

Digimarc CORP  
Form 10-K/A  
August 06, 2010  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K/A**  
**(Amendment No. 1)**

(Mark One)

**Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the fiscal year ended December 31, 2009

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 001-34108

**DIGIMARC CORPORATION**

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(Exact name of registrant as specified in its charter)

**Oregon**  
(State or other jurisdiction of  
incorporation or organization)

**26-2828185**  
(I.R.S. Employer  
Identification No.)

**9405 SW Gemini Drive, Beaverton, Oregon 97008**  
(Address of principal executive offices) (Zip Code)

**(503) 469-4800**  
(Registrant's telephone number, including area code)

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

<b>Title of Each Class</b>	<b>Name of Each Exchange on Which Registered</b>
<b>Common Stock, \$0.001 Par Value Per Share</b>	<b>The NASDAQ Stock Market LLC</b>

**Securities registered pursuant to Section 12(g) of the Act: NONE**

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

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

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

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

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

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

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Large accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Accelerated filer

Smaller reporting company

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

The aggregate market value of common stock, par value \$0.001 per share, held by non-affiliates of the registrant, based on the closing price for the common stock on The Nasdaq Global Market on the last business day of the registrant's most recently completed fiscal second quarter (June 30, 2009), was approximately \$89 million. Shares of common stock beneficially held by each officer and director have been excluded from this computation because these persons may be deemed to be affiliates.

This determination of affiliate status is not necessarily a conclusive determination for any other purposes.

As of February 17, 2010, 7,303,634 shares of the registrant's common stock were outstanding.

## DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's proxy statement pursuant to Regulation 14A for its 2010 annual meeting of stockholders are incorporated by reference into Items 10, 11, 12, 13 and 14 of Part III of this Annual Report on Form 10-K.

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**PART I**

*Unless the context otherwise requires, references in this Annual Report on Form 10-K to (i) Digimarc, we, our and us refer to Digimarc Corporation and (ii) Old Digimarc refers to the former Digimarc Corporation, which merged with and into a wholly owned subsidiary of L-1 Identity Solutions, Inc. ( L-1 ) on August 13, 2008, and its consolidated subsidiaries (other than us).*

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

*This Annual Report on Form 10-K includes trademarks and registered trademarks of Digimarc Corporation.*

**ITEM 1: BUSINESS**

*The following discussion of Digimarc's business contains forward-looking statements relating to future events or the future financial performance of Digimarc. 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 Annual Report on Form 10-K in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, under the caption Forward-Looking Statements.*

*The following discussion of our business should be read in conjunction with our consolidated financial statements and the related notes and other financial information appearing elsewhere in this Annual Report on Form 10-K.*

**The Separation of the Digital Watermarking Business from Old Digimarc**

On August 1, 2008, Old Digimarc spun off its wholly owned subsidiary, DMRC LLC, which held all of the assets and liabilities of Old Digimarc's Digital Watermarking Business.

Until August 1, 2008, we were a wholly owned subsidiary of DMRC LLC, which immediately prior to the spin-off was a wholly owned subsidiary of Old Digimarc. DMRC LLC was formed in Delaware on June 18, 2008, in anticipation of the spin-off of the Digital Watermarking Business. Prior to the spin-off, in a transaction which we refer to as the restructuring, Old Digimarc contributed all of the assets and liabilities related to its Digital Watermarking Business, together with all of Old Digimarc's cash, including cash received upon the exercise of stock options, to DMRC LLC. The restructuring did not result in the loss of any significant Digital Watermarking Business customers or contracts.

Following the restructuring, all of the limited liability company interests of DMRC LLC were transferred to a newly created trust for the benefit of Old Digimarc record holders on the basis of one limited liability company interest of DMRC LLC for every three and one-half shares of Old Digimarc common stock held by the stockholder as of the spin-off record date and time. DMRC LLC then merged with and into DMRC Corporation, and each limited liability company interest of DMRC LLC was converted into one share of common stock of DMRC Corporation. After completion of the acquisition of Old Digimarc by L-1, DMRC Corporation changed its name to Digimarc Corporation. As a result, upon effectiveness of the Form 10 on October 16, 2008, each Old Digimarc record holder received one share of Digimarc common stock for every three and one-half shares of Old Digimarc common stock held by the stockholder as of the spin-off record date and time, and we became an independent, publicly-traded company owning and operating the Digital Watermarking Business.

**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 embed persistent digital information, perceptible only to computers and digital devices, into all

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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 technology, and those of our licensees, span the range of media content, enabling our customers and those of our partners to:

Quickly identify and effectively manage music, movies, radio and 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;

Deliver new rich media experiences on mobile devices by connecting printed materials, such as newspapers and magazines, to the web and more;

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 authenticate 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 digital signals 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 packages. The digital signals 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.

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 trade secret laws, and nondisclosure agreements and other contracts. We believe we have one of the world's most extensive patent portfolios in the field of digital watermarking and related media enhancement innovations, with over 560 U.S. and foreign patents and more than 420 U.S. and foreign patent applications on file as of December 31, 2009.

Financial information about geographic areas is included in Note 4 of our financial statements.

## **History**

We were formed in Delaware on June 18, 2008 by Old Digimarc to hold and operate Old Digimarc's Digital Watermarking Business and to facilitate the separation of its Secure ID Business through the spin-off and the merger of Old Digimarc with L-1. Old Digimarc was founded to commercialize a signal processing innovation known as digital watermarking. Digital watermarking is a technology that allows our customers to embed digital data into any media content that is digitally processed at some point during its lifecycle. The technology



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can be applied to printed materials, video, audio, and images. The inclusion of these digital signals enables a wide range of improvements in security and media management, and new business models for distribution and consumption of media content. Over the years our technology and intellectual property portfolios have grown to encompass many related technologies.

Banknote counterfeit deterrence was the first commercially successful use of our technologies. Old Digimarc, in cooperation with the Central Banks, developed a system to use digital technologies to deter banknote counterfeiting. More recently, innovations based on Old Digimarc's digital watermarking technology and experience have been leveraged to create new products to deter counterfeiting and tampering of driver licenses and other government-issued secure credentials. In parallel, Old Digimarc's business partners, under patent or technology licenses from us, are delivering digital watermarking solutions to track and monitor the distribution of music, images, television and movies to consumers. In November of 2007, we announced a relationship with The Nielsen Company (US) LLC, or Nielsen, to license our patents in support of Nielsen's audience measurement across more than 95% of the television shows broadcast in the United States and to provide development services for Nielsen's new Digital Media Manager content identification and management system.

On July 1, 2009, we commenced operation of two joint ventures with Nielsen. In connection with these joint ventures, we terminated our agreement with Nielsen, dated as of October 1, 2007, to enter into the joint venture agreements, and entered into a new patent license agreement.

Under the first joint venture, TVaura LLC, Digimarc and Nielsen engage 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. Under the second joint venture, TVaura Mobile LLC, Digimarc and Nielsen engage in the development of certain enhanced television offerings, and other related products. We provide technical and development services to TVaura LLC's business, and will continue to do so through the term of the joint venture. Digimarc and Nielsen each own approximately one half of each joint venture.

**Customers and Business Partners**

Our revenues are generated through commercial and government applications of our technology. We generate a majority of our revenue from service and license fees paid to us under significant long-term contracts with the Central Banks, Nielsen and our joint venture with Nielsen, TVaura LLC. The remainder of our revenues are generated primarily from patent and technology license fees and royalties paid by commercial business partners providing media identification and management solutions to movie studios and music labels, television broadcasters, creative professionals and other customers around the world. Patent and technology licensing is expected to continue to contribute most of the revenues from our non-government customers for the foreseeable future.

In 2009, revenues from government contracts accounted for approximately 50% of total revenue, and revenues generated under our contract with the Central Banks accounted for approximately 91% of revenue generated under all of our government contracts. As part of our work with government customers, we must comply with and are affected by laws and regulations relating to the award, administration and performance of government contracts. Government contract laws and regulations affect how we do business with our customers and, in some instances, impose added costs on our business.

In some instances, these laws and regulations impose terms or rights that are more favorable to the government than those typically available to commercial parties in negotiated transactions. For example, a government agency may terminate any of our contracts and, in general, subcontracts, at its convenience, as well as for default based on performance. Upon termination for convenience of a fixed-price type contract, we normally are entitled to receive the purchase price for delivered items, reimbursement for allowable costs for work-in-process and an allowance for profit on the contract or adjustment for loss if completion of performance would have resulted in a loss. Upon termination for convenience of a cost reimbursement contract, we normally are entitled to reimbursement of allowable costs plus a portion of the fee.



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In addition, our government contracts typically span one or more base years and multiple option years. A government agency generally has the right to not exercise option periods and may not exercise an option period if the agency is not satisfied with our performance on the contract.

### **Products and Services**

We provide media identification and management solutions to commercial entities and government customers and license our technology to other solution providers. We license our technology primarily to commercial entities who use our technology and patented inventions to address opportunities in the media and entertainment industry. Our largest government customer is the Central Banks, with whom we have been developing, deploying, supporting and continuing to enhance a system to deter digital counterfeiting of currency using personal computers and digital reprographics for several years.

Commercial customers use a range of solutions from our business partners and us to identify, track, manage and protect content as it is distributed and consumed either digitally or physically and to enable new consumer applications to access networks and information from personal computers and mobile devices. Many movie studios, record labels, broadcasters, creative professionals and other customers rely on digital watermarking as a cost-effective means to:

deter piracy and illegal use of movies, music and images;

protect entertainment content from copyright infringement;

track and monitor entertainment content for rights usage and licensing compliance;

monitor advertisements to verify ad placement and measure return on investment;

enhance information access, search and marketing capabilities related to media content; and

enable fair and legitimate use of content by consumers.

Licensees of our technology or intellectual property include AquaMobile, Microsoft Corporation, The Nielsen Company, Civolution, Signum Technologies, Verance Corporation and Verimatrix, Inc.

### **Technology and Intellectual Property**

We develop and patent intellectual property to differentiate our products and technology, mitigate infringement risks, and develop opportunities for licensing. Licensing of our technology is supported by a broad patent portfolio covering a wide range of methods, applications, system architectures and business processes.

Most of our patents relate to various methods for embedding digital information in video, audio, and images, whether the content is rendered in analog or digital formats. The digital information is generally embedded by making subtle modifications to the fundamental elements of the content itself, generally at a signal processing level. The changes necessary to embed this information are so subtle that they are generally not noticeable by people during normal use. Because the message is carried by the content itself, it is file-format independent. The embedded digital information generally survives most normal content transformation procedures, including compression, edits, rotation, scaling, re-sampling, file-format transformations, copying, scanning and printing.

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 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

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related fields, with over 560 U.S. and foreign patents and more than 420

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U.S. and foreign patent applications on file as of December 31, 2009. Separately, we own registered trademarks in both the U.S. 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.

