Digimarc CORP
Form 10-Q
July 26, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

OR

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

For the transition period from to

Commission File Number: 001-34108

DIGIMARC CORPORATION

(Exact name of registrant as specified in its charter)

Oregon	**26-2828185**
(State or other jurisdiction of incorporation or organization)	**(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)

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 ¨

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 x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See 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 ¨ No x

As of July 22, 2013, there were 7,263,484 shares of the registrant s common stock, par value $0.001 per share, outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

DIGIMARC CORPORATION

CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

(UNAUDITED)

	June 30, 2013	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$ 8,305	$ 6,866
Marketable securities	26,192	25,403
Trade accounts receivable, net	4,519	4,216
Other current assets	1,306	1,016
Total current assets	40,322	37,501
Marketable securities	7,584	6,787
Property and equipment, net	1,408	1,453
Intangibles, net	6,689	6,721
Goodwill	1,114	1,114
Deferred tax assets, net	2,188	3,589
Other assets	212	166
Total assets	$ 59,517	$ 57,331
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable and other accrued liabilities	$ 1,405	$ 1,143
Deferred revenue	3,155	2,512
Total current liabilities	4,560	3,655
Deferred rent and other long-term liabilities	491	673
Total liabilities	5,051	4,328
Commitments and contingencies (Note 13)		
Shareholders equity:		
Preferred stock (par value $0.001 per share, 2,500,000 authorized, 10,000 shares issued and outstanding at June 30, 2013 and December 31, 2012)	50	50
Common stock (par value $0.001 per share, 50,000,000 authorized, 7,264,864 and 7,168,359 shares issued and outstanding at June 30, 2013 and December 31, 2012, respectively)	7	7
Additional paid-in capital	41,360	39,869
Retained earnings	13,049	13,077
Total shareholders equity	54,466	53,003
Total liabilities and shareholders equity	$ 59,517	$ 57,331

The accompanying notes are an integral part of these consolidated financial statements.

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DIGIMARC CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(UNAUDITED)

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Revenue:				
Service	$ 3,022	$ 2,609	$ 5,951	$ 5,657
Subscription	1,433	317	2,817	595
License	6,015	6,186	11,945	19,906
Total revenue	10,470	9,112	20,713	26,158
Cost of revenue:				
Service	1,432	1,485	2,835	3,182
Subscription	588	45	1,223	92
License	100	53	196	119
Total cost of revenue	2,120	1,583	4,254	3,393
Gross profit	8,350	7,529	16,459	22,765
Operating expenses:				
Sales and marketing	1,563	970	2,840	1,977
Research, development and engineering	2,822	2,146	5,547	4,144
General and administrative	2,348	2,191	4,534	4,949
Intellectual property	261	291	538	610
Total operating expenses	6,994	5,598	13,459	11,680
Operating income	1,356	1,931	3,000	11,085
Net loss from joint ventures				(1,107)
Other income, net	19	33	48	91
Income before income taxes	1,375	1,964	3,048	10,069
Provision for income taxes	(773)	(748)	(1,475)	(3,854)
Net income	$ 602	$ 1,216	$ 1,573	$ 6,215
Earnings per common share:				
Earnings per common share basic	$ 0.08	$ 0.17	$ 0.22	$ 0.88
Earnings per common share diluted	$ 0.08	$ 0.17	$ 0.21	$ 0.84
Weighted average common shares outstanding basic	6,850	6,737	6,844	6,738
Weighted average common shares outstanding diluted	7,090	6,993	7,078	6,999
Cash dividends declared per common share	$ 0.11	$ 0.11	$ 0.22	$ 0.11

The accompanying notes are an integral part of these consolidated financial statements.

