

IMMERSION CORP
Form 10-K
February 27, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2013 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
(State or other jurisdiction of incorporation or organization)

94-3180138
(IRS Employer Identification No.)

30 Rio Robles

San Jose, California 95134

(Address of principal executive offices, zip code)

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(408) 467-1900

(Registrant's telephone number, including area code)

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

Title of Each Class	Name of Each Exchange on which Registered
Common Stock, \$0.001 par value	The Nasdaq Stock Market LLC

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

None

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 No

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

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

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

Large accelerated filer

Accelerated filer

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 Act). Yes No

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant on June 28, 2013, the last business day of the registrant's most recently completed second fiscal quarter, was \$160,429,821 (based on the closing sales price of the registrant's common stock on that date). Shares of the registrant's common stock held by each officer and director and each person whom owns 5% or more of the outstanding common stock of the registrant have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes. Number of shares of common stock outstanding at February 19, 2014: 28,146,502.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the 2014 Annual Meeting are incorporated by reference into Part III hereof.

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**IMMERSION CORPORATION
2013 FORM 10-K ANNUAL REPORT**

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Forward-looking Statements

In addition to historical information this Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (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, Risk Factors and those described elsewhere in this report, and those described in our other reports filed with the Securities and Exchange Commission (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.

PART I

Item 1. Business

Overview

Immersion Corporation (Immersion) is a premier intellectual property (IP) and technology licensing company focused on the creation, design, development and licensing of haptic innovations and technologies that allow people to use their sense of touch more fully when operating a wide variety of digital devices. Our mission is to deliver groundbreaking touch feedback innovations and technologies that transform the user experience by exciting the senses in games, videos, and music; restoring mechanical feel by providing intuitive and unmistakable confirmation; improving safety by overcoming distractions; and expanding usability when audio and visual feedback are ineffective or inefficient. We are currently focusing our marketing and business development activities on the following target markets: mobile communications and consumer electronics, automotive, gaming, commercial and industrial, and medical.

Prior to April 2010, we managed these markets under two operating and reportable segments: 1) the Touch Line of Business and 2) the Medical Line of Business. In March 2010, we sold certain assets of our Endoscopy, Endovascular, and Laparoscopy medical simulation product lines. As a result, our business has been consolidated into a single segment and we now operate primarily under a licensing model. As such, we no longer report on a segment basis. See Management s Discussion and Analysis of Financial Condition and Results of Operations as well as the notes to the consolidated financial statements for further information.

In our target markets, we license our software and IP to manufacturers for use in products sold under their own brand names. We and our wholly-owned subsidiaries hold more than 1,500 issued or pending patents in the U.S. and other countries, covering a wide range of digital technologies, including many of the ways in which touch-related technology can be incorporated into and between hardware products, systems software, application software and digital content.

We were incorporated in 1993 in California and reincorporated in Delaware in 1999. We consummated our initial public offering on November 12, 1999.

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Our Business Strategy

Our goal is to continue to be the technology and market leader in haptic technologies and drive the adoption of our touch software and IP across markets and applications to improve the user experience with digital devices and systems. Key aspects of our strategy include:

Innovate: Develop and patent our innovative technology to provide haptics in mobile device, automotive, gaming, medical, and consumer electronics products to transform user experiences with unique and customizable touch feedback effects.

Drive Adoption: Communicate the advantages of our patented innovations and technologies to the relevant industries and encourage their adoption through demonstrations and incorporation in the products of world-class companies.

Expand Markets: Expand the enjoyment and use of haptics in new markets, including touch-enabled mobile advertising, entertainment content, communications technologies, and evolving form factors.

Monetize: License our patented inventions and software to customers for use in creating and enjoying haptics in their mobile device, automotive, gaming, medical, and consumer electronics products.

We believe that the successful execution of this strategy requires an exceptional and unparalleled licensing platform and business model that relies on the skills and talent of our employees. Accordingly, we seek to hire and retain employees with world class haptic expertise, as well as the executive management and operating personnel required to successfully execute our business strategy. In order to attract the quality of employees required for this business model, we have created an environment and culture that encourages, fosters, and supports research, development, and innovation in breakthrough technologies with significant opportunities for broad industry adoption through licensing. We believe that we have created a compelling company for inventors and innovators who are able to work within a business model and platform that focuses on IP development and licensing to drive strong future growth.