## **Markets**

Our technology is used in various media identification and management products and solutions supporting a variety of media objects, from movies and music, to banknotes and secure credentials. Each media object enabled by our technology creates the potential for several applications, such as:

counterfeiting and piracy deterrence;

content identification and media management;

authentication and monitoring;

linking to networks and providing access to information; and

enhanced services in support of mobile commerce.

We believe the market for these applications is in the early stages of development and that existing solutions represent only a small portion of the potential market for our products, services, and technology.

## **Competition**

No single competitor or small number of competitors is dominant in our industry. Our competitors vary depending on the application of our products and services. Our business partners and we generally compete with non-digital watermarking technologies for the security or marketing budgets of the producers and distributors of media objects, documents, products and advertising. These alternatives include, among other things, encryption-based security systems and technologies and solutions based on fingerprinting and pattern recognition. Our competitive position within the digital watermarking industry is strong because of our large, high quality, sophisticated patent position in the proprietary technology of digital watermarking and our substantial and growing amount of intellectual property in related media security and management innovations that span basic technologies, applications, system designs, and business processes. Our intellectual property portfolio allows us to use proprietary technologies that are well regarded by our customers and partners and not available to our competitors. We compete with others in our industry based on the variety of features we offer and a traditional cost/benefit analysis of our technologies against alternative technologies and solutions. We anticipate that our competitive position within some markets may be affected by factors such as reluctance to adopt new technologies and by changes in government regulations.

## **Backlog**

Based on projected commitments we have for the periods under contract with our respective customers, we anticipate our current contracts as of December 31, 2009 will generate an aggregate of approximately \$42.2 million in revenue during the remaining terms of these contracts, currently through early 2014. We expect approximately \$17.2 million of this amount to be recognized as revenue during 2010. Some factors that lead to increased backlog include:

contracts with new customers;

renewals with current customers;

add-on orders to current customers; and

contracts with longer contractual periods replacing contracts with shorter contractual periods.

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Some factors that lead to decreased backlog include:

recognition of revenue associated with backlog currently in place;

contracts with shorter contractual periods replacing contracts with longer contractual periods; and

contracts ending with existing customers.

The mix of these factors, among others, dictates whether our backlog increases or decreases for any given period. We do not assure that our backlog will result in actual revenue in any particular period, because the orders, awards and contracts included in our backlog may be subject to modification, cancellation or suspension. We may not realize revenue on certain contracts, orders or awards included in our backlog or the timing of any realization may change.

## **Employees**

At December 31, 2009, we had 93 full-time employees, including 18 in sales, marketing, technical support and customer support; 51 in research, development and engineering; and 24 in finance, administration, information technology and legal. Our future success will depend, in part, on our ability to continue to attract, retain and motivate highly qualified technical and management personnel, for whom competition is intense. We do not anticipate material turnover at this time or in the reasonably foreseeable future, especially among our technical personnel.

Our employees are not covered by any collective bargaining agreement, and we have never experienced a work stoppage. We believe that our relations with our employees are good.

## **Available Information**

We make available free of charge through our website at [www.digimarc.com](http://www.digimarc.com) our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to these and other reports filed or furnished by us pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we file these materials with the Securities and Exchange Commission.

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The selected financial data set forth below should be read in conjunction with the financial statements and the notes to the financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations, which are included elsewhere in this report. The following tables set forth our selected financial information as of and for each of the years in the five-year period ended December 31, 2009, which has been derived from audited financial statements as of December 31, 2009, 2008, 2007, 2006, and 2005, as of August 1, 2008 and for the period January 1, 2008 through August 1, 2008, and for the period August 2, 2008 through December 31, 2008 and years ended December 31, 2009, 2007, 2006 and 2005. In our opinion, the information derived from our unaudited financial statements is presented on a basis consistent with the information in our audited financial statements. The selected financial information presented may not reflect the results of operations or financial condition that would have resulted had we been operating as an independent, publicly-traded company during the periods presented, and is not necessarily indicative of our future performance as an independent company. See Risk Factors.

**Statement of Operations Data (1)**

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Total* 2008	Predecessor Year Ended December 31, 2007	Predecessor Year Ended December 31, 2006	Predecessor Year Ended December 31, 2005
Operating revenues	\$ 19,071	\$ 7,832	\$ 11,950	\$ 19,782	\$ 13,025	\$ 11,071	\$ 11,119
Gross profit percentage	67%	70%	69%	70%	69%	66%	69%
Operating income (loss)	\$ (2,565)	\$ (357)	\$ 836	\$ 479	\$ (1,310)	\$ (3,908)	\$ (5,770)
Net income (loss)	\$ (2,757)	\$ 76	\$ 1,415	\$ 1,491	\$ 55	\$ (2,687)	\$ (4,842)
Earnings (loss) per share:							
Net income (loss) per share - basic and diluted	\$ (0.39)	\$ 0.01					
Weighted average shares outstanding - basic and diluted	7,140	7,156					
Pro-forma earnings (loss) per share:							
Net income (loss) per share - basic and diluted			\$ 0.20	\$ 0.21	\$ 0.01	\$ (0.38)	\$ (0.68)
Weighted average shares outstanding - basic and diluted			7,143	7,143	7,143	7,143	7,143

\* Used for comparative purposes

**Table of Contents****Balance Sheet Data (1)**

	Successor	Successor	Predecessor	Predecessor	Predecessor	Predecessor
	Year Ended	As of	As of	Year Ended December 31,		
	December 31,	December 31,	August 1,	2007	2006	2005
	2009	2008	2008			
Cash, cash equivalents and short-term marketable securities	\$ 42,786	\$ 40,168	\$ 54,749	\$ 32,713	\$ 33,073	\$ 31,982
Long-term marketable securities	\$	\$ 5,744	\$	\$	\$	\$
Total assets	\$ 50,483	\$ 52,441	\$ 64,111	\$ 38,451	\$ 37,658	\$ 36,896
Long-term liabilities	\$ 99	\$ 257	\$ 237	\$ 215	\$ 294	\$ 295
Redeemable preferred stock	\$ 50	\$ 50	\$	\$	\$	\$

- (1) The Old Digimarc/L-1 merger agreement provided that all cash and cash equivalents, short-term marketable securities and restricted cash, collectively referred to as the aggregate cash, of Old Digimarc was treated as cash retained by Digimarc in its carved-out financial statements. As a result, the presentation of the financial statements and operating data of Digimarc during the carve-out periods reflect the cash flow of Old Digimarc, including its Secure ID Business, combined with Digimarc. For 2005 through 2007, the consolidated results of Old Digimarc reflected operating losses of \$23.6 million, \$13.1 million and \$1.6 million respectively. Cash provided by (used in) operations for those same periods was (\$3.2) million, \$9.3 million and \$16.3 million, respectively. Also, capital expenditures for those periods were \$15.5 million, \$10.5 million and \$17.7 million, respectively.

**ITEM 7A: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Our exposure to market risk for changes in interest rates relates primarily to the increase or decrease in the amount of interest income we can earn on our investment portfolio and on the increase or decrease in the amount of any interest expense we must pay with respect to outstanding debt instruments. The risk associated with fluctuating interest expense is limited, however, to the exposure related to those debt instruments and credit facilities that are tied to market rates. We do not use derivative financial instruments in our investment portfolio. We attempt to ensure the safety and preservation of our invested principal funds by limiting default risk, market risk and investment risk. We mitigate default risk by investing in low-risk securities. At December 31, 2009, we had an investment portfolio of money market funds, commercial securities and U.S. Government securities, including those classified as cash and cash equivalents, and short- and long-term marketable securities, totaling \$42.8 million. The original maturities of our investment portfolio range from 19 to 677 days with an average interest rate of 1.2%. If market interest rates were to increase immediately and uniformly by 10% from levels as of December 31, 2009, the decline of the fair market value of the fixed income portfolio and interest expense associated with capital leases would not be material.

**ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Our Financial Statements and the accompanying Notes that are filed as part of this Annual Report are listed under Part III, Item 15, Exhibits and Financial Statement Schedules and are set forth beginning on page F-1 immediately following the signature page of this Form 10-K/A.

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**PART IV**

**ITEM 15: EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

**(a)(1) Financial Statements**

The following documents are filed as part of this Annual Report on Form 10-K:

- (i) Report of Independent Registered Public Accounting Firm
- (ii) Balance Sheets as of December 31, 2009 and 2008
- (iii) Statements of Operations for the year ended December 31, 2009, the Period August 2, 2008 through December 31, 2008, the Period January 1, 2008 through August 1, 2008 and the year ended December 31, 2007
- (iv) Statements of Stockholders' Equity as of December 31, 2009 and 2008
- (v) Statements of Cash Flows for the year ended December 31, 2009, the Period August 2, 2008 through December 31, 2008, for the Period January 1, 2008 through August 1, 2008 and for the year ended December 31, 2007
- (vi) Notes to Financial Statements

**(a)(2) Financial Statement Schedules**

All schedules have been omitted since they are not required or are not applicable or the required information is shown in the financial statements or related notes.

**(a)(3) Exhibits**

See the Exhibit Index at page E-1 of this Annual Report on Form 10-K.

In reviewing the agreements included as exhibits to this Annual Report on Form 10-K, please remember they are included to provide you with information regarding their terms and are not intended to provide any other factual or disclosure information about Digimarc or the other parties to the agreements. The agreements may contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other party or parties to the applicable agreement and:

should not in all instances be treated as categorical statements of fact, but rather as a means of allocating the risk to one of the parties if those statements prove to be inaccurate;

may have been qualified by disclosures that were made to the other party or parties in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;



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may apply standards of materiality in a manner that is different from what may be viewed as material to you or other investors; and

were made only as of the date of the applicable agreement or other date or dates that may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time. Additional information about Digimarc may be found elsewhere in this Annual Report on Form 10-K and in Digimarc's other public filings, which are available without charge through the SEC's website at <http://www.sec.gov>.

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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

DIGIMARC CORPORATION

Date: August 6, 2010

By: /s/ MICHAEL McCONNELL  
**Michael McConnell**  
  
*Title: Chief Financial Officer*

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**Report of Independent Registered Public Accounting Firm**

Board of Directors and Stockholders

Digimarc Corporation

We have audited the accompanying balance sheets of Digimarc Corporation (the Company) as of December 31, 2009 and 2008 and the related statements of operations, stockholders' equity, and cash flows for the year ended December 31, 2009 and the period from August 2, 2008 through December 31, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Digimarc Corporation as of December 31, 2009 and 2008, and the results of its operations and its cash flows for the year ended December 31, 2009 and the period from August 2, 2008 through December 31, 2008 in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Digimarc Corporation's internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated February 24, 2010 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/GRANT THORNTON LLP

Portland, Oregon

February 24, 2010

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**Report of Independent Registered Public Accounting Firm**

Board of Directors and Stockholders

Digimarc Corporation

We have audited the accompanying statements of operations, stockholders' equity, and cash flows of New Digimarc Corporation (the Predecessor, a carved-out business unit of Old Digimarc Corporation) for the year ended December 31, 2007 and the period from January 1, 2008 through August 1, 2008. These financial statements are the responsibility of the Predecessor's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Predecessor is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Predecessor's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of the Predecessor for the year ended December 31, 2007 and the period from January 1, 2008 through August 1, 2008 in conformity with accounting principles generally accepted in the United States of America.

