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# U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

## FORM 10-Q

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

**For the quarterly period ended September 30, 2016**

**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 1-15288*

### **NETWORK-1 TECHNOLOGIES, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

\_\_\_\_\_  
(State or Other Jurisdiction of Incorporation or Organization)

**11-3027591**

\_\_\_\_\_  
(IRS Employer Identification No.)

**445 Park Avenue, Suite 912  
New York, New York**

\_\_\_\_\_  
(Address of Principal Executive Offices)

**10022**

\_\_\_\_\_  
(Zip Code)

**212-829-5770**

\_\_\_\_\_  
(Registrant's Telephone Number)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§223.405) of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer   
filer

Accelerated

Non-accelerated filer   
company

Smaller reporting

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

The number of shares of the registrant's common stock, \$.01 par value per share, outstanding as of November 7, 2016 was 23,329,196.

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NETWORK-1 TECHNOLOGIES, INC.

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**PART I. FINANCIAL INFORMATION**

**Item 1. Condensed Consolidated Financial Statements**

**NETWORK-1 TECHNOLOGIES, INC.**

CONDENSED CONSOLIDATED BALANCE SHEETS  
(UNAUDITED)

<b>ASSETS:</b>	<b>September 30, 2016</b>	<b>December 31, 2015</b>
	<u>                    </u>	<u>                    </u>
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 57,759,000	\$ 20,608,000
Marketable securities, available for sale	1,100,000	1,061,000
Royalty receivables	1,414,000	1,537,000
Other current assets	<u>20,000</u>	<u>196,000</u>
Total Current Assets	<u>60,293,000</u>	<u>23,402,000</u>
<b>OTHER ASSETS:</b>		
Deferred tax assets	415,000	4,958,000
Patents, net of accumulated amortization	1,246,000	2,002,000
Security deposits	<u>19,000</u>	<u>19,000</u>
Total Other Assets	<u>1,680,000</u>	<u>6,979,000</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 61,973,000</u></u>	<u><u>\$ 30,381,000</u></u>
 <b>LIABILITIES AND STOCKHOLDERS' EQUITY:</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 462,000	\$ 139,000
Accrued expenses	5,572,000	1,552,000
Income taxes payable	<u>4,080,000</u>	<u>—</u>
TOTAL LIABILITIES	<u>10,114,000</u>	<u>1,691,000</u>
 <b>COMMITMENTS AND CONTINGENCIES</b>		
<b><u>STOCKHOLDERS' EQUITY</u></b>		
Preferred stock, \$0.01 par value, authorized 10,000,000 shares; none issued and outstanding at September 30, 2016 and December 31, 2015	—	—
Common stock, \$0.01 par value; authorized 50,000,000 shares; 23,329,196 and 23,211,149 shares issued and outstanding at September 30, 2016 and December 31, 2015, respectively	233,000	232,000
Additional paid-in capital	61,540,000	61,249,000
Accumulated deficit	(9,918,000)	(32,756,000)
Accumulated other comprehensive income(loss)	<u>4,000</u>	<u>(35,000)</u>
TOTAL STOCKHOLDERS' EQUITY	<u>51,859,000</u>	<u>28,690,000</u>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u><u>\$ 61,973,000</u></u>	<u><u>\$ 30,381,000</u></u>

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

**NETWORK-1 TECHNOLOGIES, INC.**

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME  
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
REVENUE	\$ 34,326,000	\$ 3,008,000	\$ 59,963,000	\$ 10,382,000
OPERATING EXPENSES:				
Costs of revenue	16,943,000	927,000	24,183,000	3,094,000
Professional fees and related costs	633,000	475,000	1,458,000	1,248,000
General and administrative	428,000	440,000	1,256,000	1,891,000
Amortization of patents	49,000	413,000	760,000	1,239,000
Stock-based compensation	189,000	69,000	233,000	243,000
Contingent patent cost	—	—	500,000	—
TOTAL OPERATING EXPENSES	18,242,000	2,324,000	28,390,000	7,715,000
OPERATING INCOME	16,084,000	684,000	31,573,000	2,667,000
OTHER INCOME:				
Interest income, net	24,000	11,000	50,000	44,000
INCOME BEFORE INCOME TAXES	16,108,000	695,000	31,623,000	2,711,000
INCOME TAXES:				
Current	3,817,000	26,000	4,198,000	66,000
Deferred taxes, net	1,459,000	262,000	4,543,000	928,000
Total income taxes	5,276,000	288,000	8,741,000	994,000
NET INCOME	\$ 10,832,000	\$ 407,000	\$ 22,882,000	\$ 1,717,000
Net Income Per Share				
Basic	\$ 0.46	\$ 0.02	\$ 0.98	\$ 0.07
Diluted	\$ 0.43	\$ 0.02	\$ 0.93	\$ 0.07
Weighted average common shares outstanding:				
Basic	23,320,514	23,273,946	23,291,408	23,597,143
Diluted	25,198,142	24,654,699	24,700,784	24,590,487
NET INCOME	\$ 10,832,000	\$ 407,000	\$ 22,882,000	\$ 1,717,000
OTHER COMPREHENSIVE INCOME:				
Unrealized holding gain (loss) on securities available-for-sale arising during the period	(4,000)	12,000	39,000	—
COMPREHENSIVE INCOME	\$ 10,828,000	\$ 419,000	\$ 22,921,000	\$ 1,717,000

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

**NETWORK-1 TECHNOLOGIES, INC.**

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

	Nine Months Ended September 30,	
	2016	2015
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income	\$ 22,882,000	\$ 1,717,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of patents	760,000	1,239,000
Stock-based compensation	233,000	243,000
Deferred tax provision	4,543,000	928,000
Impairment of investments	—	386,000
Changes in operating assets and liabilities:		
Royalty receivables	123,000	(451,000)
Other current assets	176,000	126,000
Accounts payable	323,000	(165,000)
Accrued expenses	4,020,000	(1,082,000)
Income taxes payable	4,080,000	—
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>37,140,000</b>	<b>2,941,000</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of patents and other assets	(4,000)	(36,000)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Value of shares delivered to fund withholding taxes on exercise of options	(44,000)	—
Repurchases of common stock, net of commissions	(1,000)	(2,555,000)
Proceeds from exercise of options	60,000	—
<b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>	<b>15,000</b>	<b>(2,555,000)</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>37,151,000</b>	<b>350,000</b>
<b>CASH AND CASH EQUIVALENTS, beginning of period</b>	<b>20,608,000</b>	<b>17,662,000</b>
<b>CASH AND CASH EQUIVALENTS, end of period</b>	<b>\$ 57,759,000</b>	<b>\$ 18,012,000</b>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
<b>CASH PAID DURING THE PERIOD FOR:</b>		
Interest	\$ —	\$ —
Taxes	—	50,000

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements

**NETWORK-1 TECHNOLOGIES, INC.**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE A – BASIS OF PRESENTATION AND NATURE OF BUSINESS:**

**[1] BASIS OF PRESENTATION**

The accompanying condensed consolidated financial statements are unaudited, but, in the opinion of the management of Network-1 Technologies, Inc. (the "Company"), contain all adjustments consisting only of normal recurring items which the Company considers necessary for the fair presentation of the Company's financial position as of September 30, 2016, and the results of its operations and comprehensive income for the three and nine month periods ended September 30, 2016 and September 30, 2015 and its cash flows for the nine month periods ended September 30, 2016 and September 30, 2015. The unaudited condensed consolidated financial statements included herein have been prepared in accordance with the accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and the instructions to Form 10-Q and Regulation S-X. Accordingly, certain information and footnote disclosures normally included in the consolidated financial statements prepared in accordance with U.S. GAAP may have been omitted pursuant to such rules and regulations, although management believes that the disclosures are adequate to make the information presented not misleading. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2015 included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 30, 2016. The results of operations for the three and nine months ended September 30, 2016 are not necessarily indicative of the results of operations to be expected for the full year. The accompanying condensed consolidated financial statements include accounts of the Company and its wholly-owned subsidiary, Mirror Worlds Technologies, LLC.

**[2] BUSINESS:**

The Company is engaged in the development, licensing and protection of its intellectual property assets. The Company presently owns twenty-eight (28) patents including (i) the remote power patent (the "Remote Power Patent") covering the delivery of power over Ethernet (PoE) cables for the purpose of remotely powering network devices, such as wireless access ports, IP phones and network based cameras; (ii) the Mirror Worlds patent portfolio (the "Mirror Worlds Patent Portfolio") relating to foundational technologies that enable unified search and indexing, displaying and archiving of documents in a computer system; (iii) the Cox patent portfolio (the "Cox Patent Portfolio") relating to enabling technology for identifying media content on the Internet and taking further action to be performed based on such identification; and (iv) patents covering systems and methods for the transmission of audio, video and data over computer and telephony networks in order to achieve high quality of service (QoS) (the "QoS Patents"). As of November 1, 2016, the Company has entered into twenty-five (25) license agreements with respect to its Remote Power Patent. The Company's current strategy includes continuing to pursue licensing opportunities for its Remote Power Patent and its efforts to monetize its Cox Patent Portfolio and Mirror Worlds Patent Portfolio acquired in 2013 (see Note I[2] hereof). The Company's acquisition strategy is to focus on acquiring high quality patents which management believes have the potential to generate significant licensing opportunities as the Company has achieved with respect to its Remote Power Patent and Mirror Worlds Patent Portfolio. The Company's Remote Power Patent has generated licensing revenue in excess of \$100,000,000 from May 2007 through September 30, 2016. As a result of the Company's acquisition of the Mirror Worlds Patent Portfolio in May 2013, the Company achieved licensing and other revenue of \$47,150,000 through September 30, 2016 (See Note K [2] and Note M to our condensed consolidated financial statements included in this quarterly report). The Company continually reviews opportunities to acquire or license additional intellectual property. In addition, the Company may enter into strategic relationships with third parties to develop, commercialize, license or otherwise monetize their intellectual property.

## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Use of Estimates and Assumptions

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the unaudited condensed consolidated financial statements, and the reported amounts of revenues and expenses during the reporting periods. The significant estimates and assumptions made in the preparation of the Company's unaudited condensed consolidated financial statements include revenue recognition, the valuation of warrants and stock-based compensation, income tax payable, deferred income taxes, valuation of patents, accrued expenses and valuation of marketable securities. Actual results could be materially different from those estimates, upon which the carrying values were based.

### Patents

The Company owns patents that relate to various technologies. The Company capitalizes the costs associated with acquisition, registration and maintenance of its acquired patents and amortizes these assets over their remaining useful lives on a straight-line basis. Any further payments made to maintain or develop the patents would be capitalized and amortized over the balance of the useful life for the patents.

### Revenue Recognition

The Company recognizes revenue received from the licensing of its intellectual property and other related intellectual property activities. Revenue is recognized when (i) persuasive evidence of an arrangement exists, (ii) all obligations have been performed pursuant to the terms of the license or other applicable agreement, (iii) amounts are fixed or determinable, and (iv) collectability of amounts is reasonably assured. The Company relies on royalty reports received from third party licensees to record its revenue. From time to time the Company may audit royalties reported from licensees. Any adjusted royalty revenue as a result of such audits is recorded by the Company in the period in which such adjustment is agreed to by the Company and the licensee or otherwise determined.

### Income Taxes

The Company accounts for income taxes in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 740, "Income Taxes" (ASC 740), which requires the Company to use the assets and liability method of accounting for income taxes. Under the assets and liability method, deferred income taxes are recognized for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between financial statement carrying amounts and the tax bases of existing assets and liabilities and operating loss and tax credit carry forward. Under this accounting standard, the effect on deferred income taxes of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recognized if it is more likely than not that some portion, or all of, a deferred tax asset will not be realized.



## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

ASC 740-10, "Accounting for Uncertainty in Income Taxes," defines uncertainty in income taxes and the evaluation of a tax position as a two-step process. The first step is to determine whether it is more likely than not that a tax position will be sustained upon examination, including the resolution of any related appeals or litigation based on the technical merits of that position. The second step is to measure a tax position that meets the more-likely-than-not threshold to determine the amount of benefit to be recognized in the financial statements. A tax position is measured at the largest amount of benefit that is greater than 50 percent likelihood of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent period in which the threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not criteria should be de-recognized in the first subsequent financial reporting period in which the threshold is no longer met. The Company has no uncertain tax positions as of September 30, 2016 and December 31, 2015.

United States federal, state and local income tax returns prior to 2013 are not subject to examination by any applicable tax authorities.

Effective January 1, 2016, the Company has elected to early adopt Accounting Standards Update No. 2015-17, *Income Taxes (Topic 740); Balance Sheet Classification of Deferred Taxes* (ASU 2015-17) and classify the deferred tax assets as non-current assets on the consolidated balance sheets. See "Accounting Standards Adopted in the Period" section of this Note B for further details.

### Impairment of long-lived assets

Intangible assets with finite lives are tested for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. Accordingly, we record impairment losses on long-lived assets used in operations or expected to be disposed of when indicators of impairment exist and the undiscounted cash flows expected to be derived from those assets are less than carrying amounts of these assets. As of September 30, 2016, there was no impairment to the Company's patents.

### Stock-Based Compensation

The Company accounts for its stock-based compensation awards to employees and directors in accordance with FASB ASC Topic 718, *Compensation - Stock Compensation* ("ASC 718"). ASC 718 requires all stock-based compensation to employees, including grants of employee stock options and restricted stock units, to be recognized in the unaudited condensed consolidated statements of operations and comprehensive income based on their grant date fair values. Compensation expense related to awards to employees is recognized on a straight-line basis based on the grant date fair value over the associated service period of the award, which is generally the vesting term. Share-based compensation issued to non-employees are recorded at their fair values, and are periodically revalued as the equity instruments vest and are recognized as expense over the related service period in accordance with the provisions of ASC 718 and ASC Topic 505, *Equity*, and are expensed using an accelerated attribution model. The Company uses the Black-Scholes option pricing model to determine the grant date fair value of options granted. The fair value of restricted stock units is determined based on the number of shares granted and either the quoted market price of the Company's common stock on the date of grant for time-based and performance-based awards, or the fair value on the date of grant using the Monte Carlo Simulation model for market-based awards (see Note D for further discussion of the Company's stock – based compensation).

## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### Earnings Per Share

The Company reports earnings per share in accordance with U.S. GAAP, which requires presentation of basic and diluted earnings per share in conjunction with the disclosure of the methodology used in computing such earnings per share. Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted average common shares outstanding during the period. Diluted earnings per share takes into account the potential dilution that could occur if securities or other contracts, such as warrants and options to purchase common stock were exercised and shares were issued pursuant to outstanding restricted stock units. Common stock equivalents having an anti-dilutive effect on earnings per share are excluded from the calculation of diluted earnings per share.

### Financial Instruments

U.S. GAAP regarding fair value of financial instruments and related fair value measurements define fair value, establish a three-level valuation hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The three levels of inputs are defined as follows:

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 inputs to the valuation methodology are unobservable.

The carrying value of cash, marketable securities, royalty receivables, other assets, accounts payable, and accrued expenses approximates fair value because of the short period of time between the origination of such instruments and their expected realization and their current market rates of interest. Marketable securities available for sale are measured at fair value on a recurring basis based on Level 1 inputs (see Note H).

### Reclassification

The Company has reclassified certain amounts in prior period unaudited condensed consolidated financial statements to conform to the current period's presentation.

## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### Recent Accounting Pronouncements

In August 2016, the FASB issued ASU No. 2016-15, *Classification of Certain Cash Receipts and Cash Payments*, which amends ASC 230, *Statement of Cash Flows*. This ASU provides guidance on the statement of cash flows presentation of certain transactions where diversity in practice exists. The guidance is effective for interim and annual periods beginning after December 15, 2017, and early adoption is permitted. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's condensed consolidated financial statements.

In March 2016, the FASB issued Accounting Standards Update ("ASU") No. 2016-09, *Compensation-Stock Compensation (Topic 718): Improvement to Employee Share-based Payment Accounting (ASU 2016-09)* to simplify the accounting for share-based payment transactions, including the income tax consequences, an option to recognize gross share-based compensation expense with actual forfeitures recognized as they occur, as well as certain classifications on the statement of cash flows. This guidance will be effective for us in the first quarter of 2017, and early adoption is permitted. Management is still evaluating the effect that this guidance will have on our consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. ASU No. 2016-02 is effective for annual periods beginning after December 15, 2018, and requires a lessee to recognize assets and liabilities for leases with a maximum possible term of more than 12 months. A lessee would recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the leased asset (the underlying asset) for the lease term. Early application is permitted. The Company is currently evaluating the impact the adoption of the accounting standard will have on its unaudited condensed consolidated financial statements.

In May 2014, FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU No. 2014-09 provides for a single comprehensive model for use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The accounting standard is effective for interim and annual periods beginning after December 15, 2016 with no early adoption permitted. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which deferred the effective date of ASU No. 2014-09 to annual periods beginning after December 2017, along with an option to permit early adoption as of the original effective date. We are required to adopt the amendments in ASU No. 2014-09 using one of two acceptable methods. In April 2016, the FASB issued ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*. The ASU clarifies the following two aspects of Topic 606: (a) identifying performance obligations; and (b) the licensing implementation guidance. The ASU does not change the core principle of the guidance in Topic 606. The effective date and transition requirements for the ASU are the same as the effective date and transition requirements in Topic 606. Public entities should apply the ASU for annual reporting periods beginning after December 15, 2017, including interim reporting periods therein (i.e., January 1, 2018, for a calendar year entity). Early application for public entities is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Management is currently in the process of determining which adoption method it will apply and evaluating the impact of the guidance on our consolidated financial statements.

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**Accounting Standards Adopted in the Period

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, *Income Taxes (Topic 740); Balance Sheet Classification of Deferred Taxes* (ASU 2015-17), which simplifies the presentation of deferred income taxes by requiring that deferred tax assets and liabilities be classified as noncurrent on the balance sheet. The updated standard is effective beginning on January 1, 2017 with early application permitted as of the beginning of any interim or annual reporting period. Effective January 1, 2016, the Company has elected to early adopt the standard and classify the deferred tax assets as non-current assets on the condensed consolidated balance sheets.

**NOTE C - PATENTS**

The Company's intangible assets at September 30, 2016 include patents with estimated remaining economic useful lives ranging from 3.75 to 5 years. For all periods presented, all of the Company's patents were subject to amortization. The gross carrying amounts and accumulated amortization related to acquired intangible assets as of September 30, 2016 and December 31, 2015 are as follows:

	<u>September 30, 2016</u>	<u>December 31, 2015</u>
Gross carrying amount – patents	\$ 6,389,000	\$ 6,385,000
Accumulated amortization – patents	(5,143,000)	(4,383,000)
Patents, net	<u>\$ 1,246,000</u>	<u>\$ 2,002,000</u>

Amortization expense for the three months ended September 30, 2016 and September 30, 2015 was \$49,000 and \$413,000, respectively. Amortization expense for the nine months ended September 30, 2016 and September 30, 2015 was \$760,000 and \$1,239,000. Future amortization of current intangible assets is as follows:

**Twelve Months Ended September 30,**

2017	\$ 196,000
2018	\$ 196,000
2019	\$ 193,000
2020	\$ 189,000
2021 and thereafter	\$ 472,000
Total	<u>\$ 1,246,000</u>

The Company's Remote Power Patent expires in March 2020. The expiration dates of the patents within the Company's Mirror Worlds Patent Portfolio range from August 2017 to February 2020 (six of the patents in the Mirror Worlds Patent Portfolio have expired as of September 30, 2016 including the Company's '227 Patent which was the subject of litigation - see Note K[2] hereof). The expiration dates of the patents within the Cox Patent Portfolio range from September 2021 to November 2023 and the expiration date of the QoS Patents is June 2019.

## NOTE D – STOCK-BASED COMPENSATION

### Restricted Stock Units

During the three month period ended September 30, 2016, the Company granted, under the Company's 2013 Stock Incentive Plan, 750,000 restricted stock units (RSUs) to its Chairman and Chief Executive Officer in accordance with his new employment agreement (see Note J[1]). The 750,000 RSUs vest in three tranches, as follows: (i) 250,000 RSUs vest on July 14, 2018, subject to the Chairman and Chief Executive Officer's continued employment by the Company through the vesting date (the "Employment Condition"); (ii) 250,000 RSUs vest at any time beginning July 14, 2018 through July 14, 2021 in equal annual installments for the remaining term of employment, subject to (1) the Employment Condition being satisfied through each such annual vesting date and (2) the Company's common stock achieving a closing price (for 20 consecutive trading days) of a minimum of \$3.25 per share (subject to adjustment for stock splits) at any time during the term of employment; and (iii) 250,000 RSUs shall vest at any time beginning July 14, 2018 through July 14, 2021 in equal annual installments for the remaining term of employment subject to (1) the Employment Condition being satisfied through each such annual vesting date and (2) the Company's common stock achieving a closing price (for 20 consecutive trading days) of a minimum of \$4.25 per share (subject to adjustment for stock splits) at any time during the term of employment. Notwithstanding the aforementioned, in the event of a Change of Control (as defined), a Termination Other Than for Cause (as defined), or a termination of employment by Mr. Horowitz for Good Reason (as defined), all of the 750,000 RSUs issued to the Company's Chairman and Chief Executive Officer shall accelerate and become immediately fully vested.

During the nine month period ended September 30, 2016, the Company granted 15,000 RSUs to each of its three non-management directors. Such RSUs issued to the non-management directors vested 7,500 RSUs on June 9, 2016 (the date of grant), 3,750 RSUs on September 9, 2016 and will vest 3,750 RSUs on December 9, 2016 (subject to continued service as a member of the Board of Directors). During the nine month period ended September 30, 2016, the Company granted 50,000 RSUs to each of its Chief Financial Officer and Executive Vice President, and 40,000 RSUs to a consultant to the Company. Each of such RSUs vest 50% on the one year anniversary of grant (June 9, 2017) and 50% on the two year anniversary of grant (June 9, 2018). All of the Company's issued RSUs have dividend equivalent rights.

A summary of RSU activity for the nine months ended September 30, 2016 is as follows (each RSU represents the right to receive one share of the Company's common stock):

	<u>Number of Shares</u>	<u>Weighted-Average Grant Date Fair Value</u>
Balance of restricted stock units outstanding at December 31, 2015	—	—
Issuance of restricted stock units	935,000	\$ 2.30
Vested restricted stock units	<u>(33,750)</u>	<u>\$ (2.47)</u>
Balance of unvested restricted stock units at September 30, 2016	<u>901,250</u>	<u>\$ 2.14</u>

Restricted stock unit compensation expense was \$189,000 and \$221,000 for the three and nine months ended September 30, 2016, respectively. There was no restricted stock unit compensation expense for the three and nine month period ended September 30, 2015.

## NOTE D – STOCK-BASED COMPENSATION (continued)

The Company has an aggregate of \$1,932,000 of unrecognized RSU compensation expense as of September 30, 2016 to be expensed over a weighted average period of 2.8 years.