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DIGIMARC CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

(In thousands, except share data)

(UNAUDITED)

	Preferred Stock		Common Stock		Additional		Total
					Paid-in	Retained	Shareholders
	Shares	Amount	Shares	Amount	Capital	Earnings	Equity
BALANCE AT DECEMBER 31, 2011	10,000	$ 50	7,008,031	$ 7	$ 34,511	$ 7,149	$ 41,717
Exercise of stock options			62,500		603		603
Issuance of restricted common stock			129,220				
Forfeiture of restricted common stock			(6,360)				
Purchase and retirement of common stock			(85,019)		(2,187)		(2,187)
Stock-based compensation					2,857		2,857
Tax benefit from stock-based awards					1,538		1,538
Net income						6,215	6,215
Cash dividends declared						(779)	(779)
BALANCE AT JUNE 30, 2012	10,000	$ 50	7,108,372	$ 7	$ 37,322	$ 12,585	$ 49,964
BALANCE AT DECEMBER 31, 2012	10,000	$ 50	7,168,359	$ 7	$ 39,869	$ 13,077	$ 53,003
Exercise of stock options			7,684				
Issuance of restricted common stock			184,390				
Forfeiture of restricted common stock			(61,855)				
Purchase and retirement of common stock			(33,714)		(742)		(742)
Stock-based compensation					2,233		2,233
Tax benefit from stock-based awards							
Net income						1,573	1,573
Cash dividends declared						(1,601)	(1,601)
BALANCE AT JUNE 30, 2013	10,000	$ 50	7,264,864	$ 7	$ 41,360	$ 13,049	$ 54,466

The accompanying notes are an integral part of these consolidated financial statements.

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DIGIMARC CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(UNAUDITED)

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Cash flows from operating activities:		
Net income	$ 1,573	$ 6,215
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	320	292
Amortization and write-off of intangibles	602	154
Gain on reversal of contingent merger consideration	(190)	
Stock-based compensation	2,169	2,757
Net loss from joint ventures		1,107
Deferred income taxes	1,406	62
Tax benefit from stock-based awards		1,893
Excess tax benefit from stock-based awards		(1,538)
Changes in operating assets and liabilities:		
Trade accounts receivable, net	(303)	959
Other current assets	(271)	132
Other assets	(46)	141
Accounts payable and other accrued liabilities	228	(291)
Income taxes payable	24	1,014
Deferred revenue	637	(327)
Net cash provided by operating activities	6,149	12,570
Cash flows from investing activities:		
Purchase of property and equipment	(275)	(254)
Capitalized patent costs and purchased intellectual property	(506)	(657)
Investments in joint ventures, net		(692)
Sale or maturity of marketable securities	35,474	69,136
Purchase of marketable securities	(37,060)	(75,224)
Net cash used in investing activities	(2,367)	(7,691)
Cash flows from financing activities:		
Issuance of common stock		603
Purchase of common stock	(742)	(2,187)
Cash dividends paid	(1,601)	(779)
Excess tax benefit from stock-based awards		1,538
Net cash used in financing activities	(2,343)	(825)
Net increase in cash and cash equivalents	1,439	4,054
Cash and cash equivalents at beginning of period	6,866	3,419
Cash and cash equivalents at end of period	$ 8,305	$ 7,473

Supplemental disclosure of cash flow information:				
Cash paid for income taxes	$	46	$	842
Supplemental schedule of non-cash investing activities:				
Stock-based compensation capitalized to patent costs	$	64	$	50
Supplemental schedule of non-cash financing activities:				
Exercise of stock options	$	128	$	603

The accompanying notes are an integral part of these consolidated financial statements.

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DIGIMARC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except share and per share data)

(UNAUDITED)

1. Description of Business and Significant Accounting Policies

Description of Business

Digimarc Corporation (Digimarc or the Company), an Oregon 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. The Company s inventions provide 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 and reliably identify relevant data from vast amounts of media content.

Interim Consolidated Financial Statements

The Company has adhered to the accounting policies set forth in its Annual Report on Form 10-K for the year ended December 31, 2012 in preparing the accompanying interim consolidated financial statements.

The accompanying interim consolidated financial statements have been prepared from the Company s records without audit and, in management s opinion, include all adjustments (consisting of only normal recurring adjustments) necessary to fairly reflect the financial condition and the results of operations for the periods presented. Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (the U.S.) have been condensed or omitted in accordance with the rules and regulations of the Securities and Exchange Commission (SEC).