As more fully described in Note 1 to the financial statements, certain expenses of the Predecessor represent allocations from Old Digimarc Corporation. The accompanying financial statements include such allocations and may not necessarily be representative of the financial position or results of operations had the Predecessor operated as an unaffiliated company during the periods presented.

/s/GRANT THORNTON LLP

Portland, Oregon

August 6, 2010

**Table of Contents****DIGIMARC CORPORATION****BALANCE SHEETS**

(In thousands, except share data)

	Successor December 31, 2009	Successor December 31, 2008
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 8,884	\$ 18,928
Marketable securities	33,902	21,240
Trade accounts receivable, net	3,570	3,839
Other current assets	872	875
Total current assets	47,228	44,882
Marketable securities		5,744
Property and equipment, net	1,114	1,212
Intangibles, net	1,302	456
Investments in joint ventures	409	
Other assets, net	430	147
Total assets	\$ 50,483	\$ 52,441
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable and other accrued liabilities	\$ 1,044	\$ 937
Accrued payroll and related costs	238	42
Accrued merger related liabilities	125	386
Deferred revenue	2,318	2,418
Total current liabilities	3,725	3,783
Long-term liabilities	99	257
Total liabilities	3,824	4,040
Commitments and contingencies (Note 14)		
Stockholders' equity:		
Preferred stock (10,000 shares issued and outstanding at December 31, 2009 and 2008)	50	50
Common stock (7,205,701 and 7,279,442 shares issued and outstanding at December 31, 2009 and 2008, respectively)	7	7
Additional paid-in capital	49,283	48,268
Retained earnings (accumulated deficit)	(2,681)	76
Total stockholders' equity	46,659	48,401
Total liabilities and stockholders' equity	\$ 50,483	\$ 52,441

See Notes to Financial Statements.

**Table of Contents****DIGIMARC CORPORATION****STATEMENTS OF OPERATIONS****(In thousands, except per share data)**

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Predecessor Year Ended December 31, 2007
<b>Revenue:</b>				
Service	\$ 10,845	\$ 4,064	\$ 6,456	\$ 7,806
License and subscription	8,226	3,768	5,494	5,219
<b>Total revenue</b>	<b>19,071</b>	<b>7,832</b>	<b>11,950</b>	<b>13,025</b>
<b>Cost of revenue:</b>				
Service	6,090	2,248	3,519	3,815
License and subscription	211	114	145	217
<b>Total cost of revenue</b>	<b>6,301</b>	<b>2,362</b>	<b>3,664</b>	<b>4,032</b>
<b>Gross profit</b>	<b>12,770</b>	<b>5,470</b>	<b>8,286</b>	<b>8,993</b>
<b>Operating expenses:</b>				
Sales and marketing	3,034	1,154	1,928	2,453
Research, development and engineering	4,989	1,772	2,071	2,912
General and administrative	6,452	2,877	2,349	3,345
Intellectual property	1,013	304	1,102	1,593
Transitional services	(153)	(280)		
<b>Total operating expenses</b>	<b>15,335</b>	<b>5,827</b>	<b>7,450</b>	<b>10,303</b>
<b>Operating income (loss)</b>	<b>(2,565)</b>	<b>(357)</b>	<b>836</b>	<b>(1,310)</b>
<b>Other income (expenses):</b>				
Net loss from joint ventures	(691)			
Other	522	(443)	590	1,387
<b>Other income (expenses), net</b>	<b>(169)</b>	<b>443</b>	<b>590</b>	<b>1,387</b>
<b>Income (loss) before provision for income taxes</b>	<b>(2,734)</b>	<b>86</b>	<b>1,426</b>	<b>77</b>
Provision for income taxes	(23)	(10)	(11)	(22)
<b>Net income (loss)</b>	<b>\$ (2,757)</b>	<b>\$ 76</b>	<b>\$ 1,415</b>	<b>\$ 55</b>
<b>Earnings (loss) per share:</b>				
Net income per share basic	\$ (0.39)	\$ 0.01		
Net income per share diluted	\$ (0.39)	\$ 0.01		
Weighted average shares outstanding basic	7,140	7,156		
Weighted average shares outstanding diluted	7,140	7,156		
<b>Pro-forma earnings per share:</b>				
Net income per share basic			\$ 0.20	\$ 0.01
Net income per share diluted			\$ 0.20	\$ 0.01
Weighted average shares outstanding basic			7,143	7,143
Weighted average shares outstanding diluted			7,143	7,143

See Notes to Financial Statements.





**Table of Contents****DIGIMARC CORPORATION****STATEMENTS OF STOCKHOLDERS EQUITY**

(In thousands, except share data)

	Preferred stock		Common stock		Additional paid-in capital	Retained Earnings	Net Parent Investment	Total stockholders equity
	Shares	Amount	Shares	Amount				
<b>PREDECESSOR</b>								
<b>BALANCE AT DECEMBER 31, 2007</b>		\$		\$	\$	\$	\$ 34,839	\$ 34,839
Cash from Parent stock activity							23,862	23,862
Stock compensation allocated from Parent							914	914
Net activity with Parent							(13,237)	(13,237)
Net income							1,415	1,415
<b>BALANCE AT AUGUST 1, 2008</b>		\$		\$	\$	\$	\$ 47,793	\$ 47,793
<b>SUCCESSOR</b>								
August 2, 2008: Stock issued through spin-off of Digimarc	10,000	\$ 50	7,143,442	\$ 7	\$ 47,736	\$	\$(47,793)	\$
Issuance of restricted common stock			136,000					
Stock compensation expense					532			532
Net income						76		76
<b>BALANCE AT DECEMBER 31, 2008</b>	10,000	50	7,279,442	7	48,268	76		48,401
Issuance of common stock			28,343		273			273
Issuance of restricted common stock			22,200					
Purchase and retirement of common stock			(124,284)		(1,737)			(1,737)
Stock compensation expense					2,479			2,479
Net loss						(2,757)		(2,757)
<b>BALANCE AT DECEMBER 31, 2009</b>	10,000	\$ 50	7,205,701	\$ 7	\$49,283	\$(2,681)	\$	\$46,659

See Notes to Financial Statements.

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**DIGIMARC CORPORATION**  
**STATEMENTS OF CASH FLOWS**

(In thousands)

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Predecessor Year Ended December 31, 2007
Cash flows from operating activities:				
Net income (loss)	\$ (2,757)	\$ 76	\$ 1,415	\$ 55
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:				
Depreciation and amortization	589	198	568	612
Stock-based compensation expense	2,444	532	913	1,209
Net loss from joint ventures	691			
Increase (decrease) in allowance for doubtful accounts			(43)	
Other non-cash charges			405	
Changes in operating assets and liabilities:				
Trade accounts receivable, net	269	(762)	718	(1,311)
Other current assets	3	3,882	(4,370)	(78)
Other assets, net	(283)	40	(103)	(9)
Accounts payable and other accrued liabilities	122	(272)	744	23
Accrued payroll and related costs	196	(2,011)	1,854	(574)
Accrued merger related liabilities	(261)	(10,380)	10,766	
Deferred revenue	(112)	366	(677)	(1,098)
Other liabilities	(122)	24	20	
Net cash provided by (used in) operating activities	779	(8,307)	12,210	1,025
Cash flows from investing activities:				
Purchase of property and equipment	(460)	(76)	(799)	(367)
Capitalized patent costs	(842)	(448)		
Investments in joint ventures	(1,100)			
Sale or maturity of marketable securities	43,708	95,553	136,767	150,775
Purchase of marketable securities	(50,626)	(118,688)	(137,048)	(154,343)
Net cash used in investing activities	(9,320)	(23,659)	(1,080)	(3,935)
Cash flows from financing activities:				
Cash from Parent stock activity			23,862	2,187
Net activity with Parent			(13,237)	(3,205)
Issuance of common stock	273			
Purchase of common stock	(1,737)			
Principal payments under capital lease obligations	(39)	(6)		
Net cash provided by (used in) financing activities	(1,503)	(6)	10,625	(1,018)
Net increase (decrease) in cash and cash equivalents	(10,044)	(31,972)	21,755	(3,928)
Cash and cash equivalents at beginning of period	18,928	50,900	29,145	33,073
Cash and cash equivalents at end of period	\$ 8,884	\$ 18,928	\$ 50,900	\$ 29,145

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Supplemental disclosure of cash flow information:

Cash paid for interest	\$	4	\$	2	\$	7	\$
Cash paid for income taxes	\$	23	\$	10	\$	11	\$

See Notes to Financial Statements.

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS**

**(In thousands, except share and per share data)**

**(1) Description of Business and Summary of Significant Accounting Policies**

***Description of Business***

Digimarc Corporation ( Digimarc or the Company ) 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. The Company s 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. The Company s technology permits computers and digital devices to quickly identify relevant data from vast amounts of media content.

***Acquisition of Old Digimarc and Separation of DMRC Corporation***

On June 29, 2008, the former Digimarc Corporation ( Old Digimarc ) entered into an amended and restated merger agreement, as amended by Amendment No. 1 dated as of July 17, 2008, which we refer to as the Old Digimarc/L-1 merger agreement, with L-1 Identity Solutions, Inc. and Dolomite Acquisition Co., a wholly owned subsidiary of L-1, pursuant to which Dolomite, in a transaction which we refer to as the offer, purchased more than 90% of the outstanding shares of Old Digimarc common stock, together with the associated preferred stock purchase rights, for \$12.25 per share. On August 13, 2008, following the completion of the offer, Dolomite merged with and into Old Digimarc with Old Digimarc continuing as the surviving company and a wholly owned subsidiary of L-1.

On August 1, 2008, prior to the initial expiration of the offer, Old Digimarc contributed all of the assets and liabilities related to its digital watermarking business, which we refer to as the Digital Watermarking Business, together with all of Old Digimarc s cash, to DMRC LLC. Following the restructuring, all of the limited liability company interests of DMRC LLC were transferred to a newly created trust for the benefit of Old Digimarc record holders. DMRC LLC then merged with and into DMRC Corporation, and each limited liability company interest of DMRC LLC was converted into one share of common stock of DMRC Corporation. After completion of the Old Digimarc/L-1 merger, DMRC Corporation changed its name to Digimarc Corporation. The shares of Digimarc common stock were held by the trust until the Form 10, *General Form for Registration of Securities* , was declared effective by the Securities and Exchange Commission ( SEC ) on October 16, 2008, at which time the shares were distributed to Old Digimarc record holders, as beneficiaries of the trust, pro rata in accordance with their ownership of shares of Old Digimarc common stock on August 1, 2008 at 5:30 pm Eastern time, the spin-off record date and time. Each Old Digimarc record holder was entitled to receive one share of Digimarc common stock for every three and one half shares of Old Digimarc common stock held by the stockholder as of the spin-off record date and time.