Haptics and Its Benefits

While digital devices offer many advanced capabilities they often fail to provide users with the meaningful touch experiences that enrich their real world interactions. For example, when dialing a number or entering text on a conventional touchscreen, users feel only the touchscreen surface, without the subtle, yet confirming sensation they expect from mechanical switches and keyboards. Similarly, communications with other users and experiences with digital content can feel flat or lifeless without the accompanying tactile feedback that is an essential part of the physical world. Immersion's haptic technologies can restore these missing elements of confirmation, realism and rich communication to the digital world.

Our haptic technology breathes life into digital interfaces, allowing users to feel the vibrating force or resistance as they push a virtual button, scroll through a list or encounter the end of a menu. In a video or mobile game with haptics, users can feel the gun recoil, the engine rev, or the crack of the bat meeting the ball. When simulating the placement of cardiac pacing leads, a user can feel the forces that would be encountered when navigating the leads through a beating heart, providing a more realistic experience of performing this procedure.

Haptics can enhance the user experience through:

Improved Usability: By restoring the sense of touch to otherwise lifeless surfaces, haptics creates fulfilling multi-modal experiences that can improve usability by engaging touch, sight, and sound. From the confidence a user receives through touch confirmation when selecting a virtual button to the contextual awareness they receive through haptics in a first person shooter game, haptics improves usability by more fully engaging the user's senses.

Enhanced Realism: Haptics injects a sense of realism into user experiences by exciting the senses and allowing the user to feel the action and nuance of the application. This is particularly relevant in

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applications like games, video content, or simulations that rely on only visual and audio inputs. The inclusion of tactile feedback provides additional context that translates into a sense of realism for the user.

Enriched Communications: Haptics uses the sense of touch to communicate information to users in an unobtrusive and intuitive manner. In mobile devices, the sense of touch can enhance voice, chat, or video applications to create more engaging and emotional communications. In wearable devices, haptics can provide meaningful information to users without disruptive audio or visual feedback.

Restoration of Mechanical Feel: Today's touchscreen-driven devices lack the physical feedback that humans frequently need to fully understand the context of their interactions. By providing users with intuitive and unmistakable tactile confirmation, haptics can create a more confident user experience and can also improve safety by overcoming distractions. This is especially important when audio or visual confirmation is insufficient, or for applications that involve distractions, such as automotive and industrial applications.

We believe these features of our haptic technology are broadly applicable to a number of markets and devices. By continuing to enhance these features through further research and development, we believe we will serve as a strategic partner for our customers and partners in helping them develop a more compelling user experience for consumers.

Our Offerings

Our patented inventions and software are offered to our customers through either a software license or a patent license or a combination thereof.

We offer our customers software licenses to support the implementation and adoption of haptics in their products. Our software license offerings include a range of software developed by Immersion, including our TouchSense software that we provide for incorporation into mobile devices, video console gaming systems, consumer electronics, medical simulation and surgical robotic systems, and automotive controls. Further, under software licenses, our customers typically receive licenses to our patents necessary to implement the licensed software in their products, with the specific rights and restrictions to the applicable patents described in their license agreements.

We also offer our customers patent licenses, through which we provide a license to specified aspects of our broad portfolio of patented inventions. The patent license provides the customer with a defined right to use our patented innovations in the customer's own products, which may be limited to specific fields of use.

Our software license agreements and patent license agreements or combinations thereof are structured with fixed, variable or a hybrid of fixed and variable royalty payments over certain defined periods.

For both our software and patent licensees, we offer our expertise to help our customers design and integrate touch effects into their products. This expertise may include turn-key engineering and integration services, design kits for prototyping, authoring tools, application programming interfaces (APIs), and the development of hardware and software technologies that are compatible with industry standards.

Software Licenses

We license our software to original equipment manufacturers (OEMs) or their suppliers who then include our software in products sold under their own brand names. We license our software under the TouchSense brand, and have developed a family of TouchSense software that is intended to address the needs of our target markets.

TouchSense 1000: Targeted to the commercial and industrial and automotive markets, TouchSense 1000 software offers haptic effects for large touch screens, touch panels, and touch surfaces that are optimized for strength in demanding applications and extreme environments.

