IMMERSION CORP
Form 10-Q
May 01, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended March 31, 2015

OR

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

For the transition period from ______ to______

Commission file number 000-27969

IMMERSION CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**94-3180138**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

30 Rio Robles, San Jose, California 95134

(Address of principal executive offices)(Zip Code)

(408) 467-1900

(Registrant s telephone number, including area code)

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

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	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 ¨ No x

Number of shares of common stock outstanding at April 23, 2015: 28,015,756.

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IMMERSION CORPORATION

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PART I

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

IMMERSION CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share amounts)

(Unaudited)

	March 31, 2015	December 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 40,355	$ 14,380
Short-term investments	37,987	42,981
Accounts and other receivables (net of allowances for doubtful accounts of $36 and $28)	1,902	3,021
Deferred income taxes	9,377	9,377
Prepaid expenses and other current assets	597	845
Total current assets	90,218	70,604
Property and equipment, net	2,581	1,207
Deferred income tax assets	25,557	25,419
Intangibles and other assets, net	278	291
Total assets	$ 118,634	$ 97,521
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,670	$ 669
Accrued compensation	2,621	1,906
Other current liabilities	3,778	2,225
Deferred revenue	25,082	7,779
Total current liabilities	33,151	12,579
Long-term deferred revenue	6,313	7,827
Other long-term liabilities	631	512
Total liabilities	40,095	20,918
Contingencies (Note 12)		
Stockholders equity:		

Common stock and additional paid-in capital $0.001 par value; 100,000,000 shares authorized; 34,521,521 and 34,225,778 shares issued, respectively; 28,011,130 and 27,715,387 shares outstanding, respectively		206,870		204,876
Accumulated other comprehensive income		103		102
Accumulated deficit		(82,865)		(82,806)
Treasury stock at cost: 6,510,391 shares		(45,569)		(45,569)
Total stockholders equity		78,539		76,603
Total liabilities and stockholders equity	$	118,634	$	97,521

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

AND COMPREHENSIVE INCOME (LOSS)

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended March 31,	
	2015	**2014**
Revenues:		
Royalty and license	$ 16,012	$ 15,157
Development, services, and other	275	279
Total revenues	16,287	15,436
Costs and expenses:		
Cost of revenues (exclusive of amortization of intangibles shown separately below)	115	120
Sales and marketing	4,210	2,763
Research and development	3,727	3,058
General and administrative	8,293	6,521
Amortization of intangibles	12	20
Total costs and expenses	16,357	12,482
Operating income (loss)	(70)	2,954
Interest and other income (expense)	(25)	(7)
Income (loss) before benefit (provision) for income taxes	(95)	2,947
Benefit (provision) for income taxes	36	(1,083)
Net income (loss)	$ (59)	$ 1,864
Basic net income (loss) per share	$ 0.00	$ 0.07
Shares used in calculating basic net income (loss) per share	27,818	28,370
Diluted net income (loss) per share	$ 0.00	$ 0.06
Shares used in calculating diluted net income (loss) per share	27,818	29,382
Other Comprehensive Income (Loss)		

Change in unrealized gains on short-term investments		1		1
Total Other Comprehensive Income (Loss)		1		1
Total Comprehensive Income (Loss)	$	(58)	$	1,865

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three Months Ended March 31, 2015	2014
Cash flows provided by operating activities:		
Net income (loss)	$ (59)	$ 1,864
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	314	107
Amortization of intangibles	12	20
Stock-based compensation	1,740	1,583
Allowance (recovery) for doubtful accounts	8	0
Changes in operating assets and liabilities:		
Accounts and other receivables	1,111	(171)
Deferred income taxes	(138)	1,020
Prepaid expenses and other current assets	248	140
Other operating assets	(10)	(16)
Accounts payable	887	610
Accrued compensation and other current liabilities	1,477	(1,638)
Deferred revenue	15,789	12,947
Other long-term liabilities	119	(27)
Net cash provided by operating activities	21,498	16,439
Cash flows provided by (used in) investing activities:		
Purchases of short-term investments	(4,994)	(9,988)
Proceeds from maturities of short-term investments	10,000	10,000
Purchases of property and equipment	(783)	(325)
Net cash provided by (used in) investing activities	4,223	(313)
Cash flows provided by (used in) financing activities:		
Issuance of common stock under employee stock purchase plan	190	176
Exercise of stock options	64	149
Purchases of treasury stock	0	(6,222)
Net cash provided by (used in) financing activities	254	(5,897)
Net increase (decrease) in cash and cash equivalents	25,975	10,229
Cash and cash equivalents:		
Beginning of period	14,380	14,136

End of period	$ 40,355	$ 24,365
Supplemental disclosure of cash flow information		
Cash paid for taxes	$ 70	$ 26
Supplemental disclosure of noncash operating, investing, and financing activities		
Amounts accrued for property and equipment	$ 965	$ 15
Amounts accrued for purchase of treasury stock	$ 0	$ 660
Release of Restricted Stock Units and Awards under company stock plan	$ 2,184	$ 3,061

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

(Unaudited)

1. SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Immersion Corporation (the Company) was incorporated in 1993 in California and reincorporated in Delaware in 1999. It is an intellectual property (IP) and software licensing company focused on the creation, design, development, and licensing of patented haptic innovations and software that allow people to use their sense of touch more fully when operating a wide variety of digital devices.

Principles of Consolidation and Basis of Presentation

The condensed consolidated financial statements include the accounts of Immersion Corporation and its wholly-owned subsidiaries: Immersion Canada Inc.; Immersion International, LLC; Immersion Medical, Inc.; Immersion Japan K.K.; Immersion Ltd.; Immersion Software Ireland Ltd.; Haptify, Inc.; Immersion (Shanghai) Science & Technology Company, Ltd.; and Immersion Technology International. All intercompany accounts, transactions, and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all information and footnotes necessary for a complete presentation of the financial position, results of operations, and cash flows, in conformity with GAAP. These condensed consolidated financial statements should be read in conjunction with the Company s audited consolidated financial statements included in the Company s Annual Report on Form 10-K, for the fiscal year ended December 31, 2014. In the opinion of management, all adjustments consisting of only normal and recurring items necessary for the fair presentation of the financial position and results of operations for the interim periods presented have been included.

The results of operations for the three months ended March 31, 2015 are not necessarily indicative of the results to be expected for the full year.

Segment Information

The Company develops, licenses, and supports a wide range of software and IP that more fully engage users sense of touch when operating digital devices. The Company focuses on the following target application areas: mobility and consumer electronics, automotive, gaming, commercial and industrial, and medical. The Company s chief operating decision maker (CODM) is the Chief Executive Officer. The CODM allocates resources to and assesses the performance of the Company using information about its financial results as one operating and reporting segment.

Revenue Recognition

The Company recognizes revenues in accordance with applicable accounting standards, including ASC 605-10-S99, *Revenue Recognition* (*ASC 605-10-S99*); ASC 605-25, *Multiple Element Arrangements* (*ASC 605-25*); and ASC 985-605, *Software-Revenue Recognition* (*ASC 985-605*). The Company derives its revenues from two principal sources: royalty and license fees, and development contract and service fees. As described below, management judgments, assumptions, and estimates must be made and used in connection with the revenue recognized in any accounting period. Material differences may result in the amount and timing of revenue for any period based on the judgments and estimates made by management. Specifically, in connection with each transaction, the Company must evaluate whether: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable, and (iv) collectibility is probable. The Company applies these criteria as discussed below.

Persuasive evidence of an arrangement exists. For a license arrangement, the Company requires a written contract, signed by both the customer and the Company.

Delivery has occurred. The Company delivers software to customers physically and also delivers software electronically. For electronic deliveries, delivery occurs when the Company provides the customer access codes or keys that allow the customer to take immediate possession of the software.

The fee is fixed or determinable. The Company s arrangement fee is based on the use of standard payment terms, which are those that are generally extended to the majority of customers. For transactions involving extended payment terms, the Company deems these fees not to be fixed or determinable for revenue recognition purposes and revenue is deferred until the fees become due and payable.

Collectibility is probable. To recognize revenue, the Company must judge collectibility of fees, which is done on a customer-by-customer basis pursuant to the Company s credit review policy. The Company typically sells to customers with whom there is a history of successful collection. For new customers, the Company evaluates the customer s financial condition and ability to pay. If it is determined that collectibility is not probable based upon the credit review process or the customer s payment history, revenue is recognized when payment is received.

Royalty and license revenue The Company licenses its patents and software to customers in a variety of industries such as mobility, gaming, automotive, and medical devices. Certain of these are variable fee arrangements where the royalties earned by the Company are based on unit or sales volumes of the respective licensees. The Company also enters into fixed license fee arrangements. The terms of the royalty agreements generally require licensees to give notification of royalties due to the Company within 30 45 days of the end of the quarter during which their related sales occur. As the Company is unable to reliably estimate the licensees sales in any given quarter to determine the royalties due to it, the Company recognizes royalty revenues based on royalties reported by licensees and when all revenue recognition criteria are met. Certain royalties are based upon customer shipments or revenues and could be subject to change and may result in out of period adjustments. The Company recognizes fixed license fee revenue for licenses when earned under the terms of the agreements, which is generally recognized on a straight-line basis over the expected term of the license.

Development, services, and other revenue Development, services, and other revenue are composed of engineering services (engineering services and/or development contracts), and in limited cases, post contract customer support (PCS). Engineering services revenues are recognized under the proportional performance accounting method based on physical completion of the work to be performed or completed performance method. A provision for losses on contracts is made, if necessary, in the period in which the loss becomes probable and can be reasonably estimated. Revisions in estimates are reflected in the period in which the conditions become known. To date, such losses have not been significant. Revenue from PCS is typically recognized over the period of the ongoing obligation, which is generally consistent with the contractual term.