***Joint Venture and Patent License Agreements with The Nielsen Company***

On June 11, 2009 the Company entered into two joint venture agreements with The Nielsen Company ( Nielsen ) to launch two new companies. The two joint venture agreements and a revised patent license agreement expand and replace the previous license and services agreement between the Company and Nielsen that had been in operation since late 2007. Under the new agreements, the Company and Nielsen plan to work 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.

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

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.

Joint Venture I, TVaura LLC, will engage 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 will make 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 for the following periods for the following minimum service fees, subject to adjustment for any development service fees paid to the Company by TVaura Mobile LLC: \$1,130 for the remainder of 2009; \$2,800 in 2010; and \$2,740 in 2011.

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

Pursuant to the terms of the agreements and Accounting Standards Codification (ASC) 810 *Consolidation* (formerly Emerging Issues Task Force (EITF) Issue No. 96-16, *Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholders Have Certain Approval or Veto Rights*), the joint ventures will not be consolidated with the Company and will be separately disclosed in the financial statements and notes to financial statements.

***Basis of Accounting; Predecessor Financial Statements***

The predecessor financial statements include certain accounts of Old Digimarc and the assets, liabilities and results of operations of Old Digimarc's Digital Watermarking Business that were separated, or carved-out from Old Digimarc. The operating expenses included in the predecessor financial statements include proportional allocations of various shared services common costs of Old Digimarc because specific identification of the expenses was not practicable. The common costs include expenses from Old Digimarc related to various operating shared services cost centers, including executive, finance and accounting, human resources, legal, marketing, intellectual property, facilities and information technology.

Management believes that the assumptions underlying the predecessor financial statements are reasonable. The cost allocation methods applied to certain shared services common cost centers include the following:

*Specific identification.* Where the amounts were specifically identified to the predecessor or Old Digimarc's Secure ID Business, they were classified accordingly.

*Reasonable allocation.* Where the amounts were not clearly or specifically identified, management determined if a reasonable allocation method could be applied. For example, in the shared services human resources (HR) cost center, management allocated the costs based on the relative headcount of the predecessor and Old Digimarc's Secure ID Business. This allocation was based on the assumption that HR support costs should be relatively equal per employee. In the intellectual property cost center, management allocated the costs based on the relative number of patents that were used by each business.

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

*General allocation approach.* For consistency, when specific identification or the reasonable allocation method did not seem to fit the situation, management used a general allocation approach. This approach consisted of a blended rate based on what management determined to be the primary drivers for shared services:

Revenue ratio between the businesses.

Property and equipment balances, which served as a proxy for capital expenditures. The effort expended on capital projects is a factor in the expense and effort of shared services. To avoid fluctuations that occur in capital spending, management believes that these allocated balances represent a relative trend of capital spending between the businesses. In determining the relative balances of property, management excluded the central information technology assets because they supported the entire organization.

Headcount between the businesses.

*Other key assumptions differing from the historical accounting of Old Digimarc:*

*Cash:* All cash balances of Old Digimarc are treated as retained by Digimarc, consistent with the Old Digimarc/L-1 merger agreement. Accordingly, restricted cash on the books of Old Digimarc that related directly to its operations flowed through to Digimarc in these financial statements as non-restricted cash included in cash and cash equivalents in the predecessor financial statements. The letters of credit that required the restricted cash remained with Old Digimarc following its acquisition by L-1.

*Incentive compensation allocations to cost of services:* Cost of incentive compensation related to bonus and stock compensation charges for employees in the research, development and engineering cost centers was not considered significant to Old Digimarc's consolidated operations during the periods reported and were treated as research, development and engineering costs in Old Digimarc's financial statements. For Digimarc's reporting purposes, these incentive compensation costs have been allocated to cost of services to the extent that their pro rata salary allocations were made to the cost of services expense category. The impact for the reported periods ranged from a 1% to 3% reduction in margins compared to the results had the allocations not been made.

*Pro-forma earnings (loss) per share (unaudited):* The weighted average shares outstanding basic and diluted of 7,143,442 was calculated based on a distribution ratio of one share of Digimarc common stock for every three and one-half shares of Old Digimarc common stock, excluding shares held in treasury, outstanding at August 1, 2008, the date of the spin-off of Digimarc from Old Digimarc.

*Stock activity:* All stock activity (transactions from stock options, restricted stock, employee stock purchase plan and stock compensation) was carried on the books of Old Digimarc. All net cash from these activities was retained by Digimarc and stock-based compensation expense associated with stock activity was allocated to the predecessor in accordance with the basis of accounting methodology outlined above.

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*Capital leases:* Digimarc shares various infrastructure activities with Old Digimarc and was charged for its allocated share of capital lease costs in the form of allocated depreciation and interest expense. The assets and liabilities associated with the capital leases were carried on the books of Old Digimarc.

*Leasehold improvements:* Digimarc occupies the majority of Old Digimarc's Beaverton facility and assumed the lease and most all related furniture, fixtures and leasehold improvements when Old

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

Digimarc completed the spin-off of Digimarc. The leasehold was recorded as part of property and equipment on the balance sheet of Digimarc, and as a result, pro rata depreciation and rent expenses were allocated to Old Digimarc.

*Intercompany transactions:* With the retention by Digimarc of all of Old Digimarc cash, Digimarc's cash balances effectively funded the operations, if needed, of Old Digimarc. The net difference of cash needs for operating and capital expenditures to and from Old Digimarc is shown as net activity with Parent in the Statement of Stockholders' Equity. All intercompany transactions were eliminated.

*Merger related costs:* All Old Digimarc costs related to the Old Digimarc/L-1 merger were allocated to Old Digimarc's Secure ID Business. Digimarc was responsible for the payment of the majority of these costs.

*Commitments and contingencies:* Commitments and contingencies related to the predecessor operations are included in these financial statements, and those relating to Old Digimarc were excluded.

*Stock compensation expense:* Stock-based compensation is accounted for by Old Digimarc in accordance with ASC 718 *Compensation - Stock Compensation* (formerly Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment (Revised 2004)*), which requires the measurement and recognition of compensation for all stock-based awards made to employees and directors, including stock options, employee stock purchases under a stock purchase plan and restricted stock awards based on estimated fair values. Stock compensation expense was allocated to the predecessor based on a combination of specific and shared services resource allocations from Old Digimarc.

**The financial information in the predecessor financial statements does not include all of the expenses that would have been incurred had the predecessor been a separate, stand-alone public entity. As such, the predecessor financial information does not reflect the financial position, results of operations and cash flows of Digimarc's current business, had the predecessor operated as a separate, stand-alone public entity during the periods presented in the predecessor financial statements. Additionally, the predecessor financial statements include proportional allocations of various shared services common costs of Old Digimarc because specific identification of these expenses was not practicable. Operating costs of Digimarc on a stand-alone basis have been higher than those allocated to the predecessor operations under the shared services methodology applied in the predecessor financial statements. Consequently, the financial position, results of operations and cash flows reflected in the predecessor financial statements may not be indicative of those that would have been achieved had the predecessor operated as a separate, stand-alone entity for the periods reflected in the predecessor financial statements.**

*Use of Estimates*

The preparation of financial statements in accordance with accounting principles generally accepted in the U.S. requires Digimarc to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Certain of the Company's accounting policies require higher degrees of judgment than others in their application. These include revenue recognition on long-term service contracts, impairments and estimation of useful lives of long-lived assets and patent costs, contingencies and litigation and stock-based compensation. Digimarc bases its estimates on historical experience and on various other assumptions that are believed to be reasonable in the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.





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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

***Cash Equivalents***

The Company considers all highly liquid marketable securities with original maturities of 90 days or less at the date of acquisition to be cash equivalents. Cash equivalents include money market funds, certificates of deposit, commercial paper, and investments in government bonds totaling \$7,661, \$16,088 and \$35,950 at December 31, 2009 and 2008 and August 1, 2008, respectively. Cash equivalents are carried at cost or amortized cost, which approximates market.

***Marketable Securities***

The Company considers all investments with original maturities over 90 days that mature in less than one year to be short-term marketable securities. Both short- and long-term marketable securities include federal agency notes, company notes, and commercial paper. The Company's marketable securities are classified as held-to-maturity as of the balance sheet date and are reported at amortized cost, which approximates market. The book value of these investments approximates fair market value and, accordingly, no amounts have been recorded to other comprehensive income.

A decline in the market value of any security below cost that is deemed to be other-than-temporary results in a reduction in carrying amount of fair value. The impairment is charged to earnings and a new cost basis for the security is established. To determine whether an impairment is other-than-temporary, the Company considers whether it has the ability and intent to hold the investment until a market price recovery and considers whether evidence indicating that the cost of the investment is recoverable outweighs evidence to the contrary. There have been no other-than-temporary impairments identified or recorded by the Company.

Premiums and discounts are amortized or accreted over the life of the related security as an adjustment to yield using a method that approximates the effective interest method. Under this method, dividend and interest income are recognized when earned.

***Fair Value of Financial Instruments***

ASC 820 *Fair Value Measurements and Disclosures* (formerly SFAS 157, *Fair Value Measurements*) defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and enhances disclosures about fair value measurements. ASC 820 describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value, which are the following:

Level 1 Pricing inputs are quoted prices available in active markets for identical investments as of the reporting date.

Level 2 Pricing inputs are quoted for similar investments, or inputs that are observable, either directly or indirectly, for substantially the full term through corroboration with observable market data. Level 2 includes investments valued at quoted prices adjusted for legal or contractual restrictions specific to these investments.

Level 3 Pricing inputs are unobservable for the investment, that is, inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability. Level 3 includes private portfolio investments that are supported by little or no market activity.



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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

ASC 825 *Financial Instruments* (formerly SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ) allows an entity the irrevocable option to elect fair value for the initial and subsequent measurement for specified financial assets and liabilities on a contract-by-contract basis. The Company did not elect the fair value option under this statement as to specific assets or liabilities. Therefore, through December 31, 2009, the Company has not recognized the net change in fair value of its financial assets and liabilities.

The estimated fair values of the Company's financial instruments, which include cash and cash equivalents, short- and long-term marketable securities, accounts receivable, accounts payable and accrued payroll approximate their carrying values due to the short-term nature of these instruments. The carrying amounts of capital leases approximate fair value because the stated interest rates approximate current market rates. These items are valued using either Level 1 or Level 2 inputs.

The Company records marketable securities at amortized cost of \$37,402, including \$3,500 in cash equivalents, which approximates fair value. The fair value of the marketable securities at December 31, 2009, excluding accrued interest, was \$37,263. The fair value is based on quoted market prices in active markets for identical assets, a Level 1 input.

The Company records money market funds at cost and continues to carry those amounts at cost which approximates fair value. The fair value is based on quoted market prices in active markets for identical assets, a Level 1 input. As of December 31, 2009, the cost and fair value of the Company's money market funds were each equal to \$7,661.

