MICROVISION, INC.
Form 10-K
March 08, 2016

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

FORM 10-K

(Mark one)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

[ ] 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 001-34170

MicroVision, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**91-1600822**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

6244 185th Avenue NE, Suite 100
Redmond, Washington 98052

(Address of Principal Executive Offices, including Zip Code)

(425) 936-6847

(Registrant's Telephone Number, including Area Code)

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

Title of class	Name of exchange on which registered
Common Stock, $0.001 par value per share	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Exchange 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

o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes

o No x

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

x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files. Yes

x No o

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.

o

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer x	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes

o No x

The aggregate market value of the common stock held by non-affiliates of the registrant as of June 30, 2015 was approximately $141.6 million (based on the closing price for the registrant's common stock as reported by the NASDAQ Global Market on June 30, 2015 was $3.00 per share).

The number of shares of the registrant's common stock outstanding as of March 3, 2016 was 47,435,000.

Documents Incorporated by Reference

Portions of the registrant's definitive Proxy Statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the registrant's 2016 Annual Meeting of Shareholders (the "2016 Proxy Statement") are incorporated herein by reference in Part III of this Annual Report on Form 10-K to the extent stated herein.

MICROVISION, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE YEAR ENDED DECEMBER 31, 2015

TABLE OF CONTENTS

Part IV.

Item 15.

Exhibits, Financial Statement Schedules

Signatures

PART I

Preliminary Note Regarding Forward-Looking Statements

This report contains forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and is subject to the safe harbor created by those sections. Such statements may include, but are not limited to, projections of revenues, income or loss, capital expenditures, plans for product development and cooperative arrangements, technology development by third parties, future operations, financing needs or plans of MicroVision, Inc. ("we" or "us"), as well as assumptions relating to the foregoing. The words "anticipate," "could," "would," "believe," "estimate," "expect," "goal," "may," "plan," "project," "will," and similar expressions identify forward-looking statements. Factors that could cause actual results to differ materially from those projected in our forward-looking statements include risk factors identified below in Item 1A.

ITEM 1. BUSINESS

Overview

MicroVision, Inc. is a pioneer in laser beam scanning (LBS) technology that we market under our brand name PicoP®. We have developed our proprietary PicoP scanning technology that can be adopted by our customers to create high-resolution miniature projection and three-dimensional sensing and image capture solutions that use laser diodes as the light source. Our PicoP scanning technology incorporates our patented expertise in two-dimensional Micro-Electrical Mechanical Systems (MEMS), lasers, optics, and electronics to create a small form factor scanning engine with lower power needs than many other technologies that projects high-quality video and still image and/or uses depth sensing to capture three-dimensional data.

We have licensed our patented PicoP scanning technology to other companies for incorporation into their scanning engines for projection. We sell our licensees key components needed to produce the laser scanning engines and/or license our technology to collect a royalty for each scanning engine they sell. Companies to whom we license our PicoP scanning technology are typically original design manufacturers (ODMs) or original equipment manufacturers (OEMs) who are in the business of making component parts or products ready for sale to end users. To date, we have primarily focused on the consumer electronics market, however, we believe that our technology creates a platform that can support multiple applications and markets including enterprise, medical, industrial and automotive.

While we are optimistic about our technology and the potential for future revenues, we have incurred substantial losses since inception and we expect to incur a significant loss during the fiscal year ending December 31, 2016.

MicroVision, Inc. was founded in 1993 as a Washington corporation and reincorporated in 2003 under the laws of the State of Delaware. Our headquarters is located at 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052, and our telephone number is (425) 936-6847.

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports are available free-of-charge from the investor page of our website, www.microvision.com, as soon as reasonably practicable after such material is electronically filed with the Securities and Exchange Commission (SEC). Copies of these filings may also be obtained by visiting the Public Reference Room of the SEC at 100 F Street NE, Washington, D.C. 20549, or by calling the SEC directly at 1-800-SEC-0330 (1-800-732-0330). In addition, the SEC maintains a website, www.sec.gov, which contains current, quarterly and annual reports, proxy and information statements and other information regarding issuers that file electronically.

Technology

Our patented PicoP® scanning technology combines a MEMS scanning mirror, laser diode light sources, electronics, and optics that are controlled using our proprietary system control expertise. The bi-directional MEMS scanning mirror is a key component of our technology platform and is one of our core competencies. Our MEMS design is a silicon device with a one millimeter mirror at the center. This mirror is connected to small flexures that allow it to oscillate vertically and horizontally to capture (imaging) or reproduce (display) an image pixel-by-pixel. Our PicoP scanning technology creates a brilliant, full color, high-contrast, uniform display over the entire field-of-view, from a small and thin package. We believe that our proprietary technology offers significant advantages over traditional display and image capture systems. Depending on the specific product application, these advantages may include:

- Ability to perform projection and three-dimensional sensing and image capture from a single device;
- Focus-free operation;
- HD resolution;
- Low power requirements to enable battery operated devices and applications;
- Large screen size up to 200 inches from short distances;
- Small and thin package size;
- High-brightness, high-dynamic range, and brightness uniformity; and
- Rich, saturated color reproduction.

In addition to these advantages, an overarching benefit of our PicoP scanning technology is its ability to offer a key combination of lumens per watt per cubic centimeter: In essence, more lumens at lower power in a smaller form factor. Competing technologies may offer more lumens in total but not in as small and power efficient design as our PicoP scanning technology. This combination is of particular importance for small, portable devices operated by battery. Equally important for consumer ease-of-use and for mobile projection applications is the focus-free attribute of our PicoP scanning technology.

Business Strategy

Our business strategy is to commercialize our PicoP® scanning technology by enabling ODMs and OEMs to produce scanning engines by licensing our technology to those ODMs and OEMs, and by selling key scanning engine components to them, as needed. This approach will allow the ODMs and OEMs to integrate and embed our technology across a broad range of display and image capture product applications. We create product concept reference designs to enable ODMs and OEMs to develop and rapidly build products that capitalize on the benefits of our PicoP scanning technology. We are also developing value-added applications intended to help our customers differentiate their potential products. The key elements of our business strategy include the following:

- Continue to improve the performance of our PicoP scanning technology platform by advancing the optical system, drive electronics hardware and software design;
- Develop value-added features that complement our core technology;
- Partner with ODMs and OEMs to help them develop scanning engines based on our technology, and to help them integrate the engines into their products;
- Support ODMs to ensure availability of high-quality scanning engines in quantities to support the consumer electronics market;
- Supply key scanning engine components for products being developed by ODMs and OEMs who license our PicoP scanning technology and/or license rights to ODMs and OEMs to produce such components; and
- Maintain a position of LBS leadership with our intellectual property around our PicoP scanning technology.

