IMMERSION CORP
Form 10-Q
May 06, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(MARK ONE)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2016
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.) |

50 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 ý 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 ý 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 ý |
| 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 ý
Number of shares of common stock outstanding at April 28, 2016: 28,821,402.

Table of Contents

IMMERSION CORPORATION
INDEX

Table of Contents

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, 2016 | December 31, 2015 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $20,879 | $25,013 |
| Short-term investments | 39,927 | 39,918 |
| Accounts and other receivables (net of allowances for doubtful accounts of $15) | 4,774 | 1,213 |
| Prepaid expenses and other current assets | 2,679 | 2,790 |
| Total current assets | 68,259 | 68,934 |
| Property and equipment, net | 4,412 | 4,589 |
| Deferred income tax assets | 26,262 | 24,633 |
| Prepaid income taxes | 6,270 | 6,995 |
| Intangibles and other assets, net | 245 | 264 |
| Total assets | $105,448 | $105,415 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $2,978 | $650 |
| Accrued compensation | 2,769 | 4,840 |
| Other current liabilities | 2,782 | 2,999 |
| Deferred revenue | 6,943 | 6,696 |
| Total current liabilities | 15,472 | 15,185 |
| Long-term deferred revenue | 1,121 | 2,516 |
| Other long-term liabilities | 837 | 1,099 |
| Total liabilities | 17,430 | 18,800 |
| Contingencies (Note 12) | | |
| Stockholders' equity: | | |
| Common stock and additional paid-in capital — $0.001 par value; 100,000,000 shares authorized; 35,334,795 and 34,845,310 shares issued, respectively; 28,818,901 and 28,329,416 shares outstanding, respectively | 216,181 | 212,115 |
| Accumulated other comprehensive income | 118 | 86 |
| Accumulated deficit | (82,643) | (79,948) |
| Treasury stock at cost: 6,515,894 shares | (45,638) | (45,638) |
| Total stockholders' equity | 88,018 | 86,615 |
| Total liabilities and stockholders' equity | $105,448 | $105,415 |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

IMMERSION CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE LOSS
(In thousands, except per share amounts)
(Unaudited)

| | Three Months Ended March 31, 2016 | Three Months Ended March 31, 2015 |
|---|---|---|
| Revenues: | | |
| Royalty and license | $13,448 | $16,012 |
| Development, services, and other | 175 | 275 |
| Total revenues | 13,623 | 16,287 |
| Costs and expenses: | | |
| Cost of revenues (exclusive of amortization of intangibles shown separately below) | 23 | 115 |
| Sales and marketing | 3,803 | 4,210 |
| Research and development | 4,312 | 3,727 |
| General and administrative | 10,090 | 8,293 |
| Amortization of intangibles | 3 | 12 |
| Total costs and expenses | 18,231 | 16,357 |
| Operating loss | (4,608) | (70) |
| Interest and other income (expense) | 212 | (25) |
| Loss before benefit for income taxes | (4,396) | (95) |
| Benefit for income taxes | 1,701 | 36 |
| Net loss | $(2,695) | $(59) |
| Basic and diluted net loss per share | $(0.09) | $0.00 |
| Shares used in calculating basic and diluted net loss per share | 28,493 | 27,818 |
| Other comprehensive income | | |
| Change in unrealized gains on short-term investments | 32 | 1 |
| Total other comprehensive income | 32 | 1 |
| Total comprehensive loss | $(2,663) | $(58) |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

IMMERSION CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Cash flows provided by (used in) operating activities: | | |
| Net loss | $(2,695) | $(59) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization of property and equipment | 224 | 314 |
| Amortization of intangibles | 3 | 12 |
| Stock-based compensation | 2,334 | 1,740 |
| Allowance for doubtful accounts | — | 8 |
| Changes in operating assets and liabilities: | | |
| Accounts and other receivables | (3,561) | 1,111 |
| Deferred income taxes | (1,629) | (138) |
| Prepaid income taxes | 725 | — |
| Prepaid expenses and other current assets | 111 | 248 |
| Other operating assets | (16) | (10) |
| Accounts payable | 2,328 | 887 |
| Accrued compensation and other current liabilities | (2,270) | 1,477 |
| Deferred revenue | (1,148) | 15,789 |
| Other long-term liabilities | (262) | 119 |
| Net cash provided by (used in) operating activities | (5,856) | 21,498 |
| Cash flows provided by (used in) investing activities: | | |
| Purchases of short-term investments | (9,945) | (4,994) |
| Proceeds from maturities of short-term investments | 10,000 | 10,000 |
| Purchases of property and equipment | (65) | (783) |
| Net cash provided by (used in) investing activities | (10) | 4,223 |
| Cash flows provided by financing activities: | | |
| Issuance of common stock under employee stock purchase plan | 128 | 190 |
| Exercise of stock options | 1,604 | 64 |
| Net cash provided by financing activities | 1,732 | 254 |
| Net increase (decrease) in cash and cash equivalents | (4,134) | 25,975 |
| Cash and cash equivalents: | | |
| Beginning of period | 25,013 | 14,380 |
| End of period | $20,879 | $40,355 |
| Supplemental disclosure of cash flow information | | |
| Cash paid for taxes | $(529) | $70 |
| Supplemental disclosure of noncash operating, investing, and financing activities | | |
| Amounts accrued for property and equipment | $— | $965 |
| Release of Restricted Stock Units and Awards under company stock plan | $1,777 | $2,184 |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

IMMERSION CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2016
(Unaudited)

1. SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Immersion Corporation (the “Company”) was incorporated in 1993 in California and reincorporated in Delaware in 1999. The Company focuses on the creation, design, development, and licensing of innovative haptic technologies that allow people to use their sense of touch more fully as they engage with cutting-edge products and experience the digital world around them. The Company has adopted a “hybrid” business model, under which it provides advanced tactile software, related tools, and technical assistance to certain customers; and offers licenses to the Company's patented intellectual property (“IP”) to other customers.

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 Corporation; 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 Ltd. 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, 2015. 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, 2016 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.

Table of Contents

- 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 offered 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. In August 2015, the FASB issued ASU No. 2015-14 "Revenue from Contracts with Customers: Deferral of the Effective Date", which deferred the effective date of ASU 2014-09 for periods beginning after December 15, 2016 to December 15, 2017, with early adoption permitted but not earlier than the original effective date.

Table of Contents

Accordingly, ASU 2014-09 is effective for the Company and is expected to be adopted in the first quarter of fiscal 2018. The standard 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, and the Company is in the process of determining the method of adoption and evaluating the impact on its consolidated financial statements.
In February 2016, the FASB issued ASU 2016-02 “Leases: Topic 842” (“ASU 2016-02”) which supersedes the existing guidance for lease accounting in Topic 840, Leases. The FASB issued the standard to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. ASU 2016-02 requires lessees to recognize a lease liability and a right-of-use asset for all leases. Lessor accounting remains largely unchanged. The amendments of this ASU are effective for periods beginning after December 15, 2018, with early adoption permitted. An entity will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently in the process of evaluating the impact of this standard on its consolidated financial statements.
In March 2016, the FASB issued ASU 2016-09 “Compensation - Stock Compensation: Topic 718” (“ASU 2016-09”) which simplifies several aspects of the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification in the statement of cash flows. The standard is effective for periods beginning after December 15, 2016, with early adoption permitted. The Company is currently in the process of evaluating the impact of this standard 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 U.S. treasury securities.
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, 2016 and December 31, 2015.
Financial instruments measured at fair value on a recurring basis as of March 31, 2016 and December 31, 2015 are classified based on the valuation technique in the table below:

| | March 31, 2016 | | | |
|---|---|---|---|---|
| | 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 | $— | $ 39,927 | $ — | $39,927 |
| Money market accounts | 6,041 | — | — | 6,041 |
| Total assets at fair value | $6,041 | $ 39,927 | $ — | $45,968 |

8

Table of Contents

The above table excludes $14.8 million of cash held in banks.

| | December 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 | $— | $ 39,918 | | $39,918 |
| Money market accounts | 14,032 | — | — | 14,032 |
| Total assets at fair value | $14,032 | $ 39,918 | $ — | $53,950 |

The above table excludes $11.0 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, 2016 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Holding Gains | Gross Unrealized Holding Losses | Fair Value |
| | (In thousands) | | | |
| U.S. Treasury securities | $39,910 | $ 17 | $ — | $39,927 |
| Total | $39,910 | $ 17 | $ — | $39,927 |

| | December 31, 2015 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Holding Gains | Gross Unrealized Holding Losses | Fair Value |
| | (In thousands) | | | |
| U.S. Treasury securities | $39,933 | $ — | $ (15 ) | $39,918 |
| Total | $39,933 | $ — | $ (15 ) | $39,918 |

The contractual maturities of the Company’s available-for-sale securities on March 31, 2016 and December 31, 2015 were all due within one year. There were no transfers of instruments between Level 1 and 2 during the three months ended March 31, 2016 and the year ended December 31, 2015.