TouchSense 2000: Targeted to mass market consumer electronic devices such as microwaves, cameras and other handheld consumer electronics, TouchSense 2000 software provides haptic effects for touch screens and touch panels, providing pre-designed haptic effects and user interface (UI) support along with design recommendations oriented for mass market devices. TouchSense 2000 is offered as a direct software license to

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the OEM as well as through our integrated circuit partners who preload their integrated circuits with the TouchSense 2000 Player.

TouchSense 3000: Targeted to the mobile device and consumer electronics market, TouchSense 3000 software provides precise actuator control to single standard-definition actuator designs, creating crisp, realistic, and nuanced haptic effects. The software is easy to implement, and enables an unlimited number of haptic effects.

TouchSense 4000: Building off the TouchSense 3000 software, TouchSense 4000 software also targets the mobile communications and consumer electronics market by providing controls for higher-fidelity haptic designs which utilize multiple actuators. The TouchSense 4000 software offers a higher level of control, creating the opportunity for an increased number of haptic effects with finer resolution.

TouchSense 5000: Targeted to the mobile communications, automotive, and consumer electronics market, TouchSense 5000 software offers haptic controls for high-fidelity actuators, producing higher quality effects and creating a superior tactile user experience.

Integrator: Working in conjunction with Immersion's mobile TouchSense software, Integrator consists of modules that OEMs can choose from to easily incorporate haptic experiences into their mobile device operating system. Integrator Modules include: UI Module, which streamlines haptic integration by automatically associating haptic effects with select UI elements such as button presses and scrolling actions; Themes Module, which allows OEMs to waterfall a signature haptic feel through the UI of the device; WebKit Module, which extends the theme controls to the device internet browser experience; and Ringtones Module, which enables support of unique and distinct haptic vibrations to be used during the device silent mode.

Patent Licenses

In addition to licensing software, we also offer patent licenses to those customers who wish to develop their own proprietary haptic implementations. We license our patents across all of our target markets.

Basic Haptics: Targeted primarily to the mobile communications and consumer electronics markets, a Basic Haptics license allows customers to develop their own haptic implementations or utilize standard operating systems' implementations of haptics where the haptic effects are based on sensing a user's input on a touchscreen and associating events with a limited set of haptic effects in a multi-tasking environment.

Force Feedback: Targeted at the gaming, automotive, and medical markets, Immersion's Force Feedback license allows customers to create custom implementations of force feedback based on the unique requirements of the application including: gaming peripherals and simulation; navigation controls for automotive environments; as well as medical applications such as virtual reality training simulators for interventional and surgical procedures, robotic surgical tools, medical instrumentation, and wearable medical devices.

Haptic Expertise

For both our TouchSense and patent licensees, we offer our expertise to help them design and integrate touch effects into their products. This expertise includes turn-key engineering and integration services, design kits for prototyping, authoring tools, APIs, and the development of hardware and software technologies that are compatible with industry standards.

Turn-key Engineering and Integration Services We offer engineering assistance, including technical and design assistance and integration services that allow our licensees to incorporate our touch-enabling products and technologies into their products at a reasonable cost and in a shortened time frame. This allows them to get to market quickly by using our years of haptic development and solution deployment expertise. We offer product development solutions including product software libraries, design, prototype creation, technology transfer, actuator selection, component sourcing, development/integration kits, sample source code, comprehensive

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documentation, and other engineering services. In addition, we help ensure a quality end-user experience by offering testing and certification services to a number of licensees.

Design Kits for Prototyping We offer several design kits for customers to use for technology evaluation, internal evaluation, usability testing, and focus group testing. The kits include components and documentation that designers, engineers, and system integrators need for prototyping tactile effects into an existing or sample product or application.

Authoring Tools We license authoring tools that enable haptic designers and software developers to quickly design and incorporate customized touch feedback into their applications. Authoring tools allow designers to create, modify, experience, and save or restore haptic effects for a haptically-enabled device. Our authoring tools are the equivalent of a computer-aided design application for haptics, and support vibro-tactile haptic devices (such as mobile devices, touchscreens, and vibro-tactile gaming peripherals), as well as kinesthetic haptic devices (such as rotary devices, 2D devices, and joysticks). Various haptic effect parameters can be defined and modified, and the result immediately experienced. Our authoring tools run on mainstream operating systems such as Microsoft Windows. Commencing in March 2011, we have made Immersion's Haptic Development Platform available to Android software developers for use in integrating tactile effects into mobile games and other downloadable applications.

