after June 15, 2009. In response to this guidance, in April 2009, the SEC published ASC 320-10-S99-1 *Investments Debt and Equity Securities Overall SEC Materials Staff Accounting Bulletin (SAB) Topic 5M, Other than Temporary Impairment of Certain Investments in Equity Securities*. ASC 320-10-S99-1 maintains the staff s previous views related to equity securities and excludes debt securities from its scope. The Company adopted this standard effective April 1, 2009, the results of which are disclosed in Note 2 Fair Value Measurements.

In April 2009, the FASB issued transition guidance ASC 820-10-65-4 *Fair Value Measurement and Disclosure Overall Transition Related to FASB FSP SFAS No. 157-4*, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly,* the provisions of which have been incorporated in ASC 820-10-35-51 *Fair Value Measurement and Disclosure Overall Subsequent Measurement Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly.* ASC 820-10-35-51 provides additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased and includes guidance on identifying circumstances that indicate a transaction is not orderly. ASC 820-10-35-51 emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. This guidance is effective for interim and annual periods ending after June 15, 2009. The Company adopted this standard effective April 1, 2009, the results of which are disclosed in Note 2 Fair Value Measurements.

In December 2007, the FASB issued transition guidance ASC 805-10-65-1 *Business Combinations Overall Transition Related to* SFAS No. 141 (revised 2007), *Business Combinations* (SFAS 141(R)) and SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of Accounting Review Bulletin (ARB) No. 51* (SFAS 160), the provisions of which have been incorporated in ASC 805-10 *Business Combinations Overall* and ASC 805-20 *Business Combinations Identifiable Assets and Liabilities, and Any Noncontrolling Interest*. ASC 805-10 will significantly change current practices regarding business combinations. Among the more significant changes, ASC 805-10 expands the definition of a business and a business combination; requires the acquirer to recognize the assets acquired, liabilities assumed and noncontrolling interests (including goodwill), measured at fair value at the acquisition date; requires acquisition-related expenses and restructuring costs to be recognized separately from the business combination; requires assets acquired and liabilities assumed from contractual and non-contractual contingencies to be recognized at their acquisition-date fair values with subsequent changes recognized in earnings; and requires in-process research and development to be capitalized at fair value as an indefinite-lived intangible asset. ASC 805-20 will change the accounting and reporting for minority interests, reporting them as equity separate from the parent entity s equity, as well as requiring expanded disclosures. ASC 805-10 and ASC 805-20 are effective for financial statements issued for fiscal years beginning after December 15, 2008. The adoption of ASC 805-10 and ASC 805-20 did not have a significant impact on

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the Company s consolidated financial statements or financial position, but the nature and magnitude of the specific effects will depend upon the nature, terms and size of the acquisitions, if any, the Company completes after the effective date.

In May 2009, the FASB issued ASC 855, *Subsequent Events.* The objective of this guidance is to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. In particular, this guidance sets forth:

1. The period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements;

2. The circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements; and

3. The disclosures that an entity should make about events or transactions that occurred after the balance sheet date.

In accordance with this guidance, an entity should apply the requirements to interim or annual financial periods ending after June 15, 2009. The Company adopted this standard effective April 1, 2009 and has and will make the appropriate disclosures, as required.

In June 2009, the FASB issued transition guidance ASC 105-10-65-1, *Transition Related to SFAS No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles*, the guidance of which was incorporated in ASC 105-10 *Generally Accepted Accounting Principles (GAAP) Overall*. The *FASB Accounting Standards Codification* (Codification) will become the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission (SEC) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of this guidance, the Codification will supersede all then-existing non-SEC accounting and reporting standards. All other nongrandfathered non-SEC accounting literature not included in the Codification will become nonauthoritative. This guidance is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Company adopted this standard effective July 1, 2009, and has incorporated the current codification in this Form 10-K.

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Results of Operations

The table below shows the Consolidated Statements of Operations amounts (in thousands) and shows each as a percentage of revenue.

	Year ended December 31,					
	2009		2008		2007	
	(in thousands, except percentages)					
Revenue	$ 165,008	100.0%	$ 160,511	100.0%	$ 134,004	100.0%
Cost of revenue	67,330	40.8	61,184	38.1	48,781	36.4
Gross profit	97,678	59.2	99,327	61.9	85,223	63.6
Operating expenses:						
Research and development	38,295	23.3	34,850	21.7	27,342	20.5
Selling, general and administrative	36,752	22.3	35,256	22.0	29,537	22.0
Lease abandonment					(496)	(0.4)
Litigation expense	9,457	5.7	6,714	4.2	9,370	7.0
Patent litigation settlement (provision reversal)	(6,356)	(3.9)			9,800	7.3
Total operating expenses	78,148	47.4	76,820	47.9	75,553	56.4
Income from operations	19,530	11.8	22,507	14.0	9,670	7.2
Interest and other income	1,047	0.6	3,587	2.2	4,741	3.5
Other expense	(429)	(0.2)	(652)	(0.4)	(139)	(0.1)
Total other income, net	618	0.4	2,935	1.8	4,602	3.4
Income before income taxes	20,148	12.2	25,442	15.9	14,272	10.6
Income tax provision	474	0.3	1,216	0.8	2,692	2.0
Net income	$ 19,674	11.9%	$ 24,226	15.1%	$ 11,580	8.6%