3. ACCOUNTS AND OTHER RECEIVABLES

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| | (In thousands) | |
| Trade accounts receivable | $4,392 | $ 935 |

| | | |
|---|---|---|
| Receivables from vendors and other | 382 | 278 |
| Accounts and other receivables | $4,774 | $ 1,213 |

Table of Contents

4. PROPERTY AND EQUIPMENT

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| | (In thousands) | |
| Computer equipment and purchased software | $3,571 | $ 3,564 |
| Machinery and equipment | 959 | 923 |
| Furniture and fixtures | 1,365 | 1,361 |
| Leasehold improvements | 3,838 | 3,838 |
| Total | 9,733 | 9,686 |
| Less accumulated depreciation | (5,321 ) | (5,097 ) |
| Property and equipment, net | $4,412 | $ 4,589 |

5. INTANGIBLES AND OTHER ASSETS

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| | (In thousands) | |
| Purchased patents and other purchased intangible assets | $4,605 | $ 4,605 |
| Less: Accumulated amortization of purchased patents and other purchased intangibles | (4,602 ) | (4,599 ) |
| Purchased patents and other purchased intangible assets, net | 3 | 6 |
| Other assets | 242 | 258 |
| Intangibles and other assets, net | $245 | $ 264 |

The Company amortizes its intangible assets related to purchased patents, over their estimated useful lives, generally 10 years from the purchase date. The Company recorded $3,000 and $12,000 in amortization of purchased patents in the three months ended March 31, 2016 and 2015, respectively. The remaining $3,000 in net book value of purchased patents as of March 31, 2016 will be amortized during the remainder of 2016.

6. OTHER CURRENT LIABILITIES

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| | (In thousands) | |
| Accrued legal | $1,723 | $ 1,458 |
| Accrued services | 261 | 849 |
| Income taxes payable | 175 | 129 |
| Other current liabilities | 623 | 563 |
| Total other current liabilities | $2,782 | $ 2,999 |

7. LONG-TERM DEFERRED REVENUE

Long-term deferred revenue consisted of the following:

| | March 31, 2016 | December 31, 2015 |
|---|---|---|
| | (In thousands) | |
| Deferred revenue for Sony Computer Entertainment | $— | $ 1,263 |

| | | |
|---|---|---|
| Other deferred revenue | 1,121 | 1,253 |
| Long-term deferred revenue | $1,121 | $ 2,516 |

8. STOCK-BASED COMPENSATION

10

Table of Contents

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 seven 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.

| | March 31, 2016 |
|---|---|
| Common stock shares available for grant | 729,149 |
| Standard and market condition stock options outstanding | 3,681,244 |
| Restricted stock awards outstanding | 21,356 |
| Restricted stock units outstanding | 527,883 |

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, 2016, 621,269 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, 2016 are listed below. Shares purchased under the ESPP for the three months ended March 31, 2015 are 23,713. 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, 2016 |
|---|---|
| Shares purchased under ESPP | 17,711 |
| Average price of shares purchased under ESPP | $7.21 |
| Intrinsic value of shares purchased under ESPP | $23,000 |

Table of Contents

Summary of Standard Stock Options

The following table sets forth the summary of activity with respect to standard stock options granted under the Company's stock option plans for the three months ended March 31, 2016:

| | Three Months Ended March 31, 2016 |
|---|---|
| Beginning outstanding balance | 3,596,533 |
| Granted | 344,200 |
| Exercised | (261,421 ) |
| Forfeited | (213,831 ) |
| Expired | (9,237 ) |
| Ending outstanding balance | 3,456,244 |
| Aggregate intrinsic value of options exercised | $650,000 |
| Weighted average fair value of options granted | 4.05 |

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the exercise 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, 2016 is summarized below:

| | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (years) | Aggregate Intrinsic Value (in millions) |
|---|---|---|---|---|
| March 31, 2016 | | | | |
| Options outstanding | 3,456,244 | $ 8.57 | 4.07 | $ 3.6 |
| Options vested and expected to vest using estimated forfeiture rates | 3,298,519 | 8.51 | 3.96 | 3.6 |
| Options exercisable | 2,216,349 | 7.93 | 3.17 | 3.5 |

Summary of Market Condition Based Stock Options

The following table sets forth activity with respect to market condition based stock options granted under the Company's stock option plans for the three months ended March 31, 2016:

| | Three Months Ended March 31, 2016 |
|---|---|
| Beginning outstanding balance | 200,000 |
| Granted | 75,000 |
| Exercised | — |
| Canceled | (50,000 ) |
| Ending outstanding balance | 225,000 |
| Aggregate intrinsic value of options exercised | $ — |
| Weighted average fair value of options granted | 3.68 |

Information regarding these market condition based stock options outstanding at March 31, 2016 is summarized below:

Table of Contents

| | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (years) | Aggregate Intrinsic Value (in millions) |
|---|---|---|---|---|
| March 31, 2016 | | | | |
| Options outstanding | 225,000 | $ 8.39 | 6.25 | $ — |
| Options vested and expected to vest using estimated forfeiture rates | 201,915 | 8.37 | 6.23 | — |
| Options exercisable | 37,500 | 8.09 | 5.92 | — |

Summary of Restricted Stock Units

RSU activity for the three months ended March 31, 2016 was as follows:

| | Three Months Ended March 31, 2016 |
|---|---|
| Beginning outstanding balance | 487,423 |
| Awarded | 294,880 |
| Released | (210,353) |
| Forfeited | (44,067 ) |
| Ending outstanding balance | 527,883 |
| Weighted average grant date fair value of RSUs granted | $ 8.85 |
| Total fair value of RSUs released | 1,777,000 |

Information regarding RSUs outstanding at March 31, 2016 is summarized below:

| | Number of Shares | Weighted Average Remaining Contractual Life (years) | Aggregate Intrinsic Value (in millions) |
|---|---|---|---|
| March 31, 2016 | | | |
| RSUs outstanding | 527,883 | 1.60 | $ 4.4 |
| RSUs vested and expected to vest using estimated forfeiture rates | 403,526 | 1.56 | 3.3 |

Summary of Restricted Stock Awards

Restricted stock award activity for the three months ended March 31, 2016 was as follows:

| | Three Months Ended March 31, 2016 |
|---|---|
| Beginning outstanding balance | 21,356 |
| Awarded | — |
| Released | — |
| Forfeited | — |
| Ending outstanding balance | 21,356 |
| Weighted average grant date fair value of restricted stock awarded | $ — |
| Total fair value of restricted stock awards released | — |

Stock Plan Assumptions

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

Table of Contents

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Standard Stock Options | | |
| Expected life (in years) | 4.5 | 4.7 |
| Volatility | 57 % | 56 % |
| Interest rate | 1.3 % | 1.4 % |
| Dividend yield | N/A | N/A |

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Market Condition Based Stock Options | | |
| Expected life (in years) | 7.0 | 7.0 |
| Volatility | 59 % | 65 % |
| Interest rate | 1.6 % | 1.9 % |
| Dividend yield | N/A | N/A |

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Employee Stock Purchase Plan | | |
| Expected life (in years) | 0.5 | 0.5 |
| Volatility | 53 % | 45 % |
| Interest rate | 0.5 % | 0.1 % |
| Dividend yield | N/A | N/A |

Compensation Costs

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

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| | (In thousands) | |
| Statement of Operations Classifications | | |
| Sales and marketing | $228 | $264 |
| Research and development | 526 | 496 |
| General and administrative | 1,580 | 980 |
| Total | $2,334 | $1,740 |

As of March 31, 2016, there was $8.9 million of unrecognized compensation cost, adjusted for estimated forfeitures, related to non-vested stock options, restricted stock awards and RSUs granted to the Company’s employees and directors. This cost will be recognized over an estimated weighted-average period of approximately 2.70 years for standard options, 3.01 years for market condition based options, 2.35 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

Accumulated Other Comprehensive Income

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

Table of Contents

| | Three Months Ended March 31, 2016 | | |
|---|---|---|---|
| | Unrealized Gains and Losses on Available-for Sale Securities | Foreign Currency Items | Total |
| | (In thousands) | | |
| Beginning balance | $(15) | $ 101 | $86 |
| Other comprehensive income before reclassifications | 32 | — | 32 |
| Amounts reclassified from accumulated other comprehensive income | — | — | — |
| Net current period other comprehensive income | 32 | — | 32 |
| Ending Balance | $17 | $ 101 | $118 |

Stock Repurchase Program

On November 1, 2007, the Company announced its Board of Directors (the "Board")' authorized the repurchase of up to $50.0 million of the Company's common stock ("Stock Repurchase Program"). In addition, on October 22, 2014, the Board authorized another $30.0 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, 2016 and 2015. As of March 31, 2016, the program remains available with approximately $34.4 million that may yet be purchased under the Stock Repurchase Program.

10. INCOME TAXES

Income tax provisions consisted of the following:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| | (In thousands) | |
| Loss before benefit for income taxes | $(4,396) | $(95) |
| Benefit for income taxes | 1,701 | 36 |
| Effective tax rate | 38.7 % | 37.9 % |

The benefit for income tax for the three months ended March 31, 2016 and 2015 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. The benefit for income tax for the three months ended March 31, 2016 also includes non-cash tax expense on intercompany profit that resulted from the sale of certain IP rights to one of the Company's foreign subsidiaries as part of the Company's reorganization of its international operations during the second half of 2015. Discrete items recognized for the three months ended March 31, 2016 include a tax refund related to the settlement with a taxing authority and the release of certain reserves and related accrued interest.

On July 27, 2015, a U.S. Tax Court opinion (Altera Corporation et. al v. Commissioner) concerning the treatment of stock-based compensation expense in an intercompany cost sharing arrangement was issued. In its opinion, the U.S. Tax Court accepted Altera's position of excluding stock-based compensation from its intercompany cost sharing arrangement. On February 19, 2016, the IRS appealed the ruling to the United States Court of Appeals for the Ninth Circuit. Although the IRS has appealed the decision, based on the findings of the U.S. Tax Court, the Company has concluded that it is more likely than not that the decision will be upheld and accordingly has excluded stock-based compensation from intercompany charges during the period. The Company will continue to monitor ongoing developments and potential impacts to its condensed consolidated financial statements.

