

RAMBUS INC
Form 10-Q
October 25, 2013
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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, 2013

OR

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

For the transition period from _____ to _____

Commission File Number: 000-22339

RAMBUS INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

1050 Enterprise Way, Suite 700, Sunnyvale, CA 94089

(Address of principal executive offices) (zip code)

Registrant's telephone number, including area code: (408) 462-8000

94-3112828

(I.R.S. Employer
Identification No.)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

The number of shares outstanding of the registrant's Common Stock, par value \$.001 per share, was 112,706,137 as of September 30, 2013.

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NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (“Quarterly Report”) contains forward-looking statements. These forward-looking statements include, without limitation, predictions regarding the following aspects of our future:

- Success in the markets of our or our licensees’ products;
- Sources of competition;
- Research and development costs and improvements in technology;
- Sources, amounts and concentration of revenue, including royalties;
- Success in renewing license agreements;
- Technology product development;
- Outcome and effect of current and potential future intellectual property litigation and other significant litigation;
- Dispositions, acquisitions, mergers or strategic transactions and our related integration efforts;
- Impairment of goodwill and long-lived assets;
- Pricing policies of our licensees;
- Changes in our strategy and business model;
- Deterioration of financial health of commercial counterparties and their ability to meet their obligations to us;
- Engineering, marketing and general and administration expenses;
- Contract revenue;
- Operating results;
- International licenses and operations;
- Effects of changes in the economy and credit market on our industry and business;
- Ability to identify, attract, motivate and retain qualified personnel;
- Growth in our business;
- Methods, estimates and judgments in accounting policies;
- Adoption of new accounting pronouncements;
- Effective tax rates;
 - Realization of deferred tax assets/release of deferred tax valuation allowance;
- Trading price of our common stock;
- Internal control environment;
- Corporate governance;
- The level and terms of our outstanding debt;
- Resolution of the governmental agency matters involving us;
- Litigation expenses;
- Protection of intellectual property;
- Terms of our licenses and amounts owed under license agreements;
- Refinancing debt;

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Indemnification and technical support obligations;

Issuances of our securities, which could involve restrictive covenants or be dilutive to our existing stockholders; and

Likelihood of paying dividends or repurchasing securities.

You can identify these and other forward-looking statements by the use of words such as “may,” “future,” “shall,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “intends,” “potential,” “continue,” “projecting” or the negative terms, or other comparable terminology. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements.

Actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under Item 1A, “Risk Factors.” All forward-looking statements included in this document are based on our assessment of information available to us at this time. We assume no obligation to update any forward-looking statements.

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RAMBUS INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (Unaudited)

	September 30, 2013	December 31, 2012
	(In thousands, except shares and par value)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$307,961	\$148,984
Marketable securities	58,396	54,346
Accounts receivable	1,597	529
Prepays and other current assets	6,038	10,529
Deferred taxes	288	788
Total current assets	374,280	215,176
Intangible assets, net	132,448	153,173
Goodwill	116,899	124,969
Property, plant and equipment, net	72,772	86,905
Deferred taxes, long-term	4,806	4,458
Other assets	3,801	3,131
Total assets	\$705,006	\$587,812
LIABILITIES & STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$5,967	\$7,918
Accrued salaries and benefits	30,336	23,992
Accrued litigation expenses	1,020	9,822
Convertible notes, short-term	159,731	—
Other accrued liabilities	7,293	12,402
Total current liabilities	204,347	54,134
Convertible notes, long-term	108,316	147,556
Long-term imputed financing obligation	39,685	45,919
Long-term income taxes payable	6,497	6,533
Other long-term liabilities	3,039	12,076
Total liabilities	361,884	266,218
Commitments and contingencies (Notes 10 and 15)		
Stockholders' equity:		
Convertible preferred stock, \$.001 par value:		
Authorized: 5,000,000 shares		
Issued and outstanding: no shares at September 30, 2013 and December 31, 2012	—	—
Common stock, \$.001 par value:		
Authorized: 500,000,000 shares		
Issued and outstanding: 112,706,137 shares at September 30, 2013 and 111,525,021 shares at December 31, 2012	113	112
Additional paid-in capital	1,121,259	1,075,761
Accumulated deficit	(777,950	) (753,979
Accumulated other comprehensive loss	(300	) (300
Total stockholders' equity	343,122	321,594
Total liabilities and stockholders' equity	\$705,006	\$587,812