The following table shows our revenue by product family (amounts in thousands, except percentages):

	Year ended December 31,						Percent Change	
	2009		2008		2007		2009 to 2008	2008 to 2007
Product Family	Amount	% of Revenue	Amount	% of Revenue	Amount	% of Revenue	Change	Change
DC to DC Converters	$ 123,581	74.9%	$ 115,373	71.9%	$ 86,701	64.7%	7.1%	33.1%
LCD Backlight Inverters	27,836	16.9%	32,308	20.1%	35,713	26.7%	(13.8)%	(9.5)%
Audio Amplifiers	13,591	8.2%	12,830	8.0%	11,590	8.6%	5.9%	10.7%
Total	$ 165,008	100.0%	$ 160,511	100.0%	$ 134,004	100.0%		

Revenue. Revenue for the year ended December 31, 2009 was $165.0 million, an increase of $4.5 million, or 2.8%, from $160.5 million for the year ended December 31, 2008. The increase in revenue between these two periods resulted primarily from increased sales of our DC to DC products of $8.2 million as a result of an increase in demand for electronic products in the consumer and communications markets. This was partially offset by a decrease in the sales of our lighting control products in the amount of $4.5 million as a result of the continuing shift of notebook backlighting from CCFL solutions to WLED solutions. Sales for our audio products for the year ended December 31, 2009 remained relatively flat year over year.

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Revenue for the year ended December 31, 2008 was $160.5 million, an increase of $26.5 million, or 19.8%, from $134.0 million for the year ended December 31, 2007. The increase in revenue between these two periods resulted primarily from increased sales of our DC to DC converters of $28.7 million as a result of increased sales of consumer and communications end market devices. We experienced a decrease in the sales of our lighting control products in the amount of $3.4 million due to a decrease in product demand, particularly notebook computers. The sales of our audio products increased by $1.2 million due to increased sales of consumer electronics products.

Gross Profit. Gross profit as a percentage of revenue was 59.2% for the year ended December 31, 2009 and 61.9% for the year ended December 31, 2008. For the year ended December 31, 2009 and 2008, gross margin declined year-over-year as a result of increasing price pressure and therefore declining average selling prices, and an increase in inventory reserves resulting from a decrease in the general demand for certain of our lighting control products.

Gross profit as a percentage of revenue, or gross margin, was 61.9% for the year ended December 31, 2008 and 63.6% for the year ended December 31, 2007. Gross margin declined year-over-year as a result of a decrease in the average selling price of certain of our mature products and an increase in inventory reserves, particularly in the fourth quarter due to the deterioration in the general demand for electronic products.

Research and Development. Research and development (R&D) expenses consist of salary and benefit expenses for design and product engineers, expenses related to new product development, and related facility costs.

	Year ended December 31,			Percentage Change	
	2009	2008	2007	2009 to 2008	2008 to 2007
	(in thousands, except percentages)				
Revenue	$ 165,008	$ 160,511	$ 134,004	2.8%	19.8%
Research and development (R&D), excluding stock-based compensation	31,887	29,029	22,717	9.8%	27.8%
R&D stock-based compensation	6,408	5,821	4,625	10.1%	25.9%
Total R&D	$ 38,295	$ 34,850	$ 27,342	9.9%	27.5%
R&D as a percentage of net revenue	23.2%	21.7%	20.4%		

R&D expenses were $38.3 million, or 23.2% of revenue, for year ended December 31, 2009 and $34.9 million, or 21.7% of revenue, for the year ended December 31, 2008. The year-over-year increase was primarily due to an increase in personnel and new product development expenses to support new product development. Stock-based compensation expenses increased by $0.6 million, primarily due to the acceleration of certain awards.

R&D expenses were $34.9 million, or 21.7% of revenue, for the year ended December 31, 2008 and $27.3 million, or 20.4% of revenue, for the year ended December 31, 2007. The year-over-year increase in R&D expenses was primarily due to an increase in R&D headcount, new product development activities, additional employee bonus payments and patent-related activities. The year-over-year increase was also due to an increase in stock-based compensation expenses of $1.2 million.

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Selling, General and Administrative. Selling, general and administrative (SG&A) expenses include salary and benefit expenses, sales commissions, travel expenses, related facilities costs, outside legal and accounting fees, and fees associated with Sarbanes-Oxley compliance requirements.