Multiple element arrangements The Company enters into multiple element arrangements in which customers purchase time-based non-exclusive licenses that cannot be resold to others, which include a combination of software and/or IP licenses, engineering services, and in limited cases PCS. For arrangements that are software based and include software and engineering services, the services are generally not essential to the functionality of the software, and customers may purchase engineering services to facilitate the adoption of the Company s technology, but they may also decide to use their own resources or appoint other engineering service organizations to perform these services.

For arrangements that are in substance subscription arrangements, the entire arrangement fee is recognized ratably over the contract term, subject to any limitations related to extended payment terms. For arrangements involving upfront fees for services and royalties earned by the Company based on unit or sales volumes of the respective licensees, and the services are performed ratably over the arrangement or are front-end loaded, the upfront fees are recognized ratably over the contract term and royalties based on unit or sales volume are recognized when they become fixed and determinable. As the Company is unable to reliably estimate the licensees   sales in any given quarter to determine the royalties due to it, the Company recognizes per unit or sales volume driven royalty revenues based on royalties reported by licensees and when all revenue recognition criteria are met.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09   Revenue from Contracts with Customers: Topic 606   (ASU 2014-09) which will supersede the current revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Further, the guidance requires improved disclosures to help users of financial statements better understand the nature, amount, timing, and uncertainty of revenue that is recognized. ASU 2014-09 is effective for reporting periods beginning after December 15, 2016, and permits companies to either apply the requirements retrospectively to all prior periods presented, or apply the requirements in the year of adoption, through a cumulative adjustment. The Company is required to adopt ASU 2014-09 as of January 1, 2017, and is in the process of determining the method of adoption and evaluating the impact on its consolidated financial statements.

2. FAIR VALUE MEASUREMENTS

Cash Equivalents and Short-term Investments

The financial instruments of the Company measured at fair value on a recurring basis are cash equivalents and short-term investments.

The Company s fixed income available-for-sale securities consist of high quality, investment grade securities. The Company values these securities based on pricing from pricing vendors, who may use quoted prices in active markets for identical assets (Level 1) or inputs other than quoted prices that are observable either directly or indirectly (Level 2) in determining fair value.

The types of instruments valued based on quoted market prices in active markets include money market securities. Such instruments are generally classified within Level 1 of the fair value hierarchy.

The types of instruments valued based on quoted prices in markets that are less active, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency are generally classified within Level 2 of the fair value hierarchy and include most U.S. treasury securities and most investment-grade corporate commercial paper.

The types of instruments valued based on unobservable inputs which reflect the reporting entity s own assumptions or data that market participants would use in valuing an instrument are generally classified within Level 3 of the fair value hierarchy. The Company had no Level 3 instruments as of March 31, 2015 and December 31, 2014.

Financial instruments measured at fair value on a recurring basis as of March 31, 2015 and December 31, 2014 are classified based on the valuation technique in the table below:

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	March 31, 2015 Fair value measurements using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(In thousands)			
Assets:				
U.S. Treasury securities	$ 0	$ 37,987	$ 0	$ 37,987
Money market accounts	24,523	0	0	24,523
Total assets at fair value	$ 24,523	$ 37,987	$ 0	$ 62,510

The above table excludes $15.8 million of cash held in banks.

	December 31, 2014 Fair value measurements using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(In thousands)			
Assets:				
U.S. Treasury securities	$ 0	$ 42,981	$ 0	$ 42,981
Money market accounts	11,524	0	0	11,524
Total assets at fair value	$ 11,524	$ 42,981	$ 0	$ 54,505

The above table excludes $2.9 million of cash held in banks.

U.S. Treasury securities are classified as short-term investments, and money market accounts are classified as cash equivalents on the Company s condensed consolidated balance sheets.

Short-term Investments

March 31, 2015

	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
		(In thousands)		
U.S. Treasury securities	$ 37,985	$ 2	$ 0	$ 37,987
Total	$ 37,985	$ 2	$ 0	$ 37,987

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	December 31, 2014			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
	(In thousands)			
U.S. Treasury securities	$ 42,980	$ 1	$ 0	$ 42,981
Total	$ 42,980	$ 1	$ 0	$ 42,981

The contractual maturities of the Company s available-for-sale securities on March 31, 2015 and December 31, 2014 were all due within one year. There were no transfers of instruments between Level 1 and 2 during the three months ended March 31, 2015 and the year ended December 31, 2014.

3. ACCOUNTS AND OTHER RECEIVABLES

	March 31, 2015	December 31, 2014
	(In thousands)	
Trade accounts receivable	$ 1,530	$ 2,708
Receivables from vendors and other	372	313
Accounts and other receivables	$ 1,902	$ 3,021

4. PROPERTY AND EQUIPMENT

	March 31, 2015	December 31, 2014
	(In thousands)	
Computer equipment and purchased software	$ 3,487	$ 3,418
Machinery and equipment	865	688
Furniture and fixtures	1,065	852
Leasehold improvements	2,523	1,295
Total	7,940	6,253
Less accumulated depreciation	(5,359)	(5,046)
Property and equipment, net	$ 2,581	$ 1,207

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5. INTANGIBLES AND OTHER ASSETS

	March 31, 2015	December 31, 2014
	(In thousands)	
Purchased patents and other purchased intangible assets	$ 4,605	$ 4,605
Other assets	264	265
Gross intangibles and other assets	4,869	4,870
Accumulated amortization of purchased patents and other purchased intangibles	(4,591)	(4,579)
Intangibles and other assets, net	$ 278	$ 291

The Company amortizes its intangible assets related to purchased patents, over their estimated useful lives, generally 10 years from the purchase date. Amortization of intangibles was as follows:

	Three Months Ended March 31,	
	2015	2014
	(In thousands)	
Amortization of intangibles	$ 12	$ 20

The table below includes estimated remaining annual amortization expense for purchased patents as of March 31, 2015.

	Estimated Amortization Expense (In thousands)
Remainder of 2015	$ 8
2016	6
Total	$ 14

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6. COMPONENTS OF OTHER CURRENT LIABILITIES

	March 31, 2015	December 31, 2014
	(In thousands)	
Accrued legal	$ 1,992	$ 1,065
Accrued services	1,128	518
Income taxes payable	47	69
Other current liabilities	611	573
Total other current liabilities	$ 3,778	$ 2,225

7. LONG-TERM DEFERRED REVENUE

Long-term deferred revenue consisted of the following:

	March 31, 2015	December 31, 2014
	(In thousands)	
Deferred revenue for Sony Computer Entertainment	$ 5,604	$ 7,051
Other deferred revenue	709	776
Long-term deferred revenue	$ 6,313	$ 7,827

Deferred revenue for Sony Computer Entertainment represents deferred license revenue where payments have been received in advance of revenue recognition.

8. STOCK-BASED COMPENSATION

Stock Options and Awards

The Company s equity incentive program is a long-term retention program that is intended to attract, retain, and provide incentives for talented employees, consultants, officers, and directors and to align stockholder and employee interests. The Company may grant time based options, market condition based options, stock appreciation rights, restricted stock, restricted stock units (RSUs), performance shares, performance units, and other stock-based or cash-based awards to employees, officers, directors, and consultants. Under this program, stock options may be granted at prices not less than the fair market value on the date of grant for stock options. These options generally vest over four years and expire from five to ten years from the date of grant. In addition to time based vesting, market condition based options are subject to a market condition: the closing price of the Company stock must exceed a certain level for a number of trading days within a specified timeframe or the options will be cancelled before the expiration of the options. Restricted stock generally vests over one year. RSUs generally vest over three years. Awards granted other than an option or stock appreciation right reduce the common stock shares available for grant under the program by 1.75 shares for each share issued.

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	March 31, 2015
Common stock shares available for grant	1,440,213
Common stock options outstanding	3,875,153
Restricted stock awards outstanding	35,364
Restricted stock units outstanding	565,148

Employee Stock Purchase Plan

The Company has an Employee Stock Purchase Plan (ESPP). Under the ESPP, eligible employees may purchase common stock through payroll deductions at a purchase price of 85% of the lower of the fair market value of the Company s stock at the beginning of the offering period or the purchase date. Participants may not purchase more than 2,000 shares in a six-month offering period or purchase stock having a value greater than $25,000 in any calendar year as measured at the beginning of the offering period. A total of 1,000,000 shares of common stock have been reserved for issuance under the ESPP. As of March 31, 2015, 581,451 shares had been purchased since the inception of the ESPP in 1999. Under ASC 718-10, the ESPP is considered a compensatory plan and the Company is required to recognize compensation cost related to the fair value of the award purchased under the ESPP. Shares purchased under the ESPP for the three months ended March 31, 2015 are listed below. Shares purchased under the ESPP for the three months ended March 31, 2014 are 17,670. The intrinsic value listed below is calculated as the difference between the market value on the date of purchase and the purchase price of the shares.

	Three Months Ended March 31, 2015
Shares purchased under ESPP	23,713
Average price of shares purchased under ESPP	$ 8.00
Intrinsic value of shares purchased under ESPP	$ 33,000

Summary of Standard Stock Options

The following table sets forth the summary of standard option activity under the Company s stock option plans for the three months ended March 31, 2015 and year ended December 31, 2014:

	Three Months Ended March 31, 2015	Year Ended December 31, 2014
Beginning outstanding balance	3,486,157	3,227,167
Granted	260,175	604,620
Exercised	(10,862)	(205,744)
Forfeited	(60,317)	(102,454)
Expired	0	(37,432)
Ending outstanding balance	3,675,153	3,486,157

Aggregate intrinsic value of options exercised	$	30,000	$	1,125,000
Weighted average fair value of options granted		3.84		4.93

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The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the quoted price of the Company s common stock for the options that were in-the-money.