Markets for Our Technology

Our approach is to create a platform centered on the core capabilities and features of PicoP® scanning technology that can support multiple applications and markets. We see pico projection and automotive head up display (HUD) as the most promising applications for our technology, and we have concentrated in these areas over the past several years. We believe augmented reality (AR) and virtual reality (VR) eyewear displays and three-dimensional sensing and image capture applications can also benefit from our technology, and we are actively exploring these opportunities.

Our primary objective for the pico projection market is to enable a large screen viewing experience produced by a small projector for mobile devices such as smartphones, tablets and other consumer electronics products. The scanning engine can either be embedded in the mobile device directly or in a small standalone companion product that is paired with the mobile device wirelessly or via a protocol such as HDMI. These potential products would allow users to watch digital videos, play games, and display images and other data onto a variety of surfaces, freeing users from the limitations of a small screen. Products that incorporate our PicoP scanning technology have been announced by our licensees and their customers in 2015.

For the automotive market, an engine using our PicoP scanning technology could be combined with other components and systems to form a HUD system to be embedded into a vehicle or integrated into a portable, standalone aftermarket

HUD. We have produced prototypes that demonstrate the ability of PicoP scanning technology to project high-resolution virtual images in the driver's field-of-view, providing the driver with a variety of information related to the vehicle's operation. We have also begun to investigate opportunities to apply our technology to emerging applications for in-car connectivity and infotainment systems.

Another possible application area for our PicoP scanning technology that we have refocused on in the past year is eyewear displays, also known as AR and VR. We have a long history with this application, and the eyewear ecosystem has progressed to a point where we see future growth opportunities. We are in the exploratory phases with prospective customers in identifying which AR and VR applications offer the most promise for our technology inside their future products.

In addition to the display and projection applications, our PicoP scanning technology has the ability to capture three-dimensional information. We believe there are market opportunities to use our technology to capture images and sense objects. We are in the early stages of identifying these opportunities and developing plans with prospective customers to leverage our competitive advantages in these areas.

Products and Services

In 2015, our revenue was primarily derived from the sale of our proprietary components and license and royalty fees for PicoP® scanning technology. The key components we offer for inclusion in a scanning engine are our MEMS and Application-Specific Integrated Circuits (ASICs). Our licensees can purchase none, some, or all of the key components we offer depending on their capability and desire to manufacture them and the terms of the licensing agreement. In our business model, license and royalty can be standalone fees separate from the component prices, or in some cases, included in the component pricing.

In addition to product sales and license and royalty fees, we generate revenue from engineering services for custom development and support services for our customers. Historically, our engineering services from collaborative research and development and contract agreements have been a significant portion of our total revenue. In 2015, we transitioned our focus more to product sales and royalty revenue, and engineering services has become a smaller part of our business. We expect product sales and royalty revenue to be a significant portion of our total revenue in the future.

Research and Development

We believe our research and development efforts have placed us in a leadership position in the field of LBS technology as applied to consumer electronics, automotive and other markets. Our ability to attract customers and grow revenue will depend on our ability to maintain our LBS technology leadership, continually improve performance, reduce costs, reduce the size of component parts and scanning engines, and increase the number of applications and products enabled by our PicoP® scanning technology.

Our research and development team is located in Redmond, Washington and as of December 31, 2015, was comprised of 41 engineering and technical staff in optics, software engineering, electrical engineering, and MEMS design.

Sales and Marketing

Our sales and marketing approach is account based, business-to-business targeting of ODMs and OEMs. We license our PicoP® scanning technology and sell components used in the production of scanning engines. Our customers are typically companies that produce scanning engines incorporating our patented PicoP scanning technology. We also engage end product manufacturers and retailers in our target markets to educate them about product opportunities based on our PicoP scanning technology. From these efforts, we work with our licensees to pair them with the end product companies that are interested in proceeding with a product or products incorporating PicoP scanning technology.

We currently have sales representatives, primarily based in the United States, focused on business development in the Americas, Europe and Asia. Our sales representatives are supported by a technical sales engineering team that assists customers during the "design win" and "design in" cycles. The technical sales engineering team operates from

Redmond, Washington. Our marketing team is located in Redmond, Washington. We engage potential customers directly, participate in trade shows, use social media, and maintain a website.

Manufacturing

We currently use contract manufacturers to produce the products we sell to our licensees. Our products are components that are integral to a scanning engine incorporating our PicoP® scanning technology and include MEMS and ASICs that incorporate our designs and are produced to order by semiconductor foundries. The MEMS die that are manufactured by a contract manufacturer are consigned to a separate contract manufacturer for assembly into a MEMS package according to our specifications.

Our manufacturing is not currently subject to seasonal variations as our shipments have been relatively small and are in the early stages of product introduction. In the future, depending on our customers' product mix, we may be affected by seasonal fluctuations which could affect working capital demands.

We provide forecasts that allow our contract manufacturers to stock component parts and other materials and plan capacity. Our contract manufacturers procure raw materials in volumes consistent with our forecasts, manufacture and/or assemble the products and perform tests according to our specifications. Products are either shipped to our customers or shipped to our Redmond, Washington headquarters to be inventoried as finished goods. With the exception of the MEMS die we consign and retain title to, we generally do not own any raw materials procured by our contract manufacturers. Title to the products transfers from our contract manufacturers to us and then to our customers upon shipment from the manufacturer. If raw materials are unused, or the products are not sold within specified periods of time, we may incur carrying charges or obsolete material charges for component parts that our contract manufacturers purchased to build products to meet our forecasts or customer orders.

Many of the raw materials used in our components are standard to the consumer electronics industry. Our MEMS, MEMS die, and ASICs are currently manufactured to our specifications by separate single-source suppliers.

Human Factors, Ergonomics and Safety

We work with third party independent experts in the field of laser safety to assist in meeting safety specifications. In addition, we monitor developments in the area of permissible laser exposure limits as established by International Electrotechnical Commission (IEC) and others. Independent experts have concluded that laser exposure to the eye resulting from use of LBS devices under normal operating conditions would be below the calculated maximum permissible exposure level set by the IEC.

