

APPLICA INC  
Form 8-K  
November 04, 2004

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

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**FORM 8-K**

**CURRENT REPORT  
Pursuant to Section 13 or 15(d) of the  
Securities Exchange Act of 1934**

**Date of Report (Date of Earliest Event Reported): November 4, 2004**

**APPLICA INCORPORATED**

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(Exact name of Registrant as specified in its charter)  
Commission File Number 1-10177

**Florida**

**59-1028301**

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(State or other jurisdiction of incorporation or  
organization)

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(I.R.S. Employer Identification Number)

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**3633 Flamingo Road, Miramar, Florida**

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**33027**

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (954) 883-1000

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2 below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
  - Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
  - Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
  - Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
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**Item 2.02 Results of Operations and Financial Condition.**

On November 4, 2004, Applica Incorporated issued a press release describing its results of operations for its three and nine months ended September 30, 2004. A copy of the press release is attached as Exhibit 99 to this report. This information is not deemed to be filed for the purposes of Section 18 of the Securities Exchange Act of 1934 and is not incorporated by reference into any Securities Act registration statements.

**SIGNATURE**

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: November 4, 2004**

Applica Incorporated

By: /s/ Terry Polistina  
Terry Polistina, Senior Vice President  
and  
Chief Financial Officer of Applica  
Incorporated

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**Exhibit Index**

<u>Exhibit No.</u>	<u>Description</u>
99	Applica Incorporated Press Release dated November 4, 2004

4

Company 11% \*

Arbitron

44%

\* Less than 10%

**5. Stock-Based Compensation**

Stock-based compensation includes expense charges for all stock-based awards to employees and directors. These awards include option grants and restricted stock awards.

*Determining Fair Value*

*Preferred Stock*

The Board of Directors authorized 10,000 shares of Series A Redeemable Nonvoting Preferred stock (Series A Preferred) to be issued to the executive officers. The Series A Redeemable Nonvoting Preferred stock has no voting rights, except as required by law, and may be redeemed at the option of the Company's Board of Directors at any time on or after June 18, 2013.

The Series A Preferred is redeemable based on the stated fair value of \$5.00 per share, and the related stock compensation expense is recognized over the non-redeemable period of 5 years, or 60 months, through June 2013 using the straight-line method. The Series A Preferred has no dividend rights and no rights to the undistributed earnings of the Company.

*Stock Options*

*Valuation and Amortization Method.* The Company estimates the fair value of stock-based awards granted using the Black-Scholes option valuation model. The Company amortizes the fair value of all awards on a straight-line basis over the requisite service periods, which are generally the vesting periods. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model.

*Expected Life.* The expected life of awards granted represents the period of time that they are expected to be outstanding. For 2011, the Company determines the expected life based on historical experience with similar awards, giving consideration to the contractual terms, vesting schedules and pre-vesting and post-vesting forfeitures. For 2010, the Company determined the initial expected life based on a simplified method in accordance with SAB 110 *Shared-Based Payment*, giving consideration to the contractual terms, vesting schedules and post-vesting forfeitures. Stock options granted generally vest over four years for employee grants and one to two years for director grants, and have contractual terms of ten years.

*Expected Volatility.* For 2011, the Company estimates the volatility of its common stock at the date of grant based on the historical volatility of its common stock based on historical prices over the most recent period commensurate with the estimated expected life of the award. For 2010, the Company's estimate of volatility was based on a 50/50 blend of the Company's own historical volatility and an independent analysis of a peer

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group's historical volatility, calculated by individual entity basis, of its common stock based on historical stock prices over the most recent period commensurate with the estimated expected life of the award.

*Risk-Free Interest Rate.* The Company bases the risk-free interest rate used in the Black-Scholes option valuation model on an interest rate on a Treasury bond with a maturity commensurate with each expected life estimate.

*Expected Dividend Yield.* The Company has never paid any cash dividends on its common stock and does not anticipate paying any cash dividends in the foreseeable future. Consequently, the Company uses an expected dividend yield of zero in the Black-Scholes option valuation model.

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A summary of the weighted average assumptions and results for options granted are as follows:

	<b>2011</b>	<b>2010</b>
Expected life (in years)	5.75	5.2 - 6.0
Expected volatility	42%	52% - 55%
Risk-free interest rate	2.3%	2.5% - 3.0%
Expected dividend yield	0%	0%

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>
Fair value of stock options granted	\$ 954	\$ 893

*Expected Forfeitures.* The Company uses a zero forfeiture for both the stock options granted to employees, which vest monthly, and the stock options granted to the Company's Directors. Initial option grants, for new Directors, vest 50% on the first anniversary of the date of grant and then monthly thereafter, and annual option grants, for continuing Directors, vest monthly. The Company records stock-based compensation expense only for those awards that are expected to vest, including awards made to Directors who are expected to continue with the Company through the year following the date of grant.

*Restricted Stock*

The Compensation Committee of the Board of Directors has awarded restricted stock shares under the Company's 2008 Stock Incentive Plan to certain employees. The shares subject to the restricted stock awards vest over a certain period, usually four years, following the date of the grant. Specific terms of the restricted stock awards are governed by Restricted Stock Agreements between the Company and the award recipients.

The fair value of restricted stock awards granted is based on the fair market value of the Company's common stock on the date of the grant (measurement date), and is recognized over the vesting period of the related restricted stock using the straight-line method.

**Stock-based Compensation**

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>
Stock-based compensation:		
Cost of revenue	\$ 110	\$ 97
Sales and marketing	85	42
Research, development and engineering	158	70
General and administrative	585	507
Intellectual property	48	24
Stock-based compensation expense	986	740
Capitalized to patent costs	11	11
Total stock-based compensation	\$ 997	\$ 751

Total unrecognized compensation cost related to non-vested stock-based awards granted under all equity compensation plans, including preferred stock, stock options and restricted stock:

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	As of March 31, 2011	As of December 31, 2010
Unrecognized compensation costs	\$ 9,206	\$ 6,212

Total unrecognized compensation cost will be adjusted for any future changes in estimated forfeitures.



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The Company expects to recognize this compensation cost for stock options and restricted stock over a weighted average period through March 2015:

	Stock Options	Restricted Stock
Weighted average period	1.14 years	2.00 years

*Stock Option Activity*

As of March 31, 2011, under all of the Company's stock-based compensation plans, options to purchase an additional 929,530 shares were authorized for future grants under the plans. The Company issues new shares upon option exercises.

Options granted, exercised, canceled and expired under the Company's stock option plans are summarized as follows:

	Options	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value
<b>Three-months ended March 31, 2011:</b>				
Outstanding at December 31, 2010	993,491	\$ 10.47	\$ 6.55	
Options granted	75,000	\$ 30.01	\$ 12.72	
Options exercised				
Options canceled or expired				
Outstanding at March 31, 2011	1,068,491	\$ 11.84	\$ 6.98	\$ 18,307
Exercisable at March 31, 2011	491,080	\$ 10.56		\$ 9,008
Unvested at March 31, 2011	577,411	\$ 12.93		\$ 9,299

The aggregate intrinsic value is based on the closing price of \$28.90 per share of Digimarc common stock on March 31, 2011, which would have been received by the optionees had all of the options with exercise prices less than \$28.90 per share been exercised on that date.