	Year ended December 31,			Percentage Change	
	2009	2008	2007	2009 to 2008	2008 to 2007
	(in thousands, except percentages)				
Revenue	$ 165,008	$ 160,511	$ 134,004	2.8%	19.8%
Selling, general and administrative (SG&A), excluding stock-based compensation	28,795	28,263	23,473	1.9%	20.4%
SG&A stock-based compensation	7,957	6,993	6,064	13.8%	15.3%
Total SG&A	$ 36,752	$ 35,256	$ 29,537	4.2%	19.4%
SG&A as a percentage of net revenue	22.3%	22.0%	22.0%		

SG&A expenses were $36.8 million, or 22.3% of revenue, for the year ended December 31, 2009 and $35.3 million, or 22.0% of revenue, for the year ended December 31, 2008. For the year ended December 31, 2009, SG&A expenses increased compared to the corresponding period in the prior year due to an increase in sales and sales-related expenses. Stock-based compensation increased by $1.0 million, primarily related to certain severance arrangements and the acceleration of certain awards.

SG&A expenses were $35.3 million, or 22.0% of revenue, for the year ended December 31, 2008 and $29.5 million, or 22.0% of revenue, for the year ended December 31, 2007. SG&A expenses increased year-over-year due to an increase in headcount to support the growth in business, sales commissions, sales representative contractual obligations and bonus expenses. The year-over-year increase was also due to an increase in stock-based compensation expenses in the amount of $0.9 million.

Litigation Expense, excluding Patent Litigation Settlement and Provision Reversal, net.

	Year ended December 31,			Percentage Change	
	2009	2008	2007	2009 to 2008	2008 to 2007
	(in thousands, except percentages)				
Revenue	$ 165,008	$ 160,511	$ 134,004	2.8%	19.8%
Litigation expense	9,457	6,714	9,370	40.9%	(28.3)%
Litigation expense as a percentage of net revenue	5.7%	4.2%	7.0%		

Litigation expenses, excluding patent litigation settlements and provision reversals were $9.5 million, or 5.7% of revenue, for the year ended December 31, 2009 as compared to $6.7 million, or 4.2% of revenue, for the year ended December 31, 2008. During the year ended December 31, 2009, we incurred significant legal expenses to defend our lawsuit against O2Micro. During the year ended December 31, 2008, we incurred significant legal expenses to defend our lawsuit against Linear Technology.

Litigation expenses, excluding patent litigation settlements and provision reversals were $6.7 million, or 4.2% of revenue, for the year ended December 31, 2008 as compared to $9.4 million, or 7.0% of revenue, for the year ended December 31, 2007. We incurred significant legal expenses during the first six months of 2008 for our lawsuit with Linear Technology. For the year ended December 31, 2007, we incurred significant legal expenses to prepare for and try our cases against O2Micro and TSE.

For a more complete description of our litigation matters, please see Part I, Item 3 Legal Proceedings and Note 10 Litigation of Notes to Consolidated Financial Statements.

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Patent Litigation Settlement (Provision Reversal, net).

	Year ended December 31,			Percentage Change	
	2009	2008	2007	2009 to 2008	2008 to 2007
	(in thousands, except percentages)				
Revenue	$ 165,008	$ 160,511	$ 134,004	2.8%	19.8%
Patent litigation settlement (provision reversal)	(6,356)		9,800		
Patent litigation settlement (provision reversal) as a percentage of net revenue	(3.9)%	0.0%	7.3%		

Patent litigation provision reversal, net was $6.4 million for the year ended December 31, 2009. In 2009, we completed the litigation process with respect to the lawsuit related to TSE, a customer. The conclusion of this lawsuit resulted in recording a reversal of a patent litigation provision of approximately $7.4 million. This provision was recorded as a patent litigation provision in the second quarter of 2007 and the reversal of this provision in this fiscal year is reflected in the Patent Litigation Settlement and Provision Reversal, net item in the Consolidated Statement of Operations. In connection with the completion of this lawsuit, the Company also jointly terminated an escrow agreement with TSE and retrieved the deposit of $7.4 million. This recovery was reduced by certain litigation stipulations for other parties involved in the case in the amount of $1.0 million.

There were no patent litigation settlements or provision reversals in 2008. In July 2007, we received an unfavorable ruling in our litigation with TSE, for which we recorded an accrual for a patent litigation settlement of $9.8 million in the second quarter of 2007, of which $2.5 million was paid in the third quarter of 2007 and the remainder was held in escrow.

Lease Abandonment.

	Year ended December 31,			Percentage Change	
	2009	2008	2007	2009 to 2008	2008 to 2007
	(in thousands, except percentages)				
Revenue	$ 165,008	$ 160,511	$ 134,004	2.8%	19.8%
Lease abandonment			(496)		
Lease abandonment as a percentage of net revenue	0.0%	0.0%	(0.4)%		

We did not abandon any of our leases in 2009 and 2008. In December 2006, we abandoned our lease in Los Gatos and wrote off $1.2 million in operating expenses based on the fair value of the liability in accordance with ASC 420-10, *Exit or Disposal Cost Obligations Overall*. In May 2007, we entered into a sublease agreement to rent a portion of our Los Gatos facility for a period of 21 months commencing on June 1, 2007 during which we were to receive gross payments of $0.7 million. As the amount we expected to receive was greater than the amount we originally estimated, we reduced the estimate of our remaining liability by $0.5 million in the second quarter of 2007.