Information regarding these standard stock options outstanding at March 31, 2015 and December 31, 2014 is summarized below:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (In millions)
December 31, 2014				
Options outstanding	3,486,157	$ 8.30	4.85	$ 6.6
Options vested and expected to vest using estimated forfeiture rates	3,319,308	8.21	4.80	6.6
Options exercisable	2,023,024	7.18	4.26	6.0
March 31, 2015				
Options outstanding	3,675,153	$ 8.21	4.68	$ 6.3
Options vested and expected to vest using estimated forfeiture rates	3,529,945	8.16	4.62	6.2
Options exercisable	2,270,159	7.50	4.02	5.6

Summary of Market Condition Based Stock Options

The following table sets forth the summary of the market-based option activity under the Company s stock option plans for the three months ended March 31, 2015 and year ended December 31, 2014:

	Three Months Ended March 31, 2015	Year Ended December 31, 2014
Beginning outstanding balance	50,000	0
Granted	150,000	50,000
Exercised	0	0
Forfeited and cancelled	0	0
Ending outstanding balance	200,000	50,000
Aggregate intrinsic value of options exercised	$ 0	$ 0
Weighted average fair value of options granted	3.64	5.71

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the quoted price of the Company s common stock for the options that were in-the-money.

Information regarding these market condition based stock options outstanding at March 31, 2015 and December 31, 2014 is summarized below:

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	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (In millions)
December 31, 2014				
Options outstanding	50,000	$ 11.94	6.15	$ 0.0
Options vested and expected to vestusing estimated forfeiture rates	45,430	11.94	6.15	0.0
Options exercisable	0	0.00	0.00	0.0
March 31, 2015				
Options outstanding	200,000	$ 9.05	6.67	$ 0.2
Options vested and expected to vestusing estimated forfeiture rates	130,330	9.26	6.61	0.1
Options exercisable	0	0.00	0.00	0.0

Summary of Restricted Stock Units

RSU activity for the three months ended March 31, 2015 and year ended December 31, 2014 was as follows:

	Three Months Ended March 31, 2015	Year Ended December 31, 2014
Beginning outstanding balance	564,891	668,056
Awarded	273,290	265,630
Released	(261,168)	(317,970)
Forfeited	(11,865)	(50,825)
Ending outstanding balance	565,148	564,891
Weighted average grant date fair value of RSUs granted	$ 8.09	$ 11.35
Total fair value of RSUs released	2,185,000	3,491,000

Information regarding RSUs outstanding at March 31, 2015 and December 31, 2014 is summarized below:

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	Number of Shares	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (In millions)
December 31, 2014			
RSUs outstanding	564,891	0.84	$ 5.3
RSUs vested and expected to vestusing estimated forfeiture rates	502,411	0.80	4.8
March 31, 2015			
RSUs outstanding	565,148	1.54	$ 5.2
RSUs vested and expected to vestusing estimated forfeiture rates	437,437	1.48	4.0

Summary of Restricted Stock Awards

Restricted stock award activity for the three months ended March 31, 2015 and year ended December 31, 2014 was as follows:

	Three Months Ended March 31, 2015	Year Ended December 31, 2014
Beginning outstanding balance	35,364	44,000
Awarded	0	35,364
Released	0	(44,000)
Forfeited	0	0
Ending outstanding balance	35,364	35,364
Weighted average grant date fair value of restricted stock awarded	$ 0	$ 10.97
Total fair value of restricted stock awards released	0	483,000

Stock Plan Assumptions

The assumptions used to value option grants under the Company s stock plans were as follows:

	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014
Standard Stock Options		
Expected life (in years)	4.7	4.7
Volatility	56%	57%

Interest rate	1.4%	1.4%
Dividend yield	N/A	N/A

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	Three Months Ended March 31, 2015	2014
Market Condition Based Stock Options		
Expected life (in years)	7.0	7.0
Volatility	65%	66%
Interest rate	1.9%	2.2%
Dividend yield	N/A	N/A

	Three Months Ended March 31, 2015	2014
Employee Stock Purchase Plan		
Expected life (in years)	0.5	0.5
Volatility	45%	39%
Interest rate	0.1%	0.1%
Dividend yield	N/A	N/A

Compensation Costs

Total stock-based compensation recognized in the condensed consolidated statements of operations and comprehensive income (loss) is as follows:

	Three Months Ended March 31, 2015	2014
	(In thousands)	
Statement of Operations Classifications		
Sales and marketing	$ 264	$ 230
Research and development	496	475
General and administrative	980	878
Total	$ 1,740	$ 1,583

As of March 31, 2015, there was $9.2 million related to stock options, restricted stock awards, and RSUs of unrecognized compensation cost, adjusted for estimated forfeitures, granted to the Company s employees and directors. This cost will be recognized over an estimated weighted-average period of approximately 2.98 years for standard options, 3.67 years for market condition based options, 2.23 years for RSUs, and 0.18 years for restricted stock awards. Total unrecognized compensation cost will be adjusted for future changes in estimated forfeitures.

9. STOCKHOLDERS EQUITY

Comprehensive Income (Loss)

The changes in accumulated other comprehensive income (loss) are included in the table below.

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	Three Months Ended March 31, 2015		
	Unrealized Gains and Losses on Available-for Sale Securities	Foreign Currency Items	Total
	(In thousands)		
Beginning balance	$ 1	$ 101	$ 102
Other comprehensive income (loss) before reclassifications	1	0	1
Amounts reclassified from accumulated other comprehensive income (loss)	0	0	0
Net current period other comprehensive income (loss)	1	0	1
Ending Balance	$ 2	$ 101	$ 103

Stock Repurchase Program

On November 1, 2007, the Company announced its Board of Directors authorized the repurchase of up to $50 million of the Company s common stock (Stock Repurchase Program). In addition, on October 22, 2014, our board of directors authorized another $30 million under the share repurchase program. The Company may repurchase its stock for cash in the open market in accordance with applicable securities laws. The timing of and amount of any stock repurchase will depend on share price, corporate and regulatory requirements, economic and market conditions, and other factors. The stock repurchase authorization has no expiration date, does not require the Company to repurchase a specific number of shares, and may be modified, suspended, or discontinued at any time.

There were no stock repurchases during the three months ended March 31, 2015. During the three months ended March 31, 2014, the Company repurchased 605,419 shares for $6.9 million at an average cost of $11.20, net of transaction costs, through open market repurchases. These amounts are classified as treasury stock on the Company s condensed consolidated balance sheet. As of March 31, 2015, the program remains available with approximately $34.4 million that may yet be purchased under it.

10. INCOME TAXES

Income tax provisions consisted of the following:

	Three Months Ended March 31,	
	2015	2014
	(In thousands)	
Income (loss) before provision for income taxes	$ (95)	$ 2,947
Benefit (provision) for income taxes	36	(1,083)
Effective tax rate	37.9%	36.7%

The benefit (provision) for income tax for the three months ended March 31, 2015 and 2014 resulted primarily from the Company s federal and foreign tax recognized at statutory rates, adjusted for the tax impact of nondeductible permanent items including stock-based compensation and foreign withholding taxes.

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As of March 31, 2015, the Company had unrecognized tax benefits under ASC 740 Income Taxes , of approximately $1.8 million including interest of $75,000. The total amount of unrecognized tax benefits that would affect the Company s effective tax rate, if recognized, was $275,000. There were no material changes in the amount of unrecognized tax benefits during the three months ended March 31, 2015. The Company expects to release reserves and record a tax benefit due to the expiration of applicable statutes of limitations during the next twelve months. The Company s policy is to account for interest and penalties related to uncertain tax positions as a component of income tax provision.

Net deferred income taxes were $34.9 million as of March 31, 2015, consisting primarily of federal net operating loss carryforwards and timing differences between book and tax. Because the Company had net operating loss and credit carryforwards, there are open statutes of limitations in which federal, state, and foreign taxing authorities may examine the Company s tax returns for all years from 1998 through the current period.

The Company maintains a valuation allowance of $7.5 million against certain of its deferred tax assets, including state and certain foreign deferred tax assets. The Company has determined there is not sufficient evidence to support the release of the valuation allowance against these state and foreign deferred tax assets.

11. NET INCOME (LOSS) PER SHARE

Basic net income (loss) per share is computed using the weighted average number of common shares outstanding for the period, excluding unvested restricted stock and RSUs. Diluted net income per share is based upon the weighted average common shares outstanding for the period plus dilutive potential shares including unvested restricted stock, RSUs, and stock options using the treasury stock method. The following is a reconciliation of the numerators and denominators used in computing basic and diluted net income (loss) per share:

	Three Months Ended March 31, 2015	2014
	(in thousands except per share amounts)	
Numerator:		
Net income (loss)	$ (59)	$ 1,864
Denominator:		
Shares used in computation of basic net income (loss) per share (weighted average common shares outstanding)	27,818	28,370
Dilutive potential common shares:		
Restricted Stock and RSUs	0	316
Stock options	0	696
Shares used in computation of diluted net income (loss) per share	27,818	29,382
Basic net income (loss) per share	$ 0.00	$ 0.07
Diluted net income (loss) per share	$ 0.00	$ 0.06

As of March 31, 2015, the Company had securities outstanding that could potentially dilute basic earnings per share in the future, but these were excluded from the computation of diluted net loss per share for the three months ended March 31, 2015, since their effect would have been anti-dilutive. These outstanding securities consisted of the following:

	March 31, 2015
Outstanding stock options	3,875,153
Unvested RSUs	565,148

For the three months ended March 31, 2014, options to purchase approximately 1.4 million shares of common stock with exercise prices greater than the average fair market value of the Company s stock of $11.21 per share were not included in the calculation because the effect would have been anti-dilutive.