The following table summarizes information about stock options outstanding at March 31, 2011:

Range of Exercise Prices	Options Outstanding			Options Exercisable		
	Number Outstanding	Remaining Contractual Life (Years)	Weighted Average Price	Number Exercisable	Remaining Contractual Life (Years)	Weighted Average Price
\$9.64	827,241	7.58	\$ 9.64	402,120	7.58	\$ 9.64
\$9.91	30,000	8.08	\$ 9.91	30,000	8.08	\$ 9.91
\$14.99	106,250	8.76	\$ 14.99	28,335	8.76	\$ 14.99
\$18.01	30,000	9.08	\$ 18.01	27,500	9.08	\$ 18.01
\$30.01	75,000	9.76	\$ 30.01	3,125	9.76	\$ 30.01
\$9.64 - \$30.01	1,068,491	7.91	\$ 11.84	491,080	7.78	\$ 10.56



**Table of Contents***Restricted Stock Activity*

The following table reconciles the unvested balance of restricted stock:

	Number of Shares	Weighted Average Grant Date Fair Value
<b>Three-months ended March 31, 2011:</b>		
Unvested balance, December 31, 2010	197,760	\$ 14.25
Granted	101,180	\$ 30.01
Vested	(27,335)	\$ 14.51
Canceled		
 Unvested balance, March 31, 2011	 271,605	 \$ 20.09

**6. Trade Accounts Receivable***Trade Accounts Receivable*

Trade accounts receivable are recorded at the invoiced amount.

	March 31, 2011	December 31, 2010
Trade accounts receivable	\$ 2,725	\$ 3,481
Allowance for doubtful accounts		
 Trade accounts receivable, net	 \$ 2,725	 \$ 3,481
 Unpaid deferred revenues included in accounts receivable	 \$ 1,168	 \$ 2,045

*Allowance for doubtful accounts*

The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company determines the allowance based on historical write-off experience and current information. The Company reviews its allowance for doubtful accounts monthly. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

*Unpaid deferred revenues*

The unpaid deferred revenues that are included in accounts receivable are billed in accordance with the provisions of the contracts with the Company's customers. Unpaid deferred revenues from the Company's cash-basis revenue recognition customers are not included in accounts receivable nor deferred revenue accounts.

*Major customers*

Customers who accounted for more than 10% of accounts receivable, net, are as follows:

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	March 31, 2011	December 31, 2010
The Nielsen Company	37%	29%
Central Banks	27%	43%
Civolution	15%	11%
TVaura LLC	10%	*

\* Less than 10%

### 7. Property and Equipment

Property and equipment are stated at cost. Property and equipment under capital lease obligations are stated at the lower of the present value of minimum lease payments at the beginning of the lease term or fair value of the leased assets at the inception of the lease. Repairs and maintenance are charged to expense when incurred.

Depreciation on property and equipment is calculated using the straight-line method over the estimated useful lives of the assets, generally two to seven years. Leasehold improvements are amortized by the straight-line method over the shorter of the estimated useful life or the lease term.

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	March 31, 2011	December 31, 2010
Office furniture fixtures	\$ 294	\$ 294
Equipment	1,530	1,365
Leasehold improvements	986	986
	2,810	2,645
Less accumulated depreciation and amortization	(1,468)	(1,315)
	\$ 1,342	\$ 1,330

**8. Intangible Assets Purchased and Capitalized Patent Costs**

Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

	March 31, 2011	December 31, 2010
Gross intangible assets	\$ 2,430	\$ 2,290
Accumulated amortization	(142)	(116)
Intangible assets, net	\$ 2,288	\$ 2,174

**9. Joint Venture and Related Party Transactions**

On June 11, 2009 the Company entered into two joint venture agreements with Nielsen to launch two new companies. The two joint venture agreements and a revised patent license agreement expanded and replaced the previous license and services agreement between the Company and Nielsen that had been in operation since late 2007. Under the 2009 new agreements, the Company and Nielsen are working together to develop new products and services, including the expansion and deployment of those products and services that were in development under the prior agreement.

Under the terms of the patent license agreement, Nielsen agreed to pay Digimarc \$18,750 during the period from July 2009 through January 2014, and Digimarc granted to Nielsen a non-exclusive license to Digimarc's patents for use within Nielsen's business. Unless earlier terminated in accordance with the agreement, the license will continue until the expiration of the last to expire of the licensed patents. The payment terms extend beyond the Company's normal 30 to 60 day payment terms, thus the license revenue is recognized when the installments are due.

Joint Venture I, TVaura LLC, is engaged in the development of copyright filtering solutions, royalty/audit solutions for online video and audio rights organizations, guilds or other organizations involved in the reconciliation of royalties, residuals and other payments, and other related products. Each of the Company and Nielsen are making initial cash contributions aggregating \$3,900 payable quarterly from July 2009 through October 2011. The Company will provide technical and development services to TVaura LLC's business of minimum service fees, subject to adjustment for any development service fees paid to the Company by TVaura Mobile LLC, totaling \$6,670 during the period 2009 through 2011. Service revenue will be recognized as the services are performed.

Joint Venture II, TVaura Mobile LLC, is engaged in the development of certain enhanced television offerings, and other related products. Each of the Company and Nielsen are making initial cash contributions aggregating \$2,800 payable quarterly from July 2009 through October 2011.

Pursuant to the terms of the agreements and ASC 810 *Consolidation*, the joint ventures are not consolidated with the Company as the minority shareholder has substantive participating rights, or veto rights, such that no shareholder has majority control.

*Related Party Transactions*

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	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
TVaura LLC:		
Capital contributions	\$ 400	\$ 400
Revenue(1)	\$ 691	\$ 692
TVaura Mobile LLC:		
Capital contributions	\$ 300	\$ 300
Total:		
Capital contributions	\$ 700	\$ 700
Revenue(1)	\$ 691	\$ 692

(1) Technical and development services

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	March 31, 2011	December 31, 2010
TVaura LLC:		
Accounts receivable	\$ 283	\$ 255

Summarized financial data for TVaura LLC:

	March 31, 2011	December 31, 2010
Current assets	\$ 892	\$ 777
Noncurrent assets	\$ 29	\$ 31
Current liabilities	\$ 284	\$ 255
Noncurrent liabilities	\$	\$

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
Revenue	\$	\$
Gross profit	\$	\$
Operating expenses	\$ 717	\$ 740
Net loss from continuing operations	\$ (716)	\$ (740)
The Company's pro-rata share net loss	\$ (365)	\$ (377)

Summarized financial data for TVaura Mobile LLC:

	March 31, 2011	December 31, 2010
Current assets	\$ 1,893	\$ 1,831
Noncurrent assets	\$	\$
Current liabilities	\$ 91	\$ 279
Noncurrent liabilities	\$	\$

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
Revenue	\$	\$
Gross profit	\$	\$
Operating expenses	\$ 350	\$ 164
Net loss from continuing operations	\$ (350)	\$ (164)
The Company's pro-rata share net loss	\$ (172)	\$ (80)

**10. Income Taxes**

There was no provision for the period ended March 31, 2011. Other than the U.S. alternative minimum taxes and foreign withholding tax expense, there was no provision for current income taxes related to net income because the computation of regular taxable income was fully offset by available net operating loss carry-forwards and tax credits previously offset by a full valuation allowance.

