IMMERSION CORP
Form 10-Q
October 31, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended September 30, 2014

OR

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

For the transition period from ______ to ______

Commission file number 000-27969

IMMERSION CORPORATION

(Exact name of registrant as specified in its charter)

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

30 Rio Robles, San Jose, California 95134

(Address of principal executive offices)(Zip Code)

(408) 467-1900

(Registrant s telephone number, including area code)

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

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

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller Reporting Company	¨

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

Number of shares of common stock outstanding at October 23, 2014: 27,678,578.

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IMMERSION CORPORATION

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PART I

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

IMMERSION CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share amounts)

(Unaudited)

	September 30, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$ 10,139	$ 14,136
Short-term investments	52,989	56,976
Accounts and other receivables (net of allowances for doubtful accounts of $15 and $9)	2,992	598
Deferred income taxes	7,784	7,784
Prepaid expenses and other current assets	1,085	690
Total current assets	74,989	80,184
Property and equipment, net	1,280	944
Deferred income tax assets	27,527	29,066
Intangibles and other assets, net	299	381
Total assets	$ 104,095	$ 110,575
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,019	$ 682
Accrued compensation	1,665	4,680
Other current liabilities	1,483	1,653
Deferred revenue	13,007	8,920
Total current liabilities	17,174	15,935
Long-term deferred revenue	9,018	13,441
Other long-term liabilities	451	528
Total liabilities	26,643	29,904
Contingencies (Note 12)		
Stockholders equity:		

Common stock and additional paid-in capital $0.001 par value; 100,000,000 shares authorized; 34,188,969 and 33,619,766 shares issued, respectively; 28,055,082 and 28,637,022 shares outstanding, respectively	203,725	198,057
Accumulated other comprehensive income	117	112
Accumulated deficit	(83,823)	(86,929)
Treasury stock at cost: 6,133,887 and 4,982,744 shares, respectively	(42,567)	(30,569)
Total stockholders equity	77,452	80,671
Total liabilities and stockholders equity	$ 104,095	$ 110,575

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

AND COMPREHENSIVE INCOME

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30		Nine Months Ended September 30	
	2014	**2013**	**2014**	**2013**
Revenues:				
Royalty and license	$ 11,714	$ 10,951	$ 38,473	$ 34,580
Product sales	0	12	0	44
Development, services, and other	337	379	845	779
Total revenues	12,051	11,342	39,318	35,403
Costs and expenses:				
Cost of revenues (exclusive of amortization of intangibles shown separately below)	104	111	325	386
Sales and marketing	2,238	2,151	7,638	6,692
Research and development	2,718	2,640	8,782	7,876
General and administrative	5,274	5,606	17,745	17,433
Amortization of intangibles	15	20	55	60
Total costs and expenses	10,349	10,528	34,545	32,447
Operating income	1,702	814	4,773	2,956
Interest and other income (expense)	(30)	42	107	80
Income before provision for income taxes	1,672	856	4,880	3,036
Provision for income taxes	(599)	(257)	(1,774)	(284)
Net income	$ 1,073	$ 599	$ 3,106	$ 2,752
Basic net income per share	$ 0.04	$ 0.02	$ 0.11	$ 0.10
Shares used in calculating basic net income per share	28,505	28,558	28,420	28,047
Diluted net income per share	$ 0.04	$ 0.02	$ 0.11	$ 0.09
Shares used in calculating diluted net income per share	29,351	29,653	29,355	29,205

Other Comprehensive Income				
Change in unrealized gains on short-term investments	3	10	5	6
Total Other Comprehensive Income	3	10	5	6
Total Comprehensive Income	$ 1,076	$ 609	$ 3,111	$ 2,758