Table of Contents

As of March 31, 2016, the Company had unrecognized tax benefits under ASC 740 “Income Taxes”, of approximately $6.2 million and there was no applicable interest. The total amount of unrecognized tax benefits that would affect the Company’s effective tax rate, if recognized, was $2.4 million. The Company released reserves totaling $310,000 including interest and recorded a tax benefit due to the receipt of a tax refund related to the settlement with a taxing authority as noted above. The Company’s policy is to account for interest and penalties related to uncertain tax positions as a component of income tax provision. We do not expect to have any significant changes to unrecognized tax benefits during the next twelve months.

Net deferred income taxes were $26.3 million as of March 31, 2016, 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 $8.2 million against certain of its deferred tax assets, including federal, 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 federal, state and foreign deferred tax assets.

## 11. NET LOSS PER SHARE

Basic and diluted net loss per share is computed using the weighted average number of common shares outstanding for the period, excluding unvested restricted stock and RSUs. The following is a reconciliation of the numerators and denominators used in computing basic and diluted net loss per share:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| | (in thousands except per share amounts) | |
| Numerator: | | |
| Net loss | $(2,695) | $(59) |
| Denominator: | | |
| Shares used in computation of basic and diluted net loss per share (weighted average common shares outstanding) | 28,493 | 27,818 |
| Basic and diluted net loss per share | $(0.09) | $0.00 |

The Company includes the underlying market condition stock options in the calculation of diluted earnings per share if the performance condition has been satisfied as of the end of the reporting period and excludes such options if the performance condition has not been met.

As of March 31, 2016 and 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, 2016 and 2015, since their effect would have been anti-dilutive. These outstanding securities consisted of the following:

| | March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Outstanding stock options | 3,681,244 | 3,875,153 |
| Unvested RSUs | 527,883 | 565,148 |

## 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.

Table of Contents

In the normal course of business, the Company provides indemnification 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.

Table of Contents

## 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 licensing company focused on the creation, design, development, and licensing of innovative haptic technologies that allow people to use their sense of touch more fully as they engage with cutting-edge products and experience the digital world around them. 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. Our technologies are designed to facilitate the creation of high-quality haptic experiences, enable their widespread distribution, and ensure that their playback is optimized for end users. Our primary business is currently in the mobility, gaming, automotive and medical markets, but we believe our technology is broadly applicable and see opportunities in evolving new markets, including entertainment, social and advertising content, virtual and augmented reality, and wearables.

We have adopted a "hybrid" business model, under which we provide advanced tactile software, related tools and technical assistance to certain customers, and offer licenses to our patented IP to other customers. Our licenses enable our customers to deploy haptically-enabled devices, content and other offerings, which they typically sell under their own brand names. We and our wholly-owned subsidiaries hold more than 2,200 issued or pending patents worldwide, covering a wide range of digital technologies and including many of the ways in which touch-related technology can be incorporated into and between hardware products and components, 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, contingencies, and litigation. We base our estimates and assumptions on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates and assumptions.

Our critical accounting policies and estimates are important to the portrayal of our financial condition and results of operations, and require us to make judgments and estimates about matters that are inherently uncertain. There have been no material changes during the three months ended March 31, 2016 to the items we disclosed as our critical accounting policies and estimates in our Management Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2016 AND 2015

The following discussion and analysis includes our results of operations for the three months ended March 31, 2016 and 2015.

Table of Contents

Overview

Total revenue decreased by 16% for the three months ended March 31, 2016 compared to the three months ended March 31, 2015, driven primarily by a decrease in royalty and license revenue in our mobility business primarily as a result of the absence of revenue from Samsung, partially offset by increased royalty and license revenue from gaming, auto, and medical licensees. In the first quarter of 2016, we initiated arbitration against Samsung to recover revenue from products that were licensed under our agreement with them that expired at the end of 2015 that Samsung continues to ship following the expiration of the agreement. See Part II, Item 1. Legal Proceedings.

Our net loss was $2.7 million for the three months ended March 31, 2016 as compared to a net loss of $59,000 for the three months ended March 31, 2015. The increase in net loss was primarily due to the decrease in royalty and license revenue and an increase in operating expenses primarily as a result of our efforts to protect and preserve our intellectual property, including the initiation of litigation against Apple, AT&T, and AT&T Mobility, as well as a reduction in headcount which was the result of a rebalancing of the organization to align our employees' skill sets with our current operational and strategic outlook.

| REVENUES | March 31, 2016 | March 31, 2015 | Change | % Change |
|---|---|---|---|---|
| | (In thousands) | | | |
| Three months ended: | | | | |
| Royalty and license | $13,448 | $16,012 | $(2,564) | (16)% |
| Development, services, and other | 175 | 275 | (100) | (36)% |
| Total Revenues | $13,623 | $16,287 | $(2,664) | (16)% |

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 decrease in royalty and license revenue for the three months ended March 31, 2016 compared to the three months ended March 31, 2015 was primarily due to decreases in royalty and license revenue from our mobility licensees, primarily Samsung, partially offset by increases in royalty and license revenue from our gaming and auto licensees and a non-recurring license fee from a medical customer.

Variable royalty revenue based on shipping volumes and per unit prices decreased to $8.5 million for the three months ended March 31, 2016 from $8.6 million for the three months ended March 31, 2015. Fixed payment license revenue decreased to $4.9 million for the three months ended March 31, 2016 from $7.4 million for the three months ended March 31, 2015, primarily due to the absence of revenue from Samsung, partially offset by a non-recurring license fee of $3.0 million from a medical customer.

Royalty and license revenue from mobility customers decreased by 60%, primarily due to the absence of revenue from Samsung, and to a lesser extent due to a lower number of mobile device shipments by our licensees. We anticipate that our mobility business will continue to be of primary importance, but will fluctuate as a result of the outcomes of our various enforcement actions, the timing of introductions of new products with our technology into the market, and the recognition by mobile OEMs of the relevance of our IP.

Royalty and license revenue from medical customers increased by 135%, primarily due to a non-recurring license fee of $3.0 million from a medical customer.

Royalty and license revenue from gaming customers increased by 9%, primarily due to increased sales by our licensees of products containing our technology. Revenue from gaming customers can fluctuate based upon consumer gaming preferences, the timing of introductions of new gaming console systems, the timing of new products from third party peripheral makers that are our licensees, and the recognition by gaming customers of the relevance of our IP.

Royalty and license revenue from automotive customers increased by 11%, primarily due to increased sales by our licensees.

We expect royalty and license revenue to be the major component of our future revenue as our technology continues to be included in 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. Our mobility revenue could be adversely impacted if we receive an unfavorable result in our arbitration against Samsung. Our gaming royalty and license revenue could be adversely impacted in 2016 by the expiration of several gaming patents in 2015.

Table of Contents

We categorize our geographic information into three major regions: North America, Europe and Asia. In the three months ended March 31, 2016, revenue generated in North America, Europe and Asia represented 57%, 10% and 33% of total revenue, respectively, compared to 36%, 4% and 60% of total revenues, respectively, for the three months ended March 31, 2015. The shift in revenues among regions was mainly due to a decrease in royalty and license revenue in Asia mainly due to the absence of revenue from Samsung. The increase in royalty and license revenue in North America was mainly due to increased revenue from our medical licensees. The increase in royalty and license revenue in Europe was mainly due to increased revenue from our gaming licensees.

| OPERATING EXPENSES | March 31, 2016 | 2015 | Change | % Change |
|---|---|---|---|---|
| | (Dollars in thousands) | | | |
| Three months ended: | | | | |
| Sales and marketing | $3,803 | $4,210 | $(407) | (10)% |
| % of total revenue | 28 % | 26 % | 2 % | |
| Research and development | $4,312 | $3,727 | $585 | 16 % |
| % of total revenue | 32 % | 23 % | 9 % | |
| General and administrative | $10,090 | $8,293 | $1,797 | 22 % |
| % of total revenue | 74 % | 51 % | 23 % | |
| Amortization of intangibles | $3 | $12 | $(9) | (75)% |
| % of total revenue | — % | — % | — % | |

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 decrease in sales and marketing expense for the three months ended March 31, 2016 as compared to the three months ended March 31, 2015 was primarily due to a $550,000 decrease in marketing and advertising costs and a $96,000 decrease in travel costs mainly attributed to cost reductions related to trade shows, partially offset by a $251,000 increase in compensation, benefits, and other related costs mainly due to our rebalancing efforts. We expect that sales and marketing expenses will increase in 2016 as we continue to invest in sales and marketing to further market acceptance for our touch technologies and expand 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, 2016 as compared to the three months ended March 31, 2015 was primarily due to a $677,000 increase in compensation, benefits, and other related costs mainly due to our rebalancing efforts, partially offset by a $101,000 decrease in travel costs. We believe that continued investment in research and development is critical to our future success, and we expect to continue making investments in areas of research and technology development to support future growth including 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; patent related legal, filing, and maintenance costs; office supplies; travel; and an allocation of facilities costs. The increase in general and administrative expenses for the three months ended March 31, 2016 as compared to the three months ended March 31, 2015 was primarily due to a $984,000 increase in legal and professional fees and a $794,000 increase in compensation, benefits, and other related costs, mainly due to increased headcount and stock compensation expense. The increased legal and professional fees were primarily due to a $1.3 million increase in professional services and licensing-related legal expenses mainly in preparation for our recent litigation filings; and a $232,000 increase in patent related legal, filing, and maintenance costs; partially offset by a $541,000 decrease in litigation expense relating to completed litigation. Our general and administrative expenses will continue to be significant as we manage our business and strategic opportunities and continue to file, maintain, license, and enforce our IP and contractual rights, including in the current litigation against

Apple and AT&T Mobility, and defend any lawsuits brought against us or that we initiate against others to enforce our IP or contractual rights.