The provision for income taxes for the period ended March 31, 2010 reflects withholding tax expense in various foreign jurisdictions. Withholding taxes are computed by the Company's customers and paid to foreign jurisdictions on its behalf.





**Table of Contents****11. Commitments and Contingencies**

Certain of the Company's product license and services agreements include an indemnification provision for claims from third parties relating to the Company's intellectual property. Such indemnification provisions are accounted for in accordance with ASC 450 *Contingencies*. To date, there have been no claims made under such indemnification provisions.

Verance Corporation, a Digimarc licensee, filed a declaratory judgment action against Digimarc in the United States District Court in Delaware on September 30, 2010, alleging the invalidity and non infringement of 22 patents held by Digimarc. Verance Corp. v. Digimarc Corp., 1:10-cv-00831-UNA. Digimarc responded by filing a motion to dismiss the action, the parties filed briefs on this issue, and a hearing was held on April 13, 2011.

On December 6, 2010, Digimarc filed suit against Verance Corporation in the District of Oregon. Digimarc is seeking payment for breach of contract by Verance related to Verance's failure to make payments under the licensing agreement between Digimarc and Verance. Digimarc Corp. v. Verance Corp., CV 10-1489 JE. Verance responded by filing a motion to dismiss or stay the action, and to compel arbitration. The parties filed briefs on the issue, and a hearing was held on April 27, 2011.

Digimarc has been named as one of several defendants in a complaint filed by Walker Digital, LLC, in the U.S. District Court for the District of Delaware on April 22, 2011, case number 11-cv-00363-UNA, alleging patent infringement. The plaintiff is seeking a declaratory judgment, injunctive relief and damages. Digimarc has not yet been served with the complaint.

The Company is subject from time to time to other legal proceedings and claims arising in the ordinary course of business. Although the ultimate outcome of these matters cannot be determined, management believes that, as of March 31, 2011, the final disposition of these proceedings will not have a material adverse effect on the financial position, results of operations, or liquidity of the Company. In accordance with ASC 450, no accrual has been recorded because the amounts are not probable or reasonably estimatable, and a range of possible outcomes is not determinable.

**12. Stock Repurchases**

On January 26, 2011, the Company repurchased 552,536 shares of its common stock from Koninklijke Philips Electronics, N.V., in a privately negotiated transaction. The shares were purchased for an aggregate price of approximately \$14,927, including transaction fees. To facilitate the repurchase, the Company sold \$10,752 and \$2,996 of short- and long-term marketable securities, respectively, prior to their maturity date at an immaterial gain.

In April 2009, the Board of Directors approved a stock repurchase program authorizing the purchase, at the discretion of management, of up to \$5,000 of our common stock through either periodic open-market or private transactions at then prevailing market prices through April 30, 2010. In both April 2010 and April 2011, the Board of Directors approved an extension of the stock repurchase program for one year periods.

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Since Inception (April 2009)</b>
Shares purchased	16,873		128,540
Purchases	\$ 455	\$	\$ 2,016

As part of the Company's 2008 Stock Incentive Plan, stock options are granted to certain employees and restricted stock shares are awarded to certain employees.

Pursuant to the terms of the stock option grants, the Company purchased a number of whole shares of common stock having a fair market value (as determined by the Company as of the date of exercise) equal to the amount of the total value of the aggregate exercise price of the options exercised. In addition, the Company withheld (purchased) from shares issued from upon exercise of the stock options a number of whole shares of common stock having a fair market value (as determined by the Company as of the date of vesting) equal to the amount of tax required to be withheld by law, in order to satisfy the tax withholding obligations of the Company in connection with the exercise of such options. During the three-month periods ended March 31, 2011 and 2010, there were no purchases of shares related to stock option exercises.

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Pursuant to the terms of the restricted stock award agreement, the Company withheld (purchased) from fully vested shares of common stock otherwise deliverable to any employee, a number of whole shares of common stock having a fair market value (as determined by the Company as of the date of vesting) equal to the amount of tax required to be withheld by law, in order to satisfy the tax withholding obligations of the Company in connection with the vesting of such shares.

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	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>
Restricted shares withheld (purchased) for tax	10,876	1,149
Tax withholding obligations	\$ 322	\$ 22

**13. Subsequent Events**

In accordance with ASC 855 *Subsequent Events*, the Company has evaluated subsequent events.

**14. Quarterly Financial Information**

<b>Quarter ended: 2011</b>	<b>March 31</b>
Service revenue	\$ 3,069
License and subscription revenue	6,022
Total revenue	9,091
Total cost of revenue	1,649
Gross profit	7,442
Gross profit percent, service revenue	48%
Gross profit percent, license and subscription revenue	99%
Gross profit percent, total	82%
Sales and marketing	1,102
Research, development and engineering	1,775
General and administrative	2,847
Intellectual property	301
Operating income	1,417
Net income	938
Earnings per share:	
Net income per share basic	\$ 0.14
Net income per share diluted	\$ 0.12
Weighted average shares outstanding basic	6,864
Weighted average shares outstanding diluted	7,505

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<b>Quarter ended:</b> <b>2010</b>	<b>March 31</b>	<b>June 30</b>	<b>September 30</b>	<b>December 31</b>
Service revenue	\$ 3,514	\$ 2,918	\$ 2,761	\$ 3,131
License and subscription revenue	6,678	2,330	2,476	7,342
Total revenue	10,192	5,248	5,237	10,473
Total cost of revenue	1,857	1,540	1,469	1,834
Gross profit	8,335	3,708	3,768	8,639
Gross profit percent, service revenue	49%	49%	49%	43%
Gross profit percent, license and subscription revenue	99%	98%	98%	99%
Gross profit percent, total	82%	71%	72%	82%
Sales and marketing	741	759	953	1,092
Research, development and engineering	1,259	1,321	1,471	1,636
General and administrative	1,885	1,687	1,842	2,450
Intellectual property	257	319	315	312
Operating income (loss)	4,193	(378)	(813)	3,149
Net income (loss)	3,776	(896)	(1,460)	2,754
Earnings (loss) per share:				
Net earnings (loss) per share basic	\$ 0.53	\$ (0.13)	\$ (0.21)	\$ 0.38
Net earnings (loss) per share diluted	\$ 0.51	\$ (0.13)	\$ (0.21)	\$ 0.35
Weighted average shares outstanding basic	7,096	7,097	7,098	7,190
Weighted average shares outstanding diluted	7,387	7,097	7,098	7,859