### Stock Options

During the nine month period ended September 30, 2016, the Company's Chief Financial Officer and Executive Vice President exercised stock options to purchase 100,000 shares of the Company's common stock, at an exercise price of \$1.59 per share, and 240,000 shares of common stock, at an exercise price of \$1.60 per share, respectively. The options were exercised on a partial cashless (net exercise) basis by delivery to the Company of an aggregate of 249,820 shares of the Company's common stock (Chief Financial Officer – 50,857 shares and Executive Vice President - 198,963 shares) and \$60,000. In addition, an aggregate of 22,655 shares (Chief Financial Officer – 5,563 shares and Executive Vice President – 17,092 shares) were delivered to fund payroll withholding taxes on exercise, resulting in net shares of 43,580 and 23,945 issued to the Chief Financial Officer and Executive Vice President, respectively, with respect to such option exercises. During the nine month period ended September 30, 2016, a consultant to the Company exercised a stock option to purchase 90,000 shares of the Company's common stock, at an exercise price of \$1.60 per share. Such option was exercised on a cashless (net exercise) basis by delivery to the Company of 72,727 shares of common stock resulting in 17,273 net shares issued to the consultant with respect to such option exercise.

During the nine month period ended September 30, 2015, the Company granted 5-year stock options as an annual grant to each of its three non-management directors to purchase 35,000 shares of its common stock at an exercise price of \$2.34 per share. Such options vest over a one-year period in four equal quarterly amounts which began on April 22, 2015, subject to continued service on the Board.

During the nine month period ended September 30, 2015, the Company's Executive Vice President exercised a stock option to purchase 150,000 shares of the Company's common stock at an exercise price of \$0.90 per share. The option was exercised on a cashless (net exercise) basis by delivery to the Company of 60,000 shares of common stock resulting in 90,000 net shares issued to the Company's Executive Vice President with respect to such option exercise. In addition, during the nine month period ended September 30, 2015, a consultant to the Company exercised a stock option to purchase 50,000 shares of the Company's common stock at an exercise price of \$0.90 per share. The option was exercised on a cashless (net exercise) basis by delivery to the Company of 19,651 shares of common stock resulting in 30,349 net shares issued to the consultant with respect to such option exercise.

The fair value of each option grant on the date of grant is estimated using the Black-Scholes option-pricing model. On the date of grant, the following weighted average assumptions were utilized for options granted during the nine months ended September 30, 2015 (no stock options were granted during the nine month period ended September 30, 2016):

	<b>Nine Months Ended September 30, 2015</b>
Risk-free interest rates	1.39%
Expected option life in years	5 years
Expected stock price volatility	30.24%
Expected dividend yield	-0-

**NOTE D – STOCK-BASED COMPENSATION (continued)**

The following table presents information relating to all stock options outstanding and exercisable at September 30, 2016:

<b>Range of Exercise Price</b>	<b>Options Outstanding</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Life in Years</b>	<b>Options Exercisable</b>	<b>Weighted Average Exercise Price</b>
\$0.83 - \$2.34	2,410,000	\$1.29	2.90	2,410,000	\$1.29

The Company recorded stock-based compensation related to stock option grants of \$0 and \$69,000 for the three months ended September 30, 2016 and September 30, 2015, respectively.

The Company recorded stock based compensation related to stock option grants of \$12,000 and \$243,000 for the nine months ended September 30, 2016 and September 30, 2015, respectively. The Company had no unrecognized stock-based compensation cost as of September 30, 2016. The aggregate intrinsic value of options exercisable at September 30, 2016 was \$3,482,000.

**Warrants**

As of September 30, 2016, the following are the outstanding warrants to purchase shares of the Company's common stock:

	<b>Number of Warrants</b>	<b>Exercise Price</b>	<b>Expiration Date</b>
	250,000	\$2.10	May 21, 2018
	250,000	\$1.40	May 21, 2018
	125,000	\$2.10	July 26, 2018
	125,000	\$1.40	July 26, 2018
Total	750,000		

All of the aforementioned warrants were issued to Recognition Interface, LLC in connection with the Company's acquisition of the Mirror Worlds Patent Portfolio (see Note I[2]).

## NOTE E – INCOME TAXES

Significant components of the income taxes were as follows for the nine and three months ended:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2016	2015	2016	2015
Current				
State	\$ 173,000	\$ 22,000	\$ 89,000	\$ 12,000
Federal	4,025,000	44,000	3,728,000	14,000
Total Current Tax Expense	<u>4,198,000</u>	<u>66,000</u>	<u>3,817,000</u>	<u>26,000</u>
Deferred				
State	154,000	16,000	30,000	16,000
Federal	4,389,000	912,000	1,429,000	246,000
Total Deferred Tax Expense	<u>4,543,000</u>	<u>928,000</u>	<u>1,459,000</u>	<u>262,000</u>
Total income taxes	<u>\$ 8,741,000</u>	<u>\$ 994,000</u>	<u>\$ 5,276,000</u>	<u>\$ 288,000</u>

Significant components of deferred tax assets as of September 30, 2016 and December 31, 2015 consist of the following:

	September 30, 2016	December 31, 2015
Deferred tax assets:		
Net operating carryforwards	—	\$ 6,819,000
Options, warrants and RSUs	415,000	419,000
	<u>\$ 415,000</u>	<u>\$ 7,238,000</u>
Valuation allowance	—	(2,280,000)
Net deferred tax assets	<u>\$ 415,000</u>	<u>\$ 4,958,000</u>

The personal holding company ("PHC") rules under the Internal Revenue Code impose a 20% tax on a PHC's undistributed personal holding company income ("PHC Income"), which means, in general, taxable income subject to certain adjustments. For a corporation to be classified as a PHC, it must satisfy two tests: (i) that more than 50% in value of its outstanding shares must be owned directly or indirectly by 5 or fewer individuals at anytime during the second half of the year (after applying constructive ownership rules to attribute stock owned by entities to their beneficial owners and among certain family members and other related parties) (the "Ownership Test") and (ii) at least 60% of its adjusted ordinary gross income for a taxable year consists of dividends, interest, royalties, annuities and rents (the "Income Test"). In the second half of 2016 to date (as well as



**NOTE E – INCOME TAXES (continued)**

prior years), the Company did not meet the Ownership Test. Due to the significant number of shares held by the Company's largest shareholders, the Company continually assesses its share ownership to determine whether it meets the Ownership Test. If the Ownership Test were met and the income generated by the Company were determined to constitute "royalties" within the meaning of the Income Test, the Company would constitute a PHC and the Company would be subject to a 20% tax on the amount of any PHC Income (which cannot be offset by NOLs) that it does not distribute to its shareholders.

**NOTE F – EARNINGS PER SHARE**

Basic Earnings per share is calculated by dividing the net income (loss) by the weighted average number of outstanding common shares during the period. Diluted per share data includes the dilutive effects of options, warrants and restricted stock units. Potential shares of 4,061,250 and 3,605,000 at September 30, 2016 and September 30, 2015, respectively, consisted of options, warrants and restricted stock units. Computations of basic and diluted weighted average common shares outstanding are as follows:

	<b>Nine Months Ended</b>		<b>Three Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
Weighted-average common shares outstanding – basic	23,291,408	23,597,143	23,320,514	23,273,946
Dilutive effect of options, warrants and restricted stock units	1,409,376	993,344	1,877,628	1,380,753
Weighted-average common shares outstanding – diluted	<u>24,700,784</u>	<u>24,590,487</u>	<u>25,198,142</u>	<u>24,654,699</u>
Options, warrants and restricted stock units excluded from the computation of diluted income (loss) per share because the effect of inclusion would have been anti-dilutive	<u>141,304</u>	<u>105,000</u>	<u>423,913</u>	<u>105,000</u>

## NOTE G – CASH AND CASH EQUIVALENTS

The Company places cash investments in high quality financial institutions insured by the Federal Deposit Insurance Corporation ("FDIC"). At September 30, 2016, the Company maintained a cash balance of \$57,109,000 in excess of FDIC limits.

The Company considers all highly liquid short-term investments purchased with an original maturity of three months or less to be cash equivalents.

Cash and cash equivalents as of September 30, 2016 and December 31, 2015 are composed of:

	<u>September 30, 2016</u>	<u>December 31, 2015</u>
Cash	\$ 17,583,000	\$ 6,283,000
Money market fund	40,176,000	14,325,000
Total	<u>\$ 57,759,000</u>	<u>\$ 20,608,000</u>

## NOTE H - MARKETABLE SECURITIES

Marketable securities are classified as available-for-sale and are recorded at fair market value. Unrealized gains and losses are reported as other comprehensive income or loss. Realized gains and losses are reclassified from other comprehensive income or loss to net income or loss in the period they are realized. At September 30, 2016 and December 31, 2015, the Company's marketable securities consisted of two corporate bonds (aggregate face value \$1,000,000) with a 3.9% and 4.5% coupon and term of greater than three months when purchased. The Company's marketable securities mature in 2021 and it is not the intention of the Company to hold such securities until maturity.

## NOTE I – COMMITMENTS AND CONTINGENCIES

### [1] Legal Fees:

Russ, August & Kabat provides legal services to the Company with respect to its pending patent litigations filed in April 2014 and December 2014 against Google Inc. and YouTube, LLC in the United States District Court for the Southern District of New York relating to certain patents within the Company's Cox Patent Portfolio (see Note K[1] hereof). The terms of the Company's agreement with Russ, August & Kabat provides for legal fees on a full contingency basis ranging from 15% to 30% of the net recovery (after deduction of expenses) depending on the stage of the proceeding in which the result (settlement or judgment) is achieved. The Company is responsible for all of the expenses incurred with respect to this litigation.

Dovel & Luner, LLP provided legal services to the Company with respect to its patent litigation commenced in May 2013 against Apple Inc., Microsoft, Inc. and other major vendors of document system software and computer systems in the United States District Court of Texas, Tyler Division, for infringement of U.S. Patent No. 6,006,227 (part of the Mirror Worlds Patent Portfolio - see Note K[2] hereof). The terms of the Company's agreement with Dovel & Luner LLP provided for legal fees on a contingency basis ranging from 25% to 40% of the net recovery (after deduction of expenses) depending upon the stage of proceeding in which a result (settlement or judgment) is achieved, subject to certain agreed upon contingency fee caps depending upon the amount of the net recovery. The Company paid a certain portion of the expenses incurred with respect to the litigation. For the three and nine month periods ended September 30, 2016, the Company incurred contingent aggregate legal fees and expenses with respect to the litigation of \$10,649,000 to Dovel & Luner, LLP.

## NOTE I – COMMITMENTS AND CONTINGENCIES (continued)

Dovel & Luner, LLP provides legal services to the Company with respect to its patent litigation filed in September 2011 against sixteen (16) data networking equipment manufacturers in the United States District Court for the Eastern District of Texas, Tyler (see Note K[3]). The terms of the Company's agreement with Dovel & Luner LLP essentially provide for legal fees on a full contingency basis ranging from 12.5% to 35% (with certain exceptions) of the net recovery (after deduction for expenses) depending on the stage of the proceeding in which a result (settlement or judgment) is achieved. For the three month period ended September 30, 2016 and September 30, 2015, the Company incurred aggregate contingent legal fees with respect to the litigation of \$2,348,000 and \$442,000, respectively, to Dovel & Luner, LLP. For the nine month period ended September 30, 2016 and September 30, 2015, the Company incurred aggregate contingent legal fees with respect to the litigation of \$2,706,000 and \$665,000. The Company is responsible for a certain portion of the expenses incurred with respect to the litigation.

Dovel & Luner, LLP provided legal services to the Company with respect to the litigation settled in July 2010 against Cisco and several other major data networking equipment manufacturers (see Note K[4]). The terms of the Company's agreement with Dovel & Luner, LLP with respect to this litigation provided for legal fees of a maximum aggregate cash payment of \$1.5 million plus a contingency fee of 24% (based on the settlement being achieved at the trial stage). As a result of the royalty payments payable quarterly by Cisco in accordance with the Company's settlement and license agreement with Cisco, the Company has an obligation to pay Dovel & Luner, LLP (including local counsel) 24% of such royalties received. During the three months ended September 30, 2016 and September 30, 2015, the Company incurred aggregate legal fees to Dovel & Luner LLP, of \$264,000 and \$322,000, respectively, with respect to the litigation. During the nine months ended September 30, 2016 and September 30, 2015, the Company incurred aggregate legal fees to Dovel & Luner, LLP of \$1,824,000 and \$1,868,000 respectively, with respect to the litigation.