Table of Contents

| BENEFIT FOR TAXES | March 31, 2016 | 2015 | Change | % Change |
|---|---|---|---|---|
| | (Dollars in thousands) | | | |
| Three months ended: | | | | |
| Benefit for income taxes | $ 1,701 | $ 36 | $ 1,665 | 4,625 % |
| Loss before benefit for income taxes | (4,396 ) | (95 ) | | |
| Effective tax rate | 38.7 % | 37.9 % | | |

Benefit for Income Taxes — For the three months ended March 31, 2016 we recorded a benefit for income taxes of $1.7 million yielding an effective tax rate of 38.7%. 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%. The effective tax rates used for each year were estimated based upon a forecast of our full year results and include the tax impact of nondeductible permanent items, including stock-based compensation incurred for the period. The benefit for income tax for the three months ended March 31, 2016 also includes non-cash tax expense on intercompany profits resulting from the sale of certain IP rights to one of our foreign subsidiaries as part of the reorganization of our international operations that occurred in the second half of 2015. The change in benefit for income taxes results primarily from the effects of the above described reorganization, the change in loss before benefit for income taxes, and discrete items recognized for the three months ended March 31, 2016, including a tax refund related to the settlement with a taxing authority and the release of certain reserves and related accrued interest.

We expect that the reorganization of our international operations will result in a lower percentage of pre-tax income being subject to the U.S. federal statutory tax rate. However, our ability to realize the expected tax benefits of this reorganization is contingent upon numerous factors, including our ability to achieve our projected revenue and earnings both domestically and in the various countries in which the reorganization took place and the judgments of tax authorities in several jurisdictions. A change in these factors in future periods relative to our current assumptions may result in additional income tax expense being recorded in future filings.

In 2016, 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. Although we expect to reduce taxes paid in cash, our effective tax rate could fluctuate significantly on a quarterly basis and could be adversely affected to the extent actual earnings are lower than anticipated in countries that have lower statutory rates and higher in countries that have higher statutory rates. Based upon activity during the three months ended March 31, 2016, we continue to maintain a valuation allowance of $1.5 million against U.S. federal deferred tax assets and a valuation allowance of $6.7 million against our state and certain other foreign deferred tax assets, as there was not sufficient evidence to support the release of such valuation allowances as of March 31, 2016.

We also maintain liabilities for uncertain tax positions. The Company released reserves totaling $310,000 including interest and recorded a tax benefit due to the receipt of a tax refund related to the settlement with a taxing authority as noted above. As of March 31, 2016, we had unrecognized tax benefits under ASC 740 "Income Taxes", of approximately $6.3 million and there was no applicable interest. The total amount of unrecognized tax benefits that would affect our effective tax rate, if recognized, is $2.6 million.

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, within stockholders' equity.

On March 31, 2016, our cash, cash equivalents, and short-term investments totaled $60.8 million, a decrease of $4.1 million from $64.9 million on December 31, 2015.

Cash provided by (used in) operating activities

Net cash used in operating activities during the three months ended March 31, 2016 was $5.9 million, a decrease of $27.4 million from the $21.5 million provided by operating activities during the three months ended March 31, 2015. Cash used in operating activities during the three months ended March 31, 2016 was primarily the result of our net loss of $2.7 million, a decrease of $3.6 million due to a change in accounts receivable mainly as a result of the timing of invoices and cash collections, a decrease of $2.3 million due to a change in accrued compensation and other liabilities mainly from a decrease in

Table of Contents

accruals for compensation and benefit related items, a decrease of $1.6 million due to a change in deferred income taxes during the period, and a decrease of $1.1 million in deferred revenue mainly due to recognition of revenue from customers that had previously been deferred. These decreases were partially offset by an increase of $2.3 million due to a change in accounts payable primarily arising from the timing of payments to vendors, and an increase of $725,000 due to a change in prepaid income taxes. Cash used in operating activities during the current period was also affected by noncash charges of $2.6 million, including $2.3 million of noncash stock-based compensation and $227,000 in depreciation and amortization.

Cash provided by (used in) investing activities

Net cash used in investing activities during the three months ended March 31, 2016 was $10,000, a decrease of $4.2 million compared to the $4.2 million provided by investing activities during the three months ended March 31, 2015. Net cash used in investing activities was due to purchases of short-term investments of $9.9 million and purchases of property and equipment of $65,000, partially offset by the maturation of short-term investments of $10.0 million

Cash provided by financing activities

Net cash provided by financing activities during the three months ended March 31, 2016 was $1.7 million compared to $254,000 provided by financing activities during the three months ended March 31, 2015, an increase in cash provided of $1.5 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.

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. Of our total cash, cash equivalents, and short-term investments of $60.8 million as of March 31, 2016, less than 19% was held by our foreign subsidiaries and subject to repatriation tax effects. Our intent is to permanently reinvest all of our earnings from foreign operations, and current plans do not anticipate that we will need funds generated from foreign operations to fund our domestic operations. We will continue to invest in, protect, and defend our extensive IP portfolio, which is expected to result in the continued use of cash. At March 31, 2016, there was $34.4 million remaining under our previously-approved share repurchase program. We anticipate that capital expenditures for property and equipment for the year ended December 31, 2016 will be less than $1.0 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, 2015. Our principal commitments as of March 31, 2016 consisted of obligations under operating leases. There have been no material changes in those obligations during the three months ended March 31, 2016.

As of March 31, 2016, we had a liability for unrecognized tax benefits totaling $6.3 million with no applicable interest, of which approximately $2.6 million could be payable in cash.

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.

Table of Contents

## 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 $46.0 million as of March 31, 2016, 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 $182,000 in the fair value of our cash equivalents and short-term investments as of March 31, 2016.

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, 2016, our management with the participation of our Chief Executive Officer and interim Chief Financial Officer, have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) 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 interim 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, 2016 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 interim 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.

Table of Contents

PART II

OTHER INFORMATION
ITEM 1. LEGAL PROCEEDINGS
Immersion Corporation vs. Apple, Inc., AT&T Inc., and AT&T Mobility LLC
On February 11, 2016, we filed a complaint against Apple, Inc. ("Apple"), AT&T, Inc. ("AT&T"), and AT&T Mobility LLC ("AT&T Mobility") with the U.S. International Trade Commission (the “ITC”) and a complaint against Apple, AT&T and AT&T Mobility in the U.S. District Court for the District of Delaware alleging that the Apple iPhone 6, iPhone 6 Plus, iPhone 6s, iPhone 6s Plus, Apple Watch, Apple Watch Sport and Apple Watch Edition infringe certain of our patents that cover haptic feedback systems and methods.
In the ITC complaint, we are seeking an exclusion order preventing the importation, sale for importation, and sale after importation of infringing Apple devices into the United States by the defendants and appropriate cease and desist orders. In the U.S. District Court suit, we are alleging infringement of the same patents and are seeking to stop further infringement by the defendants, and to recover damages.
The complaints assert infringement by the Apple iPhone 6, Apple iPhone 6 Plus, Apple iPhone 6s, Apple iPhone 6s Plus, Apple Watch, Apple Watch Sport and Apple Watch Edition of the following two Immersion patents:
U.S. Patent No. 8,619,051: "Haptic Feedback System with Stored Effects"
U.S. Patent No. 8,773,356 (the ‘356 patent): "Method and Apparatus for Providing Tactile Sensations"
The complaints also assert infringement by the iPhone 6s and iPhone 6s Plus of the following Immersion patent:
U.S. Patent No. 8,659,571: "Interactivity Model for Shared Feedback on Mobile Devices"
On March 14, 2016, the ITC issued a Notice of Institution of Investigation stating that the ITC instituted an investigation to investigate our allegations of infringement and determine whether violations of section 337 of the Tariff Act of 1930 have occurred. The investigation bears the designation Inv. No. 337-TA-990. On April 5, 2016, the Chief Administrative Law Judge (“Chief ALJ”) overseeing the investigation scheduled a claim construction hearing on July 20, 2016, a hearing before the Chief ALJ on November 14-18, 2016, and a Target Date of June 19, 2017 for the ITC to complete its investigation. On April 6, 2016, the Chief ALJ entered an order terminating Respondent AT&T from the investigation, based on the stipulation and joint motion of the parties to terminate AT&T from the investigation in a manner that preserved our ability to obtain discovery and compliance with any relief the ITC may order. On April 4, 2016, Respondents Apple and AT&T Mobility served responses to the complaint denying the material allegations of the complaint and alleging affirmative defenses, including among others that the asserted patents are not infringed, invalid and unenforceable. Respondents also alleged that the ‘356 patent is unenforceable for alleged inequitable conduct before the United States Patent Office. We will respond to the allegations of Respondents during the investigation on the procedural schedule set by the Chief ALJ. The proceedings in the ITC with respect to Apple and AT&T Mobility are ongoing, and the parties are in the process of conducting discovery.
On March 21, 2016, pursuant to 28 U.S.C. § 1659(a), the U.S. District Court entered an order staying the U.S. District Court case pending a final determination in the ITC investigation.
Although we believe we have strong claims, this litigation is at its early stages and the outcome of litigation is inherently uncertain. Furthermore, Apple and AT&T Mobility have significant resources and therefore, this litigation could be protracted.
On May 5, 2016, we filed another complaint against Apple, AT&T and AT&T Mobility with the ITC and a complaint against Apple, AT&T and AT&T Mobility in the U.S. District Court for the District of Delaware alleging that the Apple iPhone 6, iPhone 6 Plus, MacBook and MacBook Pro with Retina Display infringe certain of our patents, including patents covering pressure-related haptics.
In the ITC complaint, we are seeking an exclusion order preventing the importation, sale for importation, and sale after importation of infringing Apple devices into the United States by the defendants and appropriate cease and desist orders. In the U.S. District Court suit, we are alleging infringement of the same patents and are seeking to stop further infringement by the defendants, and to recover damages.
The complaints assert against Apple, AT&T and AT&T Mobility claims of infringement by the Apple iPhone 6s and Apple iPhone 6s Plus of the following three Immersion patents:

U.S. Patent No. 8,749,507, “Systems and Methods for Adaptive Interpretation of Input from a Touch-Sensitive Input Device”
U.S. Patent No. 7,808,488, “Method and Apparatus for Providing Tactile Sensations”

Table of Contents

U.S. Patent No. 8,581,710, “Systems and Methods for Haptic Confirmation of Commands”
The complaints also assert against Apple claims of infringement by the Apple MacBook and Apple MacBook Pro with Retina display of the following Immersion patent:
U.S. Patent No. 7,336,260, “Method and Apparatus for Providing Tactile Sensations”
Although we believe we have strong claims, this litigation is at its early stages and the outcome of litigation is inherently uncertain. Furthermore, Apple, AT&T and AT&T Mobility have significant resources and therefore, this litigation could be protracted.

Amit Agarwal v. Immersion Corporation
On March 29, 2016, Amit Agarwal, an individual, filed in the United States Patent and Trademark Office a petition for inter partes review of U.S. Patent No. 8,773,356 entitled: "Method and Apparatus for Providing Tactile Sensations." The petition bears Case No. IPR2016-00807. The petition challenges the patentability of certain claims of the ’356 patent in light of alleged prior art references. We have not yet responded to the petition and the Patent Office’s Patent Trial and Appeal Board has not yet determined whether to institute the IPR. Our response to the petition is due ninety days from the petition’s filing date.

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 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

Table of Contents

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. On April 21, 2015 we filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit. The appeal has been docketed as Case No. 15-1574. The appeal is fully briefed, and oral argument was heard on May 6, 2016.

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 actions, and we are unable to estimate any potential liability we may incur.

Samsung Electronics America, Inc.:

On December 31, 2015, our amended and restated license agreement (the “Samsung License”) with Samsung expired. On January 13, 2016, we filed an Application for Emergency Measures with the International Chamber of Commerce (“ICC”), asking that the ICC order Samsung to comply with its contractual obligations and enjoin Samsung from selling devices previously licensed under the Samsung License. On January 25, 2016, we also filed an arbitration demand with the ICC. The ICC appointed an Emergency Arbitrator, who on January 30, 2016 issued an Order denying the Application for Emergency Measures. The Emergency Arbitrator ruled that under the Samsung License, we could not file an arbitration demand until a 90-day negotiating period had passed, and that the 90 days began on December 4, 2015.

Based on the Emergency Arbitrator's Order, we withdrew our arbitration demand on February 1, 2016 and refiled it on March 4, 2016, requesting that Samsung be ordered to comply with its obligations under the Samsung License, including ceasing distributing devices previously licensed under the Samsung License and paying damages suffered by us. On April 12, 2016, Samsung filed a response to our arbitration demand. The arbitration is now in the arbitrator selection process. The arbitration will be conducted by a panel of three arbitrators, one to be nominated by us, another to be nominated by Samsung, and a third to be appointed by the ICC. There is not yet a schedule in place for the arbitration. It is not possible to predict the outcome of the arbitration.

26

Table of Contents

Sony Computer Entertainment America, Inc.

On October 2, 2014, we filed an arbitration demand with JAMS against Sony Computer Entertainment America, LLC and Sony Computer Entertainment, Inc. (collectively, “Sony”). The issue to be resolved was whether Sony’s DS4 Wireless Controller sold in Japan is covered by one of our Japanese patents and thus is a royalty-bearing product under a 2007 license agreement between us and Sony. On January 20, 2016, the arbitrator ruled in our favor, finding that Sony's DS4 Wireless Controllers manufactured, sold or distributed in Japan after April 8, 2014 were and are ‘royalty bearing’ products as defined by Paragraph 5.4 of the 2007 license agreement.

On February 19, 2016, we petitioned for confirmation of the award in the United States District Court for the Northern District of California. On March 18, 2016, Sony opposed the petition to confirm the award and moved to vacate the award. On April 26, 2016, the District Court issued an order granting our petition to confirm the arbitral award and denying Sony’s motion vacate the award.

On March 17, 2016, we filed an arbitration demand seeking a ruling that Sony game controllers sold in the United States are covered by U.S. Patent Nos. 6,686,901 and 7,969,288 and therefore are royalty-bearing products under our license agreement with Sony. Sony filed a response on April 12, 2016. The parties have agreed on a retired judge who will serve as the single arbitrator, and there is not yet a schedule in place for the arbitration.

We cannot predict the ultimate outcome of the above-mentioned federal and arbitral actions, 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.

### 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 price, 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.

27

Table of Contents

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

Three customers accounted for 24%, 19% and 16% of our total revenues, respectively, for the three months ended March 31, 2016. Samsung Electronics accounted for approximately 31% and two other customers accounted for 14% and 13% of our total revenues, for the three months ended March 31, 2015. 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, including Samsung whose agreement with us expired on December 31, 2015.

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. In addition, if potential customers or customers with expiring agreements view the loss of one of our major customers as an indicator of the value of our software and/or the strength of our intellectual property, they may choose not to take or renew a license which could adversely affect our operating results.

For example, as described in Part II, Item 1, "Legal Proceedings," we are currently in arbitration proceedings against Samsung. An unfavorable outcome in in the arbitration proceedings could result in the following:

- We may not receive the amount of damages we anticipate from Samsung which would have a material adverse effect on our business;
- Samsung may not enter into a new license with us which could cause our revenue to decline if we are unable to replace the lost revenue with revenue from other sources, and could cause existing and potential customers to perceive our technology as less valuable in the marketplace and, consequently, be less likely to license our technology if influenced by Samsung's actions not to enter into a new license;
- We may expend substantial time and resources in the arbitration proceedings against Samsung, which may be exacerbated in the case of an unfavorable outcome; and
- We may need to protect our intellectual property by engaging in litigation against Samsung, which may be expensive, disruptive and time-consuming.

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, including current litigation we initiated against Apple and AT&T Mobility, companies with significantly greater financial resources than us. 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, given the significant resources available to our current adverse parties, 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 cause our technology to be perceived as less valuable in the marketplace, which could reduce our sales and adversely affect our business. Further, any unfavorable outcome could adversely affect our business. For additional background on our litigation, please see Part II, Item 1, "Legal Proceedings".

If we fail to protect and enforce our IP rights or if we fail to continuously develop or acquire successful innovations and obtain patents on these innovations, our ability to license our technologies and generate revenues would be impaired.

Our business depends on generating revenues by licensing our IP rights and by customers selling products that incorporate our technologies. We rely on our significant patent portfolio to protect our proprietary rights. If we are not able to protect and enforce those rights, our ability to obtain future licenses or maintain current licenses and royalty revenue could be impaired. In addition, if a court or patent office were to limit the scope, declare unenforceable, or invalidate any of our patents, current licensees may refuse to make royalty payments, or they may choose to challenge one or more of our patents. It is also possible that:

- our pending patent applications may not result in the issuance of patents;
- our patents may not be broad enough to protect our proprietary rights; and
- effective patent protection may not be available in every country, particularly in Asia, where we or our licensees do business; and
- our pending litigation against Apple and AT&T Mobility LLC may be unsuccessful or may result in one or more of the patents asserted becoming limited in scope, declared unenforceable or invalidated.

In addition, our patents will continue to expire according to their terms, including the expiration of several gaming patents in 2015. We may experience a decrease in gaming royalty and license revenue due to expiration of these patents. Our failure to continuously develop or acquire successful innovations and obtain patents on those innovations could significantly harm our

Table of Contents

business, financial condition, results of operations, or cash flows. In addition, we also rely on licenses, confidentiality agreements, other contractual agreements, and copyright, trademark, and trade secret laws to establish and protect our proprietary rights. It is possible that:

- laws and contractual restrictions may not be sufficient to prevent misappropriation of our technologies or deter others from developing similar technologies; and
- policing unauthorized use of our patented technologies, trademarks, and other proprietary rights would be difficult, expensive, and time-consuming, within and particularly outside of the United States.

We have in the past initiated legal proceedings to protect our intellectual property and may need to continue to do so in the future, and we are currently in litigation against Apple and AT&T Mobility for patent infringement. We may need to continue to initiate legal proceedings in the future. Any legal or administrative proceeding initiated by us to protect or enforce our IP rights may result in substantial legal expenses and risk, could lead to counterclaims and adverse rulings affecting our patents, and may divert our management’s time and attention away from our other business operations, which could significantly harm our business.