Application Programming Interfaces Our APIs provide haptic-effect generation capability. This allows designers and software programmers to focus on adding haptic effects to their applications instead of struggling with the mechanics of programming real-time algorithms and handling communications between computers and devices. Some of our haptic APIs are device independent (for example, they work with scroll wheels, rotary knobs, 2D joysticks, and other devices) to allow flexibility and reusability. Others are crafted to meet the needs of a particular customer or industry.

Platform Independent Solutions Our software driver and API technology have been designed to be easily ported to a variety of operating systems including Android, Tizen, Linux, and Windows.

Products and Markets

Mobile Communications and Consumer Electronics We offer both TouchSense software and patent licenses to OEMs in the mobile device and consumer electronics markets. In addition, our integrated circuit partners preload their integrated circuits with our TouchSense software and offer these integrated circuits to OEMs in the mobile device market.

Our licensees currently include some of the top makers of mobile devices in the world including: Samsung, Motorola, LG Electronics, Fujitsu, NEC, Xiaomi, and Toshiba, as well as integrated circuit manufacturers such as Texas Instruments and Atmel.

For the years ended December 31, 2013, 2012, and 2011, respectively, 66%, 46%, and 44% of our total revenues were generated from customers in the mobile communications market.

Gaming Devices We have licensed our patents to Microsoft Corporation for use in its gaming products and to Sony Computer Entertainment Inc. (Sony) for use in its legacy and current PlayStation console gaming products. We have also licensed our patents to over a dozen gaming peripheral manufacturers and distributors, including Logitech and Mad Catz, Inc., to bring haptic technology to PC platforms including Microsoft Windows operating systems, as well as to video game consoles.

In the video game console peripheral market, we have licensed our patents for use in hundreds of spinning mass tactile feedback devices and force feedback devices such as steering wheels and joysticks to various manufacturers, including: Bensussen Deutsch & Associates Inc., Datel Design & Inc., dreamGear LLC, Logitech Inc., Mad Catz, Inc., Microsoft Corporation, Performance Designed Products (formerly Electro Source LLC) , Razer PTE Ltd, Guillemot Corporation, and Sony. These products are designed to work with one or more video

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game consoles including the Xbox, Xbox 360, and Xbox One from Microsoft; the PlayStation, PlayStation 2, PlayStation 3, and PlayStation 4 from Sony; and the N64, GameCube, and Wii from Nintendo. Currently, products sold to consumers using Immersion technology include PC joysticks, steering wheels, and gamepads from various licensees.

For the years ended December 31, 2013, 2012, and 2011, respectively, 21%, 28%, and 31% of our total revenues were generated from customers in the PC and console gaming markets.

Automotive We offer both TouchSense software and patent licenses to automotive component suppliers. Our current licensees include: ALPS Electric Co., Ltd, Methode Electronics, Inc., Visteon, SMK Corporation, Tokai Rika Co., Ltd., and Panasonic Corp.

For the years ended December 31, 2013, 2012, and 2011, respectively, 5%, 6%, and 6% of our total revenues were from automotive customers.

Medical Throughout 2011 and 2012, we maintained a single medical simulation product line, the Virtual IV system, which simulated needle-based procedures such as intravenous catheterization and phlebotomy. This product was produced for Laerdal Medical A/S, who distributed it on a world-wide basis. In December of 2012, we signed a licensing agreement for this product line with Laerdal Medical A/S. As of January, 2013, we continued to license patents to the medical market, but no longer manufactured any product lines. Our current licensees include: MAKO Surgical Corp., SOFAR S.P.A., CAE Healthcare, Symbionix, and Laerdal Medical A/S.

For the years ended December 31, 2013, 2012, and 2011, respectively 8%, 16%, and 15% of our total revenues were from the medical market.