See Notes to Unaudited Condensed Consolidated Financial Statements

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RAMBUS INC.
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,		
	2013	2012	2013	2012	
	(In thousands, except per share amounts)				
Revenue:					
Royalties	\$71,013	\$57,361	\$194,244	\$175,127	
Contract and other revenue	2,281	169	3,835	1,481	
Total revenue	73,294	57,530	198,079	176,608	
Operating costs and expenses:					
Cost of revenue*	8,958	7,529	22,857	22,032	
Research and development*	27,553	30,674	91,178	107,415	
Marketing, general and administrative*	18,698	24,255	57,937	91,283	
Gain from sale of intellectual property	—	—	(1,388) —	
Costs of restatement and related legal activities	—	79	19	192	
Restructuring charges	1,129	6,622	3,335	6,622	
Impairment of goodwill and long-lived assets	8,070	35,471	8,070	35,471	
Gain from settlement	(179	) —	(179) —	
Total operating costs and expenses	64,229	104,630	181,829	263,015	
Operating income (loss)	9,065	(47,100) 16,250	(86,407)
Interest income and other income (expense), net	66	(12	) (1,373	) 175
Interest expense	(8,552) (7,121) (23,290) (20,420)
Interest and other income (expense), net	(8,486) (7,133) (24,663) (20,245)
Income (loss) before income taxes	579	(54,233) (8,413) (106,652)
Provision for income taxes	6,304	3,865	15,558	11,552	
Net loss	\$(5,725) \$(58,098) \$(23,971) \$(118,204)
Net loss per share:					
Basic	\$(0.05) \$(0.52) \$(0.21) \$(1.07)
Diluted	\$(0.05) \$(0.52) \$(0.21) \$(1.07)
Weighted average shares used in per share calculation:					
Basic	112,640	110,826	112,144	110,580	
Diluted	112,640	110,826	112,144	110,580	

* Includes stock-based compensation:

Cost of revenue	\$7	\$5	\$12	\$20
Research and development	\$1,630	\$2,221	\$5,166	\$7,572
Marketing, general and administrative	\$1,726	\$2,863	\$6,707	\$10,438

See Notes to Unaudited Condensed Consolidated Financial Statements

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RAMBUS INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Unaudited)

(In thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net loss	\$ (5,725	) \$ (58,098	) \$ (23,971	) \$ (118,204)
Other comprehensive income (loss):				
Unrealized gain (loss) on marketable securities, net of tax	(4	) 8	—	80
Total comprehensive loss	\$ (5,729) \$ (58,090) \$ (23,971) \$ (118,124)
See Notes to Unaudited Condensed Consolidated Financial Statements				

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RAMBUS INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
	2013	2012
	(In thousands)	
Cash flows from operating activities:		
Net loss	\$(23,971	) \$(118,204)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Stock-based compensation	11,885	18,030
Depreciation	11,566	9,583
Amortization of intangible assets	21,420	23,535
Non-cash interest expense and amortization of convertible debt issuance costs	13,369	10,856
Impairment of investment in non-marketable equity security	1,400	
Impairment of goodwill and long-lived assets	8,070	35,471
Deferred tax benefit	605	(39)
Non-cash restructuring	653	—
Gain from sale of intellectual property	(1,388) —
Change in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	(1,068	) 574
Prepaid expenses and other assets	5,898	6,744
Accounts payable	(399	) (9,171)
Accrued salaries and benefits and other accrued liabilities	(8,787	) 3,968
Accrued litigation expenses	(8,802	) (467)
Income taxes payable	380	(665)
Net cash provided by (used in) operating activities	30,831	(19,785)
Cash flows from investing activities:		
Purchases of property, plant and equipment	(5,942	) (15,802)
Acquisition of intangible assets	(2,500	) (1,700)
Purchases of marketable securities	(101,596	) (77,562)
Maturities of marketable securities	97,300	149,486
Proceeds from sale of intellectual property	2,250	—
Acquisition of businesses, net of cash acquired	—	(46,278)
Net cash provided by (used in) investing activities	(10,488	) 8,144
Cash flows from financing activities:		
Proceeds from issuance of convertible senior notes	138,000	—
Issuance costs related to the issuance of convertible senior notes	(3,603) —
Proceeds received from issuance of common stock under employee stock plans	4,610	1,728
Principal payments against lease financing obligation	(119	) (17)
Payments under installment payment arrangement	(84	) (149)
Net cash provided by financing activities	138,804	1,562
Effect of exchange rate changes on cash and cash equivalents	(170	) 41
Net increase (decrease) in cash and cash equivalents	158,977	(10,038)
Cash and cash equivalents at beginning of period	148,984	162,244
Cash and cash equivalents at end of period	\$307,961	\$152,206
Non-cash investing and financing activities during the period:		