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.

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 appealing a judgment invalidating three of our patents. At this time, the briefing for the appeal and the hearing has been completed. 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.

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

Table of Contents

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.

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

We currently have sales personnel in Japan, Korea, and China. 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 establishing and 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.

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, differing or inconsistent government interpretation, 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.

Competing technologies may harm our business.

Table of Contents

One of our biggest sources of competition is derived from decisions made by internal design groups at our customers and potential 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 customer is unwilling to enter into a license agreement, we may elect to pursue litigation which would harm our relationship with the customer 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 license 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 a customer, the customer'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.

We also license to semiconductor manufacturers who incorporate certain of our less fully-featured software 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 customers may elect to implement haptics using less fully-featured software 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 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 comes 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. Finally, as some of our key patents have expired related to video game peripherals, we may need to persuade our licensees that other patents in our portfolio continue to be relevant which could result in the expenditure of significant resources and/or failure to persuade the licensee of the relevance of the patents.

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 option packages if our technology is an option (for example, a navigation unit) or medical device, which is likely to be determined by many factors beyond our control.

If we fail to successfully manage our new content and media initiative, our results of operations could be negatively impacted.

We seek to find new applications and markets for our technologies. We have invested and continue to invest significant resources in the development of technologies and software related to enhancing mobile content with haptics. For example, we have announced the introduction of haptics-enabled mobile game applications from well-known publishers and haptics-enabled advertisements and movie trailers. Market acceptance of these new technologies and software offerings will be dependent in part on our ability to show that mobile content enhanced with haptics generates greater levels of consumer engagement, improves customer acquisition and retention measures, increases monetization, improves long-term content recall and generates more positive levels of enjoyment and brand sentiment. While our early pilot and user studies are encouraging, such data is preliminary and may be inaccurate or may not be accepted by third parties. While we do not anticipate any significant revenue associated with this initiative in 2016, if we are unable to successfully establish these new offerings, our results of operations could be negatively impacted. In addition, if we fail to properly manage the licensing of rights in our OEM and content businesses, we may inadvertently impair our ability to monetize our technology in one of these businesses and our results of operations would be negatively impacted.

We have little or no control or influence on our licensees’ design, manufacturing, quality control, promotion, distribution, or pricing of their products incorporating our touch-enabling technologies, upon which we generate royalty revenue.

A key part of our business strategy is to license our software and IP to companies that manufacture and sell products incorporating our touch-enabling technologies. For the three months ended March 31, 2016 and 2015, 99% and 98% of our total revenues were royalty and license revenues, respectively. We do not control or influence the design, manufacture, quality control, promotion, distribution, or pricing of products that are manufactured and sold by our licensees, nor can we control consolidation within an industry which could either reduce the number of licensable products available or reduce royalty rates for the combined licensees. In addition, we generally do not have commitments from our licensees that they will continue to use our technologies in current or future products. As a result, products incorporating our technologies may not be brought to market, achieve commercial acceptance, or otherwise generate meaningful royalty revenue for us. For us to generate royalty and license revenue, licensees that pay us per-unit royalties must manufacture and distribute products incorporating our touch-enabling technologies in a timely fashion and generate consumer demand through marketing and other promotional activities. If our licensees’ products fail to achieve commercial success, or if their products are recalled because of quality control problems or if they do not ship products incorporating our touch-enabling technologies in a timely fashion or fail to achieve strong sales, our revenues will not grow and could decline.

We had an accumulated deficit of $83 million as of March 31, 2016 and may not return to profitability in the future.

As of March 31, 2016, we had an accumulated deficit of $83 million. We need to generate significant ongoing revenue to return to consistent profitability. We will continue to incur expenses as we:

- engage in research and develop our technologies;
- increase our sales and marketing efforts;

- attempt to expand the market for touch-enabled technologies and products;
- protect and enforce our IP;
- expand our international presence in connection with the recently implemented reorganization of our corporate organization;
- incur costs related to litigation; and
- acquire IP or other assets from third-parties.

32

Table of Contents

If our revenues grow more slowly than we anticipate or if our operating expenses exceed our expectations, we may not return to profitability.

We have limited engineering, customer service, technical support, quality assurance and operations resources to design and meet delivery schedules and to provide support for our various technologies and, as a result, we could fail to deliver software and services in a timely way, with sufficient levels of quality, or at all, which may reduce our revenue.

We deploy our limited engineering, customer service, technical support, quality assurance, and operations resources on a variety of different projects and programs intended to provide sufficient levels of quality necessary for channels and customers. Our success in various markets may depend on timely deliveries and overall levels of sustained quality and customer service. Our failure to provide high quality customer deliverables in a timely fashion or at all, or our failure to maintain sufficient customer service levels, could disrupt our customer relationships, harm our brand, and reduce our revenues.

Our business depends in part on access to third-party platforms and technologies, and if the access is withdrawn, denied, or is not available on terms acceptable to us, or if the platforms or technologies change, our business and operating results could be adversely affected.

Many of our current and future software technologies are designed for use with third-party platforms and technologies. Our business relies on our access to these platforms and technologies of third parties, which can be withdrawn, denied or not be available on terms acceptable to us.

Our access to third-party platforms and technologies may require paying royalties or other amounts, which lowers our margins, or may otherwise be on terms that are not acceptable to us. In addition, the third-party platforms or technologies used to interact with our software technologies can be delayed in production or can change in ways that negatively impact the operation of our software.

If we are unable to access third-party platforms or technologies, or if our access is withdrawn, denied, or is not available on terms acceptable to us, or if the platforms or technologies are delayed or change, our business and operating results could be adversely affected.

Because we have a fixed payment license with Microsoft, our royalty revenue from licensing in the gaming market and other consumer markets has previously declined and may further do so if Microsoft increases its volume of sales of touch-enabled products at the expense of our other licensees.

Under the terms of our present agreement with Microsoft, Microsoft receives a royalty-free, perpetual, irrevocable license (including sublicense rights) to our worldwide portfolio of patents. This license permits Microsoft to make, use, and sell hardware, software, and services, excluding specified products, covered by our patents. We will not receive any further revenues or royalties from Microsoft under our current agreement with Microsoft, including with respect to Microsoft's Xbox One gaming product or any other haptic related product. Microsoft has a significant share of the market for touch-enabled console gaming computer peripherals and is pursuing other consumer markets such as mobile devices, tablets, personal computers, and virtual and augmented reality. Microsoft has significantly greater financial, sales, and marketing resources, as well as greater name recognition and a larger customer base than some of our other licensees. In the event that Microsoft increases its share of these markets, our royalty revenue from other licensees in these market segments may decline.

The market for certain touch-enabling technologies and touch-enabled products is at an early stage and if market demand does not develop, we may not achieve or sustain revenue growth.

The market for certain of our touch-enabling technologies and certain of our licensees' touch-enabled products is at an early stage. If we and our licensees are unable to develop demand for our touch-enabling technologies and products, we may not achieve or sustain revenue growth. We cannot accurately predict the growth of the markets for these technologies and products, the timing of product introductions, or the timing or likelihood of these products achieving widespread commercial adoption.

We expect that we will need to continue to pursue extensive and expensive marketing and sales efforts to educate prospective licensees, component customers, and end users about the uses and benefits of our technologies and to persuade software developers and content producers to create products that utilize our technologies. Negative product reviews or publicity about our company, our technologies, our licensees' products, haptic features, or haptic technology in general could have a negative impact on market adoption, our revenue, and/or our ability to license our technologies in the future.

Table of Contents

Our business may suffer if third parties assert that we violate their IP rights.
Third parties have previously claimed and may in the future claim that we or our customers are infringing upon their IP rights. Even if we believe that such claims are without merit or that we are not responsible for them under the indemnification or other terms of our customer license agreements, they can be time-consuming and costly to defend against and may divert management's attention and resources away from our business. Furthermore, third parties making such claims may be able to obtain injunctive or other equitable relief that could block our ability to further develop or commercialize some or all of our software technologies or services in the United States and abroad. Claims of IP infringement also might require us to enter into costly settlement or license agreements or pay costly damage awards. Even if we have an agreement that provides for a third party to indemnify us against such costs, the indemnifying party may be unable or unwilling to perform its contractual obligations.

We license some technologies from third parties. We must rely upon the owners of these technologies for information on the origin and ownership of the technologies. As a result, our exposure to infringement claims may increase. We generally obtain representations as to the origin and ownership of acquired or licensed technologies and indemnification to cover any breach of these representations. However, representations may not be accurate and indemnification may not provide adequate compensation for breach of the representations. If we cannot or do not license the infringed IP at all or on reasonable terms, or substitute similar technology from another source, our business, financial position, results of operations or cash flows could suffer.
Changes to U.S. patent laws and proposed changes to the rules of the U.S. Patent and Trademark Office may adversely impact our business.