***Concentrations of Business and Credit Risk***

A significant portion of our business depends on a limited number of large contracts. The loss of any large contract may result in loss of revenue and margin on a prospective basis.

Financial instruments that potentially subject Digimarc to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities, and trade accounts receivable. Digimarc places its cash and cash equivalents with major banks and financial institutions and at times deposits may exceed insured limits. Other than cash used for operating needs, which may include short-term marketable securities with our principal banks, our investment policy limits its credit exposure to any one financial institution or type of financial instrument by limiting the maximum of 5% or \$1,000, whichever is greater, to be invested in any one issuer except for the U.S. Government and U.S. federal agencies, which have no limits, at the time of purchase.

***Software Development Costs***

Under ACS 985 *Software* (formerly SFAS No. 86, *Accounting for the Cost of Computer Software to Be Sold, Leased, or Otherwise Marketed* ), software development costs are to be capitalized beginning when a product's technological feasibility has been established and ending when a product is made available for general release to customers. To date, the establishment of technological feasibility of the Company's products has occurred shortly before general release and, therefore, software development costs qualifying for capitalization have been immaterial. Accordingly, the Company has not capitalized any software development costs and has charged all such costs to research and development expense.

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

***Impairment of Long-Lived Assets***

The Company accounts for long-lived assets in accordance with the provisions of ASC 360 *Property, Plant and Equipment* (formerly SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*). This statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Fair value is determined based on discounted cash flows or appraised values, depending on the nature of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Through December 31, 2009, there have been no such impairment losses.

***Research and Development***

Research and development costs are expensed as incurred as defined in ASC 730 *Research and Development* (formerly SFAS No. 2, *Accounting for Research and Development Costs*). Digimarc accounts for amounts received under its funded research and development arrangements in accordance with the provisions of ASC 730 (also formerly SFAS No. 68, *Research and Development Arrangements*). Under the terms of the arrangements, Digimarc is not obligated to repay any of the amounts provided by the funding parties. As a result, Digimarc recognizes revenue as the services are performed.

***Patent Costs***

Costs associated with the application and award of patents in the U.S. and various other countries are capitalized and amortized on a straight-line basis over the term of the patents as determined at award date, which varies depending on the pendency period of the application, generally approximating seventeen years. Capitalized patent costs include internal legal labor, professional legal fees, government filing fees and translation fees related to obtaining the Company's patent portfolio. Such costs were expensed in the predecessor financial statements.

Costs associated with the maintenance and annuity fees of patents are accounted for as prepaid assets at the time of payment and amortized over the respective periods, generally from one to four years. These costs were expensed in the predecessor financial statements.

***Revenue Recognition***

The Company's revenue consists of subscription revenue, which includes hardware and software sales, royalties and revenues from the licensing of digital watermarking products and related authentication services. The Company's revenue recognition policy follows ASC 605 *Revenue Recognition*, ASC 985 (formerly Statement of Position (SOP) No. 97-2, *Software Revenue Recognition*, as amended by SOP No. 98-9, *Modification of SOP No. 97-2, Software Recognition, With Respect to Certain Transactions*, and SOP 81-1 *Accounting for the Performance of Construction Type and Certain Production-Type Contracts*, and EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*), and SEC Staff Accounting Bulletin (SAB) No. 104 *Revenue Recognition*.

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

***Other income (expense), net***

The Company's other income (expense), net consists primarily of interest income earned on cash and short- and long-term marketable securities and the net income (loss) from the joint ventures with The Nielsen Company, TVaura LLC and TVaura Mobile LLC. Some minor amounts are included in this category in the predecessor financials that relate to interest expense for capital lease allocations from Old Digimarc and for other non-operating items.

***Stock-Based Compensation***

ASC 718 requires the measurement and recognition of compensation for all stock-based awards made to employees and directors including stock options and restricted stock based on estimated fair values.

The Company uses the Black-Scholes option pricing model as its method of valuation for stock-based awards. The Company's determination of the fair value of stock-based awards on the date of grant using an option pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the expected life of the award, our expected stock price volatility over the term of the award and actual and projected exercise behaviors.

***Income Taxes***

The Company accounts for income taxes under the asset and liability method. Under the asset and liability method, deferred income taxes reflect the future tax consequences of differences between the tax bases of assets and liabilities and their financial reporting amounts at each year-end. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce tax assets to the amount expected to be realized.

**(2) Recent Accounting Pronouncements**

In October 2009, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2009-14, *Software: Certain Revenue Arrangements That Include Software Elements a consensus of the FASB Emerging Issues Task Force* , which will significantly improve the reporting of certain transactions to more closely reflect the underlying economics of the transactions. By excluding from its scope certain software-enabled devices, multiple-element arrangements that include such software-enabled devices will now be evaluated for separation and allocation using the guidance in ASU No. 2009-13 (described below). ASU No. 2009-14 is effective for revenue arrangements entered or materially modified in fiscal years beginning on or after June 15, 2010. The Company is currently assessing the potential impact of this standard, but does not expect the adoption of the standard will have a material impact on the financial condition or results of operations of the Company.

In October 2009, the FASB issued ASU No. 2009-13, *Revenue Recognition: Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force* , which eliminates the use of the residual method for allocating consideration, as well as the criteria that requires objective and reliable evidence of fair value of undelivered elements in order to separate the elements in a multiple-element arrangement. By removing the criterion requiring the use of objective and reliable evidence of fair value in separately accounting for deliverables, the recognition of revenue will more closely align with certain revenue arrangements. The standard

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

also will replace the term fair value in the revenue allocation guidance with selling price to clarify that the allocation of revenue is based on entity-specific assumptions rather than assumptions of a marketplace participant. ASU No. 2009-13 is effective for revenue arrangements entered or materially modified in fiscal years beginning on or after June 15, 2010. The Company is currently assessing the potential impact of this standard, but does not expect the adoption of the standard will have a material impact on the financial condition or results of operations of the Company.

In June 2009, the FASB issued ASU 2009-01, *Amendments based on Statement of Financial Accounting Standards No. 168 The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles*, to codify in ASC 105, *Generally Accepted Accounting Principles*, FASB Statement 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles*, which was issued to establish the Codification as the sole source of authoritative U.S. GAAP recognized by the FASB, excluding SEC guidance, to be applied by nongovernmental entities. The guidance in ASC 105 is effective for financial statements issued for interim and annual periods ending after September 15, 2009 and does not modify existing U.S. GAAP. The Company has revised its references to pre-Codification GAAP.

**(3) Revenue Recognition**

Revenue is recognized in accordance with ASC 985 and SAB 104 when the following four criteria are met:

- (i) persuasive evidence of an arrangement exists,
- (ii) delivery has occurred,
- (iii) the fee is fixed or determinable, and
- (iv) collection is probable.

Some customer arrangements encompass multiple deliverables, such as software, maintenance fees, and software development fees. If the deliverables meet the criteria in ASC 605 (formerly EITF Issue No. 00-21), the deliverables are divided into separate units of accounting and revenue is allocated to the deliverables based on their relative fair values. The criteria specified in ASC 605 are as follows:

- (i) the delivered item has value to the customer on a stand-alone basis,
- (ii) there is objective and reliable evidence of the fair value of the undelivered item, and
- (iii) if the arrangement includes a general right of return relative to the delivered item, delivery or performance of the undelivered item is considered probable and substantially in the control of the vendor.

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For the Company's purposes, fair value is generally defined as the price at which a customer could purchase each of the elements independently from other vendors or as the price that the Company has sold the element separately to another customer. Management applies judgment to ensure appropriate application of ASC 605, including value allocation among multiple deliverables, determination of whether undelivered elements are essential to the functionality of delivered elements and timing of revenue recognition, among others.

ASC 985 (formerly AICPA SOP No. 98-9) requires that revenue be recognized using the residual method in circumstances when vendor specific objective evidence (VSOE) exists only for undelivered elements. Under the residual method, revenue is recognized as follows: (1) the total fair value of undelivered elements, as

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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

indicated by VSOE, is deferred and subsequently recognized in accordance with the relevant sections of ASC 685, and (2) the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements.

Applicable revenue recognition criteria is considered separately for each separate unit of accounting as follows:

Revenue from professional service arrangements is generally determined based on time and materials. Revenue for professional services is recognized as the services are performed. Billing for services rendered generally occurs within one month after the services are provided.

Royalty revenue is recognized when the royalty amounts owed to the Company have been earned, are determinable, and collection is probable. Subscriptions are paid in advance and revenue is recognized ratably over the term of the subscription. These revenues include the licensing of digital watermarking products and services for use in authenticating documents, detecting fraudulent documents and deterring unauthorized duplication or alteration of high-value documents, for use in communicating copyright, asset management and business-to-business image commerce solutions, and for use in connecting analog media to a digital environment.

Software revenue is recognized in accordance with ASC 985 (formerly AICPA SOP No. 97-2, as amended by AICPA SOP No. 98-9). Revenue for licenses of the Company's software products is recognized upon the Company meeting the following criteria: persuasive evidence of an arrangement exists; delivery has occurred; the vendor's fee is fixed or determinable; and collectibility is probable. Software revenue is recognized over the term of the license, which is generally twelve months, or upon delivery and acceptance if the Company grants a perpetual license with no further obligations.

Maintenance revenue is recognized when the maintenance amounts owed to the Company have been earned, are determinable, and collection is probable. Maintenance contracts are, at times, paid in advance and revenue is recognized ratably on a straight-line basis over the term of the service period.

The Company records revenue from some customers upon cash receipt as a result of collectibility not being reasonably assured.

Revenue earned which has not been invoiced at the last day of the period, but which are generally billed within one to two weeks of the last day of the period, is included in the balance of trade receivables, net in the balance sheets.

Deferred revenue consists of billings in advance for professional services, licenses, subscriptions and hardware for which revenue has not been earned.

**(4) Segment Information**

***Geographic Information***

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The Company derives its revenue from a single reporting segment: media management solutions. Revenue is generated in this segment through licensing of intellectual property, subscriptions to various products and services, and the delivery of services pursuant to contracts with various customers. The Company markets its products in the U.S. and in non-U.S. countries through its sales personnel.

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**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

Revenue, based upon the bill-to location, by geographic area is as follows:

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Predecessor Year Ended December 31, 2007
Domestic	\$ 8,673	\$ 3,425	\$ 6,274	\$ 3,696
International	10,398	4,407	5,676	9,329
<b>Total</b>	<b>\$ 19,071</b>	<b>\$ 7,832</b>	<b>\$ 11,950</b>	<b>\$ 13,025</b>

***Major Customers***

Customers who accounted for more than 10% of the Company's revenues are as follows:

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Predecessor Year Ended December 31, 2007
Central Banks	46%	46%	39%	60%
The Nielsen Company	24%	31%	38%	*
Verance	*	*	*	10%

\* 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.