Interest and Other Income. For the years ended December 31, 2009, 2008 and 2007, interest and other income was $1.0 million, $3.6 million and $4.7 million, respectively. Despite year over year increases cash, cash equivalents and investment balances, interest income decreased due to significant declines in interest rates resulting from the global financial crisis.

Other Expense. Other expense, comprised mainly of foreign exchange losses, was $0.4 million, $0.7 million and $0.1 million for the years ended December 31, 2009, 2008 and 2007 respectively.

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Income Tax Provision. The income tax provision for the year ended December 31, 2009 was $0.5 million or 2.4% of the pre-tax income, respectively. This differs from the U.S. federal statutory rate of 34% primarily because our foreign income is taxed at lower rates and because of the benefit that we realized as a result of stock options exercised and restricted units released.

The income tax provision for the year ended December 31, 2008 was $1.2 million or 4.8% of our income before income taxes. This was lower than the U.S. federal statutory rate of 34% due primarily to a benefit from earnings in low foreign tax jurisdictions and a decrease in prior-year uncertain tax position reserves under ASC 740-10, which was partially offset by an increase in current-year ASC 740-10 reserves, additional ASC 740-10 interest accruals, an increase in the valuation allowance in the U.S. and non-deductible stock option compensation expenses.

The income tax provision for the year ended December 31, 2007 was $2.7 million or 18.9% of our pre-tax income. This differed from the U.S. federal statutory rate primarily because we recorded an increase in the valuation allowance of our deferred tax assets in the amount of $1.5 million as we no longer expected that our deferred tax assets will be realized. Furthermore, we provided a full valuation allowance against the tax benefits from the unpaid portion of the TSE litigation settlement, which was offset by deductions from stock option exercises and the paid portion of the TSE litigation settlement in the second quarter of 2007.

For additional information, see Note 8 Income Taxes of the Notes to Consolidated Financial Statements.

Liquidity and Capital Resources

As of December 31, 2009, we had working capital of $179.6 million, including cash and cash equivalents of $46.7 million and short-term investments of $118.9 million compared to working capital of $117.4 million, including cash and cash equivalents of $83.3 million and short-term investments of $21.9 million as of December 31, 2008. Our working capital increased year-over-year primarily due to cash generated from operating activities, the reclassification of $16.9 million in auction-rate securities from long-term to short-term investments because of the UBS put right, which is an auction-rate security rights offering from UBS to sell up to $16.9 million in face value of eligible auction-rate securities commencing in June 2010 and proceeds from the issuance of common stock.

For the year ended December 31, 2009, net cash provided by operating activities was $31.8 million, primarily due to strong operating results during the year. This was offset by an increase in accounts receivable as a result of increased shipments at the end of the quarter ended December 31, 2009 for which collections had not yet been made and a decrease in accrued and long-term liabilities. For the year ended December 31, 2008, net cash provided by operating activities was $39.6 million, primarily due to strong operating results. For the year ended December 31, 2007, net cash provided by operating activities was $26.1 million, primarily due to strong operating results, partially offset by an increase in inventory purchases in anticipation of future demand requirements.

For the year ended December 31, 2009, net cash used in investing activities was $82.1 million, primarily related to the purchase of short-term investments. For the year ended December 31, 2008, net cash used in investing activities was $29.6 million, primarily related to the purchase of $28.1 million in auction-rate securities, which became illiquid in February 2008 and which we have not been able to sell, and the purchase of $5.2 million in capital equipment. This was offset by the release of $8.6 million in restricted assets as a result of an agreement between O2Micro and us relating to certain legal proceedings in Taiwan. For the year ended December 31, 2007, net cash used by investing activities was $13.9 million, primarily due to capital equipment purchases of $6.7 million. In addition, we placed in escrow $7.4 million in connection with the TSE litigation, for which we could have been

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liable subject to the outcome of certain legal activities. The conclusion of this lawsuit resulted in recording a reversal of a patent litigation provision of approximately $7.4 million due to the release of the restricted cash in escrow in the third quarter of 2009.

We use professional investment management firms to manage the majority of our invested cash. Within the U.S., the fixed income portfolio is primarily invested in municipal bonds. Outside of the U.S., our fixed income portfolio is primarily invested in U.S. Treasury notes and other sovereign obligations, and highly rated corporate notes. The balance of the fixed income portfolio is managed internally and invested primarily in money market funds for working capital purposes.