12. CONTINGENCIES

From time to time, the Company receives claims from third parties asserting that the Company s technologies, or those of its licensees, infringe on the other parties IP rights. Management believes that these claims are without merit. Additionally, periodically, the Company is involved in routine legal matters and contractual disputes incidental to its normal operations. In management s opinion, the resolution of such matters will not have a material adverse effect on the Company s condensed consolidated financial condition, results of operations, or liquidity.

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In the normal course of business, the Company provides indemnifications of varying scope to customers against claims of IP infringement made by third parties arising from the use of the Company s IP, technology, or products. Historically, costs related to these guarantees have not been significant, and the Company is unable to estimate the maximum potential impact of these guarantees on its future results of operations.

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

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). The forward-looking statements involve risks and uncertainties. Forward-looking statements are identified by words such as anticipates, believes, expects, intends, may, will, and other similar expressions. However, these words are not the only way we identify forward-looking statements. In addition, any statements, which refer to expectations, projections, or other characterizations of future events, or circumstances, are forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of a number of factors, including those set forth below in Management s Discussion and Analysis of Financial Condition and Results of Operations and Risk Factors , those described elsewhere in this report, and those described in our other reports filed with the SEC. We caution you not to place undue reliance on these forward-looking statements, which speak only as of the date of this report, and we undertake no obligation to update these forward-looking statements after the filing of this report. You are urged to review carefully and consider our various disclosures in this report and in our other reports publicly disclosed or filed with the SEC that attempt to advise you of the risks and factors that may affect our business.

OVERVIEW

We are a premier IP and software licensing company focused on the creation, design, development, and licensing of patented haptic innovations and software that allow people to use their sense of touch more fully when operating a wide variety of digital devices. Our mission is to innovate touch technology that informs, humanizes, and excites while working with customers and partners to bring these tactile experiences to consumers. While we believe that our innovations are broadly applicable, we are currently focusing our marketing and business development activities on the following target markets: mobile devices, wearables, and consumer mobile entertainment and other content; console gaming; automotive; medical; and commercial. We manage these market areas under one operating and reportable segment.

In our target markets, we license our software and IP to manufacturers for use in products sold under their own brand names. We and our wholly-owned subsidiaries hold more than 1,900 issued or pending patents in the U.S. and other countries, covering a wide range of digital technologies, including many of the ways in which touch-related technology can be incorporated into and between hardware products, systems software, application software and digital content.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these condensed consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates and assumptions, including those related to revenue recognition, stock-based compensation, income taxes, short-term investments, contingencies, and litigation. We base our estimates and assumptions on historical

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experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates and assumptions.

We believe the following are our most critical accounting policies as they require our significant judgments and estimates in the preparation of our condensed consolidated financial statements:

Revenue Recognition

We recognize revenues in accordance with applicable accounting standards, including Accounting Standards Codification (ASC) 605-10-S99, Revenue Recognition (ASC 605-10-S99); ASC 605-25, Multiple Element Arrangements (ASC 605-25); and ASC 985-605, Software-Revenue Recognition (ASC 985-605). We derive our revenues from two principal sources: royalty and license fees, and development contract and service fees. As described below, management judgments and estimates must be made and used in connection with the revenue recognized in any accounting period. Material differences may result in the amount and timing of our revenue for any period based on the judgments and estimates made by our management. Specifically, in connection with each transaction, we must evaluate whether: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable, and (iv) collectibility is probable. We apply these criteria as discussed below.

Persuasive evidence of an arrangement exists. For a license arrangement, we require a written contract, signed by both the customer and us.

Delivery has occurred. We deliver software to our customers physically and also deliver software electronically. For electronic deliveries, delivery occurs when we provide the customer access codes or keys that allow the customer to take immediate possession of the software.

The fee is fixed or determinable. Our arrangement fee is based on the use of standard payment terms which are those that are generally extended to the majority of customers. For transactions involving extended payment terms we deem these fees not to be fixed or determinable for revenue recognition purposes and revenue is deferred until the fees become due and payable.

Collectibility is probable. To recognize revenue, we must judge collectibility of fees, which we do on a customer-by-customer basis pursuant to our credit review policy. We typically sell to customers with whom we have a history of successful collection. For new customers, we evaluate the customer s financial condition and ability to pay. If we determine that collectibility is not probable based upon our credit review process or the customer s payment history, we recognize revenue when payment is received.

Royalty and license revenue We license our patents and software to customers in a variety of industries such as mobility, gaming, automotive, and medical devices. Certain of these are variable fee arrangements where the royalties earned by us are based on unit or sales volumes of the respective licensees. We also enter into fixed license fee arrangements. The terms of the royalty agreements generally require licensees to give notification of royalties due to us within 30 45 days of the end of the quarter during which their related sales occur. As we are unable to reliably estimate the licensees sales in any given quarter to determine the royalties due to us, we recognize royalty revenues based on royalties reported by licensees and when all revenue recognition criteria are met. Certain royalties are based upon customer shipments or revenues and could be subject to change and may result in out of period adjustments. We recognize fixed license fee revenue for licenses when earned under the terms of the agreements, which is generally recognized on a straight-line basis over the expected term of the license.

Development, services, and other revenue Development, services, and other revenue are composed of engineering services (engineering services and/or development contracts), and in limited cases, PCS. Engineering services revenues are recognized under the proportional performance accounting method based on physical completion of the work to be performed or completed performance method. A provision for losses on contracts is made, if necessary, in the period in which the loss becomes probable and can be reasonably estimated. Revisions in estimates are reflected in the period in which the conditions become known. To date, such losses have not been significant. Revenue from PCS is typically recognized over the period of the ongoing obligation, which is generally consistent with the contractual term.

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Multiple element arrangements We enter into multiple element arrangements in which customers purchase time-based non-exclusive licenses that cannot be resold to others, which include a combination of software and/or IP licenses, engineering services, and in limited cases PCS. For arrangements that are software based and include software and engineering services, the services are generally not essential to the functionality of the software, and customers may purchase engineering services to facilitate the adoption of our technology, but they may also decide to use their own resources or appoint other engineering service organizations to perform these services. For arrangements that are in substance subscription arrangements, the entire arrangement fee is recognized ratably over the contract term, subject to any limitations related to extended payment terms. For arrangements involving upfront fees for services and royalties earned by us based on unit or sales volumes of the respective licensees, and the services are performed ratably over the arrangement or are front-end loaded, the upfront fees are recognized ratably over the contract term and royalties based on unit or sales volume are recognized when they become fixed and determinable. As we are unable to reliably estimate the licensees sales in any given quarter to determine the royalties due to us, we recognize per unit or sales volume driven royalty revenues based on royalties reported by licensees and when all revenue recognition criteria are met.

Stock-based Compensation Stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis over the requisite service period, which is the vesting period.

Valuation and amortization methods We use the Black-Scholes-Merton option pricing model (Black-Scholes model), single-option approach to determine the fair value of standard stock options and ESPP shares. All share-based payment awards are amortized on a straight-line basis over the requisite service periods of the awards, which are generally the vesting periods. Stock-based compensation expense recognized at fair value includes the impact of estimated forfeitures. We estimate future forfeitures at the date of grant and revise the estimates if necessary, in subsequent periods if actual forfeitures differ from these estimates. The determination of the fair value of stock-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of complex and subjective variables. These variables include actual and projected employee stock option exercise behaviors that impact the expected term, our expected stock price volatility over the term of the awards, risk-free interest rate, and expected dividends.

We use the Monte-Carlo Simulation model to value our stock options with a market condition. Valuation techniques such as the Monte-Carlo Simulation model have been developed to value path-dependent awards. The Monte-Carlo Simulation model is a generally accepted statistical technique used, in this instance, to simulate a range of future stock prices for us.

The Black-Scholes model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable, characteristics not present in our option grants and ESPP shares. Existing valuation models, including the Black-Scholes model and the Monte-Carlo Simulation model, may not provide reliable measures of the fair values of our stock-based compensation. Consequently, there is a risk that our estimates of the fair values of our stock-based compensation awards on the grant dates may bear little resemblance to the actual values realized upon the exercise, expiration, early termination, or forfeiture of those stock-based payments in the future. Certain stock-based payments, such as employee stock options, may expire and be worthless or otherwise result in zero intrinsic value as compared to the fair values originally estimated on the grant date and reported in our financial statements. Alternatively, value may be realized from these instruments that are significantly higher than the fair values originally estimated on the grant date and reported in our financial statements. There currently is no market-based mechanism or other practical application to verify the reliability and accuracy of the estimates stemming from these valuation models, nor is there a means to compare and adjust the estimates to actual values.

If factors change and we employ different assumptions for estimating stock-based compensation expense in future periods, or if we decide to use a different valuation model, the future periods may differ significantly from what we have recorded in the current period and could materially affect our operating results.

See Note 8 to the condensed consolidated financial statements for further information regarding stock-based compensation.

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Accounting for Income Taxes

We use the asset and liability method of accounting for income taxes. Under this method, income tax expense is recognized for the amount of taxes payable or refundable for the current year. In addition, deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for operating losses and tax credit carryforwards. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized and are reversed at such time that realization is believed to be more likely than not.

Our judgments, assumptions, and estimates relative to the current provision for income tax take into account current tax laws, our interpretation of current tax laws, and possible outcomes of current and future audits conducted by foreign and domestic tax authorities. We have established reserves for income taxes to address potential exposures involving tax positions that could be challenged by tax authorities. Although we believe our judgments, assumptions, and estimates are reasonable, changes in tax laws or our interpretation of tax laws and any future tax audits could significantly impact the amounts provided for income taxes in our condensed consolidated financial statements.