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Property, plant and equipment received and accrued in accounts payable and other accrued liabilities	\$252	\$2,686
Non-cash obligation for property, plant and equipment	\$—	\$2,008
See Notes to Unaudited Condensed Consolidated Financial Statements		

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RAMBUS INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Rambus Inc. ("Rambus" or the "Company") and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in the accompanying unaudited condensed consolidated financial statements. Investments in entities with less than 20% ownership or in which the Company does not have the ability to significantly influence the operations of the investee are being accounted for using the cost method and are included in other assets.

In the opinion of management, the unaudited condensed consolidated financial statements include all adjustments (consisting only of normal recurring items) necessary to state fairly the financial position and results of operations for each interim period presented. Interim results are not necessarily indicative of results for a full year.

The unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (the "SEC") applicable to interim financial information. Certain information and Note disclosures included in the financial statements prepared in accordance with generally accepted accounting principles have been omitted in these interim statements pursuant to such SEC rules and regulations. The information included in this Form 10-Q should be read in conjunction with the consolidated financial statements and notes thereto in Form 10-K for the year ended December 31, 2012.

Operating Segment Definitions

Operating segments are based upon Rambus' internal organization structure, the manner in which its operations are managed, the criteria used by its Chief Operating Decision Maker ("CODM") to evaluate segment performance and availability of separate financial information regularly reviewed for resource allocation and performance assessment.

The Company determined its CODM to be the Chief Executive Officer and determined its operating segments to be:

(1) Memory and Interfaces Division ("MID"), which focuses on the design, development and licensing of technology that is related to memory and interfaces; (2) Cryptography Research, Inc. ("CRI"), which focuses on the design, development and licensing of technologies for chip and system security and anti-counterfeiting; (3) Lighting and Display Technologies ("LDT"), which focuses on the design, development and licensing of technologies for lighting; and (4) CTO, which is a centralized engineering, research and development and business incubation organization that consolidates early-stage investments, longer-term research activities and worldwide engineering.

For the three and nine months ended September 30, 2013 and 2012, only MID and CTO were reportable segments as each of them met the quantitative thresholds for disclosure as a reportable segment. The results of the remaining other operating segments were combined and shown under "All Other."

Reclassifications

Certain prior periods' amounts were reclassified to conform to the current year's presentation. None of these reclassifications had an impact on reported net loss for any of the periods presented.

2. Summary of Significant Accounting Policies

Revenue Recognition

Overview

Rambus recognizes revenue when persuasive evidence of an arrangement exists, Rambus has delivered the product or performed the service, the fee is fixed or determinable and collection is reasonably assured. If any of these criteria are not met, Rambus defers recognizing the revenue until such time as all criteria are met. Determination of whether or not these criteria have been met may require the Company to make judgments, assumptions and estimates based upon current information and historical experience.

Certain revenue contracts consist of service fees associated with integration of Rambus' solutions into its customers' products and fees associated with providing training, evaluation and test equipment to its customers. Under the accounting guidance, if the deliverables have standalone value upon delivery, Rambus accounts for each deliverable separately. When

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multiple deliverables included in an arrangement are separated into different units of accounting, the arrangement consideration is allocated to the identified separate units based on a relative selling price hierarchy. Rambus determines the relative selling price for a deliverable based on its best estimate of selling price (“BESP”). Rambus has determined that vendor-specific objective evidence of selling price for each deliverable is not available as there lacks a consistent number of standalone sales and third-party evidence is not a practical alternative due to differences in its service offerings compared to other parties and the availability of relevant third-party pricing information. Rambus determined BESP by considering its overall pricing objectives and market conditions. Significant pricing practices taken into consideration include discounting practices, the size and volume of transactions, the customer demographic, the geographic area where services are sold, price lists, go-to-market strategy, historical standalone sales and contract prices. The determination of BESP is made through consultation with and approval by management, taking into consideration the go-to-market strategy. As the go-to-market strategies evolve, Rambus may modify its pricing practices in the future, which could result in changes in relative selling prices. In most cases, the relative values of the undelivered components are not material to the overall arrangement and are typically delivered within twelve months after the core product has been delivered. In such agreements, selling price is determined for each component and any difference between the total of the separate BESP and total contract consideration (i.e. discount) is allocated pro-rata across each of the components in the arrangement.