### **[2] Patent Acquisitions:**

On February 28, 2013, the Company completed the acquisition of four patents (as well as a pending patent application) from Dr. Ingemar Cox (these patents together with subsequent related patent issuances comprise the Cox Patent Portfolio), a technology leader in digital watermarking content identification, digital rights management and related technologies, for a purchase price of \$1,000,000 in cash and 403,226 shares of the Company's common stock. In addition, the Company is obligated to pay Dr. Cox 12.5% of the net proceeds (after deduction of expenses) generated by the Company from licensing, sale or enforcement of the patents. Since the acquisition of the patent portfolio from Dr. Cox, the Company has been issued eight additional related patents (five patent applications are pending) by the U.S. Patent and Trademark Office ("USPTO"). Professional fees and filing fees of \$169,000 were capitalized as patent cost.

On May 21, 2013, the Company's wholly-owned subsidiary, Mirror Worlds Technologies, LLC, acquired all of the patents previously owned by Mirror Worlds, LLC (which subsequently changed its name to Looking Glass LLC ("Looking Glass")), consisting of nine issued United States patents and five pending applications covering foundational technologies that enable unified search and indexing, displaying and archiving of documents in a computer system (these patents together with subsequent related patent issuances comprise the Mirror Worlds Patent Portfolio). As consideration for the patent acquisition, the Company paid Looking Glass

## NOTE I – COMMITMENTS AND CONTINGENCIES (continued)

\$3,000,000 in cash, and issued 5-year warrants to purchase an aggregate of 1,750,000 shares of the Company's common stock (875,000 shares of common stock at an exercise price of \$1.40 per share and 875,000 shares of common stock at an exercise price of \$2.10 per share) (the "Looking Glass Warrants"). On June 3, 2014, the Company repurchased the Looking Glass Warrants from Looking Glass at a cost of \$505,000.

As part of the acquisition of the Mirror Worlds Patent Portfolio, the Company also entered into an agreement with Recognition Interface, LLC ("Recognition"), an entity that financed the commercialization of the patent portfolio prior to its sale to Mirror Worlds, LLC and also retained an interest in the licensing proceeds of the patent portfolio held by Mirror Worlds, LLC. Pursuant to the terms of the Company's agreement with Recognition, Recognition received (i) 5-year warrants to purchase 250,000 shares of the Company's common stock at an exercise price of \$1.40 per share, and (ii) 5-year warrants to purchase 250,000 shares of common stock at an exercise price of \$2.10 per share. Recognition also received from the Company an interest in the net proceeds realized from the monetization of the Mirror Worlds Patent Portfolio, as follows: (i) 10% of the first \$125 million of net proceeds; (ii) 15% of the next \$125 million of net proceeds; and (iii) 20% of any portion of the net proceeds in excess of \$250 million. For the three and nine month periods ended September 30, 2016, the Company paid Recognition \$1,427,000 and \$2,909,000, respectively, with respect to such net proceeds interest related to the Mirror Worlds Patent Portfolio (see Note K[2] and Note M). In addition, Abacus and Associates, Inc. ("Abacus"), an entity affiliated with Recognition, received a 60-day warrant to purchase 500,000 shares of the Company's common stock at an exercise price of \$2.05 per share. In accordance with the Company's agreement with Recognition, as a result of the exercise of the 60-day warrant by Abacus in July 2013, additional 5-year warrants to purchase an aggregate of 250,000 shares of the Company's common stock were issued to Recognition (125,000 shares at an exercise price of \$2.10 per share and 125,000 shares at an exercise price of \$1.40 per share). As part of the acquisition of the Mirror Worlds Patent Portfolio, professional fees and filing fees of \$409,000 were capitalized as patent cost.

### **[3] Amended Patent Purchase Agreement:**

In January 2005, the Company and Merlot Communications, Inc., the successor of which is BAXL Technologies, Inc. (the "Seller"), amended the Patent Purchase Agreement originally entered into in November 2003 (the "Amendment") pursuant to which the Company paid an additional purchase price of \$500,000 to Seller for the restructuring of future contingent payments to Seller from the licensing or sale of the patents (including the Remote Power Patent and the QoS Patents). The Amendment provided for future contingent payments by the Company to Seller of \$1.0 million upon achievement of \$25 million of Net Royalties (as defined) which payment was made in 2012, an additional \$1.0 million contingent payment upon achievement of \$50 million of Net Royalties (the "Second Contingent Payment") and an additional \$500,000 contingent payment upon achievement of \$62.5 million of Net Royalties from the licensing or sale of the patents acquired from Seller. On March 11, 2015, the Company entered into an agreement with a secured creditor of the Seller, who had all rights with respect to the Second Contingent Payment, pursuant to which the Company paid the secured creditor \$900,000 in full satisfaction of the Second Contingent Payment of \$1.0 million. During the second quarter of 2016, the Company accrued the above final contingent payment of \$500,000 which payment has been made.

## NOTE I – COMMITMENTS AND CONTINGENCIES (continued)

### [4] Services Agreement:

Pursuant to a master services agreement, dated November 30, 2004 (the "Services Agreement"), between the Company and ThinkFire Services USA, Ltd. ("ThinkFire"), the Company was obligated to pay ThinkFire fees from royalty payments received from certain licensees of the Remote Power Patent over the term of the licenses in consideration for services performed on behalf of the Company. On February 10, 2015, the Company entered into an agreement with ThinkFire pursuant to which the Services Agreement was terminated with no further obligations in consideration of the Company's payment of \$285,000 to ThinkFire (\$261,000 of such payment has been included as general and administrative expenses for the nine months ended September 30, 2015).

### [5] Lease Agreements:

The Company leases its principal office space in New York City at a monthly base rent of approximately \$3,700 which lease expires on May 31, 2017.

The Company entered into a lease agreement in July 2011 to rent office space in New Canaan, Connecticut. In August 2015, the Company entered into an agreement to extend the lease for a four year period (expiring September 30, 2019) at a base rent of \$7,000 per month for the first year (increasing \$100 per month each year), which is subject to annual adjustments to reflect increases in real estate taxes and operating expenses.

Mirror Worlds Technologies, LLC, the Company's wholly-owned subsidiary, entered into a one year lease, at a base rent of \$620 per month, to rent office space in Tyler, Texas (expiring April 30, 2017).

## NOTE J - EMPLOYMENT ARRANGEMENTS AND OTHER AGREEMENTS

[1] On July 14, 2016, the Company entered into a new employment agreement ("Agreement") with its Chairman and Chief Executive Officer pursuant to which he continues to serve the Company in such positions for a five year term, at an annual base salary of \$475,000 which shall be increased by 3% per annum during the term of the Agreement. The Agreement established an annual target bonus of \$175,000 for the Chairman and Chief Executive Officer based upon performance. In addition, the Company granted to the Chairman and Chief Executive Officer, under its 2013 Stock Incentive Plan, 750,000 performance based restricted stock units (the "RSUs") which vest in three tranches, as follows: (i) 250,000 RSUs shall vest on July 14, 2018, subject to Mr. Horowitz's continued employment by the Company through the vesting date (the "Employment Condition"); (ii) 250,000 RSUs shall vest at any time beginning July 14, 2018 through July 14, 2021 in equal annual installments for the remaining term of employment, subject to (1) the Employment Condition being satisfied through each such annual vesting date and (2) the Company's common stock achieving a closing price (for 20 consecutive trading days) of a minimum of \$3.25 per share (subject to adjustment for stock splits) at any time during the term of employment; and (iii) 250,000 RSUs vest at any time beginning July 14, 2018 through July 14, 2021 in equal annual installments for the remaining term of employment subject to (1) the Employment Condition being satisfied through each such annual vesting date and (2) the Company's common stock achieving a closing price (for 20 consecutive trading days) of a minimum of \$4.25 per share (subject to adjustment for stock splits) at any time during the term of employment. Notwithstanding the aforementioned, in the event of a Change of Control (as defined), a Termination Other Than for Cause (as defined), or a termination of employment by

**NOTE J - EMPLOYMENT ARRANGEMENTS AND OTHER AGREEMENTS (continued)**

the Chairman and Chief Executive Officer for Good Reason (as defined), all of the 750,000 RSUs shall accelerate and become immediately fully vested. All of the aforementioned RSUs issued to the Company's Chairman and Chief Executive Officer have dividend equivalent rights.

Under the terms of the Agreement, so long as the Chairman and Chief Executive Officer continues to serve as an executive officer of the Company, whether pursuant to the Agreement or otherwise, the Chairman and Chief Executive Officer shall also receive incentive compensation in an amount equal to 5% of the Company's gross royalties or other payments from Licensing Activities (as defined) (without deduction of legal fees or any other expenses) with respect to its Remote Power Patent and a 10% net interest (gross royalties and other payments after deduction of all legal fees and litigation expenses related to licensing, enforcement and sale activities, but in no event shall he receive less than 6.25% of the gross recovery) of the Company's royalties and other payments relating to Licensing Activities with respect to patents other than the Remote Power Patent (including the Mirror Worlds Patent Portfolio and the Cox Patent Portfolio) (collectively, the "Incentive Compensation"). During the three months ended September 30, 2016 and September 30, 2015, the Chairman and Chief Executive Officer earned Incentive Compensation of \$2,029,000 and \$150,000, respectively. During the nine months ended September 30, 2016 and September 30, 2015, the Chairman and Chief Executive Officer earned Incentive Compensation of \$3,996,000 and \$519,000, respectively, which amounts are included in accrued expenses. As of September 30, 2016 and December 31, 2015, \$2,176,000 and \$446,000 of such compensation were included in accrued expenses, respectively. The Incentive Compensation shall continue to be paid to the Chairman and Chief Executive Officer for the life of each of the Company's patents with respect to licenses entered into with third parties during the term of his employment or at anytime thereafter, whether he is employed by the Company or not; provided, that, the Chairman and Chief Executive Officer's employment has not been terminated by the Company "For Cause" (as defined) or terminated by him without "Good Reason" (as defined). In the event of a merger or sale of substantially all of the assets of the Company, the Company has the option to extinguish the right of the Chairman and Chief Executive Officer to receive future Incentive Compensation by payment to him of a lump sum payment, in an amount equal to the fair market value of such future interest as determined by an independent third party expert if the parties do not reach agreement as to such value. In the event that the Chairman and Chief Executive Officer's employment is terminated by the Company "Other Than For Cause" (as defined) or by him for "Good Reason" (as defined), the Chairman and Chief Executive Officer shall also be entitled to (i) a lump sum severance payment of 12 months base salary, (ii) a pro-rated portion of the \$175,000 target bonus provided bonus criteria have been satisfied on a pro-rated basis through the calendar quarter in which the termination occurs and (iii) accelerated vesting of all unvested options, warrants and RSUs.

In connection with the Agreement, the Chairman and Chief Executive Officer has also agreed not to compete with the Company as follows: (i) during the term of the Agreement and for a period of 12 months thereafter if his employment is terminated "Other Than For Cause" (as defined) provided he is paid his 12 month base salary severance amount and (ii) for a period of two years from the termination date, if terminated "For Cause" by the Company or "Without Good Reason" by the Chairman and Chief Executive Officer.

