

IMMERSION CORP
Form 10-Q
November 07, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended September 30, 2012

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 (I.R.S. Employer Identification No.)
30 Rio Robles, San Jose, California 95134 (Address of principal executive offices) (Zip Code)	
(408) 467-1900 (Registrant's telephone number, including area code)	

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller Reporting Company <input type="checkbox"/>

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

Number of shares of common stock outstanding at October 26, 2012: 27,273,391.

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Table of Contents**PART I****FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****IMMERSION CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share amounts)****(Unaudited)**

	September 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 13,889	\$ 7,298
Short-term investments	33,985	48,987
Accounts and other receivables (net of allowances for doubtful accounts as of: September 30, 2012 \$134 and December 31, 2011 \$21)	1,402	1,487
Inventories	359	423
Deferred income taxes	215	215
Prepaid expenses and other current assets	773	479
Total current assets	50,623	58,889
Property and equipment, net	1,426	1,737
Intangibles and other assets, net	15,447	14,053
Total assets	\$ 67,496	\$ 74,679
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 1,717	\$ 365
Accrued compensation	2,412	2,830
Other current liabilities	2,478	2,054
Deferred revenue and customer advances	4,651	4,120
Total current liabilities	11,258	9,369
Long-term deferred revenue	10,999	13,229
Deferred income tax liabilities	215	215
Other long-term liabilities	584	245
Total liabilities	23,056	23,058
Contingencies (Note 13)		
Stockholders' equity:		
Common stock and additional paid-in capital \$0.001 par value; 100,000,000 shares authorized; shares issued: September 30, 2012 32,256,135 and December 31, 2011 31,786,030; shares outstanding: September 30, 2012 27,359,441 and December 31, 2011 27,857,824	185,950	182,508
Accumulated other comprehensive income	107	118
Accumulated deficit	(111,521)	(106,157)
	(30,096)	(24,848)

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Treasury stock at cost: September 30, 2012 4,896,694 shares and December 31, 2011 3,928,206 shares

Total stockholders' equity		44,440		51,621
Total liabilities and stockholders' equity		\$ 67,496		\$ 74,679

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE LOSS

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Revenues:				
Royalty and license	\$ 6,371	\$ 5,875	\$ 21,386	\$ 20,110
Product sales	529	345	1,145	1,892
Development contracts and other	242	275	778	943
Total revenues	7,142	6,495	23,309	22,945
Costs and expenses:				
Cost of revenues (exclusive of amortization, impairment, and abandonment of intangibles shown separately below)	273	192	802	913
Sales and marketing	1,632	1,643	5,072	5,402
Research and development	2,088	2,183	6,406	6,525
General and administrative	5,750	3,195	14,882	9,367
Amortization, impairment, and abandonment of intangibles	337	324	1,071	1,016
Total costs and expenses	10,080	7,537	28,233	23,223
Operating loss	(2,938)	(1,042)	(4,924)	(278)
Interest and other income	66	58	144	172
Loss from continuing operations before provision for income taxes	(2,872)	(984)	(4,780)	(106)
Provision for income taxes	(118)	(428)	(737)	(1,289)
Loss from continuing operations	(2,990)	(1,412)	(5,517)	(1,395)
Discontinued operations (Note 10) :				
Gain on sales of discontinued operations net of provision for income taxes of \$0, \$0, \$97, and \$39	0	0	153	61
Net loss	\$ (2,990)	\$ (1,412)	\$ (5,364)	\$ (1,334)
Basic and diluted net loss per share				
Continuing operations	(0.11)	(0.05)	(0.20)	(0.05)
Discontinued operations	0.00	0.00	0.01	0.00
Total	\$ (0.11)	\$ (0.05)	\$ (0.19)	\$ (0.05)
Shares used in calculating basic and diluted net loss per share	27,658	28,918	27,885	28,595
Other Comprehensive Income (loss)				
Change in unrealized gains (losses) on short-term investments	6	(3)	(11)	19

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Total Other Comprehensive Income (loss)	6	(3)	(11)	19
Total Comprehensive loss	\$ (2,984)	\$ (1,415)	\$ (5,375)	\$ (1,315)