Competitive Conditions

The information display and image capture industry is highly competitive. Potential products incorporating our PicoP® scanning technology will compete with manufacturers of established technologies, such as miniaturized cathode ray tube and flat panel display devices, as well as companies developing new display and image capture technologies. Our competitors include companies such as Texas Instruments, Intel, Micron Technology, Syndiant, and others, some of which have much greater financial, technical and other resources than us. Many of our competitors are currently developing alternative miniature display and image capture technologies. Our competitors may succeed in developing innovative technologies and products that could render our technology or our proposed products commercially infeasible or technologically obsolete.

Pico projectors are an emerging class of miniaturized projectors that are generally handheld, battery operated, mobile projectors. Most of the competing projectors currently on the market are either liquid crystal on silicon (LCOS) panel solutions or Texas Instruments' DLP™ display technology primarily using light-emitting diode (LED) light sources. Each of these projection solutions can create images of varying resolution, brightness, image quality, battery life, and ease of use.

The information display and image capture industry has been characterized by rapid and significant technological advances. Our PicoP scanning technology platform and potential products may not remain competitive with such advances, and we may not have sufficient funds to invest in new technologies, products or processes. Although we believe our technology platform and proposed products could deliver images of a substantially higher quality and resolution from a smaller form factor device than those of commercially available miniaturized liquid crystal displays (LCD) and cathode ray tube based display products, manufacturers of competing technologies may develop further improvements to screen display and image capture technology that could reduce or eliminate the anticipated advantages of our proposed products.

Intellectual Property and Proprietary Rights

We create intellectual property from three sources: internal research and development activities, technology acquisitions, and performance on development contracts. The inventions covered by our patent applications generally relate to systems controls in our PicoP® scanning technology, component miniaturization, power reduction, feature enhancements, specific implementation of various system components, and design elements to facilitate mass production. Protecting these key-enabling technologies and components is a fundamental aspect of our strategy to penetrate diverse markets with unique products. As such, we intend to continue to develop our portfolio of proprietary and patented LBS technologies at the system, component, and process levels.

We believe our extensive patent portfolio is the largest, broadest, and earliest filed LBS technology portfolio and includes applications such as automotive HUD, augmented reality, range finding, portable media devices, image capture, and projection applications. We have over 500 issued patents, pending patents and licensed patents worldwide.

Since our inception in 1993, we have acquired under license agreements exclusive rights to various LBS technologies, including, among others, rights related to the ability to superimpose images on the user's field-of-view with a retinal display, and rights related to the design and fabrication of micro-miniature devices using semiconductor fabrication techniques. In some cases, the licensors have retained limited, non-commercial rights with respect to the technology, including the right to use the technology for non-commercial research and for instructional purposes.

Our ability to compete effectively in the information display and image capture markets may depend, in part, on our ability and the ability of our licensors to maintain the proprietary nature of these technologies.

We also rely on unpatented proprietary technology. To protect our rights in these areas, we require all employees, and where appropriate, contractors, consultants, advisors and collaborators, to enter into confidentiality and non-compete agreements. There can be no assurance, however, that these agreements will provide meaningful protection for our trade secrets, know-how or other proprietary information in the event of any unauthorized use, misappropriation or disclosure of such trade secrets, know-how or other proprietary information.

We have registered the name "PicoP®" and have filed for the registration of various other marks with the United States Patent and Trademark Office.

Employees

As of March 3, 2016, we had 67 full-time employees. None of our employees are represented by a labor union.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below together with the other information set forth in this report, which could materially affect our business, financial condition and future results. The risks described below are not the only risks facing our company. Risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and operating results.

Risk Factors Related to Our Business and Industry

We have a history of operating losses and expect to incur significant losses in the future.

We have had substantial losses since our inception. We cannot assure you that we will ever become or remain profitable.

- As of December 31, 2015, we had an accumulated deficit of $483.4 million.
- We incurred consolidated net losses of $437.6 million from inception through 2012, $13.2 million in 2013, $18.1 million in 2014, and $14.5 million in 2015.

The likelihood of our success must be considered in light of the expenses, difficulties and delays frequently encountered by companies formed to develop and commercialize new technologies. In particular, our operations to date have focused primarily on research and development of our PicoP® scanning technology platform and development of demonstration units. We are unable to accurately estimate future revenues and operating expenses based upon historical performance.

We cannot be certain that we will succeed in obtaining additional development revenue or commercializing our technology or products. In light of these factors, we expect to continue to incur significant losses and negative cash flow at least through 2016 and likely thereafter. We cannot be certain that we will achieve positive cash flow at any time in the future.

We will require additional capital to fund our operations and to implement our business plan. If we do not obtain additional capital, we may be required to curtail our operations substantially. Raising additional capital may dilute the value of current shareholders' shares.

Based on our current operating plan, and assuming no additional funds from our existing At-the-Market (ATM) facility, we anticipate that we have sufficient cash and cash equivalents to fund our operations through June 2016. We will require additional cash to fund our operating plan past that time. We plan to obtain additional cash through the issuance of equity or debt securities and/or product sales and licensing activities.

We are introducing new technology into an emerging market which creates significant uncertainty about our ability to accurately project revenue, costs and cash flows. Our capital requirements will depend on many factors, including, but not limited to, the rate at which ODMs and OEMs introduce products incorporating our PicoP® scanning technology and the market acceptance and competitive position of such products. If revenues are less than we anticipate, if the mix of revenues and the associated margins varies from anticipated amounts or if expenses exceed the amounts budgeted, we may require additional capital earlier than expected to fund our operations. In addition, our operating plan provides for the development of strategic relationships with suppliers of components, products and systems, and equipment manufacturers that may require additional investments by us.

Additional capital may not be available to us, or if available, on terms acceptable to us or on a timely basis. Raising additional capital may involve issuing securities with rights and preferences that are senior to our common stock and may dilute the value of our current shareholders' shares. If adequate funds are not available on a timely basis, we may consider limiting our operations substantially to extend funds as we pursue other financing opportunities and business relationships. This limitation of operations could include reducing investments in our production capabilities or research and development projects, staff, operating costs, and capital expenditures. Reducing operations may jeopardize our ability to achieve our business goals or satisfy our customer requirements.

Qualifying a new or alternative contract manufacturer or foundry for our products could cause us to experience delays that result in lost revenues and damaged customer relationships.

We rely on single or limited-source suppliers to manufacture our products, including our MEMS die in wafer form. The lead time to establish a relationship with a new or alternative contract manufacturer(s) or foundry is a time-consuming process, as our unique technology may require significant manufacturing process adaptation to achieve full manufacturing capacity. Accordingly, we may be unable to establish a relationship with new or alternative contract manufacturers in the short-term, or at all, at prices or on other terms that are acceptable to us.