Manufactured Products

As of December 2013, we ceased selling manufactured products and now only license our patents and software. Our product solutions, which did not represent a material part of our business, were limited to components used for design kits. Through 2012, we manufactured products including the Virtual IV system which was produced on a private label basis for a customer (See Product and Markets Medical). All products produced were from contracted manufacturing services.

Sales

Our sales have been seasonal with typically an increase in the first quarter reflecting holiday shipments of our customer's products with integrated Immersion technology. Both mobile devices and gaming products are subject to shipment increases in the fourth quarter which is reflected in our first quarter revenue. Seasonal fluctuations have not been extremely significant to our overall revenue trends in the past. As we are increasingly entering into license agreements that include recurring fixed payments to us, we anticipate that our sales may become less seasonal over time.

We employ a consolidated direct sales force in the United States, Europe, and Asia to license our software and patents across our target markets and augment that sales force via partnerships and licensing agreements with component suppliers and system integrators.

Additional information about significant customers is incorporated herein by reference to Note 17 of our consolidated financial statements and related financial information in Item 8. *Financial Statements and Supplementary Data*.

Competition

Our biggest source of competition derives from decisions made by internal design groups at our OEM customers and potential OEM customers. We expect that these internal design groups will continue to make choices regarding whether to implement haptics or not, or whether to develop their own haptic solutions.

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In the event we have granted or grant a license to our patent portfolio to an OEM, its internal design group may design technology that is less expensive to implement or that enables products with higher performance or additional features. In some cases, the OEM may elect not to include haptics in its products due to the higher bill of materials costs associated with incorporating haptics.

In addition to licensing OEMs directly, our business also includes licensing to semiconductor manufacturers who incorporate certain of our lower-tiered technology in their integrated circuits for use in certain electronic devices.

The principal competitive factors are the strength of the patents underlying the technology, the technological expertise and design innovation and the use, reliability and cost-effectiveness of the solutions. We believe we compete favorably in all these areas.

For licensed applications, our competitive position is partially dependent on the competitive positions of our licensees that pay a license fee and/or royalty. Our licensees' markets are highly competitive. We believe that the principal competitive factors in our licensees' markets include price, performance, user-centric design, ease-of-use, quality, and timeliness of products, as well as the manufacturer's responsiveness, capacity, technical abilities, established customer relationships, retail shelf space, advertising, promotional programs, and brand recognition. Touch-related benefits in some of these markets may be viewed simply as enhancements and compete with nontouch-enabled technologies.

Research and Development

Our success depends on our ability to invent, improve, and reduce the cost of our technologies in a timely manner; to design and develop software to meet specifications based on research and our understanding of customer needs and expectations; and to collaborate with our licensees who are integrating our technologies into theirs.

Immersion Engineering We have assembled a multi-disciplinary team of highly skilled engineers and scientists with the experience required for development of touch-enabling technology. The team's experience includes skills related to mechanical engineering, electrical engineering, embedded systems and firmware, control techniques, software, quality control, haptic content design, and project and process management. This team continues to generate patents that strengthen our IP position.

Application Engineering and Technical Support We may provide application engineering and technical support during integration of our touch-enabling technology into customer products. To facilitate the validation and adoption of touch-enabling technology, we have developed various design kits. These kits may include actuators, mounting suggestions, controller boards, software libraries, programming examples, and documentation. Our application engineers support customer use of these design kits, including through phone and e-mail technical support and onsite training. This team continues to generate patents that strengthen our IP position.

Research We have multidisciplinary expertise in usability and multimodal user interface design, actuator design, sensors, integration, material science, real-time simulation algorithms, control, and software development. Our research team works with existing and potential partners to help them assess and prove the value of haptics in their field of interest, creating main competitive differentiator and value added solutions. This team continues to generate patents, actively contributing to the reinforcement of Immersion's IP position.

User Experience We have a dedicated team of user interaction specialists, focusing on user research and design to enable new and improved applications of haptics. We have unique expertise in haptics, usability and interface design. Our team works with existing and potential partners to help them determine the best implementation of haptics in their specific application. This team works on the cutting edge of new user interface paradigms using haptics, resulting in an ongoing generation of patents, actively contributing to the development of new IP for us.

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For the years ended December 31, 2013, 2012, and 2011, research and development expenses were \$10.9 million, \$8.4 million, and \$8.4 million respectively.