The market for auction-rate securities with interest rates that reset through a Dutch auction every 7 to 35 days, became illiquid in 2008. As of December 31, 2009, our investment portfolio included $35.6 million, net of impairment charges of $1.8 million, in government-backed student loan auction-rate securities. The portfolio also included a UBS auction-rate put right, which was valued at $0.7 million in accordance with the fair value measurement provisions of ASC 820-10-35. During the year ended December 31, 2009, auction rate securities with a face value of $1.3 million were sold at par through successful auctions. However, the remaining auction rate securities in the portfolio with a face value of approximately $37.4 million have failed to reset through successful auctions and it is unclear as to when these investments will regain their liquidity. The underlying maturity of these auction-rate securities is up to 38 years and the underlying credit quality of these instruments in which we have invested remain generally AAA rated, with $12.1 million of our auction rate securities having been downgraded by Moody s to Aa1-Baa3.

We adopted the provisions of ASC 320-10-35 *Investments Debt and Equity Securities Overall Subsequent Measurement* and ASC 320-10-50 *Investments Debt and Equity Securities Overall Disclosure,* effective April 1, 2009 and used the guidelines therein to determine whether the impairment is temporary or other-than temporary. Temporary impairment charges are recorded in accumulated other comprehensive income (loss) within equity and have no impact on net income. Other-than-temporary impairment charges exist when the entity has the intent to sell the security or it will more likely than not be required to sell the security before anticipated recovery. Other-than-temporary impairment charges are recorded in other income (expenses) in the Consolidated Statement of Operations.

In October 2008, we accepted an offer to participate in an auction-rate security rights offering from UBS to sell up to $18.2 million in face value amount of eligible auction-rate securities commencing in June 2010. Since then, $1.3 million of these auction-rate securities were called at par, leaving $16.9 million in eligible auction-rate securities remaining at UBS. The offer gives us the right but not the obligation to sell these securities at par to UBS and allows us to borrow up to $16.9 million. In accepting the offer, we also entered into a release of claims in favor of UBS.

Since we accepted this put right from UBS, we intend to sell these auction-rate securities at par to UBS commencing in June 2010. These securities have been reclassified as trading securities and the cumulative impairment related to these auction-rate securities was $0.7 million and $1.3 million at December 31, 2009 and 2008, respectively. Therefore, the impairment related to these securities has been recorded in other income (expense) in the Consolidated Statement of Operations.

Having accepted UBS rights offering, we valued the put right at fair value, which was estimated to be equal to the par value of the auction-rate securities less their fair value as determined by management. The value of the put right was $0.7 million and $1.3 million, at December 31, 2009 and 2008, respectively, the effect of which has been recorded by the Company in other income in the Consolidated Statement of Operations. The UBS rights offering is being accounted for as a fair-value instrument under ASC 820-10-35 and as such, all future changes in the fair value of these instruments will be recognized in other income (expense) in the Consolidated Statement of Operations.

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For the remaining auction-rate securities for which the rights offering (described above) does not apply, and which have a face value of $20.5 million and $20.6 million as of December 31, 2009 and 2008, respectively, management concluded that as of December 31, 2009 and 2008, the cumulative impairment of $1.1 million and $1.4 million, respectively, was temporary based on the following analysis:

1. The decline in the fair value of these securities is not attributable to adverse conditions specifically related to these securities or to specific conditions in an industry or in a geographic area;

2. Management possesses both the intent and ability to hold these securities for a period of time sufficient to allow for any anticipated recovery in fair value;

3. Management believes that it is more likely than not that the Company will not have to sell these securities before recovery of its cost basis;

4. Except for the credit loss of $70,000 recognized in year ended December 31, 2009 for the Company s holdings in auction rate securities described below, the Company does not believe that there is any additional credit loss associated with other auction-rate securities because the Company expects to recover the entire amortized cost basis;

5. All securities were AAA rated at December 31, 2008. The majority of the securities remain AAA rated, with $9.0 million of the auction rate securities having been downgraded by Moody s to A3-Baa3, and there have been no downgrades in the three months ended December 31, 2009; and

6. All scheduled interest payments have been made pursuant to the reset terms and conditions.

Based on the guidance of ASC 320-10-35 and ASC 320-10-50, the Company evaluated the potential credit loss of each of the auction-rate securities for which a put right was not provided. Based on such analysis, the Company determined that those securities that are not 100% FFELPS guaranteed are potentially subject to credit risks based on the extent to which the underlying debt is collateralized and the security-specific student-loan default rates. MPS portfolio includes three such securities, one of which has a senior parity ratio of approximately 115%, which is substantially above the expected student-loan default rate for that security. Conversely, the senior parity ratio for the other two securities is approximately 105%. If, therefore, the student-loan default rate and borrowing rate increases for these issuers, the remaining balance in these trusts may not be sufficient to cover the senior debt. The Company therefore concluded that there is potential credit risk for these two securities and as such, used the discounted cash flow model to determine the amount of credit loss to be recorded. In valuing the potential credit loss, the following parameters were used: 20 year expected term, cash flows based on the 90-day t-bill rates for 20 year forwards and a risk premium of 5.9%, the amount of interest that the Company was receiving on these securities when the market was last active. The potential credit loss associated with these securities was $70,000, which the Company recorded in other expense in its Consolidated Statement of Operations during the year ended December 31, 2009.