Our assumptions, judgments, and estimates relative to the value of a deferred tax asset take into account predictions of the amount and category of future taxable income, such as income from operations or capital gains income. Actual operating results and the underlying amount and category of income in future years could render inaccurate our current assumptions, judgments, and estimates of recoverable net deferred tax assets. Any of the assumptions, judgments, and estimates mentioned above could cause our actual income tax obligations to differ from our estimates, thus materially impacting our financial position and results of operations.

See Note 10 to the condensed consolidated financial statements for further information concerning income taxes.

Short-term Investments

Our short-term investments consist primarily of U.S. treasury bills and government agency securities purchased with an original or remaining maturity of greater than 90 days on the date of purchase. We classify all debt securities with readily determinable market values as available-for-sale . Even though the stated maturity dates of these debt securities may be one year or more beyond the balance sheet date, we have classified all debt securities as short-term investments as they are available for current operations and reasonably expected to be realized in cash or sold within one year. These investments are carried at fair market value, and using the specific identification method, any unrealized gains and losses considered to be temporary in nature are reported as a separate component of other comprehensive income (loss) within stockholders equity.

For debt securities in an unrealized loss position, we are required to assess whether (i) we have the intent to sell the debt security or (ii) it is more likely than not that we will be required to sell the debt security before its anticipated recovery. If either of these conditions is met, an other-than-temporary impairment on the security must be recognized in earnings equal to the entire difference between its fair value and amortized cost basis.

For debt securities in an unrealized loss position which are deemed to be other-than-temporary where neither of the criteria in the paragraph above are present, the difference between the security s then-current amortized cost basis and fair value is separated into (i) the amount of the impairment related to the credit loss (i.e., the credit loss component) and (ii) the amount of the impairment related to all other factors (i.e., the non-credit loss component). The credit loss component is recognized in earnings. The non-credit loss component is recognized in accumulated other comprehensive loss. The credit loss component is the excess of the amortized cost of the security over the best estimate of the present value of the cash flows expected to be collected from the debt security. The non-credit component is the residual amount of the other-than-temporary impairment.

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When calculating the present value of expected cash flows to determine the credit loss component of the other-than-temporary impairment, we estimate the amount and timing of projected cash flows on a security-by-security basis. These calculations reflect our expectations of the performance of the underlying collateral and of the issuer to meet payment obligations as applicable. The expected cash flows are discounted using the effective interest rate of the security prior to any impairment. The amortized cost basis of a debt security is adjusted for credit losses recorded to earnings. The difference between the cash flows expected to be collected and the new cost basis is accreted to investment income over the remaining expected life of the security.

Further information about short-term investments may be found in Note 2 to the condensed consolidated financial statements.

The above listing is not intended to be a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP, with no need for management s judgment in its application. There are also areas in which management s judgment in selecting any available alternative would not produce a materially different result.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2015 AND 2014

The following discussion and analysis includes our results of operations for the three months ended March 31, 2015 and 2014.

Overview

Total revenue increased by 6% for the three months ended March 31, 2015 compared to the three months ended March 31, 2014, driven by a 6% increase in royalty and license revenue. The increase in royalty and license revenue for the three-month period was primarily due to increased revenue from our automotive and mobility licensees, partially offset by decreases from our gaming and medical licensees.

Our net loss was $59,000 for the three months ended March 31, 2015 as compared to net income of $1.9 million for the three months ended March 31, 2014. The change from net income to net loss was primarily due to a $1.8 million increase in compensation, benefits, and other related costs mainly due to increased headcount over the last year, as well as a $906,000 increase in litigation expenses; partially offset by an $855,000 increase in royalty and license revenue.

In 2015, we expect royalty and license revenue, mainly from our mobility and gaming lines of business, to be the major component of our revenue as our technology continues to be included in more of our licensees products, and as we continue to execute our patent licensing program relating to the use of a simple form of haptics that we sometimes refer to as Basic Haptics. IP litigation may cause us to expend significant financial resources in the future and may have an adverse effect on the results of our operations. Additionally, our success could be limited by various factors, including global economic conditions, the timely release of our new products and our licensees products, continued market acceptance of our products and technology, and the introduction of new products by existing or new competitors. For a further discussion of these and other risk factors, see Part II, Item 1A Risk Factors.

REVENUES	March 31, 2015	2014	Change	% Change
	(In thousands)			
Three months ended:				
Royalty and license	$ 16,012	$ 15,157	$ 855	6%
Development, services, and other	275	279	(4)	(1)%
Total Revenues	$ 16,287	$ 15,436	$ 851	6%

Royalty and license revenue Royalty and license revenue is composed of royalties earned on sales by our licensees and license fees charged for our IP. The increase in royalty and license revenue for the three months ended March 31, 2015 compared to the three months ended March 31, 2014 was primarily due to increases in royalty and license revenue from our automotive and mobility licensees, partially offset by decreases in royalty and license revenue from our gaming and medical licensees.

Variable royalty revenue based on shipping volumes and per unit prices increased to $8.6 million for the three months ended March 31, 2015 from $7.5 million for the three months ended March 31, 2014, due to an increased level of sales by our mobility and automotive customers, partially offset by a decreased level of sales by our gaming customers. Fixed payment license revenue decreased to $7.4 million for the three months ended March 31, 2015 from $7.7 million for the three months ended March 31, 2014, due to decreased license fees from medical licensees.

Royalty and license revenue from automotive customers increased by 37%, due to our technology being incorporated in an increased volume of vehicles sold by our licensees.

Royalty and license revenue from mobility customers increased by 25%, primarily due to increased product volume sold by existing licensees. We anticipate that the mobility line of business will continue to be of primary importance as mobile device manufacturers continue to recognize the value of our IP and technology and as we expand our presence in Asia.

Royalty and license revenue from gaming customers decreased by 21%, primarily due to a decreased volume of sales by our licensees. Revenue from gaming customers can fluctuate based upon consumer gaming preferences, the timing of introductions of new gaming console systems, and the timing of new products from third party peripheral makers that are our licensees.

Royalty and license revenue from medical customers decreased by 8%, primarily due to decreased license fees from these licensees.

We expect royalty and license revenue to be the major component of our future revenue as our technology continues to be included in more products and as we continue our efforts to monetize our IP. We typically experience seasonally higher revenue from our gaming and mobility customers due to the reporting of holiday sales in the first calendar quarter compared to other calendar quarters.

We categorize our geographic information into three major regions: North America, Europe and Asia. In the three months ended March 31, 2015 and 2014, revenue generated in North America, Europe and Asia represented 36%, 4% and 60% of total revenue, respectively. There was no significant shift in revenues among regions as royalty and license revenues in each region increased at relatively consistent rates. The increase in royalty and license revenue in North America was primarily due to an increase in revenue from our mobility licensees, partially offset by decreased revenue from our gaming and medical

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customers. The increase in royalty and license revenue in Europe was primarily due to an increase in revenue from automotive and medical licensees, partially offset by decreased revenue from our gaming customers. The increase in royalty and license revenue in Asia was primarily due to an increase in revenue from our mobility customers, partially offset by decreased revenue from our gaming customers.

OPERATING EXPENSES	March 31, 2015	2014	Change	% Change
	(Dollars in thousands)			
Three months ended:				
Sales and marketing	$ 4,210	$ 2,763	$ 1,447	52%
% of total revenue	26%	18%	8%	
Research and development	$ 3,727	$ 3,058	$ 669	22%
% of total revenue	23%	20%	3%	
General and administrative	$ 8,293	$ 6,521	$ 1,772	27%
% of total revenue	51%	42%	9%	
Amortization of intangibles	$ 12	$ 20	$ (8)	(40)%
% of total revenue	0%	0%	0%	

Sales and Marketing Our sales and marketing expenses are composed primarily of employee compensation and benefits, sales commissions, advertising, trade shows, collateral marketing materials, market development funds, travel, and an allocation of facilities costs. The increase in sales and marketing expense for the three months ended March 31, 2015 as compared to the three months ended March 31, 2014 was primarily due to increased compensation, benefits, and other related costs of $835,000, mainly due to increased headcount; increased marketing, advertising, and public relations costs of $478,000 due to current marketing initiatives and tradeshows; and increased travel of $81,000 mainly due to increased headcount and current marketing and sales initiatives. We expect that sales and marketing expenses will increase in 2015 as we continue to invest in sales and marketing to further our focus on increasing market acceptance for our touch technologies and expanding our focus on the content and media business.

Research and Development Our research and development expenses are composed primarily of employee compensation and benefits, consulting fees, tooling and supplies, and an allocation of facilities costs. The increase in research and development expenses for the three months ended March 31, 2015 as compared to the three months ended March 31, 2014 was primarily due to a $497,000 increase in compensation, benefits, and other related costs and a $100,000 increase in travel costs, mainly due to increased headcount. We believe that continued significant investment in research and development is critical to our future success, and we expect to make increased investments in areas of research and technology development to support future growth including investment in our content and media business.

General and Administrative Our general and administrative expenses are composed primarily of employee compensation and benefits, legal and professional fees, external legal costs for patents, office supplies, travel, and an allocation of facilities costs. The increase in general and administrative expenses for the three months ended March 31, 2015 as compared to the three months ended March 31, 2014 was primarily due to a $1.4 million increase in legal, professional and license fee expenses and a $473,000 increase in compensation, benefits, and other related costs. The increase in compensation, benefits, and other related costs was primarily due to increased headcount and stock compensation expense. The

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increased legal, professional and license fee expenses were primarily due to a $906,000 increase in litigation expense relating to the HTC litigation and a $556,000 increase in other professional services and license fee expenses, partially offset by an $87,000 decrease in patent related legal costs. Our general and administrative expenses will continue to be significant as we manage our growing business and strategic opportunities and continue to license and product our IP and contractual rights and defend any lawsuits brought against us.