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine Months Ended September 30	
	2014	**2013**
Cash flows provided by operating activities:		
Net income	$ 3,106	$ 2,752
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	364	459
Amortization of intangibles	55	60
Stock-based compensation	4,058	3,438
Allowance (recovery) for doubtful accounts	3	7
Loss on disposal of equipment	19	12
Changes in operating assets and liabilities:		
Accounts and other receivables	(2,397)	1,577
Inventories	0	141
Deferred income taxes	1,539	0
Prepaid expenses and other current assets	(395)	(164)
Other assets	(20)	(58)
Accounts payable	337	281
Accrued compensation and other current liabilities	(3,209)	1,206
Income taxes payable	35	0
Deferred revenue	(336)	5,076
Other long-term liabilities	(77)	(68)
Net cash provided by operating activities	3,082	14,719
Cash flows provided by (used in) investing activities:		
Purchases of available-for-sale investments	(37,960)	(71,955)
Proceeds from maturities of available-for-sale investments	42,000	63,000
Purchases of property and equipment	(734)	(174)
Net cash provided by (used in) investing activities	3,306	(9,129)
Cash flows provided by (used in) financing activities:		
Issuance of common stock under employee stock purchase plan	381	198
Exercise of stock options	1,229	6,318
Purchases of treasury stock	(11,995)	0
Net cash provided by (used in) financing activities	(10,385)	6,516
Net increase (decrease) in cash and cash equivalents	(3,997)	12,106

Cash and cash equivalents:		
Beginning of period	14,136	4,558
End of period	$ 10,139	$ 16,664
Supplemental disclosure of cash flow information		
Cash paid for taxes	$ 46	$ 13
Supplemental disclosure of noncash operating, investing, and financing activities		
Amounts accrued for property and equipment	$ 8	$ 0
Amounts accrued for purchase of treasury stock	$ 3	$ 0
Release of Restricted Stock Units and Awards under company stock plan	$ 3,745	$ 3,183

See accompanying Notes to Condensed Consolidated Financial Statements

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IMMERSION CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2014

(Unaudited)

1. SIGNIFICANT ACCOUNTING POLICIES

Description of Business

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

Principles of Consolidation and Basis of Presentation

The condensed consolidated financial statements include the accounts of Immersion Corporation and its wholly-owned subsidiaries: Immersion Canada Inc.; Immersion International, LLC; Immersion Medical, Inc.; Immersion Japan K.K.; Immersion Ltd.; Immersion Software Ireland Ltd.; Haptify, Inc.; and Immersion (Shanghai) Science & Technology Company, 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, 2013. 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 and nine months ended September 30, 2014 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.

Intangible Assets

During the fourth quarter 2013, the Company elected to change its method of accounting for external patent-related costs associated with its internally developed patents and trademarks. Prior to the change the Company capitalized the external legal, filing, continuation or annuity fees associated with patent and trademark applications. These costs were amortized on a straight-line basis over their estimated economic useful lives which were generally ten years from the date of issuance. Under the current method of accounting, external patent-related costs are expensed as incurred and classified as general and administrative expenses in the Company s condensed consolidated statement of income consistent with the classification of internal legal costs associated with internally developed patents and trademarks. Costs

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associated with acquired patents and other intangible assets continue to be capitalized as incurred. These costs are amortized utilizing the straight-line method, which approximates the pattern of consumption over the estimated useful lives of the respective assets, generally ten years.

In accordance with Accounting Standards Codification (ASC) 250, Accounting Changes and Error Corrections, the change in accounting method has been retrospectively applied to all prior periods presented herein. Comparative financial statements of prior years have been adjusted to apply the new method retrospectively.

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 three principal sources: royalty and license fees, development contract and service fees, and, previously, product sales. As described below, management judgments, assumptions, and estimates must be made and used in connection with the revenue recognized in any accounting period. Material differences may result in the amount and timing of revenue for any period based on the judgments and estimates made by management. Specifically, in connection with each transaction, the Company must evaluate whether: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable, and (iv) collectibility is probable. The Company applies these criteria as discussed below.

Persuasive evidence of an arrangement exists. For a license arrangement, the Company requires a written contract, signed by both the customer and the Company. For a stand-alone product sale, the Company requires a purchase order or other form of written agreement with the customer.

Delivery has occurred. The Company delivers software and product to customers physically and also delivers software electronically. For physical deliveries not related to software, the transfer terms typically include transfer of title and risk of loss at the Company s shipping location. For electronic deliveries, delivery occurs when the Company provides the customer access codes or keys that allow the customer to take immediate possession of the software.

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

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

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

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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 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.

Product sales The Company recognizes revenue from the sale of products and the license of associated software, if any, and expenses all related costs of products sold, once delivery has occurred and customer acceptance, if required, has been achieved. The Company typically grants to customers a warranty that guarantees the products will substantially conform to the Company s current specifications for generally three to twelve months from the delivery date pursuant to the terms of the arrangement. Historically, warranty-related costs have not been significant.