Changes in our supply chain may result in increased cost and delay and may subject us to risks and uncertainties regarding, but not limited to, product warranty, product liability and quality control standards. The loss of any single or limited-source supplier, the failure of any of these suppliers to perform as expected or the disruption in the supply chain of components from these suppliers could cause significant delays in product deliveries, which may result in lost revenues and damaged customer relationships. To the extent that we are not able to establish a relationship with a new or alternative contract manufacturer(s) or foundry in a timely manner, we may be unable to meet contract or production milestones, which could have a material adverse effect on our financial condition, results of operations and cash flows.

Our success will depend, in part, on our ability to secure significant third party manufacturing resources.

Our success will depend, in part, on our ability to provide our components and future products in commercial quantities at competitive prices and on schedule. Accordingly, we will be required to obtain access, through business partners or contract manufacturers, to manufacturing capacity and processes for the commercial production of our expected future products.

Our foreign contract manufacturers could experience severe financial difficulties or other disruptions in their business, and such continued supply could be significantly reduced or terminated. In addition, we cannot be certain that we will successfully obtain access to needed manufacturing resources concurrent with a significant increase in our planned production levels. Future manufacturing limitations of our suppliers could constrain the number of products that we are able to develop and produce.

We are dependent on third parties in order to develop, manufacture, sell and market products incorporating our PicoP

® scanning technology and the scanning engine components.

Our business strategy for commercializing our technology in products incorporating PicoP scanning technology includes entering into development, manufacturing, sales and marketing arrangements with ODMs, OEMs and other third parties. These arrangements reduce our level of control over production and distribution and may subject us to risks and uncertainties regarding, but not limited to, product warranty, product liability and quality control standards. We cannot be certain that we will be able to negotiate arrangements on acceptable terms, if at all, or that these arrangements will be successful in yielding commercially viable products. If we cannot establish these arrangements, we would require additional capital to undertake such activities on our own and would require extensive manufacturing, sales and marketing expertise that we do not currently possess and that may be difficult to obtain.

In addition, we could encounter significant delays in introducing our PicoP scanning technology or find that the development, manufacture or sale of products incorporating our technology would not be feasible. To the extent that we enter into development, manufacturing, sales and marketing or other arrangements, our revenues will depend upon the performance of third parties. We cannot be certain that any such arrangements will be successful.

We cannot be certain that our technology platform or products incorporating our PicoP

® scanning technology will achieve market acceptance. If our technology platform or products incorporating our technology do not achieve market acceptance, our revenues may not grow.

Our success will depend in part on customer acceptance of our PicoP scanning technology. Our technology may not be accepted by manufacturers who use display and image capture technologies in their products, by systems integrators, ODMs, and OEMs who incorporate the scanning engine components into their products or by end users of these products. To be accepted, our PicoP scanning technology must meet the expectations of our current and potential customers in the consumer electronics, automotive, and other markets. If our technology platform or products incorporating our PicoP scanning technology do not achieve market acceptance, we may not be able to continue to develop our technology.

Future products incorporating our PicoP

® scanning technology are dependent on advances in technology by other companies.

Our PicoP scanning technology will continue to rely on technologies, such as laser light sources and other components that are developed and produced by other companies. The commercial success of certain future products incorporating our PicoP scanning technology will depend, in part, on advances in these and other technologies by other companies. We may, from time to time, contract with and support companies developing key technologies in order to accelerate the development of them for our or our customers' specific uses. There are no guarantees that such activities will result in useful technologies or products that will be profitable.

We are dependent on a small number of customers for our revenue. Our quarterly performance may vary substantially and this variance, as well as general market conditions, may cause our stock price to fluctuate greatly and potentially expose us to litigation.

In 2015, 98% of our total revenue was generated from sales to one commercial customer. In 2014 and 2013, two commercial customers in each year accounted for 65% and 86% of our revenue, respectively. Our customers take time to obtain, and the loss of a significant customer could negatively affect our revenue. Our quarterly operating results may vary significantly based upon:

- Market acceptance of products incorporating our PicoP® scanning technology;
- Changes in evaluations and recommendations by any securities analysts following our stock or our industry generally;
- Announcements by other companies in our industry;

- Changes in business or regulatory conditions;
- Announcements or implementation by our competitors of technological innovations or new products;
- The status of particular development programs and the timing of performance under specific development agreements;
- Economic and stock market conditions; or
- Other factors unrelated to our company or industry.

In one or more future quarters, our results of operations may fall below the expectations of securities analysts and investors and the trading price of our common stock may decline as a consequence. In addition, following periods of volatility in the market price of a company's securities, shareholders often have instituted securities class action litigation against that company. If we become involved in a class action suit, it could divert the attention of management and, if adversely determined, could require us to pay substantial damages.

We or our customers may fail to perform under open orders, which could adversely affect our operating results and cash flows.

Our backlog of open orders totaled $11.0 million as of December 31, 2015. We may be unable to meet the performance requirements, including performance specifications or delivery dates, required by such purchase orders. Furthermore, our customers may be unable or unwilling to perform their obligations thereunder on a timely basis, or at all if, among other reasons, our products and technologies do not achieve market acceptance, our customers' products and technologies do not achieve market acceptance or our customers otherwise fail to achieve their operating goals. To the extent we are unable to perform under such purchase orders or to the extent customers are unable or unwilling to perform, our operating results and cash flows could be adversely affected.

It may become more difficult to sell our stock in the public market or maintain our listing on the NASDAQ Global Market.

Our common stock is listed on The NASDAQ Global Market. To maintain our listing on this market, we must meet NASDAQ's listing maintenance standards. If we are unable to continue to meet NASDAQ's listing maintenance standards for any reason, our common stock could be delisted from The NASDAQ Global Market. If our common stock were delisted, we likely would seek to list our common stock on The NASDAQ Capital Market, the American Stock Exchange or on a regional stock exchange. Listing on such other market or exchange could reduce the liquidity of our common stock. If our common stock were not listed on The NASDAQ Capital Market or an exchange, trading of our common stock would be conducted in the Over-the-Counter (OTC) market on an electronic bulletin board established for unlisted securities or directly through market makers in our common stock. If our common stock were to trade in the OTC market, an investor would find it more difficult to dispose of, or to obtain accurate quotations for the price of, the common stock.

A delisting from The NASDAQ Global Market and failure to obtain listing on another market or exchange would subject our common stock to so-called penny stock rules that impose additional sales practice and market-making requirements on broker-dealers who sell or make a market in such securities. Consequently, removal from The NASDAQ Global Market and failure to obtain listing on another market or exchange could affect the ability or willingness of broker-dealers to sell or make a market in our common stock and the ability of purchasers of our common stock to sell their securities in the secondary market.