BENEFIT (PROVISION) FOR TAXES	March 31, 2015	2014	Change	% Change
	(Dollars in thousands)			
Three months ended:				
Benefit (provision) for income taxes	$ 36	$ (1,083)	$ 1,119	(103)%
Income (loss) before benefit (provision) for income taxes	$ (95)	$ 2,947		
Effective tax rate	37.9%	36.7%		

Benefit (provision) for Income Taxes For the three months ended March 31, 2015 we recorded a benefit for income taxes of $36,000 yielding an effective tax rate of 37.9% For the three months ended March 31, 2014, we recorded a provision for income taxes of $1.1 million yielding an effective tax rate of 36.7%. The effective tax rates used for each year were estimated based upon a forecast of our full year results and include foreign tax withholding expense incurred for the period. The change in tax benefit (provision) results primarily from the change in income (loss) before provision for income taxes.

In 2015, we expect to use a 35% tax rate to record the federal portion of our income tax provision expense, but expect there to be a limited cash impact as we will use our net operating losses and other deferred tax assets that have been carried forward to reduce taxes paid in cash. Our effective tax rate may differ from the federal tax rate due to the impact of certain planning strategies that we may undertake during the year.

We also maintain liabilities for uncertain tax positions. We expect to release reserves and record a tax benefit due to the expiration of the applicable statute of limitations during the next twelve months. As of March 31, 2015, the total amount of unrecognized tax benefits that would affect our effective tax rate, if recognized, is $275,000.

LIQUIDITY AND CAPITAL RESOURCES

Our cash, cash equivalents, and short-term investments consist primarily of money market funds and treasury bills and government agency securities. All of our short-term investments are classified as available-for-sale. The securities are stated at market value, with unrealized gains and losses reported as a component of accumulated other comprehensive income (loss), within stockholders equity.

On March 31, 2015, our cash, cash equivalents, and short-term investments totaled $78.3 million, an increase of $20.9 million from $57.4 million on December 31, 2014.

Cash provided by operating activities

Net cash provided by operating activities during the three months ended March 31, 2015 was $21.5 million, an increase of $5.1 million from the $16.4 million provided by operating activities during the three months ended March 31, 2014. Cash provided by operating activities during the quarter ended March 31, 2015 was primarily the result of an increase of $15.8 million in deferred revenue mainly due to additional upfront payments from customers, an increase of $1.5 million due to a change in accrued compensation and other liabilities mainly from an increase in accruals for compensation and benefit related items, an increase of $1.1 million due to a change in accounts receivable mainly as a result of the timing of invoices and cash collections, and an increase of $887,000 due to a change in accounts payable primarily arising from the timing of payments to vendors. These increases were partially offset by our net loss of $59,000. Cash provided by operating activities during the current period was also affected by noncash charges of $2.1 million, including $1.7 million of noncash stock-based compensation and $326,000 in depreciation and amortization.

Cash provided by (used in) investing activities

Net cash provided by investing activities during the three months ended March 31, 2015 was $4.2 million, an increase of $4.5 million compared to the $313,000 used in investing activities during the three months ended March 31, 2014. Net cash provided by investing activities was due to the maturation of short-term investments of $10.0 million, partially offset by purchases of short-term investments of $5.0 million and purchases of property and equipment of $783,000.

Cash provided by (used in) financing activities

Net cash provided by financing activities during the three months ended March 31, 2015 was $254,000 compared to $5.9 million used in financing activities during the three months ended March 31, 2014, an increase in cash provided of $6.1 million. Net cash provided by financing activities during the current period consisted primarily of exercises of stock options and the issuance of common stock under our ESPP of $254,000.

We believe that our cash, cash equivalents, and short-term investments will be sufficient to meet our working capital needs for at least the next twelve months. We will continue to invest in, protect, and defend our extensive IP portfolio, which is expected to result in the continued use of cash. On November 1, 2007, our board of directors authorized a share repurchase program of $50 million and on October 22, 2014 authorized another $30 million. At March 31, 2015, there was $34.4 million remaining under the share repurchase program. We anticipate that capital expenditures for property and equipment for the year ended December 31, 2015 will be less than $4.0 million. Cash from operations could also be affected by various risks and uncertainties, including, but not limited to the risks detailed in Part II, Item 1A titled Risk Factors . Additionally, if we acquire businesses, patents, or technology, our cash or capital requirements could increase substantially. In the event of such an acquisition, or should any unanticipated circumstances arise that significantly increase our capital requirements, we may elect to raise additional capital through debt or equity financing. Any of these events could result in substantial dilution to our stockholders. There is no assurance that such additional capital will be available on terms acceptable to us, if at all.

SUMMARY DISCLOSURES ABOUT CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

We presented our contractual obligations in our Annual Report on Form 10-K for the year ended December 31, 2014. Our principal commitments as of March 31, 2015 consisted of obligations under operating leases. There have been no material changes in those obligations during the three months ended March 31, 2015.

As of March 31, 2015, we had a liability for unrecognized tax benefits totaling $1.8 million including interest of $75,000, of which approximately $275,000 could be payable in cash. We expect to release reserves and record a tax benefit due to the expiration of statute of limitations during the next twelve months.

RECENT ACCOUNTING PRONOUNCEMENTS

See Note 1 to the condensed consolidated financial statements for information regarding the effect of new accounting pronouncements on our financial statements.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to financial market risks, including changes in interest rates and foreign currency exchange rates. Changes in these factors may cause fluctuations in our earnings and cash flows. We evaluate and manage the exposure to these market risks as follows:

Cash Equivalents and Short-term Investments We had cash equivalents and short-term investments of $62.5 million as of March 31, 2015, which are subject to interest rate fluctuations. An increase in interest rates could adversely affect the market value of our cash equivalents and short-term investments. A hypothetical 100 basis point increase in interest rates would result in a decrease of approximately $197,000 in the fair value of our cash equivalents and short-term investments as of March 31, 2015.

We limit our exposure to interest rate and credit risk by establishing and monitoring clear policies and guidelines for our cash equivalents and short-term investment portfolios. The primary objective of our policies is to preserve principal while at the same time maximizing yields, without significantly increasing risk. Our policy s guidelines also limit exposure to loss by limiting the sums we can invest in any individual security and restricting investments to securities that meet certain defined credit ratings. We do not use derivative financial instruments in our investment portfolio to manage interest rate risk.

Foreign Currency Exchange Rates A substantial majority of our revenue, expense, and capital purchasing activities are transacted in U.S. dollars. However, we do incur certain operating costs for our foreign operations in other currencies but these operations are limited in scope and thus we are not materially exposed to foreign currency fluctuations. Additionally we have some reliance on international revenues that are subject to the risks of fluctuations in currency exchange rates. Because a substantial majority of our international revenues, as well as expenses, are typically denominated in U.S. dollars, a strengthening of the U.S. dollar could cause our products to become relatively more expensive to customers in a particular country, leading to a reduction in sales or profitability in that country. We have no foreign exchange contracts, option contracts, or other foreign currency hedging arrangements and we do not expect to have such arrangements in the foreseeable future.

ITEM 4. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Based on their evaluation as of March 31, 2015, our management with the participation of our Chief Executive Officer and Chief Financial Officer, have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) were effective to ensure that the information required to be disclosed by us in this quarterly report on Form 10-Q was (i) recorded, processed, summarized and reported within the time periods specified in the SEC s rules and regulations and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

There were no changes to internal controls over financial reporting that occurred during the quarter ended March 31, 2015 that have materially affected, or are reasonably likely to materially affect our internal controls over financial reporting.

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any within Immersion, have been detected.

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PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Immersion Corporation vs. Motorola Mobility, Inc., Motorola Mobility Holdings, Inc., HTC Corporation, HTC America Holding, Inc., HTC America, Inc., HTC (B.V.I.) Corporation, Exedea, Inc., Brightstar Corporation, and Brightpoint, Inc.

On February 7, 2012, we filed a complaint against Motorola with the U.S. International Trade Commission (the ITC) alleging that certain Motorola mobile electronic devices, including smartphones and cellular phones, infringe six of our patents that cover various uses of haptic effects in connection with touchscreens (the ITC Complaint). We amended the ITC Complaint on March 2, 2012 to add the following parties: HTC Corporation, HTC America Holding, Inc., HTC America, Inc., HTC (B.V.I.) Corporation, Exedea, Inc., Brightstar Corporation and Brightpoint, Inc. We subsequently withdrew HTC America Holding, Inc., HTC (B.V.I.) Corporation, Exedea, Brightstar, and Brightpoint from the ITC Complaint. The ITC instituted an investigation against Motorola Mobility, Inc., Motorola Mobility Holdings, Inc., HTC Corporation, and HTC America, Inc. on April 2, 2012.

On March 2, 2012, we filed a complaint against HTC Corporation, HTC America Holding, Inc., HTC America, Inc., HTC (B.V.I.) Corporation, Exedea, Inc., Brightstar Corporation and Brightpoint, Inc. (collectively, HTC) in the U.S. District Court for the District of Delaware (the HTC Delaware Complaint) alleging that certain of HTC s mobile electronic devices, including smartphones and cellular phones, infringed six of our patents that cover various uses of haptic effects. The HTC Delaware Complaint covered the same patents as the ITC Complaint. The HTC Delaware Complaint sought damages and injunctive relief. The parties stipulated to stay the case pending the completion of the ITC investigation.