Unless another rights offering or other similar offers are made to redeem at par and accepted by us, we intend to hold the balance of these investments through successful auctions at par, which we believe could take approximately 2.0 years.

The valuation of the auction-rate securities is subject to fluctuations in the future, which will depend on many factors, including the collateral quality, potential to be called or restructured, underlying final maturity, insurance guaranty, liquidity and market conditions, among others. To determine the fair value of the auction-rate securities at December 31, 2009, September 30, 2009, June 30, 2009, March 31, 2009 and December 31, 2008, we used a discounted cash flow model,

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for which there are three valuation parameters, including time-to-liquidity, discount rate and expected return. The following are the values used in the discounted cash flow model:

	December 31, 2008	March 31, 2009	June 30, 2009	September 30, 2009	December 31, 2009
Time-to-Liquidity	18 months	24 months	21 months	24 months	24 months
Expected Return (Based on the requisite treasury rate, plus a contractual penalty rate)	2.3%	1.6%	2.1%	2.1%	2.4%
Discount Rate (Based on the requisite LIBOR, the cost of debt and a liquidity risk premium)	6.8%	5.5% 8.5%, depending on the credit-rating of the security	5.3% 10.1%, depending on the credit-rating of the security	4.8% 9.6%, depending on the credit-rating of the security	5.2% 10.0%, depending on the credit-rating of the security

From the fourth quarter of 2008 to the first quarter of 2009, we increased the time-to-liquidity from 1.5 years to 2.0 years, as we did not believe that liquidity would return to the market until then. We also experienced a downgrade in certain of our auction-rate securities by Moody s. These changes increased the impairment of these securities. However, there was a decrease in the FFELPS-guaranteed student-loan credit default swap spread from 325 basis points at the end of the fourth quarter of 2008 to 150 basis points at the end of the first quarter of 2009, which significantly reduced the impairment of these securities. As a result of offsetting charges, the total cumulative impairment charge of $2.7 million did not change from December 31, 2008. However, the temporary impairment charge increased from $1.4 million at the end of 2008 to $1.5 million at the end of the first quarter of 2009. Other-than-temporary impairment charges decreased from $1.3 million at the end of 2008 to $1.2 million at the end of the first quarter of 2009.

From the first quarter of 2009 to the second quarter of 2009, we decreased the time to liquidity from 2.0 years to 1.8 years, as three months had elapsed between periods. We also experienced a decrease in the FFELPS-guaranteed student-loan credit default swap spread from 150 basis points at the end of the first quarter of 2009 to 80 basis points at the end of the second quarter of 2009. Based on the quarterly change in the parameters used in the discounted cash flow model, the total cumulative impairment charge decreased from $2.7 million at the end of the first quarter of 2009 to $2.0 million at the end of the second quarter of 2009. Temporary impairment charges decreased from $1.5 million at the end of the first quarter of 2009 to $1.1 million at the end of the second quarter of 2009. We also recognized $70,000 in credit losses in other income (expense) in the Consolidated Statement of Operations as detailed in Note 8 Fair Value Measurements.

From the second quarter of 2009 to the third quarter of 2009, we increased the time to liquidity from 1.8 years to two years even though $1.3 million of our holdings in auction rate securities were called at par. The credit markets for these types of securities remained tight and it was unclear as to when the markets would regain its liquidity. We also experienced a decrease in the FFELPs-guaranteed student loan credit default swap spread from 80 basis points at the end of the second quarter of 2009 to 30 basis points at the end of the third quarter of 2009. Based on the quarterly change in the parameters used in the discounted cash flow model, the cumulative impairment decreased from $2.0 million at the end of the second quarter to $1.8 million at the end of the third quarter. Temporary impairment charges remained relatively constant between quarters. However, we experienced a $0.2 million decrease in other-than-temporary impairment charges related to the auction-rate securities held at UBS, which was fully offset by the change in the value of the UBS put right.

From the third quarter of 2009 to the fourth quarter of 2009, we held the time to liquidity to two years. The parameters used in the discounted cash flow model remained relatively constant and as such, the cumulative impairment did not change from $1.8 million in the prior quarter.

Net cash provided by financing activities for the year ended December 31, 2009 was $13.6 million, primarily from the issuance of common stock in the amount of $13.0 million and excess tax benefits from stock option transactions in the amount of $0.6 million.

Net cash used by financing activities for the year ended December 31, 2008 was $9.8 million, primarily from the repurchase of $25.0 million of our common stock of which our Board approved a repurchase of up to $25.0 million. This was partially offset by the proceeds related to the issuance of common stock in the amount of $14.5 million and excess tax benefits related to the exercise of options of $0.8 million. Net cash provided by financing activities for the year ended December 31, 2007 was $20.0 million, primarily from the proceeds related to the issuance of common stock in the amount of $17.3 million and excess tax benefits related to the exercise of options in the amount of $2.7 million.