Rambus’ revenue consists of royalty revenue and contract and other revenue derived from MID, CRI and LDT operating segments. Royalty revenue consists of patent license and solutions license royalties. Contract and other revenue consists of fixed license fees, fixed engineering fees and service fees associated with integration of Rambus’ technology solutions into its customers’ products as well as sale of LED edge-lit products.

Royalty Revenue

Rambus recognizes royalty revenue upon notification by its customers and when deemed collectible. The terms of the royalty agreements generally either require customers to give Rambus notification and to pay the royalties within 60 days of the end of the quarter during which the sales occur or are based on a fixed royalty that is due within 45 days of the end of the quarter. Many of Rambus’ customers have the right to cancel their licenses. In such arrangements, revenue is only recognized to the extent that is consistent with the cancellation provisions. Cancellation provisions within such contracts generally provide for a prospective cancellation with no refund of fees already remitted by customers for products provided and payment for services rendered prior to the date of cancellation. Rambus has two types of royalty revenue: (1) patent license royalties and (2) solutions license royalties.

Patent licenses - Rambus licenses its broad portfolio of patented inventions to companies who use these inventions in the development and manufacture of their own products. Such licensing agreements may cover the license of part, or all, of Rambus’ patent portfolio. The contractual terms of the agreements generally provide for payments over an extended period of time. For the licensing agreements with fixed royalty payments, Rambus generally recognizes revenue from these arrangements as amounts become due. For the licensing agreements with variable royalty payments which can be based on either a percentage of sales or number of units sold, Rambus earns royalties at the time that the customers’ sales occur. Rambus’ customers, however, do not report and pay royalties owed for sales in any given quarter until after the conclusion of that quarter. As Rambus is unable to estimate the customers’ sales in any given quarter to determine the royalties due to Rambus, it recognizes royalty revenues based on royalties reported by customers during the quarter and when other revenue recognition criteria are met.

In addition, Rambus may enter into certain settlements of patent infringement disputes. The amount of consideration received upon any settlement (including but not limited to past royalty payments, future royalty payments and punitive damages) is allocated to each element of the settlement based on the fair value of each element. In addition, revenues related to past royalties are recognized upon execution of the agreement by both parties, provided that the amounts are fixed or determinable, there are no significant undelivered obligations and collectability is reasonably assured.

Rambus does not recognize any revenues prior to execution of the agreement since there is no reliable basis on which it can estimate the amounts for royalties related to previous periods or assess collectability. Elements that are related to royalty revenue in nature (including but not limited to past royalty payments and future royalty payments) will be recorded as royalty revenue in the consolidated statements of operations. Elements that are not related to royalty revenue in nature (including but not limited to punitive damage and settlement) will be recorded as gain from

settlement which is reflected as a separate line item within the operating expenses section in the consolidated statements of operations.

Solutions licenses - Rambus develops proprietary and industry-standard products that it provides to its customers under solutions license agreements. These arrangements include royalties, which can be based on either a percentage of sales or number of units sold. Rambus earns royalties on such licensed products sold worldwide by its customers at the time that the customers' sales occur. Rambus' customers, however, do not report and pay royalties owed for sales in any given quarter until after the conclusion of that quarter. As Rambus is unable to estimate the customers' sales in any given quarter to determine the

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royalties due to Rambus, it recognizes royalty revenues based on royalties reported by customers during the quarter and when other revenue recognition criteria are met.

Contract and Other Revenue

Rambus generally recognizes revenue using percentage of completion for development contracts related to licenses of its solutions that involve significant engineering and integration services. For agreements accounted for using the percentage-of-completion method, Rambus determines progress to completion using input measures based upon contract costs incurred. Part of these contract fees may be due upon the achievement of certain milestones, such as provision of certain deliverables by Rambus or production of chips by the customer. The remaining fees may be due on pre-determined dates and include significant up-front fees.

A provision for estimated losses on fixed price contracts is made, if necessary, in the period in which the loss becomes probable and can be reasonably estimated. If the Company determines that it is necessary to revise the estimates of the total costs required to complete a contract, the total amount of revenue recognized over the life of the contract would not be affected. However, to the extent the new assumptions regarding the total efforts necessary to complete a project are less than the original assumptions, the contract fees would be recognized sooner than originally expected.