These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2012, which was filed with the SEC on February 22, 2013. The results of operations for the interim periods presented in these consolidated financial statements are not necessarily indicative of the results for the full year.

Reclassifications

Certain prior period amounts in the accompanying consolidated financial statements and notes thereto have been reclassified to conform to current period presentation. These reclassifications had no material effect on the results of operations or financial position for any period presented. The Company has historically combined license and subscription revenue on the consolidated statement of operations, but given the increase in subscription revenue in the current year, the Company is now presenting license revenue and subscription revenue separately.

Goodwill

The Company reviews for impairment in June of each year to determine if events or changes in business conditions indicate that the carrying value of goodwill may not be recoverable. Such reviews assess the fair value of the assets compared to the carrying values.

The Company is considered one reporting unit. The Company estimated the fair value of its single reporting unit using a market approach. The market approach estimates fair value in part on market capitalization plus an estimated control premium.

In connection with the Company s annual impairment test of goodwill as of June 30, 2013, it was concluded that there was no impairment as the estimated fair value of the Company s reporting unit substantially exceeds the carrying value.

2. Fair Value of Financial Instruments

Accounting Standards Certification (ASC) 820 *Fair Value Measurements and Disclosures* (ASC 820) defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles in the U.S., 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 assets as of the reporting date.

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

Level 3 Pricing inputs are unobservable for the assets; that is, the inputs reflect the reporting entity s own assumptions about the assumptions market participants would use in pricing the asset.

The estimated fair values of the Company s financial instruments, which include cash and cash equivalents, accounts receivable, accounts payable and other accrued liabilities approximate their carrying values due to the short-term nature of these instruments. The Company records marketable securities at amortized cost, which approximates fair value.

The Company s fair value hierarchy for its cash equivalents and marketable securities as of June 30, 2013 and December 31, 2012, respectively, was as follows:

June 30, 2013	Level 1	Level 2	Level 3	Total
Money market securities	$ 6,047	$	$	$ 6,047
Certificates of deposits		492		492
U.S. federal agency notes		333		333
Pre-refunded and other municipal bonds (1)		31,858		31,858
Corporate notes		2,838		2,838
Total	$ 6,047	$ 35,521	$	$ 41,568

December 31, 2012	Level 1	Level 2	Level 3	Total
Money market securities	$ 901	$	$	$ 901
Certificates of deposits		491		491
U.S. treasuries		289		289
U.S. federal agency notes		1,637		1,637
Pre-refunded and other municipal bonds (1)		22,036		22,036
Corporate notes		10,100		10,100
Commercial paper		2,614		2,614
Total	$ 901	$ 37,167	$	$ 38,068

(1) Pre-refunded municipal bonds collateralized by U.S. treasuries.

The fair value maturities of the Company s cash equivalents and marketable securities as of June 30, 2013 were as follows:

		Maturities by Period			
	Total	Less than 1 year	1-5 years	5-10 years	More than 10 years
Cash equivalents and marketable securities	$ 41,568	$ 33,984	$ 7,584	$	$

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 pre-refunded municipal bonds totaling $7,792 and $5,878 at June 30, 2013 and December 31, 2012, respectively. Cash equivalents are carried at cost or amortized cost, which approximates fair value, due to their short maturities.

3. Acquisition of Attributor Corporation (Attributor)

The Company accounted for the acquisition of Attributor in December 2012 using the acquisition method of accounting. Under the acquisition method of accounting, the total purchase price was allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values. The purchase price was allocated using the information currently available, and Digimarc may adjust the preliminary purchase price allocation after obtaining more information. The final purchase price allocation is pending the completion of the Company s review of the acquired tax assets and liabilities, which is expected to be completed by the end of the third quarter of 2013.