Although cash requirements will fluctuate based on the timing and extent of many factors such as those discussed above, we believe that cash generated from operations, together with the liquidity provided by existing cash balances and short term investments, will be sufficient to satisfy our liquidity requirements for the next 12 months. For further details regarding our operating, investing and financing activities, see the Consolidated Statement of Cash Flows.

Contractual Obligations

We lease our headquarters and sales offices in San Jose, California under a non-cancelable operating lease which expires in October 2016. Although we relocated our headquarters from Los Gatos, California to San Jose, we had a non-cancelable lease on our Los Gatos facility which expired in February 2009, for which we signed an agreement in May 2007 to sublease a portion of the property for the remaining term. In the second quarter of 2007, we reversed $0.5 million of the $1.3 million write-off that we recorded in the fourth quarter of 2006 as a result of the aforementioned sublease. Certain of our facility leases provide for periodic rent increases. In addition, as described below, we have a five-year lease arrangement which we entered into in September 2004 for our manufacturing facility located in Chengdu, China, which will expire in March 2011. We also lease our sales offices in Japan, China, Taiwan and Korea.

In the fourth quarter of 2007, we qualified a second source foundry and have incorporated their wafers in our production units. As of December 31, 2009, our total outstanding purchase commitments were $13.2 million, which includes wafer purchases from our two foundries, the purchase of assembly services primarily from multiple contractors in Asia and purchase commitments related to the construction of our Chengdu facility. This compares to purchase commitments of $10.3 million as of December 31, 2008.

In September 2004, we signed an agreement with a Chinese local authority to construct a facility in Chengdu, China, initially for the testing of our ICs. Pursuant to this agreement, we agreed to contribute capital in the form of cash, in-kind assets, and/or intellectual property, of at least $5.0 million to our wholly-owned Chinese subsidiary as the registered capital for the subsidiary and exercised the option to purchase land use rights for the facility of approximately $0.2 million. We also have the option to acquire the facility after a five-year lease term for the original construction cost less rents paid, which is currently estimated at $2.0 million, which option becomes exercisable in March 2011. We will likely enter into a purchase agreement for this facility at the end of the lease term.

We are currently in the process of constructing a 140,000 square foot research and development facility in Chengdu, China which will be operational in mid-2010 and for which we have outstanding purchase commitments which are included in the table below.

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The following table summarizes our contractual obligations at December 31, 2009, and the effect such obligations are expected to have on our liquidity and cash flow over the next five years (in thousands).

	Payments by Period						
	Total	2010	2011	2012	2013	2014	Thereafter
Operating leases	$ 8,278	$ 1,432	$ 1,213	$ 1,080	$ 1,124	$ 1,168	$ 2,261
Outstanding purchase commitments	$ 13,214	$ 13,214	$	$	$	$	$
	$ 21,492	$ 14,646	$ 1,213	$ 1,080	$ 1,124	$ 1,168	$ 2,261

Because of the uncertainty as to the timing of payments related to our liabilities for unrecognized tax benefits, we have excluded estimated obligations of $4.9 million from the table above.

Off Balance Sheet Arrangements

As of December 31, 2009, we had no off-balance sheet arrangements as defined in Item 303(a)(4) of the Securities and Exchange Commission s Regulation S-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

Our cash equivalents and investments are subject to market risk, primarily interest rate and credit risk. Our investments are managed by outside professional managers within investment guidelines set by us. Such guidelines include security type, credit quality and maturity and are intended to limit market risk by restricting our investments to high quality debt instruments with relatively short-term maturities.

We do not use derivative financial instruments in our investment portfolio. Investments in debt securities are classified as available-for-sale or trading. For available-for-sale investments, no gains or losses are recognized by us in our results of operations due to changes in interest rates unless such securities are sold prior to maturity or are determined to be other-than-temporarily impaired. Available-for-sale investments are reported at fair value with the related unrealized gains or losses being included in accumulated other comprehensive income, a component of stockholders equity. Trading securities are reported at fair value with unrealized gains and losses included in earnings.

Fluctuations in interest rates of +/- 10% could impact our annual results of operations by approximately $0.1 million.

Foreign Currency Exchange Risk

Our sales outside the United States are transacted in U.S. dollars. Accordingly, our sales are not generally impacted by foreign currency rate changes. In 2009, the primary functional currency of the Company s offshore operations was the local currency, primarily the New Taiwan Dollar and the Chinese Yuan. To date, fluctuations in foreign currency exchange rates have not had a material impact on our results of operations. However, fluctuations of +/- 10% in such local currencies could impact our annual results of operations by approximately $2.6 million.

Value Change to Investments

As of December 31, 2009, all of our holdings in auction rate securities, which have a face value of $37.4 million, have failed to reset as a result of current market conditions. Should these auctions

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continue to fail and if the credit rating for these securities decline, a 10% decline in the fair value could impact our results of operations by approximately $3.7 million.