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### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

*The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements relating to future events or the future financial performance of Digimarc, which involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements. Please see the discussion regarding forward-looking statements included in this Quarterly Report on Form 10-Q under the caption "Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995."*

*The following discussion should be read in conjunction with our financial statements and the related notes and other financial information appearing elsewhere in this Quarterly Report on Form 10-Q. Readers are also urged to carefully review and consider the disclosures made in Part II, Item 1A (Risk Factors) of this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2010 filed on March 3, 2011 (the "2010 Annual Report") and in the audited financial statements and related notes included in our 2010 Annual Report, and other reports and filings made with the Securities and Exchange Commission ("SEC").*

*Unless the context otherwise requires, references in this Quarterly Report on Form 10-Q to Digimarc, we, our and us refer to Digimarc Corporation.*

*All dollar amounts are in thousands, unless otherwise noted.*

### **Overview**

Digimarc Corporation enables governments and enterprises around the world to give digital identities to media and objects that computers can sense and recognize and to which they can react. Our technology provides the means to infuse persistent digital information, perceptible only to computers and digital devices, into all forms of media content. The unique digital identifier placed in media generally persists with it regardless of the distribution path and whether it is copied, manipulated or converted to a different format, and does not affect the quality of the content or the enjoyment or other traditional uses of it. Our technology permits computers and digital devices to quickly identify relevant data from vast amounts of media content.

Our technologies, and those of our licensees, span a range of media content, enabling our customers and those of our partners to:

Quickly identify and effectively manage music, movies, television programming, digital images, documents and other printed materials, especially in light of new non-linear distribution over the internet;

Deter counterfeiting of money, media and goods, and piracy of movies and music;

Support new digital media distribution models and methods to monetize media content;

Leverage the power of ubiquitous computing to instantly link consumers to a wealth of information and/or interactive experiences related to the media and objects they encounter each day;

Provide consumers with more choice and access to media content when, where and how they want it;

Enhance imagery and video by associating metadata or authenticating media content for government and commercial uses; and

Better secure identity documents to enhance national security and combat identity theft and fraud.

At the core of our intellectual property is a signal processing technology innovation known as "digital watermarking" which allows imperceptible digital information to be embedded in all forms of digitally designed, produced or distributed media content and some physical objects, including photographs, movies, music, television, personal identification documents, financial instruments, industrial parts and product

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packages. The digital information can be detected and read by a wide range of computers, mobile phones, and other digital devices.

We provide technology-based solutions directly and through our licensees. Our proprietary technology has proven to be a powerful element of document security, giving rise to our long-term relationship with a consortium of central banks, which we refer to as the Central Banks, and many leading companies in the information technology industry. We and our licensees have successfully propagated digital watermarking in music, movies, television broadcasts, images and printed materials. Digital watermarks have been used in these applications to improve media rights and asset management, reduce piracy and counterfeiting losses, improve marketing programs, permit more efficient and effective distribution of valuable media content and enhance consumer entertainment and commercial experiences.

Our patent portfolio contains a number of innovations in digital watermarking, pattern recognition (sometimes referred to as fingerprinting), digital rights management and related fields. To protect our significant efforts in creating our technology, we have implemented an extensive intellectual property protection program that relies on a combination of patent, copyright, trademark and

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trade secret laws, and nondisclosure agreements and other contracts. As a result, we believe we have one of the world's most extensive patent portfolios in digital watermarking and related fields, with nearly 1,100 granted and pending U.S. and foreign filings as of March 31, 2011. Separately, we own registered trademarks in both the United States and other countries and have applied for additional trademarks. We continue to develop and broaden our portfolio of patented technology in the fields of media identification and management technology and related applications and systems. We devote significant resources to developing and protecting our technology and continuously seek to identify and evaluate potential licensees for our patents. Most of these patents are subject to an exclusive patent licensing arrangement as described further below.

For a discussion of activities and costs related to our research and development, please read the sections titled "Research, development and engineering" under Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

As part of our intellectual property marketing initiative and patent monetization strategy, on October 5, 2010, we entered into a patent licensing arrangement with IV Digital Multimedia Inventions, LLC, a Delaware limited liability company affiliated with Intellectual Ventures (IV), pursuant to which we granted an exclusive license to sublicense, subject to pre-existing encumbrances and a grant-back license, an aggregate of approximately 900 patents and applications held by us.

We believe recent intellectual property licensing initiatives we have commenced represent substantial opportunities for us to grow our license and subscription revenues, as well as our service revenues. These initiatives, however, may require additional investment in our intellectual property enforcement program and research and development.

## **Critical Accounting Policies and Estimates**

Detailed information on our critical accounting policies and estimates are set forth in our 2010 Annual Report in Part II, Item 7 thereof ("Management's Discussion and Analysis of Financial Condition and Results of Operations"), under the caption "Critical Accounting Policies and Estimates," which is incorporated by reference into this Quarterly Report on Form 10-Q.

**Table of Contents****Results of Operations**

The following table presents statements of operations data for the periods indicated as a percentage of total revenue. Unless otherwise indicated, all references in this Management's Discussion and Analysis of Financial Condition and Results of Operations to the three-month period relate to the three-month period ended March 31, 2011 and all changes discussed with respect to such period reflect changes compared to the three-month period ended March 31, 2010.

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>
<b>Revenue:</b>		
Service	34%	34%
License and subscription	66	66
Total revenue	100	100
<b>Cost of revenue:</b>		
Service	17	17
License and subscription	1	1
Total cost of revenue	18	18
Gross profit	82	82
<b>Operating expenses:</b>		
Sales and marketing	12	7
Research, development and engineering	20	12
General and administrative	32	19
Intellectual property	3	3
Total operating expenses	67	41
Operating income	15	41
Net loss from joint ventures	(6)	(5)
Interest income, net	1	1
Income before provision for income taxes	10	37
Provision for income taxes		
Net income	10%	37%

Continuing with the success in our licensing and service activities, revenues from our largest six customers grew more than \$4 million compared to the prior year, including a \$3 million revenue contribution of our newest relationship, Intellectual Ventures, with whom we entered a long term collaborative relationship in the fourth quarter of 2010. Although our total revenue for the three-month period in 2011 decreased 11% to \$9.1 million compared to the same period in the prior year, the prior year included a one-time payment of license fees of \$4.5 million from Arbitron and we generated revenues from some non-linear government services contracts during that period. In 2011, we continued to invest in our strategic initiatives, including the marketing of our intellectual property, our joint ventures with Nielsen, development of additional intellectual property, and development and marketing of Digimarc Discover; all centered on our vision of enhancing computers, networks and other digital devices to see, hear, understand and respond to their surroundings. In addition, we incurred legal expenses in connection with our litigation with Verance. Notwithstanding the decreased revenues and increased investments in executing our strategy, we achieved profitability and positive cash flow from operations for the three-months ended March 31, 2011.