Intellectual Property

We believe that IP protection is crucial to our business. We rely on a combination of patents, copyrights, trade secrets, trademarks, nondisclosure agreements with employees and third parties, licensing arrangements, and other contractual agreements with third parties to protect our IP. We maintain and support an active program to protect our IP, primarily through the filing of patent applications and the defense of issued patents against infringement.

Our failure to obtain or maintain adequate protection for our IP rights for any reason could hurt our competitive position. There is no guarantee that patents will be issued from the patent applications that we have filed or may file. Our issued patents may be challenged, invalidated, or circumvented, and claims of our patents may not be of sufficient scope or strength, or issued in the proper geographic regions, to provide meaningful protection or any commercial advantage.

At the end of 2013, we and our wholly owned subsidiaries had over 1,500 currently issued or pending patents in the U.S. and other countries that cover various aspects of our technologies. The duration of our issued patents is determined by the laws of the country of issuance and for the United States is typically 17 years from the date of issuance of the patent or 20 years from the date of filing of the patent application resulting in the patent. Some of our U.S. patents began expiring in 2007.

During the fourth quarter 2013, we elected to change our method of accounting for external patent-related costs associated with our internally developed patents and trademarks. Prior to the change we 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 new method of accounting, external patent-related costs are expensed as incurred and classified as general and administrative expenses in our consolidated statement of operations consistent with the classification of internal legal costs associated with internally developed patents and trademarks. Costs 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. Additional information about our patents is incorporated by reference to Notes 1 and 6 to the consolidated financial statements and related financial information in Item 8. *Financial Statements and Supplementary Data*.

Financial Information About Industry Segments and Geographic Areas

We manage our operations and allocate resources as a single reporting segment. Additional information about our business segments and geographic areas is incorporated herein by reference to Note 17 of our consolidated financial statements and related financial information in Item 8. *Financial Statements and Supplementary Data*. In addition, financial information regarding our operations, assets and liabilities, including our total net revenue and net income (loss) for the years ended December 31, 2013, 2012 and 2011 and our total assets as of December 31, 2013 and 2012, is included in our consolidated financial statements and related financial information in Item 8. *Financial Statements and Supplementary Data*.

Investor Information

You can access financial and other information in the Investor Relations section of our web site at www.immersion.com. We make available, on our Web site, free of charge, copies of our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC.

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The charters of our audit committee, our compensation committee, and our nominating/corporate governance committee, and our Code of Business Conduct and Ethics (including code of ethics provisions that apply to our principal executive officer, principal financial officer, controller, and senior financial officers) and our Corporate Governance Principles are also available at our web site under Corporate Governance. These items are also available to any stockholder who requests them by calling +1 408.467.1900.

The SEC maintains an Internet site that contains reports, proxy, and information statements, and other information regarding issuers that file electronically with the SEC at www.sec.gov.

Employees

As of December 31, 2013, we had 105 full-time and part-time employees, including 55 in research and development, 21 in sales and marketing, and 29 in legal, finance, and administration. We also use independent contractors. None of our employees are represented by a labor union, and we consider our employee relations to be positive.

Executive Officers

The following table sets forth information regarding our executive officers as of February 19, 2014.

<u>Name</u>	<u>Position with the Company</u>	<u>Age</u>
Victor Viegas	Chief Executive Officer and member of the Board of Directors	56
Dennis Sheehan	Senior Vice President, Sales and Marketing	52
Paul Norris	Chief Financial Officer	51
Jason Patton	Vice President & General Manager of Content & Media Business	40

Victor Viegas was named our Chief Executive Officer in April 2010, and served as our Interim Chief Financial Officer from December 2011 until May 2012. He served as our Interim Chief Executive Officer from October 2009 to April 2010, and has served as a member of the Board of Directors since October 2002. Mr. Viegas was our Chief Executive Officer from October 2002 through April 2008, and President from February 2002 through April 2008. Mr. Viegas was also Chairman of the Board of Directors from October 2007 to February 2009, and assumed the role of interim Chief Financial Officer from December 2011 through May 2012. Mr. Viegas also served as Chief Financial Officer until February 2005, having joined us in August 1999 as Chief Financial Officer, Vice President, Finance. From June 1996 to August 1999, he served as Vice President, Finance and Administration and Chief Financial Officer of Macrovision Corporation, a developer and licensor of video and software copy protection technologies. From October 1986 to June 1996, he served as Vice President of Finance and Chief Financial Officer of Balco Incorporated, a manufacturer of advanced automotive service equipment. He holds a B.S. in Accounting and an M.B.A. from Santa Clara University. Mr. Viegas is also a Certified Public Accountant in the State of California, on inactive status.