In valuing the auction-rate securities using the discounted cash flow model, a change in either the liquidity risk premium or time-to-liquidity by 10% would result in a $0.1 million change in the value of our auction-rate securities portfolio.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

MONOLITHIC POWER SYSTEMS, INC.

CONSOLIDATED FINANCIAL STATEMENTS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders

of Monolithic Power Systems, Inc.

We have audited the accompanying consolidated balance sheets of Monolithic Power Systems, Inc. and subsidiaries (collectively, the Company) as of December 31, 2009 and 2008, and the related consolidated statements of operations, stockholders equity, and cash flows for each of the three years in the period ended December 31, 2009. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Monolithic Power Systems, Inc. and subsidiaries as of December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company s internal control over financial reporting as of December 31, 2009, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated February 12, 2010 expressed an unqualified opinion on the Company s internal control over financial reporting.

/s/ Deloitte & Touche LLP

San Jose, California

February 12, 2010

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders

of Monolithic Power Systems, Inc.

We have audited the internal control over financial reporting of Monolithic Power Systems, Inc. and subsidiaries (collectively, the Company) as of December 31, 2009, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management s Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

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We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2009, of the Company and our report dated February 12, 2010 expressed an unqualified opinion on those consolidated financial statements.

/s/ Deloitte & Touche LLP

San Jose, California

February 12, 2010

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MONOLITHIC POWER SYSTEMS, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share amounts)

	December 31, 2009	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 46,717	$ 83,266
Short-term investments	118,914	21,922
Accounts receivable, net of allowances of $0 in both 2009 and 2008	15,521	9,115
Inventories	19,616	18,887
Deferred income tax assets, net current	5	75
Prepaid expenses and other current assets	2,726	2,622
Restricted cash		7,360
Total current assets	203,499	143,247
Property and equipment, net	17,968	14,163
Long-term investments	19,445	37,425
Deferred income tax assets, net long-term	175	19
Other assets	734	438
Restricted assets		7
Total assets	$ 241,821	$ 195,299
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 7,787	$ 4,674
Accrued compensation and related benefits	8,454	7,848
Accrued liabilities	7,681	13,360
Total current liabilities	23,922	25,882
Non-current income tax liability	4,915	4,762
Other long-term liabilities	27	10
Total liabilities	28,864	30,654
Commitments and contingencies (Notes 9 and 10)		
Stockholders equity:		
Common stock, $0.001 par value, $35 and $34 in 2009 and 2008, respectively; shares authorized: 150,000,000; shares issued and outstanding: 35,165,316 and 33,646,821 in 2009 and 2008, respectively	175,518	147,298
Retained earnings	37,085	17,411
Accumulated other comprehensive income (loss)	354	(64)
Total stockholders equity	212,957	164,645
Total liabilities and stockholders equity	$ 241,821	$ 195,299

See accompanying notes to consolidated financial statements.

MONOLITHIC POWER SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Year Ended December 31,		
	2009	**2008**	**2007**
Revenue	$ 165,008	$ 160,511	$ 134,004
Cost of revenue	67,330	61,184	48,781
Gross profit	97,678	99,327	85,223
Operating expenses:			
Research and development	38,295	34,850	27,342
Selling, general and administrative	36,752	35,256	29,537
Lease abandonment			(496)
Litigation expense	9,457	6,714	9,370
Patent litigation settlement (provision reversal)	(6,356)		9,800
Total operating expenses	78,148	76,820	75,553
Income from operations	19,530	22,507	9,670
Other income (expense):			
Interest and other income	1,047	3,587	4,741
Other expense	(429)	(652)	(139)
Total other income, net	618	2,935	4,602
Income before income taxes	20,148	25,442	14,272
Income tax provision	474	1,216	2,692
Net income	$ 19,674	$ 24,226	$ 11,580
Basic income per share	$ 0.57	$ 0.72	$ 0.37
Diluted income per share	$ 0.54	$ 0.67	$ 0.33
Weighted-average common shares outstanding	34,310	33,509	31,703
Stock options and restricted stock	2,324	2,611	3,387
Diluted weighted-average common equivalent shares outstanding	36,634	36,120	35,090

See accompanying notes to consolidated financial statements.

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MONOLITHIC POWER SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(in thousands, except share amounts)

	Common Stock					
	Shares	Amount	Deferred Stock Compensation	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance as of December 31, 2006	**30,369,381**	**$ 113,168**	**$ (487)**	**$ (17,458)**	**$ (198)**	**$ 95,025**
Cumulative effect of adopting FIN 48 adjustment to retained earnings				(937)		(937)
Components of comprehensive loss:						
Net income				11,580		11,580
Unrealized gains					46	46
Foreign exchange gain					617	617
Total comprehensive income						12,243
Exercise of stock options, including net excess tax benefit of $2,684						