Conversely, if the newly estimated total efforts necessary to complete a project are longer than the original assumptions, the contract fees will be recognized over a longer period.

Rambus recognizes revenue from the sale of LED edge-lit products when risk of loss and title have transferred to customers, provided all other revenue recognition criteria have been met. Revenue from distributors is recognized on the shipment or delivery of the related products, provided all other revenue recognition criteria have been met. The Company's agreements with these distributors have terms which are generally consistent with the standard terms and conditions for the sale of the Company's products to end users, and do not provide for product rotation or pricing allowances. The Company accrues for warranty based on the standard market experience.

3. Recent Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2013-11 "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists." ASU No. 2013-11 is a new accounting standard on the financial statement presentation of unrecognized tax benefits. The new accounting standards update provides that a liability related to an unrecognized tax benefit would be presented as a reduction of a deferred tax asset for a net operating loss carryforward, a similar tax loss or a tax credit carryforward if such settlement is required or expected in the event the uncertain tax position is disallowed. The new standard becomes effective for the Company on January 1, 2014 and it should be applied prospectively to unrecognized tax benefits that exist at the effective date with retrospective application permitted. The Company is currently assessing the impact of this new standard.

In February 2013, the FASB issued ASU No. 2013-02 "Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." ASU No. 2013-02 requires an entity to disaggregate the total change of each component of other comprehensive income either on the face of the income statement or as a separate disclosure in the notes. The new guidance became effective for the Company's interim period ended March 31, 2013. The Company adopted this guidance and the adoption did not have any impact on its financial position, results of operations or cash flows as the amounts reclassified out of accumulated other comprehensive loss were not material.

4. Earnings (Loss) Per Share

Basic earnings (loss) per share is calculated by dividing the net income (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings (loss) per share is calculated by dividing the earnings (loss) by the weighted average number of common shares and potentially dilutive securities outstanding during the period. Potentially dilutive common shares consist of incremental common shares issuable upon exercise of stock options, employee stock purchases, restricted stock and restricted stock units and shares issuable upon the conversion of convertible notes. The dilutive effect of outstanding shares is reflected in diluted earnings per share by application of the treasury stock method. This method includes consideration of the amounts to be paid by the employees, the amount of excess tax benefits that would be recognized in equity if the instrument was exercised and the amount of

unrecognized stock-based compensation related to future services. No potential dilutive common shares are included in the computation of any diluted per share amount when a net loss is reported.

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The following table sets forth the computation of basic and diluted net loss per share:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Basic and diluted net loss per share:	(In thousands, except per share amounts)			
Numerator:				
Net Loss	\$(5,725)	\$(58,098)	\$(23,971)	\$(118,204)
Denominator:				
Weighted-average shares outstanding	112,640	110,826	112,144	110,580
Basic and diluted net loss per share	\$(0.05)	\$(0.52)	\$(0.21)	\$(1.07)

For the three months ended September 30, 2013 and 2012, options to purchase approximately 5.9 million and 13.4 million shares, respectively, and for the nine months ended September 30, 2013 and 2012, options to purchase approximately 10.2 million and 13.3 million shares, respectively, were excluded from the calculation because they were anti-dilutive after considering proceeds from exercise, taxes and related unrecognized stock-based compensation expense. For the three months ended September 30, 2013 and 2012, an additional 3.4 million and 6.9 million potentially dilutive shares, respectively, and for the nine months ended September 30, 2013 and 2012, an additional 3.7 million and 7.0 million potentially dilutive shares, respectively, have been excluded from the weighted average dilutive shares because there were net losses for the periods.

5. Intangible Assets and Goodwill

Goodwill

During the third quarter of 2013, the Company curtailed its immersive media platform spending and redirected some of its resources to other strategic programs. Under generally accepted accounting principles, when indicators of potential impairment are identified, companies are required to conduct a review of the carrying amounts of goodwill and other long-lived assets to determine if impairment exists. The Company conducted this impairment review as a result of the change of its strategy related to the immersive media platform. As a result of this impairment review, the Company recorded \$8.1 million of impairment of goodwill related to the Mobile Technology Division (“MTD”) reporting unit which is part of the CTO reportable segment. This impairment was reflected in impairment of goodwill and long-lived assets in the condensed consolidated statements of operations. The Company estimated the fair value of MTD reporting unit using the income approach which was determined using Level 3 fair value inputs. The utilization of the income approach to determine fair value requires estimates of future operating results and cash flows discounted using an estimated discount rate. Cash flow projections are based on management's estimates of revenue growth rates and operating margins, taking into consideration industry and market conditions. The discount rate used is based on a weighted average cost of capital adjusted for the relevant risk associated with the characteristics of the business and the projected cash flows. Certain estimates used in the income approach involve information from a business with developing revenue models and limited financial history, which increase the risk of differences between the projected and actual performance.