[2] On April 9, 2014, the Company's Chief Financial Officer entered into an offer letter with the Company pursuant to which he continues to serve, on an at-will basis, at an annual base salary of \$157,500 and is eligible to receive incentive or bonus compensation on an annual basis in the discretion of the Company's Compensation Committee. The Chief Financial Officer

## NOTE J - EMPLOYMENT ARRANGEMENTS AND OTHER AGREEMENTS (continued)

received an annual bonus of \$30,000 for the year ended December 31, 2015 and December 31, 2014. In connection with the offer letter, the Chief Financial Officer was issued, under the Company's 2013 Stock Incentive Plan, a 5-year stock option to purchase 50,000 shares of the common stock, at an exercise price of \$1.65 per share, which option vested in two equal amounts (25,000 shares each) on each of December 31, 2014 and December 31, 2015. In addition, in the event the Chief Financial Officer's employment is terminated without "Good Cause" (as defined), he shall receive (i) (a) 6 months base salary or (b) 12 months base salary in the event of a termination without "Good Cause" within 6 months following a "Change of Control" of the Company (as defined) and (ii) accelerated vesting of all remaining unvested shares underlying his options or any other awards he may receive in the future.

In June 2016, the Board of Directors of the Company approved an increase in the annual base salary for its Chief Financial Officer to \$175,000 per annum.

## NOTE K - LEGAL PROCEEDINGS

[1] On April 4, 2014 and December 3, 2014, the Company initiated litigation against Google Inc. and YouTube, LLC in the United States District Court for the Southern District of New York for infringement of several of its patents within the Cox Patent Portfolio acquired from Dr. Ingemar Cox which relate to the identification of media content on the Internet. The lawsuits allege that Google and YouTube have infringed and continue to infringe certain of the Company's patents by making, using, selling and offering to sell unlicensed systems and related products and services, which include YouTube's Content ID system.

In December 2014, Google Inc. filed four petitions to institute *Inter Partes* Review (the "IPRs") at the United States Patent and Trademark Office ("USPTO") pertaining to patents within the Company's Cox Patent Portfolio. Google in each of the four IPRs sought to invalidate certain claims of the patents at issue within the Cox Patent Portfolio which have been asserted in our litigations against Google and YouTube in the United States District Court for the Southern District of New York as described above. On June 23, 2015, the Patent Trial and Appeal Board ("PTAB") of the USPTO issued an order instituting for oral hearing each of the four IPR petitions. The consolidated oral hearing at the PTAB was held on March 9, 2016. On June 21, 2016, the PTAB issued its Final Written Decisions in the four pending IPRs finding eighty-six (86) claims "not unpatentable" (valid) and, in total, one hundred and nineteen (119) out of one hundred and twenty-nine (129) or 92% of the challenged claims of the patents have survived Google's challenges in the IPRs. None of the claims of the patents being asserted in the pending litigations against Google and YouTube were found invalid. On August 18, 2016, Google filed Notices of Appeal to appeal the Final Written Decisions on the IPRs to the United States Court of Appeals for the Federal Circuit.

On April 13, 2015, Google filed a Petition for *Covered Business Method* Review (CBM) at the PTAB seeking to invalidate claims pertaining to the Company's U.S. Patent No. 8,904,464, the patent asserted in the Company's litigation against Google and YouTube filed on December 3, 2014 as referenced above. On October 19, 2015, the PTAB issued an order instituting the *Covered Business Method* Review on certain grounds. The oral hearing took place on May 11, 2016. On October 18, 2016, the PTAB issued its Final Written Decision in favor of the Company with respect to the CBM and ruled that Google had failed to show that any of the thirty-four (34) claims of the Company's patent at issue were unpatentable.

**NOTE K - LEGAL PROCEEDINGS (continued)**

[2] On May 23, 2013, the Company's wholly-owned subsidiary, Mirror Worlds Technologies, LLC, initiated patent litigation in the United States District Court for the Eastern District of Texas, Tyler Division, against Apple, Inc., Microsoft, Inc., Hewlett-Packard Company, Lenovo Group Ltd., Lenovo (United States), Inc., Dell, Inc., Best Buy Co., Inc., Samsung Electronics America, Inc. and Samsung Telecommunications America L.L.C., for infringement of U.S. Patent No. 6,006,227 (the "227 Patent") (one of the patents the Company acquired as part of the acquisition of the Mirror Worlds Patent Portfolio).

On November 6, 2015, the Company entered into a settlement agreement with Microsoft pursuant to which Microsoft (including its customers) received a non-exclusive fully paid license for the Mirror Worlds Patent Portfolio for their remaining life in consideration of a lump sum payment to the Company of \$4,650,000. In addition, as customers of Microsoft, the pending litigation was also dismissed against Hewlett-Packard Corporation, Lenovo Group Ltd., Lenovo (United States), Inc., Dell, Inc., Best Buy Co., Inc., Samsung Electronics of America, Inc. and Samsung Telecommunications America L.L.C.

On July 8, 2016, Mirror Worlds Technologies, LLC, the Company's wholly-owned subsidiary, entered into a settlement agreement with Apple Inc. ("Apple") in connection with litigation in the United States District Court for the Eastern District of Texas, for infringement of the Company's '227 Patent. Under the terms of the settlement agreement, Apple received a fully paid-up non-exclusive license to the '227 Patent for its full term (which expired in June 2016), along with certain rights to other patents in the Company's portfolio. The Company received \$25,000,000 from Apple in consideration for the settlement and fully paid-up license.

[3] In September 2011, the Company initiated patent litigation against sixteen (16) data networking equipment manufacturers (and affiliated entities) in the United States District Court for the Eastern District of Texas, Tyler Division, for infringement of its Remote Power Patent. As of September 30, 2016, the Company had entered into settlements eleven (11) of the defendants, who each entered into non-exclusive license agreements with the Company for its Remote Power Patent. During the three months ended September 30, 2016, the Company entered into settlements with Dell, Inc. (\$6,000,000), Alcatel and ALE, USA (\$4,200,000) aggregating \$10,200,000 of which \$2,300,000 is contingent upon a Court ruling with respect to a pending motion finding any asserted claim of the Company's Remote Power Patent is valid. As a result of the aforementioned settlements, as of September 30, 2016 there were five remaining defendants. The litigation is currently scheduled for trial in March 2017.

[4] In July 2010, the Company settled its patent litigation pending in the United States District Court for the Eastern District of Texas, Tyler Division, against Adtran, Inc, Cisco Systems, Inc. and Cisco-Linksys, LLC, (collectively, "Cisco"), Enterasys Networks, Inc., Extreme Networks, Inc., Foundry Networks, Inc., and 3Com Corporation, Inc. As part of the settlement, Adtran, Cisco, Enterasys, Extreme Networks and Foundry Networks each entered into a settlement agreement with the Company and entered into non-exclusive licenses for the Company's Remote Power Patent (the "Licensed Defendants"). Under the terms of the licenses, the Licensed Defendants paid the Company upon settlement approximately \$32,000,000 and also agreed to license the Remote Power Patent for its full term, which expires in March 2020. In accordance with the Settlement and License Agreement, dated May 25, 2011, Cisco is obliged to pay the Company royalties (which began in the first quarter of 2011) based on its sales of PoE products up to maximum royalty payments per year of \$8,000,000 through 2015 and \$9,000,000 per year thereafter for the remaining term of the patent. The royalty payments are subject to certain



**NOTE K - LEGAL PROCEEDINGS (continued)**

conditions including the continued validity of the Company's Remote Power Patent, and the actual royalty amounts received may be less than the caps stated above. Under the terms of the Agreement, if the Company grants other licenses with lower royalty rates to third parties (as defined in the Agreement), Cisco shall be entitled to the benefit of the lower royalty rates provided it agrees to the material terms of such other license. Under the terms of the Agreement, the Company has certain obligations to Cisco and if it materially breaches such terms, Cisco will be entitled to stop paying royalties to the Company. This would have a material adverse effect on the Company's business, financial condition and results of operations.

**NOTE L – STOCK REPURCHASE**

On August 22, 2011, the Company announced that its Board of Directors approved a share repurchase program to repurchase up to \$2,000,000 of shares of its common stock over the next 12 months ("Share Repurchase Program"). On June 9, 2016, the Board of Directors authorized an extension of the Share Repurchase Program to repurchase up to \$2,654,000 of common stock over the subsequent 12 month period (for a total of up to \$14,000,000 since inception of the program in August 2011). The common stock may be repurchased from time to time in open market transactions or privately negotiated transactions in the Company's discretion. The timing and amount of the shares repurchased is determined by management based on its evaluation of market conditions and other factors. The Share Repurchase Program may be increased, suspended or discontinued at any time.

Since inception of the Share Repurchase Program through September 30, 2016, the Company has repurchased an aggregate of 6,883,104 shares of its common stock at an average price per share of \$1.65 or an aggregate cost of \$11,346,000 (exclusive of commissions). All such repurchased shares have been cancelled. During the nine months ended September 30, 2016, the Company repurchased 500 shares of its common stock at \$1.95 per share. The Company did not repurchase any shares of its common stock during the three month period ended September 30, 2016.

**NOTE M – REVENUE FROM PROFESSIONAL LIABILITY SETTLEMENT**

On April 22, 2016, Mirror Worlds Technologies, LLC ("MWT"), the Company's wholly-owned subsidiary, entered into an agreement pursuant to which it received \$17,500,000 in connection with the settlement of a professional liability claim relating to services rendered in 2008-2010. The Company, through MWT, acquired the claim in May 2013 as part of its acquisition of the Mirror Worlds Patent Portfolio.

**NOTE N – CONCENTRATIONS**

Revenue from three licensees constituted approximately 96% and 90% of the Company's revenue for the three and nine month periods ended September 30, 2016 (exclusive of non-licensing revenue from our professional liability settlement – see Note M above). At September 30, 2016 and December 31, 2015, royalty receivables from two licensees (including one of the licensees referenced in the prior sentence) constituted approximately 82% and 81% of the Company's royalty receivables, respectively.

## **NOTE O – OTHER INVESTMENTS**

During 2013 and 2014 the Company made investments in Lifestreams Technologies Corporation aggregating \$576,000 (the original investment was part of the Company's acquisition of the Mirror Worlds Patent Portfolio – see Note I[2] hereof). Since the Company owned less than 20% of the outstanding equity of Lifestreams and did not have significant influence or control, the Company's investment in Lifestreams was recorded at cost. A portion of the Company's investment in Lifestreams consisted of secured promissory notes (the "Notes"). The Notes all matured on March 31, 2015. At September 30, 2015, Lifestreams remained in default of the Notes and had not completed any additional material financing. As a result, the Company had an impairment of \$386,000 with respect to the investment which had a carrying value at September 30, 2015 of \$190,000 compared with a carrying value at December 31, 2014 of \$576,000. The carrying value of \$190,000 at September 30, 2015 reflected management's estimate at September 30, 2015 of the fair value of the investment (see Note B hereof). The impairment of \$386,000 was included in general and administrative expenses in the Company's Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2015. At December 31, 2015, the balance of the carrying value of \$190,000 at September 30, 2015 was written-off.

## **NOTE P – SUBSEQUENT EVENTS**

**[1]** On October 3, 2016, the Company entered into a settlement agreement with Polycom, Inc. ("Polycom") with respect to litigation pending in the United States District Court for the Eastern District of Texas, Tyler Division, for infringement of Network-1's Remote Power Patent (See Note K[3] hereof). Under the terms of the settlement, Polycom licensed on a non-exclusive basis the Remote Power Patent for its full term (expiring in March 2020), and is obligated to pay a license initiation fee of \$5,000,000 for past sales of its Power over Ethernet ("PoE") products and shall also pay ongoing royalties based on its sales of PoE products. \$2,000,000 of the license initiation fee has been paid and the balance will be paid in three annual installments of \$1,000,000 beginning in October, 2017. Payments due in October 2018 and October 2019 need not be paid by Polycom if all asserted claims of the Company's Remote Power Patent have been found invalid.