*Revenue*



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	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Decrease</b>	<b>Percent Decrease</b>
<b>Revenue:</b>				
Service	\$ 3,069	\$ 3,514	\$ (445)	(13)%
License and subscription	6,022	6,678	(656)	(10)%
<b>Total</b>	<b>\$ 9,091</b>	<b>\$ 10,192</b>	<b>\$ (1,101)</b>	<b>(11)%</b>
<b>Revenue (as % of total revenue):</b>				
Service	34%	34%		
License and subscription	66%	66%		
<b>Total</b>	<b>100%</b>	<b>100%</b>		

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We derive our revenue primarily from:

- 1) development services provided to government and commercial customers and
- 2) licensing our patents.

*Service.* Service revenue consists primarily of software development and consulting services. The majority of service revenue arrangements are structured as time and materials consulting agreements, or fixed price consulting agreements. The majority of our services revenue is derived from contracts with the Central Banks, Nielsen, the joint venture TVaura LLC, government agencies and IV. The agreements range from several months to several years in length, and our longer term contracts are subject to work plans that are reviewed and agreed upon at least annually. These contracts generally provide for billing hours worked at predetermined rates and, to a lesser extent, for cost reimbursement for third party costs and services. Increases or decreases in the services provided under these contracts are generally subject to both volume and price changes. The volume of work is generally negotiated at least annually and can be modified as the customer's needs change. We also have provisions in our longer term contracts that allow for specific hourly rate price increases on an annual basis to account for cost of living variables. Contracts with other government agencies are generally shorter term in nature, are less linear in billings and less predictable than our longer terms contracts because the contracts with other government agencies are subject to government budgets and funding.

The decrease in service revenue for the three-month period was due primarily to the fact that in the prior period we completed a number of government contracts for which revenue was earned upon completion. Excluding the revenue earned upon completion of these government contracts in the prior period, service revenue for the three-month period increased primarily by the revenue earned for the support services rendered to IV in support of IV's efforts to monetize the licensed patents.

*License and subscription.* License revenue originates primarily from licensing our technology and patents where we receive royalties as our income stream. Subscription revenue consists primarily of royalty revenue from the sale of our web-based subscriptions related to various software products, which are more recurring in nature. Revenues from our licensed products have minimal associated direct costs, and thus are highly profitable.

The decrease in license and subscription revenue for the three-month period was due primarily to the fact that the prior period included a one-time licensing payment of \$4.5 million from Arbitron. Excluding this payment in the prior period, license and subscription revenue for the three-month period increased primarily by \$2.8 million from IV and, to a lesser extent, by increased license and royalty revenues received from other customers in the three-month period.

*Revenue by Geography*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase (Decrease)</b>	<b>Percent Increase (Decrease)</b>
<b>Revenue by geography:</b>				
Domestic	\$ 6,070	\$ 7,240	\$ (1,170)	(16)%
International	3,021	2,952	69	2%
Total	\$ 9,091	\$ 10,192	\$ (1,101)	11%
<b>Revenue (as % of total revenue):</b>				
Domestic	67%	71%		
International	33%	29%		
Total	100%	100%		

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The decrease in domestic revenue decreased for the three-month period was due primarily to the fact that the prior period included a one-time licensing payment of \$4.5 million from Arbitron. Excluding this payment in the prior period, domestic revenue for the three-month period reflects increased license and service revenues of \$3.0 million from IV and, to a lesser extent, increased license and royalty revenues received from other customers in the three-month period. International revenue remained relatively consistent for the three-month period.

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We anticipate revenue growth for the remainder of 2011, compared to the same period in 2010, from our existing customers and from new customers as we continue expand the marketing and monetization of our intellectual property portfolio.

*Cost of Revenue*

*Service.* Cost of service revenue primarily includes costs that are allocated from research, development, engineering and sales and marketing that relate directly to performing services under our customer contracts, and, to a lesser extent, direct costs of program delivery for both personnel and operating expenses. Allocated costs include:

salaries, a payroll tax and benefit factor, incentive compensation and related costs of our software developers, quality assurance personnel, product managers, business development managers and other personnel where we bill our customers for time and materials costs;

payments to outside contractors that are billed to customers;

charges for equipment directly used by the customer;

depreciation charges for machinery, equipment and software;

travel costs directly attributable to service and development contracts; and

charges for infrastructure and centralized costs of facilities and information technology.

*License and subscription.* Cost of license and subscription revenue primarily includes:

patent or software license costs for any patents licensed from third parties where the party receives a portion of royalties or license revenue received by Digimarc;

internet service provider connectivity charges and image search data fees to support the services offered to our subscription customers; and to a lesser extent

amortization of capitalized patent costs.

*Gross Profit*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Decrease</b>	<b>Percent Decrease</b>
Gross Profit:				
Service	\$ 1,485	\$ 1,714	\$ (229)	(13)%

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License and subscription	5,957	6,621	(664)	(10)%
Total	\$ 7,442	\$ 8,335	\$ (893)	(11)%

### Gross Profit (as % of related revenue components):

Service	48%	49%
License and subscription	99%	99%
Total	82%	82%

The decrease in gross profit for the three-month period primarily reflected the fact that in the prior period we completed a number of government contracts for which a significant amount of the revenue was earned upon completion, and received a one-time licensing payment in the amount of \$4.5 million from Arbitron. Excluding the revenue earned upon completion of these government contracts and the Arbitron licensing payment in the prior period, gross profit for the three-month period increased as a result of the licensing revenue earned from IV and other licensees. Gross profit as a percentage of revenue for the three-month period remained relatively consistent.

### *Operating Expenses*

#### *Sales and marketing*

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	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase</b>	<b>Percent Increase</b>
Sales and marketing	\$ 1,102	\$ 741	\$ 361	49%
Sales and marketing (as % of total revenue)	12%	7%		
Sales and marketing expenses consist primarily of:				

compensation, benefits and related costs of sales and marketing employees and product managers;

travel and market research costs, and costs associated with marketing programs, such as trade shows, public relations and new product launches;

professional services and outside contractors for product and marketing initiatives;

incentive compensation in the form of stock-based compensation expense; and

charges for infrastructure and centralized costs of facilities and information technology.

We allocate certain costs of sales and marketing to cost of service revenue when they relate directly to our service contracts. For direct billable labor hours, we allocate to cost of service revenue:

salaries;

a payroll tax and benefits factor; and

incentive compensation related to our stock compensation plans.

We record all remaining, or residual, costs as sales and marketing costs.