Dennis Sheehan assumed the role as Immersion's SVP of Sales & Marketing, responsible for leading all sales, product & corporate marketing activities for Immersion's TouchSense software and technology licenses, in October 2012. Previously, Mr. Sheehan was our Vice President of Marketing from January 2009 to October 2012. Prior to joining Immersion, Mr. Sheehan was the Senior Director of Product Management at SiRF technology, a leading supplier of GPS semiconductor solutions for mobile phones and personal navigation devices from June 2006 to December 2009. From March 2005 to November 2005, Mr. Sheehan was the Vice President of Business Development and Strategy for Varatouch, an IP components and software company. Earlier in his career, Mr. Sheehan held various marketing and management positions at Intel. He holds a B.S. in Chemical Engineering from Stanford University and an M.B.A. from Northwestern University's Kellogg School of Management.

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Paul Norris joined Immersion as Chief Financial Officer in May 2012. Prior to joining Immersion, Mr. Norris served as a partner at Accanto Partners, LLC, an investment fund focusing on technology and digital media companies from July 2011 to May 2012. Prior to that, from June 2005 to February 2011, Mr. Norris served in various executive positions at Sonic Solutions, a digital media software and entertainment solutions provider, acting as its Senior Vice President and General Counsel from June 2005 to February 2008, and its Executive Vice President, Chief Financial Officer and General Counsel February 2008 until its acquisition by Rovi Corporation, a digital entertainment technology solutions provider in February 2011. From February 2011 through June 2011, Mr. Norris assisted Rovi in its integration activities as an Executive Advisor. Mr. Norris holds a Bachelor of Arts from Yale University and a Juris Doctor degree from Harvard Law School.

Jason Patton joined Immersion in January 2014. He is responsible for the development and management of our Content & Media line of business. Prior to joining Immersion, Patton was Senior Vice President, Business Development & Technology of YOD China, a publicly-traded company focused entirely on bringing advanced TV offerings featuring premium Hollywood content to mainland China, from October 2010 to December 2013. From June 2001 to November 2009, Patton managed business development for In Demand Networks, the joint venture owned by Comcast, Cox and Time Warner Cable serving most recently as Senior Vice President, Business Development. Patton has also worked at AT&T in both business development and mergers & acquisitions. Patton holds a B.S. in broadcast journalism from Boston University, a B.S. in business administration from Boston University, and an M.B.A. from the Harvard Business School.

Item 1A. Risk Factors

You should carefully consider the following risks and uncertainties, as well as other information in this report and our other SEC filings, in considering our business and prospects. If any of the following risks or uncertainties actually occurs, our business, financial condition, or results of operations could be materially adversely affected. The following risks and uncertainties are not the only ones facing us. Additional risks and uncertainties of which we are unaware or that we currently believe are immaterial could also materially adversely affect our business, financial condition, or results of operations. In any case, the trading price of our common stock could decline, and you could lose all or part of your investment. See also the Forward-looking Statements discussion in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

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 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;

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challenges in demonstrating the compelling value of our technologies and challenges associated with customers' ability to easily implement our technologies;

difficulties in obtaining new licensees for yet-to-be commercialized technology because their suppliers may not be ready to meet stringent quality and parts availability requirements;

difficulties in entering into or renewing gaming licenses if video console makers choose not to license third parties to make peripherals for their new consoles, if video console makers no longer require peripherals to play video games, if video console makers no longer utilize technology in the peripherals that are covered by our patents or if the overall market for video consoles deteriorates substantially;

reluctance of content developers or distributors, mobile device manufacturers, and service providers to sign license agreements without a critical mass of other such inter-dependent supporters of the mobile device industry also having a license, or without enough similar devices in the market that incorporate our technologies; and

inability of current or prospective licensees to ship certain devices if they are involved in IP infringement claims by third parties that ultimately prevent them from shipping products or that impose substantial royalties on their products.