The Company recorded a $190 liability in the preliminary purchase price allocation reflecting the estimated fair value of the contingent merger consideration on the acquisition date, which was presented in deferred rent and other long-term liabilities at December 31, 2012. At March 31, 2013, the Company determined that the estimated fair value of the contingent merger consideration

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was $0 based on the Company s most recent projections and therefore reversed the liability. As of June 30, 2013, the Company continued to believe the estimated fair value of the contingent merger consideration was $0. The reversal of the $190 liability is reflected as a reduction in general and administrative expense within the consolidated statements of operations for the six-month period ended June 30, 2013.

4. Revenue Recognition

The Company derives its revenue primarily from development services, subscriptions and licensing of its patent portfolio:

Service revenue consists primarily of software development and consulting services. The majority of service revenue arrangements are structured as time and materials consulting agreements and fixed price consulting agreements.

Subscription revenue includes subscriptions for products and services, is more recurring in nature, is generally paid in advance and recognized over the term of the subscription.

License revenue, including royalty revenue, originates primarily from licensing the Company s technology and patents where the Company receives royalties as its income stream.

Revenue is recognized in accordance with ASC 605 *Revenue Recognition* and ASC 985 *Software* 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 reasonably assured.

Some customer arrangements encompass multiple deliverables, such as patent license, professional services, software subscriptions, and maintenance fees. For arrangements that include multiple deliverables, the Company identifies separate units of accounting at inception based on the consensus reached under ASC 605-25 *Multiple-Element Arrangements*, which provides that revenue arrangements with multiple deliverables should be divided into separate units of accounting if certain criteria are met. The consideration for the arrangement is allocated to the separate units of accounting using the relative selling price method.

The relative selling price method allocates the consideration based on the Company s specific assumptions rather than assumptions of a marketplace participant, and any discount in the arrangement proportionally to each deliverable on the basis of each deliverable s selling price.

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.

Subscription revenue, which includes subscriptions for products and services, is generally paid in advance and recognized over the term of the subscription, which is generally one month to twenty-four months.

License revenue is recognized when amounts owed to the Company have been earned, are fixed or determinable (within the Company s normal 30 to 60 day payment terms), and collection is reasonably assured. If the payment terms extend beyond the normal 30 to 60 days, the fee may not be considered to be fixed or determinable, and the revenue would then be recognized when installments are due.

The Company records revenue from certain license agreements upon cash receipt as a result of collectability not being reasonably assured.

The Company s standard payment terms for license arrangements are 30 to 60 days. Extended payment terms increase the likelihood the Company will grant a customer a concession, such as reduced license payments or additional rights, rather than hold firm on minimum commitments in an agreement to the point of losing a potential advocate and licensee of patented technology in the marketplace. Extended payment terms on patent license arrangements are not considered to be fixed or determinable if payments are due beyond the Company s standard payment terms, primarily because of the risk of substantial modification present in the Company s patent licensing business. As such, revenue on license arrangements with extended payment terms are recognized as fees become fixed or determinable.

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

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5. Segment Information

Geographic Information

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 of 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 and licensing personnel.

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

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Domestic	$ 6,241	$ 5,522	$ 12,366	$ 19,093
International(1)	4,229	3,590	8,347	7,065
Total	$ 10,470	$ 9,112	$ 20,713	$ 26,158

(1) Revenue from the Central Banks, comprised of a consortium of central banks around the world, is classified as international revenue. Reporting revenue by country for this customer is not practical.

Major Customers

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

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Intellectual Ventures	34%	35%	34%	25%
Central Banks	30%	30%	29%	21%
Verance Corporation (Verance)	*	12%	*	38%
The Nielsen Company (Nielsen)	*	11%	*	*

* Less than 10%

On January 30, 2012, the Company and Verance, a longtime cash based revenue customer, settled all disputes regarding breach of contract and patent infringement claims. In connection with the resolution of these matters, Verance paid the Company $8,852 for amounts due to Digimarc through December 31, 2011 and all claims between the parties were dismissed. Revenue from this payment was recorded in the quarter ended March 31, 2012.