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents**IMMERSION CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands) (unaudited)**

	Nine Months Ended September 30,	
	2012	2011
Cash flows from operating activities:		
Net loss	\$ (5,364)	\$ (1,334)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization of property and equipment	490	717
Amortization, impairment, and abandonment of intangibles	1,071	1,016
Stock-based compensation	2,346	2,705
Allowance (recovery) for doubtful accounts	113	(25)
Loss on disposal of equipment	27	3
Gain on sales of discontinued operations	(153)	(61)
Changes in operating assets and liabilities:		
Accounts and other receivables	(28)	61
Inventories	64	(173)
Prepaid expenses and other current assets	(294)	3,117
Other assets	(45)	(89)
Accounts payable	1,214	32
Accrued compensation and other current liabilities	622	(1,282)
Deferred revenue and customer advances	(1,699)	(2,454)
Other long-term liabilities	339	(56)
Net cash provided by (used in) operating activities	(1,297)	2,177
Cash flows provided by (used in) investing activities:		
Purchases of available-for-sale investments	(29,956)	(44,910)
Proceeds from maturities of available-for-sale investments	45,000	45,000
Additions to intangibles	(2,323)	(2,406)
Purchases of property and equipment	(931)	(84)
Proceeds from sales of discontinued operations	250	100
Net cash provided by (used in) investing activities	12,040	(2,300)
Cash flows provided by (used in) financing activities:		
Issuance of common stock under employee stock purchase plan	122	145
Exercise of stock options	974	2,244
Purchase of treasury stock	(5,248)	0
Net cash provided by (used in) financing activities	(4,152)	2,389
Net increase in cash and cash equivalents	6,591	2,266
Cash and cash equivalents:		
Beginning of the period	7,298	12,243
End of the period	\$ 13,889	\$ 14,509
Supplemental disclosure of cash flow information:		
Cash paid (received) for taxes	\$ 21	\$ (3,302)

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Supplemental disclosure of non-cash operating, investing, and financing activities:

Amounts accrued for property and equipment, and intangibles	\$ 647	\$ 636
Issuance of shares from Employee Stock Purchase Plan and Release of Restricted Stock Units and Awards under company stock plan	\$ 1,298	\$ 1,305

See accompanying Notes to Condensed Consolidated Financial Statements.

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IMMERSION CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2012

(Unaudited)

1. SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Immersion Corporation (the Company) was incorporated in 1993 in California and reincorporated in Delaware in 1999 and develops, manufactures, licenses, and supports a wide range of hardware and software technologies and products that enhance digital devices with touch interaction.

Principles of Consolidation and Basis of Presentation

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

The accompanying condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all information and footnotes necessary for a complete presentation of the financial position, results of operations, and cash flows, in conformity with GAAP. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements included in the Company's Annual Report on Form 10-K, for the fiscal year ended December 31, 2011. In the opinion of management, all adjustments consisting of only normal and recurring items necessary for the fair presentation of the financial position and results of operations for the interim periods presented have been included.

The results of operations for the interim periods ended September 30, 2012 are not necessarily indicative of the results to be expected for the full year.

Revenue Recognition

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

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

Delivery has occurred. The Company delivers software and product to customers physically and also delivers software electronically. For physical deliveries not related to

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software, the transfer terms typically include transfer of title and risk of loss at the Company's shipping location. For electronic deliveries, delivery occurs when the Company provides the customer access codes or keys that allow the customer to take immediate possession of the software.

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

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

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

Development contracts and other revenue Development contracts and other revenue are comprised of professional services (consulting services and/or development contracts). Professional services revenues are recognized under the proportional performance accounting method based on physical completion of the work to be performed or completed performance method. A provision for losses on contracts is made, if necessary, in the period in which the loss becomes probable and can be reasonably estimated. Revisions in estimates are reflected in the period in which the conditions become known. To date, such losses have not been significant.