On March 3, 2016, the closing price of our common stock was $2.91 per share.

Our lack of financial and technical resources relative to our competitors may limit our revenues, potential profits, overall market share or value.

Our products and potential products incorporating our PicoP® scanning technology will compete with established manufacturers of existing products and companies developing new technologies. Many of our competitors have substantially greater financial, technical and other resources than we have. Because of their greater resources, our

competitors may develop products or technologies that may be superior to our own. The introduction of superior competing products or technologies could result in reduced revenues, lower margins or loss of market share, any of which could reduce the value of our business.

We may not be able to keep up with rapid technological change and our financial results may suffer.

The information display and image capture industry has been characterized by rapidly changing technology, accelerated product obsolescence and continuously evolving industry standards. Our success will depend upon our ability to further develop our PicoP® scanning technology platform and to cost effectively introduce new products and features in a timely manner to meet evolving customer requirements and compete with competitors' product advances. We may not succeed in these efforts due to:

- Delays in product development;
- Lack of market acceptance for our technology or products incorporating our PicoP scanning technology; or
- Lack of funds to invest in product research, development and marketing.

The occurrence of any of the above factors could result in decreased revenues, market share and value of our business.

We could face lawsuits related to our use of PicoP® scanning technology or other technologies. Defending these suits would be costly and time-consuming. An adverse outcome, in any such matter, could limit our ability to commercialize our technology or products incorporating our PicoP scanning technology, reduce our revenues and increase our operating expenses.

We are aware of several patents held by third parties that relate to certain aspects of light scanning displays and image capture products. These patents could be used as a basis to challenge the validity, limit the scope or limit our ability to obtain additional or broader patent rights of our patents or patents we have licensed. A successful challenge to the validity of our patents or patents we have licensed could limit our ability to commercialize our technology or products incorporating our PicoP scanning technology and, consequently, materially reduce our revenues. Moreover, we cannot be certain that patent holders or other third parties will not claim infringement by us with respect to current and future technology. Because U.S. patent applications are held and examined in secrecy, it is also possible that presently pending U.S. applications will eventually be issued with claims that will be infringed by our products or our technology.

The defense and prosecution of a patent suit would be costly and time-consuming, even if the outcome were ultimately favorable to us. An adverse outcome in the defense of a patent suit could subject us to significant costs, require others and us to cease selling products incorporating our technology, require us to cease licensing our technology or require disputed rights to be licensed from third parties. Such licenses, if available, would increase our operating expenses. Moreover, if claims of infringement are asserted against our future co-development partners or customers, those partners or customers may seek indemnification from us for any damages or expenses they incur.

If we fail to manage expansion effectively, our revenue and expenses could be adversely affected.

Our ability to successfully offer products incorporating PicoP® scanning technology and implement our business plan in a rapidly evolving market requires an effective planning and management process. The growth in business and relationships with customers and other third parties has placed, and will continue to place, a significant strain on our management systems and resources. We will need to continue to improve our financial and managerial controls, reporting systems and procedures, and will need to continue to train and manage our work force.

If we fail to adequately reduce and control our manufacturing, supply chain and operating costs, our business, financial condition, and operating results could be adversely affected.

We incur significant costs related to procuring components and increasing our production capabilities to manufacture our products. We may experience delays, cost overruns or other unexpected costs associated with an increase in production. If we are unsuccessful in our efforts to reduce and control our manufacturing, supply chain and operating costs and keep costs aligned with the levels of revenues we generate, our business and financial condition could

suffer.

Our technology and products incorporating our PicoP

® scanning technology may be subject to future environmental, health and safety regulations that could increase our development and production costs.

Our technology and products incorporating our PicoP scanning technology could become subject to future environmental, health and safety regulations or amendments that could negatively impact our ability to commercialize our technology and products incorporating our PicoP scanning technology. Compliance with any such new regulations

would likely increase the cost to develop and produce products incorporating our PicoP scanning technology, and violations may result in fines, penalties or suspension of production. If we become subject to any environmental, health, or safety laws or regulations that require us to cease or significantly change our operations to comply, our business, financial condition and operating results could be adversely affected.

Our operating results may be adversely impacted by worldwide political and economic uncertainties and specific conditions in the markets we address.

In the recent past, general worldwide economic conditions have experienced a downturn due to slower economic activity, concerns about inflation, increased energy costs, decreased consumer confidence, reduced corporate profits and capital spending, and adverse business conditions. Any continuation or worsening of the current global economic and financial conditions could materially adversely affect: (i) our ability to raise, or the cost of, needed capital, (ii) demand for our current and future products, and (iii) our ability to commercialize products. We cannot predict the timing, strength, or duration of any economic slowdown or subsequent economic recovery, worldwide, regionally or in the display industry.

Because we plan to continue using foreign contract manufacturers, our operating results could be harmed by economic, political, regulatory and other factors in foreign countries.

We currently use foreign contract manufacturers and plan to continue to use foreign contract manufacturers to manufacture current and future products, where appropriate. These international operations are subject to inherent risks, which may adversely affect us, including, but not limited to:

- Political and economic instability;
- High levels of inflation, historically the case in a number of countries in Asia;
- Burdens and costs of compliance with a variety of foreign laws, regulations and sanctions;
- Foreign taxes and duties;
- Changes in tariff rates or other trade and monetary policies; and
- Changes or volatility in currency exchange rates and interest rates.

Our contract manufacturers' facilities could be damaged or disrupted by a natural disaster or labor strike, either of which would materially affect our financial position, results of operations and cash flows.

A major catastrophe, such as an earthquake, monsoon, flood or other natural disaster, labor strike, or work stoppage at our contract manufacturers' facilities, our suppliers, or our customers, could result in a prolonged interruption of our business. A disruption resulting from any one of these events could cause significant delays in product shipments and the loss of sales and customers, which could have a material adverse effect on our financial condition, results of operations, and cash flows.

If our licensors and we are unable to obtain effective intellectual property protection for our products, processes and technology, we may be unable to compete with other companies.

Intellectual property protection for our products, processes and technology is important and uncertain. If we do not obtain effective intellectual property protection for our products, processes and technology, we may be subject to increased competition. Our commercial success will depend, in part, on our ability and the ability of our licensors, to maintain the proprietary nature of our PicoP® scanning technology and other key technologies by securing valid and enforceable patents and effectively maintaining unpatented technology as trade secrets.