The HTC Delaware Complaint asserted infringement of the following patents:

U.S. Patent No 6,429,846 (the 846 patent): Haptic Feedback for Touchpads and Other Touch Controls

U.S. Patent No 7,969,288 (the 288 patent): Force Feedback System Including Multi-Tasking Graphical Host Environment and Interface Device

U.S. Patent No 7,982,720 (the 720 patent): Haptic Feedback for Touchpads and Other Touch Controls

U.S. Patent No 8,031,181 (the 181 patent): Haptic Feedback for Touchpads and Other Touch Controls

U.S. Patent No 8,059,105 (the 105 patent): Haptic Feedback for Touchpads and Other Touch Controls

HTC asserted that the patents are not infringed, are invalid, and are unenforceable.

On November 21, 2012, we entered into a confidential settlement agreement with Motorola. On January 15, 2013, the Administrative Law Judge issued an Initial Determination terminating the ITC investigation as to Motorola. On March 15, 2013, we dismissed the Motorola Delaware Complaint.

On March 12, 2013, we filed motions to suspend the procedural schedule and to terminate the ITC investigation against HTC. The Administrative Law Judge issued an order granting the motion to suspend the procedural schedule on March 19, 2013 and issued an Initial Determination terminating the ITC investigation as to HTC on March 27, 2013. The decision became final on April 26, 2013.

We requested that the U.S. District Court for the District of Delaware re-open the case against HTC filed in that Court, and the case was reopened on May 1, 2013. We filed an amended complaint on May 3,

2013. HTC answered the amended complaint on June 28, 2013, stating affirmative defenses of (1) non-infringement, (2) invalidity, (3) prosecution history estoppel, (4) equitable estoppel, exhaustion, license, and/or waiver, (5) intervening rights, (6) unclean hands, (7) patent misuse, (8) inequitable conduct based on 720 patent reexamination, (9) inequitable conduct (846 patent family), (10) inequitable conduct (288 patent), (11) double patenting, (12) failure to comply with 35 U.S.C. § 120, and (13) failure to mark / failure to mitigate.

On October 3, 2014, HTC filed five motions with the Court: (1) motion to exclude the testimony of Immersion s damages expert; (2) motion for partial summary judgment shortening the damages period for U.S. Patent Nos. 7,969,288; 7,982,720, and 8,031,18; (3) motion for summary judgment of invalidity of U.S. Patent Nos. 8,059,105; 8,031,181; and 7,982,720; (4) motion for summary judgment of non-infringement of U.S. Patent No. 7,969,288, and; (5) motion for summary judgment of non-infringement of U.S. Patent Nos. 6,429,846; 7,982,720; 8,031,181; and 8,059,105. A hearing on claim construction and the latter three motions was held on November 25, 2014. A hearing on the first motion was held on January 30, 2015. On February 11, 2015, the Court issued rulings on claim construction and on four of HTC s five motions. The Court denied the motion for summary judgment of non-infringement of the 288 patent (because the Court found the 720 and 181 patents invalid as anticipated, it did not address HTC s arguments with regard to these patents); granted in part the motion for summary judgment of non-infringement of the 846, 720, 181, and 105 patents, finding that the HTC s products do not literally infringe the 846, and 105 patents; and granted the motions for partial summary judgment shortening the damages period of the 288 patent, and for summary judgment of invalidity of the 105, 181, and 720 patents. On February 24, 2015 the Court denied in part and granted in part the first motion, ruling that our damages expert may testify about reasonable royalties but not about lost profits.

Trial was scheduled to begin on March 23, 2015. On March 23, 2015, we announced that we agreed to enter into a settlement and license agreement with HTC, resolving the patent infringement litigation, but preserving our right to appeal the invalidity ruling affecting three of our patents. Under the settlement and license agreement, HTC will pay an undisclosed amount of compensation for prior shipments of its devices containing Basic Haptics and an additional undisclosed amount of compensation for a license to continue to manufacture and sell devices with Basic Haptics. On March 31, 2015 the Court entered a Final Judgment providing that HTC does not infringe the 105, 181, and 720 patents solely because the Court ordered that HTC prevailed on its affirmative defense of invalidity, and dismissing our claims of infringement of the 846 and 288 patents pursuant to the settlement and license agreement.

In the U.S. Patent Office, HTC filed requests for ex-parte reexamination of three of our patents: the 288, 999, and 720 patents. Reexamination of the 288 patent was requested on July 30, 2012. The U.S. Patent Office granted the request on October 24, 2012. Reexamination of the 999 patent was requested on September 6, 2012. The U.S. Patent Office granted the request on November 26, 2012. Reexamination of the 720 patent was requested on September 10, 2012. The U.S. Patent Office granted the request on November 28, 2012. On July 24, 2013, the U.S. Patent Office issued a Reexamination Certificate for the 999 patent, after certain claims were cancelled and other claims were amended. On February 18, 2014, the U.S. Patent Office issued a Reexamination Certificate for the 720 patent after certain claims were cancelled and other claims were amended. On February 10, 2014 the U.S. Patent Office issued a Reexamination Certificate for the 288 patent after certain claims were cancelled and claim 18 was amended.

We cannot predict the ultimate outcome of the above-mentioned federal action, and we are unable to estimate any potential liability we may incur.

ITEM 1A. RISK FACTORS

As previously discussed, our actual results could differ materially from our forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to those discussed below. These and many other factors described in this report could adversely affect our operations, performance and financial condition.

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Company Risks

If we are unable to enter into new and renewed licensing arrangements with our existing licensees and with additional third-parties for our touch-enabling technologies, our royalty and license revenue may not grow and could decline.

Our revenue growth is largely dependent on our ability to enter into new and renewed licensing arrangements. Our failure to enter into new or renewed licensing arrangements will cause our operating results to suffer. We face numerous risks in obtaining new or renewed licenses on terms consistent with our business objectives and in maintaining, expanding, and supporting our relationships with our current licensees. These risks include:

- the competition we may face from third parties and/or the internal design teams of existing and potential licensees;
- difficulties in persuading third parties to work with us, to rely on us for critical technology, and to disclose to us proprietary product development and other strategies;
- difficulties in persuading existing licensees who compensate us for including our software in certain of their touch-enabled products to also license and compensate us for our patents that cover other touch-enabled products of theirs that do not include our software;
- challenges in demonstrating the compelling value of our technologies and challenges associated with customers ability to easily implement our technologies;
- difficulties in obtaining new licensees for yet-to-be commercialized technology because their suppliers may not be ready to meet stringent quality and parts availability requirements;
- difficulties in entering into or renewing gaming licenses if video console makers choose not to license third parties to make peripherals for their new consoles, if video console makers no longer require peripherals to play video games, if video console makers no longer utilize technology in the peripherals that are covered by our patents or if the overall market for video consoles deteriorates substantially;
- reluctance of content developers or distributors, mobile device manufacturers, and service providers to sign license agreements without a critical mass of other such inter-dependent supporters of the mobile device industry also having a license, or without enough similar devices in the market that incorporate our technologies; and
- inability of current or prospective licensees to ship certain devices if they are involved in IP infringement claims by third parties that ultimately prevent them from shipping products or that impose substantial royalties on their products.

A limited number of customers account for a significant portion of our revenue, and the loss of major customers could harm our operating results.

Samsung Electronics accounted for approximately 31% and two other customers accounted for 14% and 13% of our total revenues, respectively, for the three months ended March 31, 2015. Samsung Electronics accounted for approximately 32% and another two customers accounted for 18% and 10% of our total revenues, respectively, for the three months ended March 31, 2014. We cannot be certain that customers that have accounted for significant revenue in past periods, individually or as a group, will continue to generate similar revenue in any future period. If we fail to renew or lose a major customer or group of customers, our revenue could decline if we are unable to replace the lost revenue with revenue from other sources.

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Future revenue is difficult to predict, and our failure to predict revenue accurately may cause our results to be below our expectations or those of investors and result in our stock price declining.

Our lengthy and costly license negotiation cycle and any IP litigation that we may engage in make the amount and/or timing of future revenue difficult to predict because we may not be successful in entering into or renewing licenses with our customers on our estimated timelines, and we may be reliant on litigation timelines, which are difficult to control, with unpredictable results.

Some of our license agreements provide for per-unit royalty payments and may also be subject to adjustments based on volume. The sales volume and prices of our licensees products in any given period can be difficult to predict. In addition, in certain product markets, we have entered into licensing agreements pursuant to which customers make fixed recurring payments to us in exchange for use of our IP and technology. As a result, a portion of the revenue we report each quarter results from the recognition of deferred revenue from fixed payments we have received from these customers during previous quarters. If we were to experience significant decline in our ability to renew these agreements or enter into new agreements that include fixed recurring payments, our reported financial results might not reflect such downturns until future periods. Moreover, to the extent our business model depends on fixed payments that we recognize over time, it may also be difficult for us to rapidly increase our revenues through additional sales in any period, as revenue from new customers will be recognized over multiple quarters. Additionally, if we have agreed that a customer may pay us a fixed amount for use of our IP and technology during a given time period, we may receive lower revenues than we would have received under a per unit royalty arrangement if the customer s business grows or it otherwise performs better than we anticipated at the time we entered into our licensing agreement with the customer.

In addition, a portion of our revenue comes from development and support services provided to our licensees, or may be part of a contractual arrangement involving multiple elements. Depending upon the nature of the services or elements, all or a portion of the revenue may be recognized ratably over time or may be deferred in part or in whole.

All of these factors make it difficult to predict future revenue and may result in our revenue being below our previously announced guidance or analysts estimates, which would likely cause our stock price to decline.

Our international expansion efforts subject us to additional risks and costs.