Multiple element arrangements The Company enters into multiple element arrangements in which customers purchase time-based licenses, which include a combination of software and/or intellectual property licenses, professional services and in limited cases, post contract customer support. For arrangements that are software based and include software and professional services, the services are generally not essential to the functionality of the software, and customers may purchase consulting services to facilitate the adoption of the Company's technology, but they may also decide to use their own resources or appoint other professional service organizations to perform these services. For these arrangements, including those with post contract customer support, revenue is recognized either over the period of the ongoing obligation which is generally consistent with the contractual term, or when all deliverables including services have been completed.

Also affecting revenue recognition for contracts that have multiple element arrangements are two Accounting Standards Updates (ASU). In September 2009, the Financial Accounting Standards Board (FASB) ratified ASU 2009-13 (update to ASC 605), Revenue Arrangements with Multiple Deliverables (ASU 2009-13 (update to ASC 605)). This guidance addresses criteria for separating the consideration in multiple-element arrangements. ASU 2009-13 (update to ASC 605) requires companies to allocate the overall consideration to each deliverable by using a best estimate of the selling price of

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individual deliverables in the arrangement in the absence of vendor-specific objective evidence or other third-party evidence of the selling price. ASU 2009-13 (update to ASC 605) was effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The Company adopted ASU 2009-13 (update to ASC 605) as of January 1, 2011, and its application has had no impact on the Company's condensed consolidated financial statements to date. In September 2009, the FASB ratified ASU 2009-14 (update to ASC 605), Certain Revenue Arrangements That Include Software Elements (ASU 2009-14 (update to ASC 605)). ASU 2009-14 (update to ASC 605) provides guidance to exclude (a) non-software components of tangible products and (b) software components of tangible products that are sold, licensed, or leased with tangible products when the software components and non-software components of the tangible product function together to deliver the tangible product's essential functionality. ASU 2009-14 (update to ASC 605) had an effective date that is consistent with ASU 2009-13 (update to ASC 605) above. The Company adopted ASU 2009-14 (update to ASC 605) as of January 1, 2011, and its application has had no impact on the Company's condensed consolidated financial statements to date.

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

Recent Accounting Pronouncements

In June 2011, the FASB ratified ASU 2011-05 Comprehensive Income (Topic 220): Presentation of Comprehensive Income. ASU 2011-05 requires that all nonowner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements, eliminating the option to present other comprehensive income in the statement of changes in equity. Under either choice, items that are reclassified from other comprehensive income to net income are required to be presented on the face of the financial statements where the components of net income and the components of other comprehensive income are presented. In December 2011 the FASB ratified ASU 2011-12 Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. ASU 2011-12 defers those changes in ASU 2011-05 that relate to the presentation of reclassification adjustments. These amendments are effective for reporting periods beginning after December 15, 2011, and have been applied retrospectively. These amendments have changed the manner in which the Company presents comprehensive income by reporting comprehensive income information in the condensed consolidated statements of operations and comprehensive loss.

2. FAIR VALUE MEASUREMENTS

Cash Equivalents and Short-term Investments

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

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

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

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

The types of instruments valued based on unobservable inputs which reflect the reporting entity's own assumptions or data that market participants would use in valuing an instrument are generally classified within Level 3 of the fair value hierarchy.

In May 2011, FASB issued ASU No. 2011-04, Fair Value Measurements (Topic 820). This ASU provides additional guidance on fair value disclosures. This guidance contains certain updates to the measurement guidance as well as enhanced disclosure requirements. The most significant change in disclosures is an expansion of the information required for Level 3 measurements including enhanced disclosure for: (1) the valuation processes used by the reporting entity; and (2) the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, if any. This guidance is effective for interim and annual periods beginning on or after December 15, 2011, with early adoption prohibited. The Company adopted the updated guidance which was effective for the Company on January 1, 2012. The adoption of this new guidance did not have a material impact on the Company's condensed consolidated financial statements.