6. Stock-Based Compensation

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

Stock-based compensation expense related to internal legal labor is capitalized to patent costs based on direct labor hours charged to capitalized patent costs.

Determining Fair Value

Preferred Stock

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

The Series A Preferred is redeemable based on the stated fair value of $5.00 per share. The Series A Preferred has no dividend rights and no rights to the undistributed earnings of the Company.

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Stock Options

Valuation and Amortization Method. The Company estimates the fair value of stock options granted using the Black-Scholes option pricing model as of the date of grant (measurement date). 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.

Expected Life. The expected life of awards granted represents the period of time that they are expected to be outstanding. The Company determines the expected life based on historical experience with similar awards, giving consideration to the contractual terms, vesting schedules and pre-vesting and post-vesting forfeitures. Stock options granted generally vest over three to four years for employee grants and one to two years for director grants, and have contractual terms of ten years.

Expected Volatility. The Company estimates the volatility of its common stock at the date of grant based on the historical volatility of its common stock based on historical prices over the most recent period commensurate with the expected life of the award.

Risk-Free Interest Rate. The Company determines the risk-free interest rate using current U.S. treasury yields for bonds with a maturity commensurate with the expected life of the award.

Expected Dividend Yield. The expected dividend yield is derived using a formula which uses the Company s expected annual dividend rate over the expected term divided by the fair value of the Company s common stock at the grant date.

There were no stock options granted during the three- or six-month periods ended June 30, 2013 and 2012.

The Company records stock-based compensation expense for stock option awards only for those awards that are expected to vest.

Restricted Stock

The Compensation Committee of the Board of Directors has awarded restricted stock shares under the Company s 2008 Stock Incentive Plan to certain employees and directors. The shares subject to the restricted stock awards vest over a certain period, usually one to four years for employees and one year for directors. Specific terms of the restricted stock awards are governed by Restricted Stock Agreements between the Company and the award recipients. Restricted stock awards are treated as outstanding when granted.

The fair value of restricted stock awarded 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 using the straight-line method.

The Company records stock-based compensation expense for restricted stock awards only for those awards that are expected to vest.

Stock-based Compensation

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Stock-based compensation:				
Cost of revenue	$ 139	$ 154	$ 296	$ 338
Sales and marketing	83	137	195	233
Research, development and engineering	232	212	488	397
General and administrative	560	830	1,066	1,664
Intellectual property	63	68	124	125
Stock-based compensation expense	1,077	1,401	2,169	2,757
Capitalized to patent costs	31	23	64	50

Total stock-based compensation	$ 1,108	$ 1,424	$ 2,233	$ 2,807

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The following table sets forth total unrecognized compensation cost related to non-vested stock-based awards granted under all equity compensation plans, including preferred stock, stock options and restricted stock:

	As of June 30, 2013	As of December 31, 2012
Unrecognized compensation costs	$ 8,937	$ 8,333

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

The Company expects to recognize the unrecognized compensation costs as of June 30, 2013 for stock options and restricted stock over a weighted average period through June 2017 as follows:

	Stock Options	Restricted Stock
Weighted average period	0.92 years	1.71 years

Stock Option Activity

As of June 30, 2013, under all of the Company s stock-based compensation plans, equity awards to purchase an additional 716,210 shares were authorized for future grants under the plans. The Company issues new shares upon option exercises.

The following table reconciles the outstanding balance of stock options:

Three- and six-months ended June 30, 2013:	Options	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value
Outstanding at December 31, 2012	855,988	$ 15.16	$ 7.88	
Options granted				
Options exercised	(13,300)	$ 9.64	$ 6.30	
Options canceled or expired				
Outstanding at June 30, 2013	842,688	$ 15.24	$ 7.90	$ 6,176
Exercisable at June 30, 2013	724,739	$ 13.53		$ 6,083
Unvested at June 30, 2013	117,949	$ 25.81		$ 93