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

Samsung Electronics accounted for approximately 47% of our total revenues for the year ended December 31, 2013 and approximately 24% of our total revenues for the year ended December 31, 2012. Two customers accounted for approximately 33% of our total revenues for the year ended December 31, 2011, one of which was Samsung. We cannot be certain that customers that have accounted for significant revenue in past periods, individually or as a group, will continue to generate similar revenue in any future period. If we fail to renew or lose a major customer or group of customers, our revenue could decline if we are unable to replace the lost revenue with revenue from other sources.

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 our 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 geographic and product markets, we have increasingly 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.

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

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

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

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

compliance with multiple, conflicting and changing governmental laws and regulations;

laws and business practices favoring local competitors;

foreign exchange and currency risks;

import and export restrictions, duties, tariffs, quotas and other barriers;

difficulties staffing and managing foreign operations;

difficulties and expense in enforcing IP rights;

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

multiple conflicting tax laws and regulations;

political and economic instability; and

the possibility of an outbreak of hostilities 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 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.

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We are currently involved in litigation and administrative proceedings involving some of our key patents; any invalidation or limitation of the scope of our key patents could significantly harm our business.

As more fully described under Part I, Item 3- Legal Proceedings, we are currently involved in litigation involving some of our patents. The defendant in this litigation has challenged the validity, scope, enforceability and ownership of our patents. In addition, reexamination requests have been filed in the U.S. Patent and Trademark Office (PTO) with respect to patent claims at issue in our litigation. Under a reexamination

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proceeding and upon completion of the proceeding, the PTO may leave a patent in its present form, narrow the scope of the patent or cancel some or all of the claims of the patent. If some or all of the claims of the patents that are subject to reexamination are canceled, our business may be significantly harmed.

We cannot predict the outcome of pending litigation or reexaminations. If there is an adverse ruling in any legal or administrative proceeding relating to the infringement, validity, enforceability or ownership of any of our patents, or if a court or an administrative body such as the PTO limits the scope of the claims of any of our 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 significantly reduced. The resulting reduction in license fees and royalties could significantly harm our business, consolidated financial position, results of operations or cash flows, or the trading price of our common stock.

Furthermore, regardless of the merits of any claim, the continued maintenance of these legal and administrative proceedings may result in substantial legal expenses and diverts our management's time and attention away from our other business operations, which could significantly harm our business. The time to resolution and complexity of our litigation, its significance to our business, the propensity for delay in patent litigation, and the potential that we may lose particular motions as well as the overall litigation could cause significant volatility in our stock price and materially adversely affect our business and consolidated financial position, results of operations and cash flows.

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

We have been in the past and are currently a party to various legal proceedings. Due to the inherent uncertainties of litigation, we cannot accurately predict how these cases will ultimately be resolved. We anticipate that currently pending litigation will continue to be costly and that future litigation will result in additional legal expenses, and there can be no assurance that we will be successful or be able to recover the costs we incur in connection with litigation. We expense litigation costs as incurred, and only accrue for costs that have been incurred but not paid to the vendor as of the financial statement date. Litigation has diverted, and could continue to divert, the efforts and attention of some of our key management and personnel. As a result, until such time as it is resolved or concluded, litigation could adversely affect our business. Further, any unfavorable outcome could adversely affect our business. For additional background on this and our other litigation, please see Note 13 to the consolidated financial statements in Part II, Item 8 Financial Statements and Supplementary Data and Part I, Item 3 Legal Proceedings .

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

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

Due to the continuing evolution of market sectors, product categories, and licensee business models, and to the compromises inherent in the drafting and negotiation of License Provisions, our licensees may interpret License Provisions in their agreements in a way that is different from our interpretation of such License Provisions, or in a way that is in conflict with the rights that we have granted to other licensees. Such interpretations by our licensees may lead to claims that we have granted rights to one licensee that are inconsistent with the rights that we have granted to another licensee. Many of our customers report royalties to us based on their shipments or their revenues and their interpretation and allocation of contracted royalty rates. It is

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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.

Competing technologies may harm our business.

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

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

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

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

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

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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 operat