**[2]** On November 2, 2016, the Court issued its ruling on the Markman hearing (claim construction) and defendants' motion for Summary Judgment regarding improper claim broadening in the Company's pending patent infringement litigation against Hewlett Packard Company, Avaya Inc., Juniper Networks, Inc. and Axis Communications Inc. involving its Remote Power Patent (see Note K[3] hereof and "Legal Proceedings" at pages 37-38 of the quarterly report). The Court found that all of the original asserted claims of the Remote Power Patent survived the challenge and only one claim (Claim 13 obtained during a Reexamination of the Remote Power Patent at the USPTO in 2014) was invalid due to improper claim broadening.

## **ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION**

THIS QUARTERLY REPORT ON FORM 10-Q CONTAINS FORWARD-LOOKING STATEMENTS WHICH ARE STATEMENTS THAT INCLUDE INFORMATION BASED UPON BELIEF OF OUR MANAGEMENT, AS WELL AS ASSUMPTIONS MADE BY AND INFORMATION AVAILABLE TO MANAGEMENT. STATEMENTS CONTAINING TERMS SUCH AS "BELIEVES", "EXPECTS", "ANTICIPATES", "INTENDS" OR SIMILAR WORDS ARE INTENDED TO IDENTIFY FORWARD LOOKING STATEMENTS. ACTUAL RESULTS, EVENTS AND CIRCUMSTANCES (INCLUDING FUTURE PERFORMANCE, RESULTS AND TRENDS) COULD DIFFER MATERIALLY FROM THOSE SET FORTH IN SUCH STATEMENTS DUE TO VARIOUS RISKS AND UNCERTAINTIES, INCLUDING, BUT NOT LIMITED TO, THOSE DISCUSSED ON PAGES 14-25 OF OUR ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2015 FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON MARCH 30, 2016 AND IN THIS QUARTERLY REPORT.

### **OVERVIEW**

Our principal business is the development, licensing and protection of our intellectual property assets. We presently own twenty-eight (28) patents including (i) our Remote Power Patent covering the delivery of power over Ethernet cables for the purpose of remotely powering network devices, such as wireless access ports, IP phones and network based cameras; (ii) our Mirror Worlds Patent Portfolio relating to foundational technologies that enable unified search and indexing, displaying and archiving of documents in a computer system; (iii) our Cox Patent Portfolio relating to enabling technology for identifying media content on the Internet and taking further action to be performed based on such identification; and (iv) our QoS Patents covering systems and methods for the transmission of audio, video and data in order to achieve high quality of service (QoS) over computer and telephony networks. In addition, we continually review opportunities to acquire or license additional intellectual property.

We have been actively engaged in the licensing of our Remote Power Patent (U.S. Patent No. 6,218,930). As of November 1, 2016, we have entered into twenty-five (25) license agreements with respect to our Remote Power Patent which, among others, include license agreements with Cisco Systems, Inc., Extreme Networks, Inc., Netgear, Inc., Microsemi Corporation, Motorola Solutions, Inc., NEC Corporation, Samsung Electronics Co., Ltd., Dell, Inc., Huawei Technologies Co., Ltd and ShoreTel, Inc. and several other major data networking equipment manufacturers. Our current strategy includes continuing our licensing efforts with respect to our Remote Power Patent and our efforts to monetize our Cox Patent Portfolio and our Mirror Worlds Patent Portfolio which we acquired in 2013. In addition, we continue to seek to acquire additional intellectual property assets to develop, commercialize, license or otherwise monetize such intellectual property. Our strategy includes working with inventors and patent owners to assist in the development and monetization of their patented technologies. We may also enter into strategic relationships with third parties to develop, commercialize, license or otherwise monetize their intellectual property. Our acquisition strategy is to focus on acquiring high quality patents which management believes have the potential to generate significant licensing opportunities as we have achieved with respect to our Remote Power Patent and Mirror Worlds Patent Portfolio. Our Remote Power Patent generated licensing revenue in excess of \$100,000,000 from May 2007 through September 30, 2016. As a result of our acquisition of the Mirror Worlds Patent Portfolio in May 2013, we achieved licensing and other revenue of \$47,150,000 through September 30, 2016 (see Note K[2] and Note M to our financial statements in this quarterly report).

The validity of our Remote Power Patent and certain patents within our Cox Patent Portfolio are currently being challenged in pending patent infringement litigation (see "Legal Proceedings" on pages 35-36 of this quarterly report and below). If certain claims of our Remote Power Patent are ultimately determined to be invalid, such a determination would have a material adverse effect on our business, financial condition and results of operations as our current revenue stream is largely dependent upon the continued validity of certain claims of our Remote Power Patent. If certain of the patents within our Cox Patent Portfolio are ultimately determined to be invalid, such a determination could have a material adverse effect on our ability to increase our revenue and profits in the future.

On May 22, 2013, through our wholly-owned subsidiary, Mirror Worlds Technologies, LLC, we initiated patent litigation against Apple Inc., Microsoft, Inc., Hewlett-Packard Company, Lenovo Group Ltd., Lenovo (United States), Inc., Dell, Inc., Best Buy Co., Inc., Samsung Electronics America, Inc. and Samsung Telecommunications America L.L.C., in the United States District Court for the Eastern District of Texas, Tyler Division, for infringement of U.S. Patent No. 6,006,227 (part of the Mirror Worlds Patent Portfolio). On November 6, 2015, we settled our litigation with Microsoft and its customers for \$4,650,000. On July 8, 2016, we settled our litigation with Apple Inc. for \$25,000,000 (See "Legal Proceedings" at page 37 hereof).

In September 2011, we initiated patent litigation against sixteen (16) data networking equipment manufacturers in the United States District Court for the Eastern District of Texas, Tyler Division, for infringement of our Remote Power Patent. We have since settled the litigation against twelve (12) of the defendants (see "Legal Proceedings" at pages 37-38 hereof including recent settlements achieved in July 2016 with Dell, Inc. for \$6,000,000 plus ongoing royalties, Alcatel and ALE, USA for an aggregate of \$4,200,000 (of which \$2,300,000 is contingent upon a court ruling) and in October 2016 with Polycom, Inc. for \$5,000,000 plus ongoing royalties (see Legal Proceedings at page 38 hereof). The trial with respect to this litigation is currently scheduled for March 2017.

On April 4, 2014 and December 3, 2014, we initiated litigation against Google Inc. and YouTube, LLC in the United States District Court for the Southern District of New York for infringement of several of our patents within the Cox Patent Portfolio relating to the identification of media content on the Internet. The lawsuits allege that Google and YouTube have infringed and continue to infringe certain of our patents by making, using, selling and offering to sell unlicensed systems and related products and services, which include YouTube's Content ID system. The Company has successfully defended the asserted patents and other patents within the Cox Patent Portfolio in IPR and CBM proceedings at the PTAB (see "Legal Proceedings" pages 35-36 hereof).

On April 22, 2016, Mirror Worlds Technologies, LLC, our wholly-owned subsidiary, entered into an agreement pursuant to which it received \$17,500,000 in connection with a settlement of a professional liability claim relating to services rendered in 2008 - 2010. We acquired the claim in May 2013 as part of our acquisition of the Mirror Worlds Patent Portfolio (see Note M to our financial statements included in this quarterly report).

As a result of a settlement in July 2010 of patent litigation we had initiated against Cisco Systems, Inc. and Cisco-Linksys, LLC (collectively "Cisco"), we entered into non-exclusive licenses for our Remote Power Patent with Cisco and the other defendants. For the nine months ended September 30, 2016 and September 30, 2015, our revenue from Cisco constituted 17% and 71% of our revenue (exclusive of revenue from our professional liability settlement – see Note [M] hereof), respectively. It is anticipated that one or a few of our licensees will continue to constitute a significant portion of our revenue in the foreseeable future. In accordance with our Settlement and License Agreement, dated May 25, 2011, Cisco is obligated to pay us royalties (which began in the first quarter of 2011) based on its sales of PoE products up to maximum royalty payments of \$9 million per year for the remaining term of the patent (March 2020) (\$8 million through 2015). Royalty payments are subject to certain conditions including the continued validity of certain claims of our Remote Power Patent, and the actual revenue received may be less than the caps stated above. Due to our annual royalty rate structure with Cisco which includes declining rates as the volume of PoE product sales increase during the year, royalties from Cisco are anticipated to be highest in the first quarter of the calendar year and decline for each of the remaining calendar quarters of the year.

The personal holding company ("PHC") rules under the Internal Revenue Code impose a 20% tax on a PHC's undistributed personal holding company income ("PHC Income", which means, in general, taxable income subject to certain adjustments). For a corporation to be classified as a PHC, it must satisfy two tests: (i) that more than 50% in value of its outstanding shares must be owned directly or indirectly by 5 or fewer individuals at anytime during the second half of the year (after applying constructive ownership rules to attribute stock owned by entities to their beneficial owners and among certain family members and other related parties) (the "Ownership Test") and (ii) at least 60% of its adjusted ordinary gross income for a taxable year consists of dividends, interest, royalties, annuities and rents (the "Income Test"). During the second half of 2016 to date (as well as prior years), we did not meet the Ownership Test. Due to the significant number of shares held by our largest shareholders, we will continually assess our share ownership to determine whether it meets the Ownership Test. If the Ownership Test were met and the income generated by us were determined to constitute "royalties" within the meaning of the Income Test, we would constitute a PHC and we would be subject to a 20% tax on the amount of any PHC Income (which cannot be offset by NOLs) that we do not distribute to our shareholders.

## RESULTS OF OPERATIONS

### Three Months Ended September 30, 2016 Compared to Three Months Ended September 30, 2015

*Revenue.* We had revenue of \$34,326,000 for the three months ended September 30, 2016 as compared to revenue of \$3,008,000 for the three months ended September 30, 2015. The increase in revenue of \$31,318,000 for the three months ended September 30, 2016, was due primarily to additional licensing revenue of \$32,900,000 from litigation settlements with Apple Inc. (\$25,000,000), Dell, Inc. (\$6,000,000) and Alcatel and ALE USA Inc. (\$1,900,000) (see Note K[2] and Note K[3] to our financial statements included in this quarterly report). Revenue from royalty bearing licenses for our patents (exclusive of litigation settlements) decreased \$232,000 or 14% from \$1,658,000 to \$1,426,000 for the three months ended September 30, 2016 compared to the three months ended September 30, 2015.

*Operating Expenses.* Operating expenses for the three months ended September 30, 2016 were \$18,242,000 as compared to \$2,324,000 for the three months ended September 30, 2015. The increase in operating expenses of \$15,918,000 was primarily due to increased costs of revenue related to our litigation settlements of an aggregate of \$32,900,000 for the three month period ended September 30, 2016. We had costs of revenue of \$16,943,000 and \$927,000 for the three months ended September 30, 2016 and September 30, 2015, respectively. Included in the costs of revenue for three months ended September 30, 2016 were contingent legal fees and expenses of \$13,273,000, other contractual payments of \$1,641,000 and \$2,029,000 of incentive bonus compensation payable to our Chairman and Chief Executive Officer pursuant to his employment agreement (see Note I[1], Note I[2] and Note J[1] to our financial statements included in this quarterly report). Included in the costs of revenue for the three months ended September 30, 2015 were contingent legal fees and expenses of \$777,000 payable to our patent litigation counsel and \$150,000 of incentive bonus compensation payable to our Chairman and Chief Executive Officer pursuant to his employment agreement.

General and administrative expenses decreased by \$12,000 from \$440,000 for the three months ended September 30, 2015 to \$428,000 for the three months ended September 30, 2016. Amortization of patents was \$49,000 for the three months ended September 30, 2016 as compared to \$413,000 for the three months ended September 30, 2015. Stock-based compensation expense related to the issuance of restricted stock units was \$189,000 for the three months ended September 30, 2016 as compared to \$69,000 for vesting of stock options for the three months ended September 30, 2015. Professional fees and related costs were \$633,000 for the three months ended September 30, 2016 as compared to \$475,000 for the three months ended September 30, 2015.