Stock-based compensation expense was allocated to the predecessor based on a combination of specific and shared services resource allocations from Old Digimarc. All cash flow related to stock compensation generated by Old Digimarc was retained by Digimarc. Stock-based compensation recognized in the year ended December 31, 2009 was based on the value of the portion of the stock-based awards that vested during the period. Compensation cost for all stock-based awards is recognized using the straight-line method.

***Determining Fair Value******Preferred Stock***

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The Board of Directors authorized 10,000 shares of Series A Redeemable Nonvoting Preferred stock 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 by the Board of Directors at any time on or after June 18, 2013.

The fair value of Series A Redeemable Nonvoting Preferred stock is 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.

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Table of Contents**DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)***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. 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 pre-vesting and post-vesting forfeitures. Stock options granted generally vest over four years for employee grants and two years for director grants, and have contractual terms of ten years.

*Expected Volatility.* The Company estimated the initial volatility of its common stock at the date of grant based on an independent analysis of a peer group's historical volatility of their common stock using the Black-Scholes option valuation model 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 term 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.

*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, which the initial option grants, for new Directors, vest 50% on the first anniversary of the date of grant and then monthly thereafter and which the 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. Forfeitures that occur during the month are not expensed.

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

	<b>August 2, 2008 through December 31, 2008</b>			<b>2009</b>
Expected life (in years)	5.6	6.0		5.64
Expected volatility	70%	72%		70.45%
Risk-free interest rate	2.8%	2.9%		2.17%
Expected dividend yield	0%			0%
Expected forfeiture rate	0%			0%

*Restricted Stock*

The Compensation Committee of the Board of Directors awarded restricted stock shares under the Company's 2008 Stock Incentive Plan to certain employees. The shares subject to the restricted stock awards



**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

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**

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Predecessor Year Ended December 31, 2007
Stock-based compensation:				
Cost of revenue	\$ 231	\$ 5	\$ 99	\$ 102
Sales and marketing	210	38	208	287
Research, development and engineering	187	51	34	47
General and administrative	1,747	422	537	728
Intellectual property	69	16	35	45
Total stock-based compensation	\$ 2,444	\$ 532	\$ 913	\$ 1,209

At December 31, 2009, the Company had 10,000 shares of Series A redeemable nonvoting preferred stock, 806,591 non-vested stock options and 111,000 shares of restricted stock outstanding. As of December 31, 2009, the Company had \$6.1 million of total unrecognized compensation cost related to non-vested stock-based awards granted under all equity compensation plans, including options and restricted stock. Total unrecognized compensation cost will be adjusted for any future changes in estimated forfeitures. The Company expects to recognize this compensation cost for stock options and restricted stock over a weighted average period of 1.48 years and 2.00 years, respectively, through October 2012.

Information regarding deferred stock compensation expense and information related to the assumptions used in the above calculations is further described in Note 10.

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## DIGIMARC CORPORATION

## NOTES TO FINANCIAL STATEMENTS (Continued)

(In thousands, except share and per share data)

**(6) Net Income Per Share**

Net income per share is calculated in accordance with ASC 260 *Earnings Per Share* (formerly SFAS No. 128, *Earnings per Share*), which provides that basic and diluted net income per share for all periods presented are to be computed using the weighted average number of common shares outstanding during each period, with diluted net income per share including the effect of potentially dilutive common shares.

	Year Ended December 31, 2009			Period August 2, 2008 through December 31, 2008		
	Income (000 s) (Numerator)	Shares (000 s) (Denominator)	Per Share Amount	Income (000 s) (Numerator)	Shares (000 s) (Denominator)	Per Share Amount
<b>Basic EPS</b>						
Income available to common stockholders	\$ (2,757)	7,140	\$ (0.39)	\$ 76	7,156	\$ 0.01
<b>Effect of Dilutive Securities</b>						
Options						
Restricted stock						
<b>Diluted EPS</b>						
Income available to common stockholders	\$ (2,757)	7,140	\$ (0.39)	\$ 76	7,156	\$ 0.01

Common stock equivalents related to stock options of 974 were excluded from diluted net income per share calculations for the period August 2, 2008 through December 31, 2008 as their exercise price was higher than the average market price of the underlying common stock for the period.

**(7) Trade Accounts Receivable and Allowance for Doubtful Accounts***Trade Accounts Receivable*

Trade accounts receivable are recorded at the invoiced amount and do not bear interest.

	Successor December 31, 2009	Successor December 31, 2008
Trade accounts receivable	\$ 3,570	\$ 3,839
Allowance for doubtful accounts		
Trade accounts receivable, net	\$ 3,570	\$ 3,839
Unpaid deferred revenues included in accounts receivable	\$ 1,926	\$ 2,155

*Allowance for doubtful accounts*



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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.

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**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)***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 no longer included in accounts receivable nor deferred revenue accounts.

*Major customers*

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

	Successor December 31, 2009	Successor December 31, 2008
Central Banks	38%	58%
The Nielsen Company	25%	27%

**(8) Property and Equipment**

*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.

The property and equipment related to the Company were separated from Old Digimarc and recorded at net book value (cost less accumulated depreciation) and classified as used property and equipment.

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. Property and equipment held under capital leases are amortized by the straight-line method over the shorter of the lease term or the estimated useful life. Amortization of property and equipment under capital lease is included in depreciation expense.

	Successor December 31, 2009	Successor December 31, 2008
Office furniture fixture	\$ 291	\$ 291
Equipment	1,150	793
Leasehold improvements	423	320
	1,864	1,404
Less accumulated depreciation and amortization	(750)	(192)
	\$ 1,114	\$ 1,212

Property and equipment additions for the year ended December 31, 2009, the period August 2, 2008 through December 31, 2008 and the period January 1, 2008 through August 1, 2008 totaled \$460, \$76 and \$799, respectively.

*Leases*

The Company no longer has equipment under long-term capital lease obligations as of December 31, 2009. Certain equipment under capital lease obligations at December 31, 2008 had a cost of \$43 and accumulated amortization of \$6.

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**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

Future minimum lease payments under non-cancelable operating leases are as follows:

Year ending December 31:	Operating Leases
2010	\$ 888
2011	605
2012	5
2013	1
2014	
Thereafter	
<b>Total minimum lease payments</b>	<b>\$ 1,499</b>

Rent expense on the operating leases for the year ended December 31, 2009, the periods August 2, 2008 through December 31, 2008 and January 1, 2008 through August 1, 2008, and the year ended December 31, 2007 totaled \$765, \$318, \$447 and \$758, respectively.

**(9) Intangible Assets Purchase 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.

	Successor December 31, 2009	Successor December 31, 2008
Gross intangible assets	\$ 1,339	\$ 462
Accumulated amortization	(37)	(6)
<b>Intangible assets, net</b>	<b>\$ 1,302</b>	<b>\$ 456</b>

**(10) Stockholders Equity****Preferred Stock**

In June 2008, the Board of Directors authorized 2,500,000 shares of preferred stock, par value \$0.001 per share. The Board of Directors has the authority to issue the undesignated preferred stock in one or more series and to determine the powers, preferences and rights and the qualifications, limitations or restrictions granted to or imposed upon any wholly unissued series of undesignated preferred stock and to fix the number of shares constituting any series and the designation of such series, without any further vote or action by the stockholders. The issuance of preferred stock may have the effect of delaying, deferring or preventing a change of control of our company without further action by stockholders and may adversely affect the voting and other rights of the holders of common stock.

Ten thousand shares of the authorized preferred stock have been designated as Series A Redeemable Nonvoting Preferred stock. In the event of the liquidation, dissolution or other winding up of Digimarc, before any payment or distribution is made to the holders of common stock, holders of the Series A Redeemable Nonvoting Preferred stock will be entitled to receive a value of \$5.00 per share of Series A Redeemable Nonvoting Preferred stock held by the stockholder. The Series A Redeemable Nonvoting Preferred stock has no voting rights, except as required by law,

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and may be redeemed by the Board of Directors at any time on or after June 18, 2013.

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**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

Following the spin-off, the Company issued to the executive officers an aggregate of 10,000 shares of Series A Redeemable Nonvoting Preferred stock.

***Common Stock***

In June 2008, the Board of Directors authorized 50,000,000 shares of common stock, par value \$0.001 per share. The holders of Digimarc common stock are entitled to one vote for each share held of record on all matters submitted to a vote of our stockholders, including the election of directors. Subject to preferences that may be granted to any then outstanding preferred stock, holders of common stock are entitled to receive ratably those dividends as may be declared by the Board of Directors out of funds legally available for such purpose, as well as any distributions to the Company's stockholders. In the event of the Company's liquidation, dissolution or winding up, holders of common stock are entitled to share ratably in all of the Company's assets remaining after payment of liabilities and the liquidation preference of any then outstanding preferred stock. Holders of common stock have no preemptive or other subscription or conversion rights. There are no redemption or sinking fund provisions applicable to the common stock. All outstanding shares of common stock are fully paid and non-assessable.

On October 16, 2008, each Old Digimarc record holder as of August 1, 2008 received one share of Digimarc common stock for every three and one-half shares of Old Digimarc common stock held by the stockholder. The exchange resulted in 7,143,442 shares of Digimarc common stock issued and outstanding.

***Restricted Stock***

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

The following table reconciles the unvested balance of restricted stock:

	<b>Number of Shares</b>
Unvested balance, August 2, 2008	
Granted	136,000
Vested	(15,000)
Canceled	
Unvested balance, December 31, 2008	121,000
Granted	22,200
Vested	(32,200)
Canceled	
Unvested balance, December 31, 2009	111,000

***Stock Incentive Plan***

On July 31, 2008 the Company's Board of Directors initially adopted the 2008 Incentive Plan, or the 2008 Plan. The 2008 Plan provides for the grant of stock options, stock appreciation rights, stock awards, restricted



**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

stock, stock units, performance shares, performance units, and cash-based awards, which may be granted to officers, directors, employees, consultants, agents, advisors and independent contractors who provide services to us and our affiliated companies.

The 2008 Plan authorizes the issuance of up to 2,500,000 shares of common stock. The shares authorized under the 2008 Plan are subject to adjustment in the event of a stock split, stock dividend, recapitalization or similar event. Shares issued under the 2008 Plan will consist of authorized and unissued shares or shares held by us as treasury shares. If an award granted under the 2008 Plan lapses, expires, terminates or is forfeited or surrendered without having been fully exercised or without the issuance of all the shares subject to the award, the shares covered by that award will again be available for use under the 2008 Plan. Shares that are (i) tendered by a participant or retained by us as payment for the purchase price of an award or to satisfy tax withholding obligations or (ii) covered by an award that is settled in cash, or in some manner that some or all of the shares covered by the award are not issued, will be available for issuance under the 2008 Plan. In addition, awards granted as substitute awards in connection with acquisition transactions will not reduce the number of shares authorized for issuance under the 2008 Plan.