We protect our proprietary PicoP scanning technology by seeking to obtain United States and foreign patents in our name, or licenses to third party patents, related to proprietary technology, inventions, and improvements that may be important to the development of our business. However, our patent position and the patent position of our licensors involve complex legal and factual questions. The standards that the United States Patent and Trademark Office and its

foreign counterparts use to grant patents are not always applied predictably or uniformly and can change.

Additionally, the scope of patents are subject to interpretation by courts and their validity can be subject to challenges and defenses, including challenges and defenses based on the existence of prior art. Consequently, we cannot be certain as to the extent to which we will be able to obtain patents for our new products and technology or the extent to

which the patents that we already own or license from others, protect our products and technology. Reduction in scope of protection or invalidation of our licensed or owned patents, or our inability to obtain new patents, may enable other companies to develop products that compete directly with ours on the basis of the same or similar technology.

We also rely on the law of trade secrets to protect unpatented know-how and technology to maintain our competitive position. We try to protect this know-how and technology by limiting access to the trade secrets to those of our employees, contractors and partners, with a need-to-know such information and by entering into confidentiality agreements with parties that have access to it, such as our employees, consultants and business partners. Any of these parties could breach the agreements and disclose our trade secrets or confidential information, or our competitors might learn of the information in some other way. If any trade secret not protected by a patent were to be disclosed to or independently developed by a competitor, our competitive position could be negatively affected.

We could be subject to significant product liability claims that could be time-consuming and costly, divert management attention and adversely affect our ability to obtain and maintain insurance coverage.

We could be subject to product liability claims if any of the product applications are alleged to be defective or cause harmful effects. For example, because some of the scanning engines incorporating our PicoP® scanning technology could scan a low power beam of colored light into the user's eye, the testing, manufacture, marketing and sale of these products involve an inherent risk that product liability claims will be asserted against us.

Additionally, any misuse of our technology or products incorporating our PicoP scanning technology by end users or third parties that obtain access to our technology, could result in negative publicity and could harm our brand and reputation. Product liability claims or other claims related to our products or our technology, regardless of their outcome, could require us to spend significant time and money in litigation, divert management time and attention, require us to pay significant damages, harm our reputation or hinder acceptance of our products. Any successful product liability claim may prevent us from obtaining adequate product liability insurance in the future on commercially desirable or reasonable terms. An inability to obtain sufficient insurance coverage at an acceptable cost or otherwise to protect against potential product liability claims could prevent or inhibit the commercialization of our products and our PicoP scanning technology.

Our contracts and collaborative research and development agreements have long sales cycles, which makes it difficult to plan our expenses and forecast our revenues.

Our contracts and collaborative research and development agreements have long sales cycles that involve numerous steps including determining the product application, exploring the technical feasibility of a proposed product, evaluating the costs of manufacturing a product or qualifying a new or alternative contract manufacturer for production. Our long sales cycle, which can last several years, makes it difficult to predict the quarter in which revenue recognition will occur. Delays in entering into contracts and collaborative research and development agreements could cause significant variability in our revenues and operating results for any particular period.

Our contracts and collaborative research and development agreements may not lead to any product or any products that will be profitable.

Our contracts and collaborative research and development agreements, including without limitation, those discussed in this document, are exploratory in nature and are intended to develop new types of products for new applications. Our efforts may prove unsuccessful and these relationships may not result in the development of any product or any products that will be profitable.

Loss of any of our key personnel could have a negative effect on the operation of our business.

Our success depends on our executive officers and other key personnel and on the ability to attract and retain qualified new personnel. Achievement of our business objectives will require substantial additional expertise in the areas of sales and marketing, research and product development and manufacturing. Competition for qualified personnel in these fields is intense, and the inability to attract and retain additional highly skilled personnel, or the loss of key personnel, could hinder our ability to compete effectively in the display and image capture markets and adversely affect our business strategy execution and results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We currently lease approximately 23,900 square feet of combined use office, laboratory and manufacturing space at our corporate headquarters in Redmond, Washington. The 65 month lease expires in January 2019.

ITEM 3. LEGAL PROCEEDINGS

On March 31, 2014, Asia Optical Co., Inc., a supplier pursuant to an agreement entered into in 2008, filed a complaint for arbitration with the American Arbitration Association claiming that we ordered products from them and failed to take delivery of and pay for such products. The relief sought in the complaint is $3.6 million plus attorneys' fees, interest and arbitration costs. We contest the claim and are defending against it. An adverse outcome of these proceedings could materially and adversely affect our financial condition. At this stage, we cannot predict the likelihood of an unfavorable outcome or the range of potential loss.

We are also subject to various claims and pending or threatened lawsuits in the normal course of business. We are not currently party to any other legal proceedings that we believe are reasonably possible to have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 4A. EXECUTIVE OFFICERS OF THE REGISTRANT

Executive officers are appointed by our Board of Directors and hold office until their successors are elected and duly qualified. The following persons serve as executive officers of MicroVision, Inc.:

Alexander Y. Tokman, age 54, has served as President, Chief Executive Officer and Director of MicroVision since January 2006. Mr. Tokman served as MicroVision's President and Chief Operating Officer from July 2005 to January 2006. Mr. Tokman, joined MicroVision after a 10-year tenure at GE Healthcare, a subsidiary of General Electric, where he led several global businesses, most recently as General Manager of its Global Molecular Imaging and Radiopharmacy multi-technology business unit from 2003 to 2005. Prior to that, between 1995 and 2003, Mr. Tokman served in various cross-functional and cross-business leadership roles at GE where he led the definition and commercialization of several medical modalities product segments including PET/CT, which added over $500 million of revenue growth to the company within the first three years of its commercial introduction. Mr. Tokman is a certified Six Sigma and Design for Six Sigma (DFSS) Black Belt and Master Black Belt and as one of GE's Six Sigma pioneers, he drove the quality culture change across GE Healthcare in the late 1990s. From November 1989 to March 1995, Mr. Tokman served as new technologies programs lead and the head of the I&RD office at Tracor Applied Sciences, a subsidiary of then Tracor, Inc. Mr. Tokman holds a B.S. and an M.S. in electrical engineering from the University of Massachusetts, Dartmouth.