*Interest Income.* Interest income for the three months ended September 30, 2016 was \$24,000 as compared to interest income of \$11,000 for the three months ended September 30, 2015.

*Operating Income.* We had operating income of \$16,084,000 for the three months ended September 30, 2016 compared with an operating income of \$684,000 for the three months ended September 30, 2015. The increased operating income of \$15,400,000 for the three months ended September 30, 2016 was primarily due to licensing revenue of \$32,900,000 received from litigation settlements (see Note K to our financial statements included in this quarterly report).

*Current Taxes.* Federal, state and local income taxes of \$3,817,000 and \$26,000 were recorded for the three months ended September 30, 2016 and September 30, 2015, respectively. The increase of \$3,791,000 in such taxes was related to our fully utilizing NOLs during the three month period ended September 30, 2016 in connection with significant net income.

*Deferred Tax Expense.* We recorded deferred tax expense of \$1,459,000 and \$262,000 for the three months ended September 30, 2016 and September 30, 2015, respectively. The increase of \$1,197,000 was due to utilization of NOLs in connection with significant net income. At June 30, 2016, we had deferred tax assets of \$1,874,000 which was reduced by \$1,459,000 of deferred tax expense for the three months ended September 30, 2016.

*Net Income.* As a result of the foregoing, we realized net income of \$10,832,000 or \$0.46 per share (basic) and \$0.43 per share (diluted) for the three months ended September 30, 2016 compared with net income of \$407,000 or \$0.02 per share (basic and diluted) for the three months ended September 30, 2015.

## RESULTS OF OPERATIONS

### Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015

*Revenue.* We had revenue of \$59,963,000 for the nine months ended September 30, 2016 as compared to revenue of \$10,382,000 for the nine months ended September 30, 2015. The increase in revenue of \$49,581,000 for the nine months ended September 30, 2016, was due primarily to additional licensing revenue of \$32,900,000 from litigation settlements with Apple Inc. (\$25,000,000), Dell, Inc. (\$6,000,000), and Alcatel and ALE USA Inc. (\$1,900,000) - see Note K[2] and Note K[3] to our financial statements included in this quarterly report) as well as our \$17,500,000 settlement of a professional liability claim (see Note M to our financial statements included in this quarterly report). Revenue from royalty bearing licenses for our patents (exclusive of litigation settlements) increased \$70,000 or 1% from \$8,593,000 to \$8,663,000 for the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015.

*Operating Expenses.* Operating expenses for the nine months ended September 30, 2016 were \$28,390,000 as compared to \$7,715,000 for the nine months ended September 30, 2015. The increase in operating expenses of \$20,675,000 was primarily due to an increase in costs of revenue of \$21,089,000 primarily related to patent litigation settlements of an aggregate of \$32,900,000 and our \$17,500,000 professional liability settlement (see Note K and Note M to our financial statements included in this quarterly report) We had costs of revenue of \$24,183,000 and \$3,094,000 for the nine months ended September 30, 2016 and September 30, 2015, respectively. Included in the costs of revenue for nine months ended September 30, 2016 were contingent legal fees of \$16,841,000, other contractual payments of \$3,345,000 and \$3,996,000 of incentive bonus compensation payable to our Chairman and Chief Executive Officer pursuant to his employment agreement (see Note I and Note J[1] to our financial statements included in this quarterly report). Included in the costs of revenue for the nine months ended September 30, 2015 were contingent legal fees and expenses of \$2,575,000 payable to our patent litigation counsel and \$519,000 of incentive bonus compensation payable to our Chairman and Chief Executive Officer pursuant to his employment agreement.

General and administrative expenses decreased by \$635,000 from \$1,891,000 for the nine months ended September 30, 2015 to \$1,256,000 for the nine months ended September 30, 2016, due primarily to our write-off of the balance of our investment in Lifestreams of \$386,000 (see Note O to our financial statements included herein) and termination of our services agreement of \$261,000 during the nine months ended September 30, 2015 (see Note I[4] to our financial statements included herein). Amortization of patents was \$760,000 for the nine months ended September 30, 2016 as compared to \$1,239,000 for the nine months ended September 30, 2015. Stock-based compensation expense related to the issuance of restricted stock units and the vesting of stock options was \$233,000 for the nine months ended September 30, 2016 as compared to \$243,000 for the issuance of stock options for the nine months ended September 30, 2015. Professional fees and related costs were \$1,458,000 for the nine months ended September 30, 2016 as compared to \$1,248,000 for the nine months ended September 30, 2015. Contingent patent cost was \$500,000 for the nine months ended September 30, 2016 (see Note I[2]).

*Interest Income.* Interest income for the nine months ended September 30, 2016 was \$50,000 as compared to interest income of \$44,000 for the nine months ended September 30, 2015.

*Operating Income.* We had operating income of \$31,573,000 for the nine months ended September 30, 2016 compared with operating income of \$2,667,000 for the nine months ended September 30, 2015. The increased operating income of \$28,906,000 for the nine months ended September 30, 2016 was primarily due to licensing revenue of \$32,900,000 from settlements of patent litigation and revenue of \$17,500,000 from settlement of a professional liability claim (see Note K and Note M to our financial statements included in this quarterly report).

*Current Taxes.* Federal, state and local income taxes of \$4,198,000 and \$66,000 were recorded for the nine months ended September 30, 2016 and September 30, 2015, respectively.

*Deferred Tax Expense.* We recorded deferred tax expense of \$4,543,000 and \$928,000 for the nine months ended September 30, 2016 and September 30, 2015, respectively. The increase of \$3,615,000 was due to utilization of NOLs in connection with significant net income. At December 31, 2015, we had deferred tax assets of \$4,958,000 which was reduced by \$4,543,000 of deferred tax expense for the nine month period ended September 30, 2016.

*Net Income.* As a result of the foregoing, we realized net income of \$22,882,000 or \$0.98 per share (basic) and \$0.93 per share (diluted) for the nine months ended September 30, 2016 compared with net income of \$1,717,000 or \$0.07 per share (basic and diluted) for the nine months ended September 30, 2015.

## **LIQUIDITY AND CAPITAL RESOURCES**

We have financed our operations primarily from revenue from licensing our patents. At September 30, 2016, our principal sources of liquidity consisted of cash and cash equivalents of \$57,759,000 and working capital of \$50,179,000. We believe based on our current cash position and projected licensing revenue from our existing license agreements and other revenue that we will have sufficient cash to fund our operations for the foreseeable future.

Working capital increased by \$28,468,000 to \$50,179,000 at September 30, 2016 as compared to working capital of \$21,711,000 at December 31, 2015. The increase in working capital for the nine months ended September 30, 2016 was primarily due to an increase of \$37,151,000 of cash and cash equivalents primarily as a result of litigation settlements, offset by an increase in accrued expenses of \$4,020,000 and an increase in income taxes payable of \$4,080,000.

Net cash provided by operating activities for the nine months ended September 30, 2016 increased by \$34,199,000 from \$2,941,000 for the nine months ended September 30, 2015 to \$37,140,000 for the nine months ended September 30, 2016. The increase in net cash provided by operating activities for the nine months ended September 30, 2016 was primarily due to net income of \$22,882,000, a reduction in deferred taxes of \$4,543,000 and an increase in accrued expenses of \$4,020,000 and an increase in income taxes payable at \$4,080,000.

Net cash used in investing activities for the nine months ended September 30, 2016 and September 30, 2015 was \$4,000 and \$36,000, respectively, related to the purchase of patents and other assets.

Net cash provided by (used in) financing activities for the nine months ended September 30, 2016 and September 30, 2015 was \$15,000 and \$(2,555,000), respectively, from the exercise of stock options in 2016 and our repurchase of common stock as part of our share repurchase program in 2015.

We maintain our cash primarily in money market accounts. Accordingly, we do not believe that our investments have significant exposure to interest rate risk.



## **OFF-BALANCE SHEET ARRANGEMENTS**

We do not have any off-balance sheet arrangements.

## **CONTRACTUAL OBLIGATIONS**

We do not have any long-term debt, capital lease obligations, operating lease obligations, purchase obligations or other long-term liabilities except for the lease obligations set forth in Note I[5] to our financial statements included in this quarterly report.

## **CRITICAL ACCOUNTING POLICIES**

Our discussion and analysis of our financial condition, results of operations, and cash flows are based on our unaudited condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of financial statements included in this quarterly report on Form 10-Q requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. The significant estimates and assumptions made in the preparation of our unaudited condensed consolidated financial statements include, deferred income taxes, income tax payable, valuation of warrants and stock-based payments, accrued expenses and valuation of marketable securities. Actual results could be materially different from those estimates, upon which the carrying values were based.

Our critical accounting policies include:

- Revenue recognition;
- Patents;
- Income Taxes
- Impairment of long lived assets; and
- Stock based compensation.

### **Revenue Recognition**

We recognize revenue received from the licensing of our intellectual property and other related intellectual property activities. Revenue is recognized when (i) persuasive evidence of an arrangement exists, (ii) all obligations have been performed pursuant to the terms of the license or other applicable agreement, (iii) amounts are fixed or determinable, and (iv) collectability of amounts is reasonably assured. We rely on royalty reports received from third party licensees to record our revenue. From time to time we may audit royalties reported from our licensees. Any adjusted royalty revenue as a result of such audits is recorded by us in the period in which such adjustment is agreed to by us and the licensee or otherwise determined.

### **Patents**

We own patents that relate to various technologies. We capitalize the costs associated with acquisition, registration and maintenance of our acquired patents and amortize these assets over their remaining useful lives on a straight-line basis. Any further payments made to maintain or develop the patents would be capitalized and amortized over the balance of the useful life for the patents.

## **Income Taxes**

We account for income taxes in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 740, "Income Taxes" (ASC 740), which requires us to use the assets and liability method of accounting for income taxes. Under the assets and liability method, deferred income taxes are recognized for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between financial statement carrying amounts and the tax bases of existing assets and liabilities and operating loss and tax credit carry forward. Under this accounting standard, the effect on deferred income taxes of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recognized if it is more likely than not that some portion, or all of, a deferred tax asset will not be realized.

## **Impairment of long-lived assets**

Intangible assets with finite lives are tested for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. Accordingly, we record impairment losses on long-lived assets used in operations or expected to be disposed of when indicators of impairment exist and the undiscounted cash flows expected to be derived from those assets are less than carrying amounts of these assets. At September 30, 2016 and December 31, 2015, there was no impairment to our patents.

## **Stock-based compensation**

We account for our stock-based compensation awards to employees and directors in accordance with FASB ASC Topic 718, *Compensation - Stock Compensation* ("ASC 718"). ASC 718 requires all stock-based payments to employees, including grants of employee stock options and restricted stock units, to be recognized in the unaudited condensed consolidated statements of operations and comprehensive income (loss) based on their grant date fair values. Compensation expense related to awards to employees is recognized on a straight-line basis based on the grant date fair value over the associated service period of the award, which is generally the vesting term. Share-based payments issued to non-employees are recorded at their fair values, and are periodically revalued as the equity instruments vest and are recognized as expense over the related service period in accordance with the provisions of ASC 718 and ASC Topic 505, *Equity*, and are expensed using an accelerated attribution model. We use the Black-Scholes option pricing model to determine the grant date fair value of options granted. The fair value of restricted stock units is determined based on the number of shares granted and either the quoted market price of our common stock on the date of grant for time-based and performance-based awards, or the fair value on the date of grant using the Monte Carlo Simulation model for market-based awards.