Financial instruments measured at fair value on a recurring basis as of September 30, 2012 and December 31, 2011 are classified based on the valuation technique in the table below:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	September 30, 2012 Fair value measurements using		Total
		Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
(In thousands)				
Assets:				
U.S. Treasury securities	\$ 0	\$ 38,985	\$ 0	\$ 38,985
Money market accounts	4,628	0	0	4,628
Total assets at fair value	\$ 4,628	\$ 38,985	\$ 0	\$ 43,613

The above table excludes \$4.3 million of cash held in banks.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	December 31, 2011 Fair value measurements using		Total
		Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
(In thousands)				
Assets:				
U.S. Treasury securities	\$ 0	\$ 48,987	\$ 0	\$ 48,987
Money market accounts	3,617	0	0	3,617

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Total assets at fair value	\$ 3,617	\$ 48,987	\$ 0	\$ 52,604
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The above table excludes \$3.7 million of cash held in banks.

Short-term Investments

	Amortized Cost	September 30, 2012 Gross Unrealized Holding Gains (In thousands)	September 30, 2012 Gross Unrealized Holding Losses (In thousands)	Fair Value
U.S. Treasury securities	\$ 38,979	\$ 6	\$ 0	\$ 38,985
Total	\$ 38,979	\$ 6	\$ 0	\$ 38,985

	Amortized Cost	December 31, 2011 Gross Unrealized Holding Gains (In thousands)	December 31, 2011 Gross Unrealized Holding Losses (In thousands)	Fair Value
U.S. Treasury securities	\$ 48,970	\$ 17	\$ 0	\$ 48,987
Total	\$ 48,970	\$ 17	\$ 0	\$ 48,987

The contractual maturities of the Company's available-for-sale securities on September 30, 2012 and December 31, 2011 were all due within one year.

3. ACCOUNTS AND OTHER RECEIVABLES

	September 30, 2012	December 31, 2011
	(In thousands)	
Trade accounts receivable	\$ 903	\$ 525
Receivables from vendors, lessor, and other	499	962
Accounts and other receivables	\$ 1,402	\$ 1,487

4. INVENTORIES

	September 30, 2012	December 31, 2011
	(In thousands)	
Raw materials and subassemblies	\$ 218	\$ 167
Finished goods	141	256
Inventories	\$ 359	\$ 423

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5. PROPERTY AND EQUIPMENT

	September 30, 2012	December 31, 2011
	(In thousands)	
Computer equipment and purchased software	\$ 3,753	\$ 3,696
Machinery and equipment	654	882
Furniture and fixtures	546	533
Leasehold improvements	905	837
Total	5,858	5,948
Less accumulated depreciation	(4,432)	(4,211)
Property and equipment, net	\$ 1,426	\$ 1,737

6. INTANGIBLES AND OTHER ASSETS

	September 30, 2012	December 31, 2011
	(In thousands)	
Patents and trademarks	\$ 25,754	\$ 23,617
Other assets	196	204
Gross intangibles and other assets	25,950	23,821
Accumulated amortization of patents and trademarks	(10,503)	(9,768)
Intangibles and other assets, net	\$ 15,447	\$ 14,053

The Company amortizes its intangible assets related to patents and trademarks, over their estimated useful lives, generally 10 years from the date of issuance of the patents and trademarks. Amortization of intangibles excluding impairments or abandonments was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(In thousands)		(In thousands)	
Amortization of Intangibles - excluding impairments or abandonments	\$ 264	\$ 333	\$ 777	\$ 747

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The table below includes estimated remaining annual amortization expense for issued patents and trademarks as of September 30, 2012.

	Estimated Amortization Expense (In thousands)
Remainder of 2012	\$ 254
2013	1,024
2014	913
2015	839
2016	770
Thereafter	2,212
Total	\$ 6,012

Patents in process included in patents and trademarks were as follows:

	September 30, 2012	December 31, 2011
	(In thousands)	
Patents in process	\$ 9,239	\$ 8,448

Upon issuance, in process patents will be amortized over their estimated useful lives, generally 10 years.

7. COMPONENTS OF OTHER CURRENT LIABILITIES AND DEFERRED REVENUE AND CUSTOMER ADVANCES

	September 30, 2012	December 31, 2011
	(In thousands)	
Accrued legal	\$ 1,838	\$ 727
Income taxes payable	149	23
Other current liabilities	491	1,304
Total other current liabilities	\$ 2,478	\$ 2,054
Deferred revenue	\$ 4,635	\$ 4,046
Customer advances	16	74