Stephen P. Holt, age 53, joined MicroVision in April 2013 as Chief Financial Officer. Prior to MicroVision, from May 2007 to May 2012, he served as Chief Financial Officer of PixelOptics, where he played a lead role in bringing the company's first electronic focusing eyewear product to market. At this venture capital-backed start-up, Mr. Holt raised capital and negotiated strategic partner agreements to license technology in addition to implementing policies and procedures to create an infrastructure capable of supporting rapid growth while maintaining a strong internal control

environment. From March 2006 to April 2007, he was the Chief Financial Officer of Interstate Distributors, a trucking and transportation services company. From December 2003 to March 2006, he was the Chief Financial Officer of a group of companies consisting of Activelight, Boxlight, Cinelight and Projector Wholesale Supply. These companies were value-added resellers and distributors of audio-visual and projection equipment. Mr. Holt, a Certified Management Accountant, holds a B.S. from California State University, Chico and an M.B.A. from Santa Clara University.

David J. Westgor, age 62, was appointed Vice President, General Counsel and Secretary in November 2013, after serving as General Counsel since December 2012 and Deputy General Counsel since June 2007. In his current role, Mr. Westgor oversees the legal department, advises the Board of Directors and executive team on corporate governance matters, and provides support for the company's business activities. Before joining MicroVision, Mr. Westgor was Senior Counsel at Medtronic Physio-Control, where he had primary responsibility for the legal affairs of its medical and informatics business units. Mr. Westgor graduated from Loyola Law School and practiced in the Los Angeles office of Pillsbury Winthrop. He moved to the Seattle area to become in-house counsel at Advanced Radio Telecom, a broadband telecommunications company. Mr. Westgor holds a B.A. from St. Olaf College and an M.F.A. degree from the Art Institute of Chicago.

Dale E. Zimmerman, age 56, has served as Vice President of Research and Development since June 2012 and as Director of Systems Engineering from June 2011 to May 2012. Prior to MicroVision, from February 2006 to December 2008, he served as Vice President of Product Strategy of Silicon Image, a company specializing in high speed serial interface solutions for HDTV, PC and storage products. From 1996 to 2006, he served as General Manager of DLP TV for Texas Instruments, where he played an important role in launching the first conference room projectors, home theater projectors, and HDTVs. His teams have received many awards, including three Emmys and CES Innovation Best of Show. He holds both a B.S. and an M.S. degree in electrical and electronics engineering from Massachusetts Institute of Technology (MIT) and a second M.S. in electrical engineering from Stanford University.

PART II.

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock began trading publicly on August 27, 1996. Our common stock trades on The NASDAQ Global Market under the ticker symbol "MVIS." We have never declared or paid cash dividends on our common stock. We currently anticipate that we will retain all future earnings to fund the operations of our business and do not anticipate paying dividends on the common stock in the foreseeable future.

As of March 3, 2016, there were approximately 113 holders of record of 47,435,000 shares of common stock outstanding. As many of our shares of common stock are held by brokerages and institutions on behalf of shareholders, we are unable to estimate the total number of beneficial holders of our common stock represented by these record holders.

	Common Stock	
Quarter Ended	**HIGH**	**LOW**
2014		
March 31, 2014	$ 3.38	$ 1.12
June 30, 2014	2.36	1.49
September 30, 2014	2.43	1.75
December 31, 2014	2.04	1.59
2015		
March 31, 2015	$ 4.23	$ 1.72
June 30, 2015	3.88	2.86
September 30, 2015	3.54	2.56
December 31, 2015	3.47	2.20
January 1, 2016 to March 3, 2016	$ 3.08	$ 2.28

ITEM 6. SELECTED FINANCIAL DATA

A summary of selected financial data as of and for the five years ended December 31, 2015 is set forth below. It should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this annual report on Form 10-K. A 1:8 reverse stock split of our common stock became effective on February 17, 2012. The share and per share amounts discussed and shown in the tables below have been adjusted to reflect the reverse

stock split.

(In thousands, except per share data)	Year Ended December 31, 2015	2014	2013	2012	2011
Statement of Operations Data					
Revenue	$ 9,188	$ 3,485	$ 5,852	$ 8,365	$ 5,617
Net loss available for common shareholders	(14,542)	(18,120)	(13,178)	(22,693)	(35,808)
Basic and diluted net loss per share	(0.31)	(0.44)	(0.47)	(1.05)	(2.57)
Weighted-average shares outstanding basic and diluted	46,540	41,599	28,025	21,595	13,919
Balance Sheet Data					
Cash and cash equivalents	$ 7,888	$ 8,349	$ 5,375	$ 6,850	$ 13,075
Working capital (deficit)	3,371	5,040	(3,878)	1,831	5,913
Total assets	14,042	11,945	8,447	12,938	23,870
Long-term liabilities	6,491	488	481	20	326
Total shareholders' equity (deficit)	(153)	6,872	(1,696)	5,054	10,802

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Our business strategy is to commercialize our PicoP® scanning technology by enabling ODMs and OEMs to produce scanning engines by licensing our technology to those ODMs and OEMs, and by selling key scanning engine components to them, as needed. In 2013 and 2014, our revenues were primarily derived from engineering services from collaborative research and development and contract agreements. In 2015, our revenue was primarily generated from product sales and royalty revenue, and engineering services has become a smaller part of our business. We expect product sales and royalty revenue to be a significant portion of our total revenue in the future.

In 2015, 70% of our revenue was generated from product sales, 17% was generated from performance on contracts, 13% was generated from royalties, and no revenue was generated from performance on collaborative research and development agreements. Sony Corporation accounted for 98% of our total revenue in 2015.

In 2014, 49%

of our revenue was generated from performance on collaborative research and development agreements, 40% was generated from performance on contracts, 10% was generated from product sales, and 1% was generated from royalties. Two commercial customers accounted for 65% of our total revenue in 2014.

In 2013, 50% of our revenue was generated from performance on collaborative research and development agreements, 39% was generated from product sales, 10% was generated from performance on contracts, and 1% was generated from royalties. Two commercial customers accounted for 86% of our total revenue in 2013.

We have incurred substantial losses since inception and expect to incur a significant loss during the fiscal year ending December 31, 2016.

We have received a report from our independent registered public accounting firm regarding the consolidated financial statements for the year ended December 31, 2015 that includes an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern. These financial statements were prepared assuming we will continue as a going concern.

Key accounting policies and estimates

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that materially affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent liabilities. We evaluate our estimates on a continuous basis. We base our estimates on historical data, terms of existing contracts, our evaluation of trends in the display and image capture industries, information provided by our

current and prospective customers and strategic partners, information available from other outside sources and on various other assumptions we believe to be reasonable under the circumstances. The results form the basis for making judgments regarding 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.