Transactions involving the stock incentive plan are summarized as follows:

	Number of Shares	Weighted Average Exercise Price
Options outstanding, August 2, 2008		
Granted	1,194,000	\$ 9.64
Exercised		
Canceled		
Options outstanding, December 31, 2008	1,194,000	\$ 9.64
Granted	30,000	\$ 9.91
Exercised	(28,343)	\$ 9.64
Canceled	(28,334)	\$ 9.64
Options outstanding, December 31, 2009	1,167,323	\$ 9.65

	Options Outstanding			Options Exercisable	
	Number Outstanding	Remaining Contractual Life (Years)	Weighted Average Price	Number Exercisable	Weighted Average Price
\$9.64	1,137,323	8.82	\$ 9.64	343,232	\$ 9.64
\$9.91	30,000	9.93	\$ 9.91	17,500	\$ 9.91
\$9.64 \$9.91	1,167,323	8.84	\$ 9.65	360,732	\$ 9.65

At December 31, 2009, the aggregate intrinsic value of outstanding and exercisable stock options was \$6,237 and \$1,925, respectively. The aggregate intrinsic value is based on our closing price of \$14.99 on December 31, 2009, which would have been received by the optionees had all of the options with exercise prices less than \$14.99 been exercised on that date.

The estimated weighted average fair value of outstanding stock options was \$6.28 per share at December 31, 2009.





**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)****(11) Defined Contribution Pension Plan**

The Company sponsors an employee savings plan (the Plan) which qualifies as a deferred salary arrangement under Section 401(k) of the Internal Revenue Code. The plan combines both the employee savings plan and company matching plan into one plan under Section 401(k), including a 401k Roth option. Employees become eligible to participate in the Plan at the beginning of the following month after the employees hire date. Employees may contribute up to 75% of their pay to the Plan, subject to the limitations of the Internal Revenue Code. Company matching contributions are mandatory. The previous Plan was terminated as of December 31, 2008, which was different than the revised plan in that there wasn't a 401k Roth option and a lower contribution percentage of their pay. For the year ended December 31, 2009, the period August 2, 2008 through December 31, 2008, the period January 1, 2008 through August 1, 2008 and for the year ended December 31, 2007, the Company made discretionary matching contributions in the aggregate amount of \$323, \$99, \$130, and \$273, respectively.

**(12) Other Income (Expenses), Net**

Other income (expense), net consists primarily of the net losses from the Company's joint ventures with The Nielsen Company, TVaura LLC and TVaura Mobile LLC and interest income from the Company's cash and short- and long-term marketable securities.

	Successor Year Ended December 31, 2009	Successor Period August 2, 2008 through December 31, 2008	Predecessor Period January 1, 2008 through August 1, 2008	Predecessor Year Ended December 31, 2007
Other income (expense), net:				
Net loss from joint ventures	(691)			
Interest income, net	\$ 519	\$ 462	\$ 590	\$ 1,387
Other	3	(19)		
Total other income (expense), net	\$ (169)	\$ 443	\$ 590	\$ 1,387

**(13) Income Taxes**

*Old Digimarc.* The provision for income taxes reflects withholding tax expense in various foreign jurisdictions. For all historic periods reported in the financial statements, Old Digimarc maintained valuation allowances against its net deferred tax assets, including net operating loss carry-forwards, because it was not more likely than not that such deferred taxes would be realized. The provision for income taxes included foreign taxes withheld by Old Digimarc's customers and paid to foreign jurisdictions on its behalf. The predecessor financial statements indicate cumulative losses through August 1, 2008.

Furthermore, the amounts of cumulative expenses in the financial statements that were not allowed for federal and state income tax purposes were not sufficient to result in positive taxable income which would have required the Company to record income tax expense. As a result, no Federal or state income tax benefit was recognized for the book losses that were incurred in those periods prior to 2007 and no income tax expense was recognized during the 2007 and 2008 periods because any expense was offset by the benefit of net operating loss carry-forwards. Digimarc as a separate legal entity will not benefit from any of the carry-forward tax attributes of Old Digimarc, including net operating loss carry-forwards.



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## DIGIMARC CORPORATION

## NOTES TO FINANCIAL STATEMENTS (Continued)

(In thousands, except share and per share data)

*Digimarc.* For the period from August 2, 2008 through December 31, 2008 the provision for income taxes reflects withholding tax expense in various foreign jurisdictions. These withholding taxes are computed by our customers and paid to foreign jurisdictions on our behalf. There was no provision for current income taxes related to net income because the computation of taxable income resulted in a net operating loss for the period. Furthermore, a valuation allowance has been recorded to offset our net deferred tax assets until such time that we are able to conclude that it is more likely than not the tax assets or portions thereof will be realized.

For the year ended December 31, 2009, the provision for income taxes reflects withholding tax expense in various foreign jurisdictions. These withholding taxes are computed by our customers and paid to foreign jurisdictions on our behalf. There was no provision for income taxes related to net income because the computation of taxable income results in a net operating loss for the period. Furthermore, a valuation allowance has been recorded to offset our net deferred tax assets until such time that we are able to conclude that it is more likely than not the tax assets or portions thereof will be realized.

Components of tax expense (benefit) allocated to continuing operations include the following:

	December 31, 2009	December 31, 2008
<b>Current:</b>		
Federal	\$	\$
State		
Foreign	23	10
Sub-total	23	10
<b>Deferred:</b>		
Federal		
State		
Foreign		
Sub-total		
Total tax expense	\$ 23	\$ 10

The reconciliation of the statutory federal income tax rate to the Company's effective income tax rate is as follows:

	December 31, 2009	%	December 31, 2008	%
Income taxes computed at statutory rates	\$ (929)	(34)%	\$ 30	34%
Increases (decreases) resulting from:				
State income taxes, net of federal tax benefit	(143)	(5)%	4	5%
Federal and state research and experimentation credits	(299)	(11)%		%
Change in valuation allowance	1,343	49%	(37)	(43)%
Meals and entertainment	51	2%	13	17%
Total	\$ 23	1%	\$ 10	13%



**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The tax effects of significant items comprising the Company's deferred tax assets and deferred tax liabilities are as follows:

	December 31, 2009	December 31, 2008
Deferred tax assets:		
Goodwill	\$ 1,478	\$ 1,552
Net operating loss carry-forwards	1,544	638
Stock based compensation	932	148
Fixed asset differences		17
Deferred rent	84	119
Federal and state research and experimentation credits	418	
Foreign tax credit	34	11
Other	2	47
Total gross deferred tax assets	4,492	2,532
Less valuation allowance	(3,894)	(2,345)
Net deferred tax assets	\$ 598	\$ 187
Deferred tax liabilities:		
Fixed asset differences	\$ (37)	\$
Patent expenditures	(561)	(187)
Total deferred tax liabilities	\$ (598)	\$ (187)
Net deferred tax asset (liability)	\$	\$

For the year ended December 31, 2009, the Company's valuation allowance increased by \$1,549, including \$119 out of period adjustments, \$51 due to an adjustment to the rate applied to deferrals, and \$36 that will impact additional paid-in capital. For the period August 2, 2008 through December 31, 2008, the Company's valuation allowance decreased by \$37. For the year ended December 31, 2009 and for the period August 2, 2008 through December 31, 2008, the Company has recorded a full valuation allowance against the net deferred tax assets until such time that the Company believes it is more likely than not that the deferred tax assets will be realized.

For U.S. tax purposes, the spin-off of the Digital Watermarking assets on August 2, 2008 resulted in a taxable event for Digimarc shareholders based on the fair market value of the assets. For Digimarc tax purposes, the basis of the assets and liabilities included as part of the transaction are adjusted to fair market value as the date of the spin-off. As a result of the tax basis adjustment to fair market value the Company recognized deferred tax assets, including tax deductible goodwill. No financial statement goodwill was recognized as part of the spin-off. The Company has recognized a future deductible temporary difference for tax basis goodwill in excess of financial statement goodwill.

Under ASC 740, *Income Taxes* (formerly EITF 94-10, *Accounting by a Company for the Income Tax Effects of Transactions among or with Its Shareholders under FASB Statement No. 109*), the Task Force concluded that the tax effects of all changes in the tax bases of assets and liabilities caused by transactions among or with shareholders should be included in equity. As a result, the Company has recorded the original deferred tax asset with a corresponding entry to shareholders equity (APIC).



**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

As of August 2, 2008 the Company evaluated the realizability of the deferred tax assets and concluded that it was not more-likely-than-not that the deferred tax assets would be realized. Therefore, as of August 2, 2008, the Company established a valuation allowance for existing deferred tax assets. Consistent with ASC 740 (formerly EITF 94-10) the Company recorded the establishment of the valuation allowance with a corresponding entry to shareholders equity ( APIC ).

As of December 31, 2009, the Company has federal and state net operating loss carry-forwards of \$3,938 and \$3,938, respectively, which have a carry-forward of 15 - 20 years depending on the jurisdiction. As of December 31, 2009, the Company has federal and state research and experimental tax credits of \$332 and \$85, respectively, which have a carry-forward of 5 - 20 years depending on the jurisdiction. As of December 31, 2009, the Company has foreign tax credits of \$34 which have a carry-forward of 9 - 10 years.

The Company adopted the provisions of ASC 740 (formerly FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement 109* ), on August 2, 2008.

As part of the ASC 740 (formerly FIN 48) implementation, the Company adopted a policy to record accrued interest and penalties associated with uncertain tax positions in income tax expense in the statements of operations. On initial adoption of ASC 740 (formerly FIN 48) and through December 31, 2008, the Company recognized no uncertain tax positions nor accrued interest and penalties associated with uncertain tax positions. For the year ended December 31, 2009, the Company recognized no additional uncertain tax positions nor accrued interest and penalties associated with uncertain tax positions.

A summary reconciliation of the Company's uncertain tax positions is listed below:

	December 31, 2009	December 31, 2008
Beginning balance	\$	\$
Addition for current year tax positions		
Reduction for prior year positions resolved during the current year		
Ending balance	\$	\$

The Company is subject to examination in the jurisdictions in which it operates for the tax years ending December 31, 2009 and 2008.

**(14) 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* (formerly SFAS No. 5, *Accounting for Contingencies* ). To date, there have been no claims made under such indemnification provisions.

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 December 31, 2009, 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. No accrual has been recorded because the amounts are not probable or reasonably estimatable in accordance with ASC 450.



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**DIGIMARC CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(In thousands, except share and per share data)**

**(15) Stock Repurchases**

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 over a period of up to two years through April 30, 2011. For the year ended December 31, 2009, the Company had paid \$1,560 to repurchase 111,667 shares of outstanding common stock under this program since the program's inception.

As part of the Company's 2008 Stock Incentive Plan, restricted stock shares are awarded to certain employees. 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. Of a total of 32,200 shares of restricted stock vested in the year ended December 31, 2009, 12,617 shares of common stock were withheld by the Company, in satisfaction of \$177 in required withholding tax liability.

**(16) Related Party Transactions**

In connection with the two joint ventures entered into with Nielsen in July 2009, the Company recognized \$1,222 in revenues for the year ended December 31, 2009 in connection with technical and development services provided to TVaura LLC.