The aggregate intrinsic value is based on the closing price of $20.77 per share of Digimarc common stock on June 30, 2013, which would have been received by the optionees had all of the options with exercise prices less than $20.77 per share been exercised on that date. The following table summarizes information about stock options outstanding at June 30, 2013:

Range of Exercise Prices	Options Outstanding			Options Exercisable		
	Number Outstanding	Remaining Contractual	Weighted Average	Number Exercisable	Remaining Contractual	Weighted Average

		Life (Years)	Exercise Price		Life (Years)	Exercise Price
$9.64 - $9.91	494,772	5.37	$ 9.66	494,772	5.37	$ 9.66
$14.99 - $18.01	132,916	6.58	$ 15.67	116,876	6.59	$ 15.76
$24.35 - 30.01	215,000	8.08	$ 27.84	113,091	8.03	$ 28.14
$9.64 - $30.01	842,688	6.25	$ 15.24	724,739	5.98	$ 13.53

Restricted Stock Activity

The following table reconciles the unvested balance of restricted stock:

Three-months ended June 30, 2013:	**Number of Shares**	**Weighted Average Grant Date Fair Value**
Unvested balance, March 31, 2013	466,368	$ 21.75
Granted	13,060	$ 22.56
Vested	(12,775)	$ 22.52
Canceled	(59,230)	$ 19.26
Unvested balance, June 30, 2013	407,423	$ 22.11

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Six-months ended June 30, 2013:	Number of Shares	Weighted Average Grant Date Fair Value
Unvested balance, December 31, 2012	369,083	$ 21.72
Granted	184,390	$ 21.86
Vested	(84,195)	$ 21.89
Canceled	(61,855)	$ 19.32
Unvested balance, June 30, 2013	407,423	$ 22.11

7. Earnings Per Common Share

The Company calculates basic and diluted earnings per common share in accordance with ASC 260 *Earnings Per Share*, using the two-class method as the Company s unvested restricted stock is a participating security given these awards contain non-forfeitable rights to receive dividends. Under the two-class method, net earnings are allocated to each class of common stock and participating security as if all of the net earnings for the period had been distributed.

Basic earnings per common share excludes dilution and is calculated by dividing net earnings allocable to common shares by the weighted-average number of common shares outstanding for the period. Diluted earnings per common share is calculated by dividing net earnings allocable to common shares by the weighted-average number of common shares, as adjusted for the potential dilutive effect of non-participating securities outstanding as of the balance sheet date. The following table reconciles earnings per common share for the three- and six-month periods ended June 30, 2013:

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Basic EPS:				
Net income	$ 602	$ 1,216	$ 1,573	$ 6,215
Less: Net income allocable to participating securities	(34)	(61)	(88)	(313)
Net income allocable to common shares	$ 568	$ 1,155	$ 1,485	$ 5,902
Weighted average common shares outstanding basic (in thousands)	6,850	6,737	6,844	6,738
Basic earnings per common share	$ 0.08	$ 0.17	$ 0.22	$ 0.88

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Diluted EPS:				
Net income	$ 602	$ 1,216	$ 1,573	$ 6,215
Less: Net income allocable to participating securities	(34)	(61)	(88)	(313)
Net income allocable to common shares	$ 568	$ 1,155	$ 1,485	$ 5,902
Weighted average common shares outstanding basic (in thousands)	6,850	6,737	6,844	6,738
Dilutive effect of non-participating securities (in thousands)	240	256	234	261

Weighted average common shares outstanding dilutive (in thousands)	7,090	6,993	7,078	6,999
Diluted earnings per common share	$ 0.08	$ 0.17	$ 0.21	$ 0.84

There were 215,000 common stock equivalents related to stock options that were anti-dilutive and excluded from diluted earnings per common share calculations for the three- and six-month periods ended June 30, 2013 as their exercise prices were higher than the average market price of the underlying common stock for the period.

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There were 175,000 common stock equivalents related to stock options that were anti-dilutive and excluded from diluted earnings per share calculations for the three- and six-month periods ended June, 30, 2012 as their exercise prices were higher than the average market price of th