We believe the following key accounting policies require significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue recognition

We recognize revenue when: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred and there are no uncertainties regarding customer acceptance, (iii) fees are fixed or determinable, and (iv) collection is reasonably assured.

We generate revenue from many sources and activities. We enter into arrangements that can include various combinations of product sales, services, and licensing activities. For multiple-element arrangements, we use a hierarchy to determine the contract consideration to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third party evidence of selling price (TPE), and (iii) best estimate of selling price. To date, our revenue sources can be classified as: product revenue, royalty revenue, contract revenue, or development revenue.

Product revenue

Our product sales generally include acceptance provisions. We recognize product revenue upon acceptance of the product by the customer or expiration of the contractual acceptance period, after which there are no rights of return. No estimates are made for product returns because revenue is recognized upon expiration of the contractual acceptance period.

Contract revenue

We recognize contract revenue on long-term, cost plus fixed fee, and fixed price contracts using the percentage-of-completion method. Under the percentage-of- completion method, revenue is recognized as work progresses on the contract. The percentage-of-completion method relies on estimates of total expected contract revenue and costs. At the end of each period, we estimate the labor, material and other costs required to complete the contract using data provided by our technical team, project managers, vendors, outside consultants and others and compare these to costs incurred to date.

Recognized revenues are subject to amendments for actual costs incurred. Amendments to revenue and costs to complete estimates are recognized in the period in which the facts become known. In the future, amendments to estimates could significantly impact recognized revenue in any one reporting period. If we are unable to estimate costs on a contract, revenue is recognized using the completed-contract method. Under the completed-contract method, revenue and contract costs are deferred and both are recognized when all deliverables are completed.

Development revenue

We evaluate the performance criteria and terms of our collaborative research and development agreements to determine whether revenue should be recognized under a performance-based method or milestone method. Significant items covered in our evaluation include the following:

- The nature of our obligation under the agreement;
- Whether provisions leading to variable revenues exist;
- Whether any payments are refundable;
- Whether the deliverables should be treated as a single unit of accounting or separated into multiple units;
- Whether substantive milestones exist;
- Whether milestone payments are commensurate with either our level of effort or the increase in value of the customer's rights; and
- Whether a licensing agreement exists.

At the end of each period, we evaluate total estimated costs for each agreement. Amendments to the estimated costs are recognized in the period in which the facts become known. Any related costs for work performed under collaborative research and development agreements are expensed in the periods incurred and included in the Statement of Operations in research and development expense.

Intangible assets

Our intangible assets consist exclusively of purchased patents. The patents are amortized using the straight-line method over their estimated period of benefit, ranging from one to seventeen years. We evaluate the recoverability of intangible assets periodically by taking into account events or circumstances that may warrant revised estimates of useful lives or that indicate the asset may be impaired. We compare the projected undiscounted net cash flows associated with the related intangible assets or group of assets over their remaining lives against their respective carrying amounts. Measurement of an impairment loss for our intangible assets is based on the difference between the fair value of the asset and its carrying value.

Inventory valuation

We value inventory at the lower of cost or market with cost determined on a net-realizable value basis. We make judgments and estimates to value our inventory and make adjustments to its carrying value. We review several factors in determining the market value of our inventory including: evaluating the replacement cost of the raw materials, the net-realizable value of the finished goods, and the likelihood of obsolescence. If we do not achieve our targeted sales prices, if market conditions for our components or products were to decline, or if we do not achieve our sales forecast, additional reductions in the carrying value of the inventory would be required.

Warranty

We provide a warranty on scanning engines and components incorporating our PicoP scanning technology, and we accrue warranty reserves at the time revenue is recognized. Warranty reserves include management's best estimate of the projected costs to repair or to replace any items under warranty based upon the actual units of revenue recognized in the period. We review our reserves each period to ensure that our accruals are adequate in meeting expected future warranty obligations, and we will adjust our estimates as needed. These estimates are inherently uncertain and changes to our historical or projected experience may cause material changes to our warranty reserves in the future.

Share-based compensation

We issue share-based compensation to employees in the form of options exercisable into our common stock and restricted shares of our common stock. We account for equity instruments issued to employees using the straight-line attribution method of allocating the fair value of share-based compensation expense over the requisite service period of the related award. We determine the fair value of options using the Black-Scholes option pricing model with estimates of option lives, stock price volatilities and interest rates, expensed over the periods of service allowing for pre-vest forfeitures. The fair value of restricted shares is determined by the number of shares granted and the closing price of our common stock on the NASDAQ Global Market on the date of grant. Changes in the estimated inputs or using other option valuation methods could result in materially different option values and share-based compensation expense.

Warrant liability

In combination with our registered direct offerings of common stock in May 2013 and September 2013, we issued warrants to purchase our common stock. Based on the terms in the exchange provision of the warrants issued, we made the determination to classify the warrants as a liability given that the exchange provision could result in the issuance of a variable number of shares of common stock. At each balance sheet date while such warrants were outstanding, we evaluated the fair value of the warrants and any change in value is recorded as a non-operating gain or loss on the statement of operations. Due to the conditional exchange provision of the warrants, the determination of the fair value of the warrant liability varied depending on our common stock price. Because the price of our common stock was less than the exercise price of the warrant, we calculated the fair value of the warrant liability as the fair value of the common stock that would have been required to be issued to settle the exchange provision of the warrant.

When the exchange provision was exercised by the holder, we recognized a gain or loss on the exchange based on the fair market value of the common stock issued by us to the holder to satisfy the exchange provision.

Income taxes

Significant judgment is required in evaluating our tax position and in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We record a valuation allowance when necessary to reduce deferred tax assets to the amount expected to be realized. Based on our history of losses since inception, the available objective evidence creates sufficient uncertainty regarding the realizability of the deferred tax assets. Our actual tax exposure may differ from our estimates and any such differences may impact income our tax expense in the period in which such determination is made.

The key accounting policies described above are not intended to be a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles, with no need for us to apply judgment or make estimates. There are also areas in which our judgment in selecting any available alternative would not produce a materially different result to our consolidated financial statements. Additional information about our accounting policies, and other disclosures required by generally accepted accounting principles, are set forth in the notes to our consolidated financial statements.

Inflation has not had a material impact on our revenues or income from continuing operations over the three most recent fiscal years.

Results of Operations

YEAR ENDED DECEMBER 31, 2015 COMPARED TO YEAR ENDED DECEMBER 31, 2014.

Product revenue

	2015	% of total revenue	2014	% of total revenue	$ change	% change
(In thousands)						
Product revenue	$ 6,452					