The following table presents goodwill balances and adjustments to those balances for each of the reportable segments for the nine months ended September 30, 2013:

Reportable Segment:	December 31, 2012	Additions to Goodwill	Impairment Charge of Goodwill	September 30, 2013
	(In thousands)			
MID	\$19,905	\$—	\$—	\$19,905
CTO	8,070	—	(8,070)	—
All Other	96,994	—	—	96,994
Total	\$124,969	\$—	\$(8,070)	\$116,899

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Reportable Segment:	As of September 30, 2013		
	Gross Carrying Amount	Accumulated Impairment Losses	Net Carrying Amount
	(In thousands)		
MID	\$19,905	\$—	\$19,905
CTO	8,070	(8,070)) —
All Other	110,694	(13,700)	) 96,994
Total	\$138,669	\$(21,770)	) \$116,899

Intangible Assets

The components of the Company's intangible assets as of September 30, 2013 and December 31, 2012 were as follows:

	Useful Life	As of September 30, 2013		
		Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
		(In thousands)		
Existing technology	3 to 10 years	\$195,345	\$(77,105)	) \$118,240
Customer contracts and contractual relationships	1 to 10 years	32,650	(18,509)	) 14,141
Non-compete agreements	3 years	300	(233)	) 67
Total intangible assets		\$228,295	\$(95,847)	) \$132,448
	Useful Life	As of December 31, 2012		
		Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
		(In thousands)		
Existing technology	3 to 10 years	\$191,815	\$(57,240)	) \$134,575
Customer contracts and contractual relationships	1 to 10 years	32,650	(14,194)	) 18,456
Non-compete agreements	3 years	300	(158)	) 142
Total intangible assets		\$224,765	\$(71,592)	) \$153,173

During the three months ended September 30, 2013, the Company did not purchase any intangible assets. The Company also reclassified certain intangible assets with a gross carrying amount of \$2.0 million to assets-held-for-use. These assets were previously classified as assets-held-for-sale within prepaids and other current assets in the condensed consolidated balance sheet. During the nine months ended September 30, 2013, the Company purchased intellectual property of \$2.5 million, which was recorded as intangible assets on the condensed consolidated balance sheets. During the three months ended September 30, 2013, the Company did not sell any intangible assets. During the nine months ended September 30, 2013, the Company sold portfolios of its intellectual property covering lighting technologies for \$2.3 million and the related gain was recorded as gain from sale of intellectual property in the condensed consolidated statements of operations.

During the nine months ended September 30, 2012, the Company entered into various business combinations and technology asset acquisitions. These transactions had a total purchase price of \$48.2 million. These transactions were completed to acquire patents and technology to expand the Company's existing technology for its MID and MTD groups.

The favorable contracts (included in customer contracts and contractual relationships) are acquired patent licensing agreements where the Company has no performance obligations. Cash received from these acquired favorable contracts reduces the favorable contract intangible asset. For the three months ended September 30, 2013 and 2012, the Company received \$0.9 million and \$1.1 million related to the favorable contracts, respectively. For the nine months ended September 30, 2013 and 2012, the Company received \$2.2 million and \$4.7 million related to the favorable contracts, respectively. As of September 30, 2013 and December 31, 2012, the net balance of the favorable

contract intangible assets was \$2.6 million and \$4.8 million, respectively.

Amortization expense for intangible assets for the three and nine months ended September 30, 2013 was \$7.4 million and \$21.4 million, respectively. Amortization expense for intangible assets for the three and nine months ended September 30, 2012 was \$8.0 million and \$23.5 million, respectively.