The increase in sales and marketing expense for the three-month period resulted primarily from:

increased headcount and compensation-related expenses of \$0.2 million from hiring additional sales support for our mobile device market initiatives; and

increased marketing and professional fees of \$0.1 million related to a number of sales initiatives, including our Digimarc Discover Platform.

We anticipate that we will continue to incur sales and marketing costs at higher levels to support ongoing sales initiatives.

*Research, development and engineering*

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	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase</b>	<b>Percent Increase</b>
Research, development and engineering	\$ 1,775	\$ 1,259	\$ 516	41%
Research, development and engineering (as % of total revenue)	20%	12%		

Research, development and engineering expenses arise primarily from three areas that support our business model:

### Fundamental Research:

Investigation of new watermarking algorithms to increase robustness and/or computational efficiency;

Mobile device usage models and imaging sub-systems in camera-phones;

Industry conference participation and authorship of papers for industry journals;

Survey and study of human and computer interaction models with a focus on mobile devices and modeling of intent;

Development of new intellectual property, including documentation of claims and production of supporting diagrams and materials; and

Research in fingerprinting and other content identification technologies.

### Platform Development:

Tuning and optimization of implementation models to improve resistance to non-malicious attacks and routine transformations, such as JPEG, cropping and printing; and

Mobile platform creation to leverage device specific capabilities (e.g. instruction sets and GPUs).

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Product Development:

Creation of Online Services Portal to provide campaign management and routing services for the Digimarc Discover platform;

Implementation of web-hosted image watermark embedder in support of Digimarc Discover platform; and

Iterative development and release of the Digimarc Discover application for the iTunes and Android marketplace.

Research, development and engineering expenses consist primarily of:

compensation, benefits and related costs of software developers and quality assurance personnel;

payments to outside contractors;

the purchase of materials and services for product development;

incentive compensation in the form of stock-based compensation expense; and

charges for infrastructure and centralized costs of facilities and information technology.

We allocate certain costs of research, development and engineering to cost of service revenue when they relate directly to our service contracts. For direct billable labor hours, we allocate to cost of service revenue:

salaries;

a payroll tax and benefits factor; and

incentive compensation related to our stock compensation plans.

We record all remaining, or residual, costs as research, development and engineering costs.

The increase in research, development and engineering expense for the three-month period resulted primarily from:

increased headcount and compensation-related expenses of \$0.3 million from hiring engineers and scientists to facilitate growth in our product and service offerings, including increased investments primarily related to the mobile device market; and

increased professional fees of \$0.1 million related to the mobile device market.



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We anticipate that we will continue to invest in research, development and engineering expenses at higher levels to support certain ongoing research and product initiatives.

### *General and administrative*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase</b>	<b>Percent Increase</b>
General and administrative	\$ 2,848	\$ 1,885	\$ 963	51%
General and administrative (as % of total revenue)	32%	19%		

We incur general and administrative costs in the functional areas of finance, legal, human resources, executive and board of directors. Costs for facilities and information technology are also managed as part of the general and administrative processes and are allocated to this area as well as each of the areas in costs of services, sales and marketing, and research, development and engineering.

General and administrative expenses consist primarily of:

compensation, benefits and related costs;

third party and professional fees associated with legal, accounting, human resources and costs associated with being a public company;

incentive compensation in the form of stock-based compensation expense; and

charges for infrastructure and centralized costs of facilities and information technology.

The increases in general and administrative expenses for the three-month period resulted primarily from:

increased legal fees of \$0.6 million related to the litigation matter with Verance, and

increased accounting fees of \$0.2 million related to the transition to our new auditors that we engaged in late 2010 for the 2010 audit.

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We anticipate that we will continue to incur general and administrative expenses at higher levels in the near term, particularly for legal fees related to our current litigation matters, while continuing to examine means to reduce general and administrative expenses as a percentage of revenue in the longer term.

*Intellectual property*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase</b>	<b>Percent Increase</b>
Intellectual property	\$ 301	\$ 257	\$ 44	17%
Intellectual property (as % of total revenue)	3%	3%		

We incur intellectual property expenses that arise primarily from costs associated with documenting, applying for, and maintaining domestic and international patents and trademarks.

Gross expenditures for intellectual property costs, before reflecting the effect of capitalized patent costs, primarily consist of:

compensation, benefits and related costs of attorneys and legal assistants;

third party costs including filing and governmental regulatory fees and fees for outside legal counsel and translation costs, each incurred in the patent process;

incentive compensation in the form of stock-based compensation expense; and

charges for infrastructure and centralized costs of facilities and information technology.

We allocate certain costs of intellectual property to cost of service revenue when they relate directly to our service contracts, primarily for support services provided to IV. For direct billable labor hours, we allocate to cost of service revenue:

salaries;

a payroll tax and benefits factor; and

incentive compensation related to our stock compensation plans.

Intellectual property expenses for the three-month period remained relatively constant. Intellectual property expenses, however, can vary from period to period based on:

the level of capitalized patent activity, and

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prosecution costs and direct labor hours (salaries, payroll taxes and benefits factor and incentive compensation related to our stock compensation plans) related to the patents that were exclusively licensed to IV that are allocated to cost of revenue.

We anticipate that we will continue to invest in intellectual property expenses at existing levels.

### *Stock-based compensation*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase</b>	<b>Percent Increase</b>
Cost of revenue	\$ 110	\$ 97	\$ 13	13%
Sales and marketing	85	42	43	102%
Research, development and engineering	158	70	88	126%
General and administrative	585	507	78	15%
Intellectual property	48	24	24	100%
<b>Total</b>	<b>\$ 986</b>	<b>\$ 740</b>	<b>\$ 246</b>	<b>33%</b>

The increase in stock-based compensation expense for the three-month period was primarily due to an additional layer of stock-based awards. We anticipate incurring an additional \$9,206 in stock-based compensation expense through March 2015 for awards outstanding as of March 31, 2011. Our tax accounting may also be affected by actual exercise behavior and the relative market price of our common stock at exercise of the awards.

**Table of Contents***Net loss from joint ventures*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Increase</b>	<b>Percent Increase</b>
Net loss from joint ventures	\$ (537)	\$ (457)	\$ 80	18%
Net loss from joint ventures (as % of total revenue)	(6)%	(5)%		

The increase in the net loss from joint ventures for the three-month period resulted primarily from increased research, development and engineering work in product development.

*Interest income, net*

	<b>Three Months Ended March 31, 2011</b>	<b>Three Months Ended March 31, 2010</b>	<b>Dollar Decrease</b>	<b>Percent Decrease</b>
Interest income, net	58	61	(3)	(5)%
Interest income, net (as % of total revenue)	1%	1%		

The decrease in interest income, net was primarily due to a combination of lower balances and lower interest earned on cash and investment balances, reflecting lower interest rates paid on these balances.

*Provision for Income Taxes.*

There was no provision for the period ended March 31, 2011.