Our business relies in part on the uniform and historically consistent application of U.S. patent laws and regulations. There are numerous recent changes to the patent laws and the rules of the U.S. Patent and Trademark Office, which may have a significant impact on our ability to protect our technology and enforce our IP rights. For example, on September 16, 2011, President Obama signed the Leahy-Smith America Invents Act, which codified significant changes to the U.S. patent laws, including, among other things, changing from a "first to invent" to a "first inventor to file" system, limiting where a patentee may file a patent suit, requiring the apportionment of patent damages, replacing interference proceedings with derivation actions and creating a post-grant opposition process to challenge patents after they have been issued. The U.S. Patent and Trademark Office has developed new and untested regulations and procedures to govern the full implementation of the Leahy-Smith America Invents Act, and many of the substantive changes to patent law associated with the Leahy-Smith America Invents Act, and in particular, the "first inventor to file" provisions. It is not clear what impact the Leahy-Smith Act will have on the operation of our business and the protection and enforcement of our intellectual property. In addition, in recent years, the courts have interpreted U.S. patent laws and regulations differently, and in particular the U.S. Supreme Court has decided a number of patent cases and continues to actively review more patent cases than it has in the past. Some of these changes or potential changes may not be advantageous for us, and may make it more difficult to obtain adequate patent protection or to enforce our patents against parties using them without a license or payment of royalties. These changes could increase the costs and uncertainties surrounding the prosecution of our patent applications and the enforcement or defense of our patent rights, and could have a deleterious effect on our licensing program and, therefore, the royalties we can collect.
If we fail to develop new or enhanced technologies for new applications and platforms, we may not be able to create a market for our technologies or our technologies may become obsolete, and our ability to grow and our results of operations might be harmed.
We derive a significant portion of our revenues from licenses and royalties from a relatively small number of key technologies. We devote significant engineering resources to develop new technologies to address the evolving needs of our customers and potential customers. To remain competitive, we must introduce new technologies in a timely manner and the market must adopt them. Our initiatives to develop new and enhanced technologies and to commercialize these technologies for new applications and new platforms may not be successful or timely. Any new or enhanced technologies may not be favorably received by our licensees, potential licensees, or consumers and could damage our reputation or our brand. Expanding and enhancing our technologies could also require significant

additional expenses and strain our management, financial, and operational resources.

Moreover, technology products generally have relatively short product life cycles and our current technologies may become obsolete in the future. Our ability to achieve revenue growth also depends on our continuing ability to improve and reduce the cost of our technologies, to improve their ease of integration in both hardware and software, and to introduce these technologies to the marketplace in a timely manner. If our development efforts are not successful or are significantly delayed, companies may not incorporate our technologies into their products and our revenues may not grow and could decline.

Table of Contents

The higher cost of products incorporating our touch-enabling technologies may inhibit or prevent their widespread adoption.

Mobile devices, tablets, touchscreens, personal computer and console gaming peripherals, and automotive, medical, and industrial controls incorporating our touch-enabling technologies can be more expensive than similar competitive products that are not touch-enabled. Although many OEMs have licensed our technologies, there is generally no commitment on their part to use our technologies in their devices. The greater expense of development and production of products containing our touch-enabling technologies, together with the higher price to the end customer, may be a significant barrier to their widespread adoption and sale.

If we are unable to develop open source compliant products, our ability to license our technologies and generate revenues would be impaired.

We have seen, and believe that we will continue to see, an increase in customers requesting that we develop products that will operate in an "open source" environment. Developing open source compliant products without imperiling the IP rights upon which our licensing business depends may prove difficult under certain circumstances, thereby placing us at a competitive disadvantage for new product designs. Some of our proprietary technologies incorporate open source software that may be subject to open source licenses. These open source licenses may require that source code subject to the license be released or made available to the public. Such open source licenses may mandate that software developed based on source code that is subject to the open source license, or combined in specific ways with such open source software, become subject to the open source license. We take steps to ensure that proprietary software we do not wish to disclose is not combined with, or does not incorporate, open source software in ways that would require such proprietary software to be subject to an open source license. However, few courts have interpreted open source licenses, and the manner in which these licenses may be interpreted and enforced is therefore subject to some uncertainty. We often take steps to disclose source code for which disclosure is required under an open source license, but it is possible that we have made or will make mistakes in doing so, which could negatively impact our brand or our adoption in the community, or could expose us to additional liability. In addition, we rely on multiple software programmers to design our proprietary products and technologies. Although we take steps to ensure that our programmers (both internal and outsourced) do not include open source software in products and technologies we intend to keep proprietary, we cannot be certain that open source software is not incorporated into products and technologies we intend to keep proprietary. In the event that portions of our proprietary technology are determined to be subject to an open source license, or are intentionally released under an open source license, we could be required to publicly release the relevant portions of our source code, which could reduce or eliminate our ability to commercialize our products and technologies. As a result, our revenues may not grow and could decline.

The uncertain economic environment could reduce our revenues and could have an adverse effect on our financial condition and results of operations.

The current global economic conditions and political climate could materially hurt our business in a number of ways, including longer sales and renewal cycles, exchange rate volatility, delays in adoption of our products or technologies or those of our customers, increased risk of competition, higher overhead costs as a percentage of revenue, delays in signing or failing to sign customer agreements or signing customer agreements with reduced royalty rates. In addition, our customers, potential customers, and business partners would likely face similar challenges, which could materially and adversely affect the level of business they conduct with us or the sales volume of products that include our technology.

We might be unable to retain or recruit necessary personnel, which could slow the development and deployment of our technologies.

Our technologies are complex, and we rely upon the continued service of our existing personnel to support licensees, enhance existing technologies, and develop new technologies. Accordingly, our ability to develop and deploy our technologies and to sustain our revenue growth depends upon the continued service of our management and other key personnel, many of whom would be difficult to replace. Furthermore, we believe that there are a limited number of engineering and technical personnel that are experienced in haptics. Management and other key employees may voluntarily terminate their employment with us at any time without notice. The loss of management or key personnel could delay product development cycles or otherwise harm our business.

We believe that our future success will also depend largely on our ability to attract, integrate, and retain sales, support, marketing, and research and development personnel. Competition for such personnel is intense, and we may not be successful in attracting, integrating, and retaining such personnel. Given the protracted nature of, if, how, and when we collect royalties on new design contracts, it may be difficult to craft compensation plans that will attract and retain the level of salesmanship

Table of Contents

needed to secure these contracts. Additionally, some of our executive officers and key employees hold stock options with exercise prices that may be above the current market price of our common stock or that are largely vested. Each of these factors may impair our ability to retain the services of our executive officers and key employees.

If we do not achieve increased tax benefits as a result of our recently implemented corporate restructuring, our financial condition and operating results could be adversely affected.

We have recently completed a reorganization of our corporate organization. The purpose of this reorganization was to more closely align our corporate structure with the international nature of our business activities. This corporate restructuring activity is anticipated to allow us to reduce our overall effective tax rate through changes in how we develop and use our intellectual property and the structure of our international sales operations, including by entering into transfer-pricing arrangements that establish transfer prices for our intercompany transactions.

There can be no assurance that the taxing authorities of the jurisdictions in which we operate or to which we are otherwise deemed to have sufficient tax nexus will not challenge the restructuring or the tax position that we take. In addition, future changes to U.S. or non-U.S. tax laws, including legislation to reform U.S. or other countries' taxation of international business activities, could negatively impact the anticipated tax benefits of the restructuring.

Any benefits to our tax rate will also depend on our ability to operate our business in a manner consistent with the reorganization of our corporate organization and applicable tax provisions, as well as on our achieving our forecasted revenue growth rates. If the intended tax treatment is not accepted by the applicable taxing authorities, changes in tax law negatively impact the structure or we do not operate our business consistent with the intended reorganization and applicable tax provisions, we may fail to achieve the financial efficiencies that we anticipate as a result of the reorganization and our future operating results and financial condition may be negatively impacted.

Product liability claims could be time-consuming and costly to defend and could expose us to loss.

Our products or our licensees’ products may have flaws or other defects that may lead to personal or other injury claims. If products that we or our licensees sell cause personal injury, property damage, financial loss, or other injury to our or our licensees’ customers, the customers or our licensees may seek damages or other recovery from us. In addition, even though we have transitioned from the medical products line of business, we could face product liability claims for products that we have sold or that our successors have sold or may sell in the future. Defending any claims against us, regardless of merit, would be time-consuming, expensive, and distracting to management, and could result in damages and injure our reputation, the reputation of our technology, services, or products, or the reputation of our licensees or their products. This damage could limit the market for our and our licensees’ products and harm our results of operations. In addition, if our business liability insurance coverage proves inadequate or future coverage is unavailable on acceptable terms or at all, our business, operating results and financial condition could be adversely affected.

In the past, manufacturers of peripheral products, including certain gaming products such as joysticks, wheels, or gamepads, have been subject to claims alleging that use of their products has caused or contributed to various types of repetitive stress injuries, including carpal tunnel syndrome. While we have not experienced any product liability claims to date, we could face such claims in the future, which could harm our business and reputation. Although our license agreements typically contain provisions designed to limit our exposure to product liability claims, existing or future laws or unfavorable judicial decisions could limit or invalidate the provisions.

Our technologies are complex and may contain undetected errors, which could harm our reputation and future sales.

Any failure to provide high quality and reliable technologies, whether caused by our own failure or failures of our suppliers or customers, could damage our reputation and reduce demand for our technologies. Our technologies have in the past contained, and may in the future contain, undetected errors or defects. Some errors in our technologies may only be discovered after a customer’s product incorporating our technologies has been shipped to customers. Any errors or defects discovered in our technologies after commercial release could result in product recalls, loss of revenue, loss of customers, and increased service and warranty costs, any of which could adversely affect our business.

Our customers may have difficulties obtaining the components necessary to manufacture haptic-based products, which could harm our business and results of operations.