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The estimated future amortization expense of intangible assets as of September 30, 2013 was as follows (amounts in thousands):

Years Ending December 31:	Amount
2013 (remaining 3 months)	\$9,352
2014	28,266
2015	27,115
2016	26,081
2017	24,625
Thereafter	17,009
	\$ 132,448

It is reasonably possible that the businesses could perform significantly below the Company's expectations or a deterioration of market and economic conditions could occur. This would adversely impact the Company's ability to meet its projected results, which could cause the goodwill in any of its reporting units or long-lived assets in any of its asset groups to become impaired. Significant differences between these estimates and actual cash flows could materially affect the Company's future financial results. If the LDT reporting unit is not successful in commercializing new business arrangements, or if the Company is unsuccessful in signing new license agreements or renewing its existing license agreements for the MID and CRI reporting units, the revenue and income for these reporting units could adversely and materially deviate from their historical trends and could cause goodwill or long-lived assets to become impaired. If the Company determines that its goodwill or long-lived assets are impaired, the Company would be required to record a non-cash charge that could have a material adverse effect on its results of operations and financial position.

6. Segments and Major Customers

For the three and nine months ended September 30, 2013 and 2012, MID and CTO were reportable segments as each of them met the quantitative thresholds for disclosure as a reportable segment. The results of the remaining other operating segments were combined and shown under "All Other."

The Company evaluates the performance of its segments based on segment operating income (loss), which is defined as customer licensing income ("CLI") minus segment operating expenses. Segment operating expenses are comprised of direct operating expenses and the allocation of certain engineering expenses.

CLI is defined as total cash royalties received from its customers under its licensing agreements with them and any product sales. Beginning in the third quarter of 2013, the Company bifurcated royalty payments that it received from SK hynix between revenue and gain from settlement, which was reflected as a credit to operating expenses. The Company has combined revenue from its customers, including SK hynix, and the gain from the SK hynix settlement as customer licensing income to reflect the total amounts received from all of its customers for the periods presented. In addition, customer licensing income includes other patent royalties received but not recognizable as revenue and proceeds from sale of intellectual property. In certain periods presented, certain patent royalties received from a customer were not recognized as revenue as not all revenue recognition criteria were met. Additionally, since the third quarter of 2011, the Company has received patent royalty payments from certain patent license agreements assumed in the acquisition of CRI which were treated as favorable contracts. Cash received from these acquired favorable contracts reduced the favorable contract intangible asset on the Company's balance sheet. The Company has combined these cash royalty payments as CLI to reflect the total amounts received from its customers.

Segment operating expenses do not include marketing, general and administrative expenses and the allocation of certain expenses managed at the corporate level, such as stock-based compensation, amortization, and certain bonus and acquisition costs. The "Reconciling Items" category includes these unallocated marketing, general and administrative expenses as well as corporate level expenses. The presentation of the three and nine months ended September 30, 2012 segment data has been updated to conform with the 2013 segment operating income (loss) definition applied starting in the fourth quarter of 2012.

The tables below present reported segment operating income (loss) for the three and nine months ended September 30, 2013 and 2012, respectively.

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	For the Three Months Ended September 30, 2013				For the Nine Months Ended September 30, 2013			
	MID (In thousands)	CTO	All Other	Total	MID (In thousands)	CTO	All Other	Total
Revenues	\$66,103	\$—	\$7,191	\$73,294	\$175,233	\$—	\$22,846	\$198,079
Other patent royalties received	179	—	850	1,029	5,179	—	4,479	9,658
Customer licensing income	\$66,282	\$—	\$8,041	\$74,323	\$180,412	\$—	\$27,325	\$207,737
Segment operating expenses	7,730	6,530	11,475	25,735	26,001	21,462	33,765	81,228
Segment operating income (loss)	\$58,552	\$(6,530)	\$(3,434)	\$48,588	\$154,411	\$(21,462)	\$(6,440)	\$126,509
Reconciling items				(39,523)				(110,259)
Operating income				\$9,065				\$16,250
Interest and other income (expense), net				(8,486)				(24,663)
Income (loss) before income taxes				\$579				\$(8,413)

	For the Three Months Ended September 30, 2012				For the Nine Months Ended September 30, 2012			
	MID (In thousands)	CTO	All Other	Total	MID (In thousands)	CTO	All Other	Total
Revenues	\$54,044	\$—	\$3,486	\$57,530	\$163,269	\$—	\$13,339	\$176,608
Other patent royalties received	3,750	—	1,125	4,875	3,750	—	4,740	8,490
Customer licensing income	\$57,794	\$—	\$4,611	\$62,405				