The net losses from the joint ventures included in other income (expense), net for the year ended December 31, 2009 were \$(624) for TVaura LLC and \$(67) for TVaura Mobile LLC.

There were net accounts receivable of \$190 and \$2 from TVaura, LLC and TVaura Mobile, LLC at December 31, 2009, respectively. There were no net accounts payable to either joint venture at December 31, 2009.

**(17) Subsequent Events**

In accordance with ASC 855 *Subsequent Events* (formerly SFAS 165, *Subsequent Events*), the Company is required to disclose the date through which subsequent events have been evaluated for disclosure. Subsequent events were evaluated through February 24, 2010, which is the date the Company's Annual Report on Form 10-K for the year ended December 31, 2009 was filed with the Securities and Exchange Commission.

**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)****(18) Quarterly Financial Information Unaudited**

<b>Quarter ended:</b>	<b>Successor March 31</b>	<b>Successor June 30</b>	<b>Successor September 30</b>	<b>Successor December 31</b>
<i>2009</i>				
Service revenue	\$ 2,470	\$ 2,585	\$ 2,827	\$ 2,963
License and subscription revenue	1,959	1,739	1,942	2,586
<b>Total revenue</b>	<b>4,429</b>	<b>4,324</b>	<b>4,769</b>	<b>5,549</b>
Total cost of revenue	1,485	1,528	1,541	1,747
Gross profit	2,944	2,796	3,228	3,802
Gross profit percent, service revenue	43%	43%	47%	43%
Gross profit percent, license and subscription revenue	97%	97%	98%	98%
Gross profit percent, total	66%	65%	68%	69%
Sales and marketing	745	728	753	808
Research, development and engineering	1,271	1,217	1,191	1,310
General and administrative	1,688	1,496	1,566	1,702
Intellectual property	277	217	262	257
Transitional services	(60)	(48)	(45)	
Operating loss	(977)	(814)	(499)	(275)
Net loss	(809)	(678)	(687)	(583)
Loss per share:				
Net loss per share basic & diluted	\$ (0.11)	\$ (0.09)	\$ (0.10)	\$ (0.08)
Weighted average shares outstanding basic and diluted	7,158	7,158	7,134	7,103

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**Table of Contents****DIGIMARC CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****(In thousands, except share and per share data)**

<b>Quarter ended:</b>	<b>Predecessor</b>	<b>Predecessor</b>	<b>Predecessor Period July 1 through August 1</b>	<b>Successor Period August 2 through September 30</b>	<b>Successor December 31</b>
<b>2008</b>	<b>March 31</b>	<b>June 30</b>			
Service revenue	\$ 2,548	\$ 2,987	\$ 921	\$ 1,645	\$ 2,419
License and subscription revenue	2,537	2,128	829	1,536	2,232
<b>Total revenue</b>	<b>5,085</b>	<b>5,115</b>	<b>1,750</b>	<b>3,181</b>	<b>4,651</b>
Total cost of revenue	1,408	1,704	552	934	1,428
<b>Gross profit</b>	<b>3,677</b>	<b>3,411</b>	<b>1,198</b>	<b>2,247</b>	<b>3,223</b>
Gross profit percent, service revenue	47%	45%	43%	46%	44%
Gross profit percent, license and subscription revenue	98%	97%	97%	97%	97%
Gross profit percent, total	72%	67%	69%	71%	69%
Sales and marketing	656	683	589	390	764
Research, development and engineering	922	910	239	780	992
General and administrative	980	927	442	932	1,945
Intellectual property	478	448	176	120	184
Transitional services				(196)	(84)
Operating income (loss)	641	443	(248)	221	(578)
Net income (loss)	924	664	(173)	400	(324)
Earnings (loss) per share:					
Net income (loss) per share basic & diluted				\$ 0.06	\$ (0.05)
Weighted average shares outstanding basic and diluted				7,143	7,156
Pro-forma earnings (loss) per share:					
Net income (loss) per share basic & diluted	\$ 0.13	\$ 0.09	\$ (0.02)		
Weighted average shares outstanding basic and diluted	7,143	7,143	7,143		

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In reviewing the agreements included as exhibits to this Annual Report on Form 10-K, please remember they are included to provide you with information regarding their terms and are not intended to provide any other factual or disclosure information about Digimarc or the other parties to the agreements. The agreements may contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other party or parties to the applicable agreement and:

should not in all instances be treated as categorical statements of fact, but rather as a means of allocating the risk to one of the parties if those statements prove to be inaccurate;

may have been qualified by disclosures that were made to the other party or parties in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;

may apply standards of materiality in a manner that is different from what may be viewed as material to you or other investors; and

were made only as of the date of the applicable agreement or other date or dates that may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time. Additional information about Digimarc may be found elsewhere in this Annual Report on Form 10-K and in Digimarc's other public filings, which are available without charge through the SEC's website at <http://www.sec.gov>.

**EXHIBIT INDEX**

**Exhibit**

**Number**

**Exhibit Description**

- 2.1 Separation Agreement among DMRC Corporation, DMRC LLC, Digimarc Corporation and, with respect to certain sections, L-1 Identity Solutions, Inc. (incorporated by reference to Exhibit 2.1 to Amendment No. 2 to the Company's Registration Statement on Form 10, filed with the Commission on August 13, 2008 (File No. 001-34108))
- 3.1 Restated Certificate of Incorporation of Digimarc Corporation (incorporated by reference to Exhibit 3.1 to Amendment No. 3 to the Company's Registration Statement on Form 10, filed with the Commission on September 9, 2008 (File No. 001-34108))
- 3.2 Amended and Restated Bylaws of Digimarc Corporation (incorporated by reference to Exhibit 3.2 to Amendment No. 3 to the Company's Registration Statement on Form 10, filed with the Commission on September 9, 2008 (File No. 001-34108))
- 4.1 Specimen common stock certificate of Digimarc Corporation (incorporated by reference to Exhibit 4.1 to the Company's Annual Report on Form 10-K, filed with the Commission on February 27, 2009 (File No. 001-34108))
- 4.2 Rights Agreement, dated July 31, 2008, between Digimarc Corporation and Computershare Trust Company, N.A. as Rights Agent (incorporated by reference to Exhibit 4.2 to the Company's Annual Report on Form 10-K, filed with the Commission on February 27, 2009 (File No. 001-34108))
- 4.3 Form of Certificate of Designation of Series R Preferred Stock (attached as an exhibit to the Rights Agreement filed as Exhibit 4.2 hereto)
- 4.4 Form of Rights Certificate (attached as an exhibit to the Rights Agreement filed as Exhibit 4.2 hereto)
- 10.1 License Agreement between DMRC Corporation and L-1 Identity Solutions Operating Company (incorporated by reference to Exhibit 10.2 to Amendment No. 4 to the Company's Registration Statement on Form 10, filed with the Commission on October 2, 2008 (File No. 001-34108))(1)



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**Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
10.2	Agreement, dated as of October 1, 2007, between Digimarc Corporation and The Nielsen Company (incorporated by reference to Exhibit 10.3 to Amendment No. 6 to the Company's Registration Statement on Form 10, filed on October 14, 2008 (File No. 001-34108))(1)
10.3	Counterfeit Deterrence System Development and License Agreement, dated as of January 1, 1999, between Digimarc Corporation and the Bank for International Settlements (incorporated by reference to Exhibit 10.4 to Amendment No. 6 to the Company's Registration Statement on Form 10, filed with the Commission on October 14, 2008 (File No. 001-34108))(1)
*10.4	Form of Indemnification Agreement between DMRC Corporation and each of its executive officers and directors (incorporated by reference to Exhibit 10.5 to Amendment No. 2 to the Company's Registration Statement on Form 10, filed with the Commission on August 13, 2008 (File No. 001-34108))
*10.5	Employment Agreement, dated as of October 29, 2008, between Digimarc Corporation and Bruce Davis (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the Commission on November 4, 2008 (File No. 001-34108))
*10.6	Digimarc Corporation 2008 Incentive Plan (incorporated by reference to Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on November 24, 2008 (File No. 001-34108))
*10.7	Form of Notice of Stock Option Award and Stock Option Award Agreement under the Digimarc Corporation 2008 Incentive Plan (incorporated by reference to Exhibit 10.8 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on November 24, 2008 (File No. 001-34108))
*10.8	Equity Compensation Program for Nonemployee Directors under the Digimarc Corporation 2008 Incentive Plan (incorporated by reference to Exhibit 10.9 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on November 24, 2008 (File No. 001-34108))
*10.9	Form of Indemnification Agreement between Digimarc Corporation and each of its executive officers and directors (incorporated by reference to Exhibit 10.1 to Digimarc Corporation's Annual Report on Form 10-K, as filed by Digimarc Corporation with the Securities and Exchange Commission on March 13, 2006 (File No. 000-28317))
*10.10	Form of Change of Control Retention Agreement entered into by and between Digimarc Corporation and each of Messrs. McConnell and Chamness (included in Exhibit 10.10 to Digimarc Corporation's Annual Report on Form 10-K, as filed by Digimarc Corporation with the Securities and Exchange Commission on February 24, 2010 (File No. 001-34108))
10.11	Patent License Agreement, dated as of June 11, 2009 between Digimarc Corporation and The Nielsen Company (US), LLC (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on July 31, 2009 (File No. 001-34108))(2)
10.12	Limited Liability Company I Agreement, dated June 11, 2009 between Digimarc Corporation and The Nielsen Company (US), LLC (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on July 31, 2009 (File No. 001-34108))(2)
10.13	Limited Liability Company II Agreement, dated June 11, 2009 between Digimarc Corporation and The Nielsen Company (US), LLC (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on July 31, 2009 (File No. 001-34108))(2)

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**Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
21.1	Subsidiaries (included in Exhibit 21.1 to Digimarc Corporation's Annual Report on Form 10-K, as filed by Digimarc Corporation with the Securities and Exchange Commission on February 24, 2010 (File No. 001-34108))
23.1	Consent of Independent Registered Public Accounting Firm
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

\* Management contract or compensatory plan or arrangement.

The Separation Agreement contains a brief list identifying all schedules and exhibits thereto. Such schedules and exhibits have been omitted pursuant to Item 601(b)(2) of Regulation S-K. The Registrant agrees to furnish supplementally a copy of the omitted schedules and exhibits to the Securities and Exchange Commission upon request.

- (1) Confidential treatment has been granted for certain portions omitted from this exhibit pursuant to an order granted by the Commission on October 21, 2008, under Rule 24b-2 of the Securities Exchange Act of 1934, as amended. Confidential portions of this exhibit have been separately filed with the Securities and Exchange Commission.
- (2) Confidential treatment has been granted for certain portions omitted from this exhibit pursuant to an order granted by the Commission on September 10, 2009, under Rule 24b-2 of the Securities Exchange Act of 1934, as amended. Confidential portions of this exhibit have been separately filed with the Securities and Exchange Commission.