In order to manufacture haptic-based products, our OEM customers require components such as actuators and amplifiers. The inability of suppliers to deliver adequate supplies of these components could disrupt our OEM customers’ production processes, which would harm our business and results of operations. In addition, if our OEM customers choose to use lower quality actuators as a cost-saving measure, the technical performance of our software may be adversely affected which could

Table of Contents

also harm our business and results of operations. Certain of our newer products require new types of components that we expect will be developed and sold by our ecosystem partners. Failure of our ecosystem partners to bring these products to market in a timely and quality fashion at attractive prices may negatively affect our ability to secure customers for these newer products which could harm our business and results of operations. Component suppliers to customers could also be affected by natural disasters and other similar events, including losses due to earthquakes.

Catastrophic events, such as natural disasters, war, and acts of terrorism could disrupt the business of our customers, which could harm our business and results of operations.

The production processes and operations of our customers are susceptible to the occurrence of catastrophic events, such as natural disasters, war, and acts of terrorism, all of which are outside of our control. Any such events could cause a serious business disruption to our customers' ability to manufacture, distribute and sell products incorporating our touch-enabling technologies, which may adversely affect our business and results of operation.

If our facilities were to experience catastrophic loss, our operations would be seriously harmed.

Our facilities could be subject to a catastrophic loss such as fire, flood, earthquake, power outage, or terrorist activity. A substantial portion of our research and development activities, our corporate headquarters, and other critical business operations are located near major earthquake faults in San Jose, California, an area with a history of seismic events. An earthquake at or near our facilities could disrupt our operations and result in large expenses to repair and replace the facility. While we believe that we maintain insurance sufficient to cover most long-term potential losses at our facilities, our existing insurance may not be adequate for all possible losses including losses due to earthquakes.

If we fail to establish and maintain proper and effective internal controls, our ability to produce accurate financial statements on a timely basis could be impaired, which would adversely affect our consolidated operating results, our ability to operate our business and our stock price.

We have in the past had material weaknesses in our internal control over financial reporting. Ensuring that we have adequate internal financial and accounting controls and procedures in place to produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. Any failure on our part to remedy identified material weaknesses, or any additional delays or errors in our financial reporting controls or procedures, could cause our financial reporting to be unreliable and could have a material adverse effect on our business, results of operations, or financial condition and could have a substantial adverse impact on the trading price of our common stock.

We do not expect that our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within our company will have been detected.

The nature of some of our products may also subject us to export control regulation by the U.S. Department of State and the Department of Commerce. Violations of these regulations can result in monetary penalties and denial of export privileges.

Our sales to customers or sales by our customers to their end customers in some areas outside the United States could be subject to government export regulations or restrictions that prohibit us or our licensees from selling to customers in some countries or that require us or our licensees to obtain licenses or approvals to export such products internationally. Delays or denial of the grant of any required license or approval, or changes to the regulations, could make it difficult or impossible to make sales to foreign customers in some countries and could adversely affect our revenue. In addition, we could be subject to fines and penalties for violation of these export regulations if we were found in violation. Such violation could result in penalties, including prohibiting us from exporting our products to one or more countries, and could materially and adversely affect our business.

Investment Risks

Our quarterly revenues and operating results are volatile, and if our future results are below the expectations of public market analysts or investors, the price of our common stock is likely to decline.

Our revenues and operating results are likely to vary significantly from quarter to quarter due to a number of factors, many of which are outside of our control and any of which could cause the price of our common stock to decline.

Table of Contents

These factors include:

- the establishment or loss of licensing relationships;
- the timing and recognition of payments under fixed and/or up-front license agreements, as well as other multi-element arrangements;
- seasonality in the demand for our technologies or products or our licensees' products;
- the timing of our expenses, including costs related to litigation, stock-based awards, acquisitions of technologies, or businesses;
- developments in and costs of pursuing or settling any pending litigation;
- the timing of introductions and market acceptance of new technologies and products and product enhancements by us, our licensees, our competitors, or their competitors;
- the timing of work performed under development agreements; and
- errors in our licensees' royalty reports, and corrections and true-ups to royalty payments and royalty rates from prior periods.

Changes in financial accounting standards, policies or practices may have adverse, unexpected financial reporting implications and affect our reported results of operations.

A change in accounting standards, policies, or practices, such as the new revenue accounting standard that will become effective for us in 2018, ASU No. 2014-09 "Revenue from Contracts with Customers: Topic 606", can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and may occur in the future. Changes to existing rules or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business.

Our business is subject to changing regulations regarding corporate governance and other compliance areas that will increase both our costs and the risk of noncompliance.

As a public company, we are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act of 2002, and the rules and regulations of The NASDAQ Stock Market and other regulations that may be enacted from time-to-time. The requirements of these and other rules and regulations have increased and we expect will continue to increase our legal, accounting and financial compliance costs, will make some activities more difficult, time-consuming and costly, and may also place undue strain on our personnel, systems and resources.

Our stock price may fluctuate regardless of our performance.

The stock market has experienced extreme volatility that often has been unrelated or disproportionate to the performance of particular companies. These market fluctuations may cause our stock price to decline regardless of our performance. The market price of our common stock has been, and in the future could be, significantly affected by factors such as: actual or anticipated fluctuations in operating results; announcements of technical innovations; announcements regarding litigation in which we are involved; the acquisition or loss of customers; changes by game console manufacturers to not include touch-enabling capabilities in their products; new products or new contracts; sales or the perception in the market of possible sales of large number of shares of our common stock by insiders or others; stock repurchase activity; changes in securities analysts' recommendations; personnel changes; changing circumstances regarding competitors or their customers; governmental regulatory action or inaction; developments with respect to patents or proprietary rights; inclusion in or exclusion from various stock indices; and general market conditions. In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has been initiated against that company.

Our stock repurchase program could affect our stock price and add volatility.

Any repurchases pursuant to our stock repurchase program could affect our stock price and add volatility. There can be no assurance that any repurchases will continue to be made under the program, nor is there any assurance that a sufficient number of shares of our common stock will be repurchased to satisfy the market's expectations. Furthermore, there can be no assurance that any repurchases conducted under the plan will be made at the best possible price. The existence of a stock repurchase program could also cause our stock price to be higher than it would be in the absence of such a program and could potentially reduce the market liquidity for our stock. Additionally, we are permitted to and could discontinue our stock repurchase program at any time and any such discontinuation could cause the market price of our stock to decline.

Table of Contents

Provisions in our charter documents and Delaware law could prevent or delay a change in control, which could reduce the market price of our common stock.

Provisions in our certificate of incorporation and bylaws may have the effect of delaying or preventing a change of control or changes in our board of directors or management, including the following:

- our board of directors is classified into three classes of directors with staggered three-year terms;
- only our chairperson of the board of directors, a majority of our board of directors or 10% or greater stockholders are authorized to call a special meeting of stockholders;
- our stockholders can only take action at a meeting of stockholders and not by written consent;
- vacancies on our board of directors can be filled only by our board of directors and not by our stockholders;
- our restated certificate of incorporation authorizes undesignated preferred stock, the terms of which may be established and shares of which may be issued without stockholder approval; and
- advance notice procedures apply for stockholders to nominate candidates for election as directors or to bring matters before an annual meeting of stockholders.

In addition, certain provisions of Delaware law may discourage, delay, or prevent someone from acquiring or merging with us. These provisions could limit the price that investors might be willing to pay in the future for shares.

We may engage in acquisitions that could dilute stockholders' interests, divert management attention, or cause integration problems.

As part of our business strategy, we have in the past and may in the future, acquire businesses or IP that we feel could complement our business, enhance our technical capabilities, or increase our IP portfolio. The pursuit of potential acquisitions may divert the attention of management and cause us to incur various expenses in identifying, investigating, and pursuing suitable acquisitions, whether or not they are consummated.

If we consummate acquisitions through the issuance of our securities, our stockholders could suffer significant dilution. Acquisitions could also create risks for us, including:

- unanticipated costs associated with the acquisitions;
- use of substantial portions of our available cash to consummate the acquisitions;
- diversion of management's attention from other business concerns;
- difficulties in assimilation of acquired personnel or operations;
- failure to realize the anticipated benefits of acquired IP or other assets;
- charges associated with amortization of acquired assets or potential charges for write-down of assets or goodwill associated with unsuccessful acquisitions;
- potential IP infringement or other claims related to acquired businesses, assets, product lines, or technologies; and
- potential costs associated with failed acquisition efforts.

Any acquisitions, even if successfully completed, might not generate significant additional revenue or provide any benefit to our business.

ITEM 6. EXHIBITS

The exhibits listed in the accompanying "Exhibit Index" are filed or incorporated by reference as part of this Form 10-Q.

Table of Contents

SIGNATURES

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

Date: May 6, 2016

IMMERSION CORPORATION

By /s/ Victor Viegas
Victor Viegas
President, Chief Executive Officer, Interim Chief Financial Officer and Principal Accounting Officer

Table of Contents

EXHIBIT INDEX

| Number | Description |
|---|---|
| 31.1 | Certification of Victor Viegas, Chief Executive Officer and interim Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1* | Certification of Victor Viegas, Chief Executive Officer and interim Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Report Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Label Linkbase Document |
| 101.PRE | XBRL Presentation Linkbase Document |

* This certification is deemed not filed for purposes of section 18 of the Exchange Act or otherwise subject to the liability of that section, nor shall it be deemed incorporated by reference into any filing under the Securities Act or the Exchange Act.