We currently have sales personnel in Japan, Korea, Taiwan, China, and Switzerland and we intend to continue to expand our international activities, including continued investment in Asia. International operations are subject to a number of difficulties and special costs, including:

- compliance with multiple, conflicting and changing governmental laws and regulations;
- laws and business practices favoring local competitors;
- foreign exchange and currency risks;
- import and export restrictions, duties, tariffs, quotas and other barriers;

difficulties staffing and managing foreign operations;

difficulties and expense in enforcing IP rights;

business risks, including fluctuations in demand for our technologies and products and the cost and effort to conduct international operations and travel abroad to promote international distribution and overall global economic conditions;

multiple conflicting tax laws and regulations;

political and economic instability; and

the possibility of an outbreak of hostilities or unrest in markets where major customers are located, including Korea and Hong Kong.

Our international operations could also increase our exposure to international laws and regulations. If we cannot comply with foreign laws and regulations, which are often complex and subject to variation and unexpected changes, we could incur unexpected costs and potential litigation. For example, the governments of foreign countries might attempt to regulate our products or levy sales or other taxes relating to our activities. In addition, foreign countries may impose tariffs, duties, price controls, or other restrictions on foreign currencies or trade barriers, any of which could make it more difficult for us to conduct our business. Our international operations could also increase our exposure to complex international tax rules and regulations. Changes in, or interpretations of, tax rules and regulations may adversely affect our income tax provision. In addition, our operations outside the United States may be affected by changes in trade protection laws, policies and measures, and other regulatory requirements affecting trade and investment, including the Foreign Corrupt Practices Act and local laws prohibiting corrupt payments by our employees, vendors, or agents.

The terms in our agreements may be construed by our licensees in a manner that is inconsistent with the rights that we have granted to other licensees, or in a manner that may require us to incur substantial costs to resolve conflicts over license terms.

We have entered into, and we expect to continue to enter into, agreements pursuant to which our licensees are granted rights to our technology and under our IP. These rights may be granted in certain fields of use, or with respect to certain market sectors or product categories, and may include exclusive rights or sublicensing rights. We refer to the license terms and restrictions in our agreements, including, but not limited to, field of use definitions, market sector, and product category definitions, collectively as License Provisions.

Due to the continuing evolution of market sectors, product categories, and licensee business models, and to the compromises inherent in the drafting and negotiation of License Provisions, our licensees may interpret License Provisions in their agreements in a way that is different from our interpretation of such License Provisions, or in a way that is in conflict with the rights that we have granted to other licensees. Such interpretations by our licensees may lead to claims that we have granted rights to one licensee that are inconsistent with the rights that we have granted to another licensee. Many of our customers report royalties to us based on their shipments or their revenues and their interpretation and allocation of contracted royalty rates. It is possible that the originally reported royalties could differ materially from those determined by either a customer self-reported correction or from an audit we have performed. These interpretations may also cause disagreements arising during customer audits, may lead to claims or litigation, and may have an adverse effect on the results of our operations. Further, although our agreements generally give us the right to audit books and records of our licensees, audits can be expensive, time consuming, and may not be cost justified based on our understanding of our licensees businesses. Pursuant to our license compliance program, we audit certain licensees to review the accuracy of the information contained in their royalty reports in an effort to decrease the risk of our not receiving royalty revenues to which we are entitled, but we cannot give assurances that such audits will be effective.

In addition, after we enter into an agreement, it is possible that markets and/or products, or legal and/or regulatory environments, will evolve in an unexpected manner. As a result, in any agreement, we may have granted rights that will preclude or restrict our exploitation of new opportunities that arise after the execution of the agreement.

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Competing technologies may harm our business.

One of our biggest sources of competition is derived from decisions made by internal design groups at our original equipment manufacturer (OEM) customers and potential OEM customers. These internal design groups typically make choices regarding whether to implement haptics or not, whether to use our software or other standard haptic capability (e.g., haptic capability offered by the Android operating system), or even whether to develop their own haptic solutions. In instances where the design team elects not to use our software but implements unlicensed haptic capability, we may seek to enforce our IP. If the OEM is unwilling to enter into a license agreement, we may elect to pursue litigation which would harm our relationship with the OEM and could harm our relationships with other licensees or our ability to gain new customers, who may postpone licensing decisions pending the outcome of the litigation or dispute, or who may, as a result of such litigation, choose not to adopt our technologies. In addition, these legal proceedings could be very expensive and could have a negative impact on our financial results.

In our OEM agreements, we typically grant licenses to our patent portfolio for one or more specified fields of use. Depending on the specific terms of our agreement with an OEM, the OEM s internal design group may be able to develop technology that is less expensive to implement or that enables products with higher performance or additional features than our own technology and products. Many of these internal design groups have substantially greater resources, greater financial strength and lower cost structures than we do. They also have the inherent advantage of access to internal corporate strategies, technology roadmaps and technical information. As a result, they may be able to bring alternative solutions to market more easily and quickly.

In addition to licensing OEMs directly, we also license to semiconductor manufacturers who incorporate certain of our less advanced technologies into their integrated circuits for use in certain electronic devices. While our relationships with these semiconductor manufacturers increases our distribution channels by leveraging their sales channels, it is possible that OEMs may elect to implement haptics using less advanced integrated circuit solutions rather than the higher-end solutions we offer directly, which may negatively impact our financial results.

Winning business is often subject to a competitive selection process that can be lengthy and requires us to incur significant expense, and we may not be selected.

In many cases, we must win competitive selection processes, known as design wins, before our haptic technologies are included in our customers products. These selection processes can be lengthy and can require us to incur significant design and development expenditures. We may not win the competitive selection process and may never generate any revenue despite incurring significant design and development expenditures. Because we typically focus on only a few customers in a given product area, the loss of a design win may result in our failure to have haptics added to new generation products in that area. This can result in lost sales and could hurt our position in future competitive selection processes to the extent we are not perceived as being a technology leader.

After winning a product design for one of our customers, we may still experience delays in generating revenue as a result of lengthy customer development and design cycles. In addition, a change, delay or cancellation of a customer s plans could significantly adversely affect our financial results, as we may have incurred significant expense and generated no revenue. Finally, even if a design is introduced, if our customers fail to successfully market and sell their products, it could materially adversely affect our business, financial condition, and results of operations.

We are currently involved in appealing a judgment invalidating three of our patents; any final judgment invalidation or limiting of the scope of these patents could harm our business.

As more fully described under Part II, Item 1- Legal Proceedings, we are currently involved in appealing a judgment invalidating three of our patents. We cannot predict the outcome of the appeal. If there is a final adverse ruling invalidating the patents, we could be prevented from enforcing, or earning future revenues from those patents, and the likelihood that customers will take new licenses and that current licensees will continue to agree to pay under their existing licenses could be reduced. The resulting reduction in license fees and royalties could harm our business, consolidated financial position, results of operations or cash flows, or the trading price of our common stock.

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Our current or any future litigation is expensive, disruptive, and time consuming, and will continue to be, until resolved, and regardless of whether we are ultimately successful, could adversely affect our business.

We have been in the past and are currently a party to various legal proceedings. Due to the inherent uncertainties of litigation, we cannot accurately predict how these cases will ultimately be resolved. We anticipate that currently pending or any future litigation will continue to be costly and that future litigation will result in additional legal expenses, and there can be no assurance that we will be successful or be able to recover the costs we incur in connection with litigation. We expense litigation costs as incurred, and only accrue for costs that have been incurred but not paid to the vendor as of the financial statement date. Although protecting our intellectual property is a fundamental part of our business, at times, our litigation has diverted, and could continue to divert, the efforts and attention of some of our key management and personnel away from our licensing transactions. As a result, until such time as it is resolved or concluded, litigation could adversely affect our business. Further, any unfavorable outcome could adversely affect our business. For additional background on our litigation, please see Note 12 to the condensed consolidated financial statements in Part I, Item 1- Financial Statements and Supplementary Data and Part II, Item 1- Legal Proceedings .

We may not be able to continue to derive significant revenues from makers of peripherals for popular video gaming platforms.

A significant portion of our gaming royalty revenues come from third-party peripheral makers who make licensed gaming products designed for use with popular video game console systems from Microsoft, Sony, and Nintendo. Video game console systems are closed, proprietary systems, and video game console system makers typically impose certain requirements or restrictions on third-party peripheral makers who wish to make peripherals that will be compatible with a particular video game console system. If third-party peripheral makers cannot or are not allowed to satisfy these requirements or restrictions, our gaming royalty revenues could be significantly reduced. Furthermore, should a significant video game console maker choose to omit touch-enabling capabilities from its console systems or somehow restrict or impede the ability of third parties to make touch-enabling peripherals, it could lead our gaming licensees to stop making products with touch-enabling capabilities, thereby significantly reducing our gaming royalty revenues. Also, if the gaming industry changes such that mobile or other platforms increase in popularity at the expense of traditional video game consoles, our gaming royalty revenues could be substantially reduced if we are unable to enter into replacement arrangements enabling us to license our software or IP in connection with gaming on such mobile or other platforms.

Automobiles and medical devices incorporating our touch-enabling technologies are subject to lengthy product development periods, making it difficult to predict when and whether we will receive royalties for these product types.

The product development process for automobiles and medical devices is very lengthy, sometimes longer than four years. We may not earn royalty revenue on our automotive/medical device technologies unless and until products featuring our technologies are shipped to customers, which may not occur until several years after we enter into an agreement with a manufacturer or a supplier to a manufacturer. Throughout the product development process, we face the risk that a manufacturer or supplier may delay the incorporation of, or choose not to incorporate, our technologies into its products, making it difficult for us to predict the royalties we may receive, if any. After the product launches, our royalties still depend on market acceptance of the vehicle, the