There was no provision for income taxes, other than foreign withholding taxes, for the three-month period ended March 31, 2010 since the estimated effective tax rate for the period ending December 31, 2010 was expected to be zero, with the exception of foreign withholding tax.

We continually assess the applicability of a valuation allowance. Based upon the positive and negative evidence available as of March 31, 2011, we concluded that it is not more likely than not that net deferred tax assets will be utilized. Consequently, a valuation allowance continues to offset our net deferred tax assets.

**Liquidity and Capital Resources**

	<b>March 31, 2011</b>	<b>December 31, 2010</b>
Working capital	\$ 28,405	\$ 35,526
Current (liquidity) ratio(1)	8.1:1	9.7:1
Cash, cash equivalents and short-term marketable securities	\$ 28,844	\$ 34,781
Long-term marketable securities	\$ 4,264	\$ 11,163
Total cash, cash equivalents and all marketable securities	\$ 33,108	\$ 45,944

(1) The current (liquidity) ratio is calculated by dividing total current assets by total current liabilities. The \$12.8 million decrease in cash, cash equivalents and all marketable securities resulted primarily from:

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the purchase of common stock from a shareholder, Koninklijke Philips Electronics N.V, in a privately negotiated transaction;

purchases of common stock related to the vesting of restricted stock and repurchases made under our stock repurchase program; and

cash contributions to the joint ventures with Nielsen.

*Operating Cash Flow.* The components of operating cash flows were:

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	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010	Dollar Increase (Decrease)	Percent Increase (Decrease)
Net income	\$ 938	\$ 3,776	\$ (2,838)	(75)%
Non-cash items	1,702	1,363	339	25%
Changes in operating assets and liabilities	1,223	242	981	405%
Net cash provided by operating activities	\$ 3,863	\$ 5,381	\$ (1,518)	(28)%

***Net income.***

The decrease in operating results for the three-month period reflects lower revenues primarily related to the fact that the prior period included a one-time licensing payment of \$4.5 million from Arbitron, and increased operating expenses related to our mobile device market initiatives and the litigation matter with Verance incurred in the first quarter of 2011.

***Non-cash items.***

The increase in non-cash items for the three-month period was primarily the result of an additional layer of stock-based awards and the tax benefits from stock-based awards.

***Operating assets and liabilities.***

The primary changes in the operating assets and liabilities for the three-month period related to:

collection of advanced billings, as provided in our contracts with customers; and

reimbursement from our landlord for the tenant improvement allowance.

The primary changes in the operating assets and liabilities for the prior year period relate to:

collection of advanced billings, as provided in our contracts with customers; and

a decrease in compensation related liabilities related to accrued bonuses at year-end in 2009 that were paid compared to none accrued in 2010.

***Cash flows from investing activities.***

The cash flows from investing activities for the three-month period and the same period in the prior year related to:

investments made in property and equipment, primarily in our information technology area for computer systems and related equipment used to operate our business;

investments made in the patent application and granting process;

investments made in joint ventures; and

net activity from investing our cash and cash equivalents and short- and long-term marketable securities.

***Cash flows from financing activities.***

The cash flows from financing activities for the three-month period related to the increase in purchases of common stock for the following:

purchase of common stock from a shareholder in a privately negotiated transaction;

purchases of common stock as part of our stock repurchase program; and

purchases of common stock for the withholding of shares upon the vesting of restricted stock to satisfy tax withholding obligations.

The cash flows from financing activities for the same period in the prior year were the result of purchases of common stock for the withholding of shares upon vesting of restricted stock to satisfy tax withholding obligations, partially offset by the exercise of stock options.

***Future Cash Expectations.***

As part of our stock repurchase program, of the \$5.0 million that was authorized, \$3.0 million remained available, as of March 31, 2011, to purchase our common stock in the open market or private transactions through April 30, 2012.

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In connection with the IV arrangement, we anticipate our cash flow will improve with:

- 1) payment of the license issue fee in increasing quarterly installments over three years,
- 2) consulting fees payable over five years, and
- 3) additional cost savings resulted from IV's assumption of the prosecution and maintenance costs related to the patents and patent applications that were licensed to IV that were previously borne by us.

We believe that our current cash, cash equivalents, and short-term marketable securities balances will satisfy our projected working capital and capital expenditure requirements for at least the next 12 months. Thereafter, we anticipate continuing to use cash, cash equivalents and marketable securities balances to satisfy our projected working capital and capital expenditure requirements.

We may use cash resources to fund acquisitions or investments in complementary businesses, technologies or product lines. In order to take advantage of opportunities, we may find it necessary to obtain additional equity financing, debt financing, or credit facilities. We do not believe at this time, however, that our long-term working capital and capital expenditures would require us to take steps to remedy any potential deficiencies. If it were necessary to obtain additional financing or credit facilities, we may not be able to do so, or if these funds are available, they may not be available on satisfactory terms.

**Contractual Obligations**

Pursuant to the terms of the joint venture agreements with Nielsen, we are obligated to contribute an aggregate of \$6.7 million to the joint ventures payable in quarterly installments from July 2009 through October 2011, of which \$2.1 million remained to be contributed as of March 31, 2011.

In May 2010 we entered into an amendment with the landlord of our corporate offices to extend the length of our facilities lease through August 2016 for rent payments totaling \$5.3 million.

Our obligations under non-cancelable operating leases for our facilities and various equipment leases totaled \$4.6 million as of March 31, 2011, and are payable in monthly installments through August 2016.

**Contractual Obligations**

	Total	Payment Due by Period			
		Less than 1 year	1-3 years	3-5 years	More than 5 years
Total joint venture obligations	\$ 2,100	\$ 2,100	\$	\$	\$
Total operating lease obligations	4,629	803	1,682	1,762	382
<b>Total obligations</b>	<b>\$ 6,729</b>	<b>\$ 2,903</b>	<b>\$ 1,682</b>	<b>\$ 1,762</b>	<b>\$ 382</b>

Other than as described above, as of March 31, 2011 there have been no material changes in the contractual obligations disclosed in our 2010 Annual Report.

**Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenue or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to our business.



**Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995**

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and Section 27A of the Securities Act of 1933. Words such as may, plan, should, could, expect, anticipate, intend, believe, forecast, estimate, continue, variations of such terms or similar expressions are intended to identify such forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements, or other statements made by us, are made based on our expectations and beliefs concerning future events impacting us, and are subject to uncertainties and factors (including those specified below), which are difficult to predict and, in many instances, are beyond our control. As a result, our actual results could differ materially from those expressed in or implied by any such forward-looking statements, and investors are cautioned not to place undue reliance on such statements. Forward-looking statements include but are not limited to statements relating to:

concentration of revenues with few customers comprising a large majority of the revenues;

trends and expectations in revenue growth;

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our future level of investment in our business and the joint ventures in which we have invested, including investment in research, development and engineering of products and technology, development of our intellectual property, the acquisition of new customers and development of new market opportunities;

our ability to improve margins;

anticipated expenses, costs, margins and investment activities in the foreseeable future;

anticipated revenue to be generated from current contracts and as a result of new programs;

variability of contracted arrangements;

our profitability in future periods;

business opportunities that could require that we seek additional financing;

the size and growth of our markets;

the existence of international growth opportunities and our future investment in such opportunities;

the source of our future revenue;

our expected short-term and long-term liquidity positions;

our ability to fund our working capital needs through cash flow from operations;

capital market conditions, including the recent economic crisis, interest rate volatility and other limitations on the availability of capital, which could have an impact on our cost of capital and our ability to access the capital markets;

our use of cash in upcoming quarters;

anticipated levels of backlog in future periods;

the success of our arrangements with Intellectual Ventures;

protection of our intellectual property portfolio; and

other risks detailed in our filings with the Securities and Exchange Commission, including the risk factors set forth in Part I, Item 1A of our 2010 Annual Report.

We believe that the risk factors contained in Part I, Item 1A of our 2010 Annual Report could affect our future performance and the liquidity and value of our securities and cause our actual results to differ materially from those expressed or implied by forward-looking statements made by us or on our behalf. Investors should understand that it is not possible to predict or identify all risk factors and that there may be other factors that may cause our actual results to differ materially from the forward-looking statements. All forward-looking statements made by us or by persons acting on our behalf apply only as of the date of this Quarterly Report on Form 10-Q. We do not undertake any obligation to publicly update or revise any forward-looking statements to reflect future events, information or circumstances that arise after the date of the filing of this Quarterly Report on Form 10-Q.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

The market risk disclosures as set forth in Part II, Item 7A of our 2010 Annual Report have not changed materially.

**Item 4. Controls and Procedures.**

**Evaluation of Disclosure Controls and Procedures**

We conducted an evaluation (pursuant to Rule 13a-15(b) of the Securities Exchange Act of 1934 (the Exchange Act)), under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officers, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e)) as of the end of the period covered by this Form 10-Q. These disclosure controls and procedures are designed to ensure that information required to be disclosed in our reports that are filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Our disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that this information is accumulated and communicated to management, including the principal executive and principal financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Based on the evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures were effective as of the end of the period covered by this Form 10-Q.

**Changes in Controls**

There was no change in our internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act of 1934) that occurred during the fiscal quarter ended March 31, 2011 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents****PART II. OTHER INFORMATION.****Item 1. Legal Proceedings.**

Verance Corporation, a Digimarc licensee, filed a declaratory judgment action against Digimarc in the United States District Court in Delaware on September 30, 2010, alleging the invalidity and non infringement of 22 patents held by Digimarc. Verance Corp. v. Digimarc Corp., 1:10-cv-00831-UNA. Digimarc responded by filing a motion to dismiss the action, the parties filed briefs on this issue, and a hearing was held on April 13, 2011.

On December 6, 2010, Digimarc filed suit against Verance Corporation in the District of Oregon. Digimarc is seeking payment for breach of contract by Verance related to Verance's failure to make payments under the licensing agreement between Digimarc and Verance. Digimarc Corp. v. Verance Corp., CV 10-1489 JE. Verance responded by filing a motion to dismiss or stay the action, and to compel arbitration. The parties filed briefs on the issue, and a hearing was held on April 27, 2011.

Digimarc has been named as one of several defendants in a complaint filed by Walker Digital, LLC, in the U.S. District Court for the District of Delaware on April 22, 2011, case number 11-cv-00363-UNA, alleging patent infringement. The plaintiff is seeking a declaratory judgment, injunctive relief and damages. Digimarc has not yet been served with the complaint.

**Item 1A. Risk Factors**

Detailed information about risk factors that may affect Digimarc's actual results are set forth in Part I, Item 1A of our 2010 Annual Report.

Our business, financial condition, results of operations and cash flows may be affected by a number of factors, including the factors set forth in our 2010 Annual Report. The risks and uncertainties described in our 2010 Annual Report are those risks of which we are aware and that we consider to be material to our business. If any of the risks and uncertainties develops into actual events, our business, financial condition, results of operations, or cash flows could be materially adversely affected. In that case, the trading price of our common stock could decline.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

In April 2009, the Board of Directors approved a stock repurchase program authorizing the purchase, at the discretion of management, of up to \$5.0 million in shares of our common stock through either periodic open-market or private transactions at then-prevailing market prices through April 30, 2010. In both April 2010 and April 2011, the Board of Directors approved an extension of the stock repurchase program for additional one year periods. We have paid \$2.0 million to repurchase 128,540 shares of outstanding common stock under this program since the program's inception and \$3.0 million remains available to repurchase common stock under the stock repurchase program.

In addition to the stock repurchase program described above, and the withholding (repurchase) of shares of common stock in connection with the vesting of restricted shares, described below, from time to time, we repurchase shares in connection with stock option exercises, to cover exercise price and taxes. No stock repurchases were made in connection with stock option exercises during the three-month period ended March 31, 2011.

The following table sets forth information regarding purchases of our equity securities during the three-month period ended March 31, 2011:

Period	(a) Total number of shares purchased	(b) Average price paid per share	(c) Total number of shares (or units) purchased as part of publicly announced plans or programs	(d) Maximum number (or approximate dollar value) of shares (or units) that may yet be purchased under the plans
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				<b>or programs</b>
<b>Month 1</b>				
January 1, 2011 to January 31, 2011	562,136 <sup>(1)(2)</sup>	\$ 27.07 <sup>(1)(2)</sup>		\$ 3.4 million
<b>Month 2</b>				
February 1, 2011 to February 28, 2011				\$ 3.4 million
<b>Month 3</b>				
March 1, 2011 to March 31, 2011	1,276 <sup>(1)</sup>	\$ 26.42 <sup>(1)</sup>	16,873	\$ 3.0 million
<b>Total</b>	<b>563,412</b>	<b>\$ 27.07</b>	<b>16,873</b>	

- (1) Includes fully vested shares of common stock withheld (purchased) by us in satisfaction of required withholding tax liability.
- (2) Includes 552,536 shares of our common stock purchased from Koninklijke Philips Electronics, N.V., in a privately negotiated transaction. The shares were purchased for an aggregate purchase price of approximately \$14.9 million, including transaction fees, from cash on hand and was made separate from the \$5.0 million stock repurchase program.

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**Item 6. Exhibits.**

<b>Exhibit Number</b>	<b>Exhibit Description</b>
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certification of Chief Executive Officer
32.2	Section 1350 Certification of Chief Financial Officer

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**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: April 29, 2011

DIGIMARC CORPORATION

By:

/s/ MICHAEL McCONNELL  
Michael McConnell

*Chief Financial Officer and Treasurer*

*(Duly Authorized Officer*

*and Principal Financial and Accounting Officer)*

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