## **Effect of New Accounting Pronouncements**

In August 2016, the FASB issued ASU No. 2016-15, *Classification of Certain Cash Receipts and Cash Payments*, which amends ASC 230, *Statement of Cash Flows*. This ASU provides guidance on the statement of cash flows presentation of certain transactions where diversity in practice exists. The guidance is effective for interim and annual periods beginning after December 15, 2017, and early adoption is permitted. We are currently in the process of evaluating the impact of adoption of this ASU on our condensed consolidated financial statements.

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, *Compensation-Stock Compensation (Topic 718): Improvement to Employee Share-based Payment Accounting (ASU 2016-09)* to simplify the accounting for share-based payment transactions, including the income tax consequences, to provide an option to recognize gross share-based compensation expense with actual forfeitures recognized as they occur, as well as to define certain classifications on the statement of cash flows. This guidance will be effective for us in the first quarter of 2017, and early adoption is permitted. Management is still evaluating the effect that this guidance will have on our consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. ASU No. 2016-02 is effective for annual periods beginning after December 15, 2018, and requires a lessee to recognize assets and liabilities for leases with a maximum possible term of more than 12 months. A lessee would recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the leased asset (the underlying asset) for the lease term. Early application is permitted. We are currently evaluating the impact the adoption of the accounting standard will have on our unaudited condensed consolidated financial statements.

In May 2014, FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU No. 2014-09 provides for a single comprehensive model for use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The accounting standard is effective for interim and annual periods beginning after December 15, 2016 with no early adoption permitted. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which deferred the effective date of ASU No. 2014-09 to annual periods beginning after December 2017, along with an option to permit early adoption as of the original effective date. We are required to adopt the amendments in ASU No. 2014-09 using one of two acceptable methods. In April 2016, the FASB issued ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*. The ASU clarifies the following two aspects of Topic 606: (a) identifying performance obligations, and (b) the licensing implementation guidance. The ASU does not change the core principle of the guidance in Topic 606. The effective date and transition requirements for the ASU are the same as the effective date and transition requirements in Topic 606. Public entities should apply the ASU for annual reporting periods beginning after December 15, 2017, including interim reporting periods therein (i.e., January 1, 2018, for a calendar year entity). Early application for public entities is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Management is currently in the process of determining which adoption method it will apply and evaluating the impact of the guidance on our consolidated financial statements.

#### **Accounting Standards Adopted in the Period**

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, *Income Taxes (Topic 740); Balance Sheet Classification of Deferred Taxes (ASU 2015-17)*, which simplifies the presentation of deferred income taxes by requiring deferred tax assets and liabilities be classified as noncurrent on the balance sheet. The updated standard is effective beginning on January 1, 2017 with early application permitted as of the beginning of any interim or annual reporting period. Effective January 1, 2016, the Company has elected to adopt early the standard and classify the deferred tax assets as non-current assets on our consolidated balance sheets.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not Applicable

### ITEM 4. CONTROLS AND PROCEDURES.

#### (a) Evaluation of Disclosure Controls and Procedures.

Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon this review, these officers concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in applicable rules and forms and is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

#### (b) Changes in Internal Controls

There was no change in our internal control over financial reporting that occurred during the fiscal quarter ended September 30, 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1: LEGAL PROCEEDINGS

#### *Cox Patent Portfolio – Google and YouTube Legal Proceedings*

On April 4, 2014, we initiated litigation against Google Inc. and YouTube, LLC in the United States District Court for the Southern District of New York for infringement of several of our patents within our Cox Patent Portfolio which relate to the identification of media content on the Internet. The lawsuit alleges that Google and YouTube have infringed and continue to infringe certain of our patents by making, using, selling and offering to sell unlicensed systems and related products and services, which include YouTube's Content ID system. In May 2014, the defendants filed an answer to our complaint and asserted defenses of non-infringement and invalidity.

On December 3, 2014, we initiated a second litigation against Google Inc. and YouTube, LLC in the United States District Court for the Southern District of New York for infringement of our then newly issued patent (part of the Cox Patent Portfolio) relating to the identification and tagging of media content (U.S. Patent No. 8,904,464). The lawsuit alleges that Google and YouTube have infringed and continue to infringe the patent by making, using, selling and offering to sell unlicensed systems and products and services related thereto, which include YouTube's content ID system. In January 2015, the defendants filed an answer to our complaint and asserted defenses of non-infringement and invalidity.

The above referenced litigations that we commenced in the United States District Court for the Southern District of New York in April 2014 and December 2014 against Google and YouTube are currently subject to a court ordered stay which has been in effect since July 2015 as a result of the then pending IPRs and CBM proceedings at the Patent Trial and Appeal Board (PTAB) as described below.

In December 2014, Google filed four petitions to institute *Inter Partes* Review proceedings (the "IPRs") at the PTAB pertaining to certain patents within our Cox Patent Portfolio. In each of the IPRs, Google sought to invalidate certain claims of our patents within our Cox Patent Portfolio which have been asserted in our litigations against Google and YouTube pending in the United States District Court for the Southern District of New York as described above. On June 23, 2015, the PTAB issued an order instituting each of the four IPR petitions for oral hearing. The consolidated oral hearing was held on March 9, 2016. On June 20, 2016, the PTAB issued its Final Written Decisions in the four pending IPRs finding eighty-six (86) claims "not unpatentable" (valid) and in total, one hundred nineteen (119) out of one hundred and twenty-nine (129) or 92% of the challenged claims of the patents survived. None of our asserted claims in the pending litigations against Google and YouTube were found invalid. On August 18, 2016, Google filed Notices of Appeal to appeal the PTAB's Final Written Decisions on the IPRs to the United States Court of Appeals for the Federal Circuit.

On April 13, 2015, Google filed a Petition for *Covered Business Method Review* (CBM) at the PTAB seeking to invalidate claims pertaining to our U.S. Patent No. 8,904,464, the patent asserted in our litigation against Google and YouTube filed on December 3, 2014 as referenced above. On October 19, 2015, the PTAB issued an order instituting the *Covered Business Method Review*. The oral hearing (trial) was held on May 11, 2016. On October 18, 2016, the PTAB issued its Final Written Decision in favor of us with respect to the CBM and ruled that Google had failed to show that any of the thirty-four (34) claims of our U.S. Patent 8,904,464 were unpatentable.

#### *Mirror Worlds Patent Portfolio Litigation*

On May 23, 2013, Mirror Worlds Technologies, LLC, our wholly-owned subsidiary, initiated patent litigation in the United States District Court for the Eastern District of Texas, Tyler Division, against Apple Inc., Microsoft Corporation, Hewlett-Packard Company, Lenovo Group Ltd., Lenovo (United States), Inc., Dell, Inc., Best Buy Co., Inc., Samsung Electronics America, Inc. and Samsung Telecommunications America L.L.C., for infringement of U.S. Patent No. 6,006,227 (the "'227 Patent") (one of the patents we acquired as part of our acquisition of the Mirror Worlds Patent Portfolio – see Note I[2] to our financial statements included in this quarterly report). We sought, among other things, monetary damages based upon reasonable royalties. The lawsuit alleged that the defendants have infringed and continue to infringe the claims of the '227 Patent by making, selling, offering to sell and using infringing products including Mac OS and Windows operating systems and personal computers and tablets that include versions of those operating systems, and by encouraging others to make, sell, and use these products. On December 10, 2013, the litigation was severed into two consolidated actions, *Mirror Worlds v. Apple, Inc.* (Case No. 6:13-cv-419), and *Mirror Worlds v. Microsoft, et al.* (Case No. 6:13-cv-941).

On November 6, 2015, we entered into a settlement agreement with Microsoft pursuant to which Microsoft (including its customers) received a non-exclusive fully paid license for the Mirror Worlds Patent Portfolio for its remaining life in consideration of a lump sum payment to us of \$4,650,000. In addition, as customers of Microsoft, the pending litigation was also dismissed against Hewlett-Packard Corporation, Lenovo Group Ltd., Lenovo, Inc., Dell, Inc., Best Buy Co., Inc., Samsung Electronics of America, Inc. and Samsung Telecommunications America L.L.C.

On July 8, 2016, Mirror Worlds Technologies, LLC, our wholly-owned subsidiary, entered into a settlement agreement with Apple Inc. in connection with litigation in the United States District Court for the Eastern District of Texas, for infringement of our '227 Patent (see Note K[2] to our financial statements included in this quarterly report). Under the terms of the settlement agreement, Apple received a fully paid-up non-exclusive license to the '227 Patent for its full term (which expired in June 2016), along with certain rights to other patents in our patent portfolio. We received \$25,000,000 from Apple for the settlement and fully paid non-exclusive license.

#### *Remote Power Patent Legal Proceedings*

In September 2011, we initiated patent litigation against sixteen (16) data networking equipment manufacturers (and affiliated entities) in the United States District Court for the Eastern District of Texas, Tyler Division, for infringement of our Remote Power Patent. Named as defendants in the lawsuit (excluding affiliated parties), were Alcatel-Lucent USA, Inc., Allied Telesis, Inc., Avaya Inc., AXIS Communications Inc., Dell, Inc., GarretCom, Inc., Hewlett-Packard Company, Huawei Technologies USA, Juniper Networks, Inc., Motorola Solutions, Inc., NEC Corporation, Polycom Inc., Samsung Electronics Co., Ltd., ShoreTel, Inc., Sony Electronics, Inc., and Transition Networks, Inc. We seek monetary damages based upon reasonable royalties.

In March 2012, we reached settlement agreements with defendants Motorola Solutions, Inc. ("Motorola") and Transition Networks, Inc. ("Transition Networks"). In October 2012, we reached a settlement with defendant GarretCom, Inc ("GarretCom"). In February 2013, we reached settlement agreements with Allied Telesis, Inc. ("Allied Telesis") and NEC Corporation ("NEC"). As part of the settlements, Motorola, Transition Networks, GarretCom, Allied Telesis and NEC each entered into a non-exclusive license agreement for our Remote Power Patent pursuant to which each such defendant agreed to license our Remote Power Patent for its full term (which expires in March 2020) and pay a license initiation fee and quarterly or annual royalties based on their sales of PoE products. In March 2015 and July 2015, we reached settlements with defendants Samsung Electronics Co., Ltd. ("Samsung"), Huawei Technologies Co., Ltd. ("Huawei") and ShoreTel, Inc. ("ShoreTel"). Samsung and Huawei each entered into a non-exclusive fully paid license agreement for our Remote Power Patent for its full term. ShoreTel entered into a non-exclusive license agreement for the Remote Power Patent for its full term and paid a license initiation fee and agreed to pay quarterly royalties based upon its sales of PoE products. In June 2016, we reached a settlement with Sony Corporation and affiliated entities ("Sony"). With respect to the settlement, Sony received a non-exclusive fully-paid license for our Remote Power Patent for its remaining life.

In July 2016, we reached a settlement with Dell, Inc. Under the terms of the settlement, Dell received a non-exclusive license for our Remote Power Patent for its full term, Dell paid a license initiation fee of \$6,000,000 and agreed to pay quarterly royalties based on its sales of PoE products.

In July 2016, we also reached settlement agreements with Alcatel-Lucent USA, Inc. and Alcatel-Lucent Holdings Inc. (collectively, "Alcatel") and ALE, USA. Under the terms of the settlement agreements, Alcatel and ALE, USA received a non-exclusive fully paid license for our Remote Power Patent for its remaining life. The aggregate consideration to be received by us from Alcatel and ALE for the fully-paid license is \$4,200,000 of which \$1,900,000 has been paid and the balance of \$2,300,000 is payable in three equal quarterly payments beginning no later than January 2, 2017.

On October 3, 2016, we entered a settlement agreement with Polycom, Inc. ("Polycom"). Under the terms of the settlement, Polycom entered into a non-exclusive license for our Remote Power Patent for its full term and is obligated to pay a license initiation fee of \$5,000,000 for past sales of its Power over Ethernet ("PoE") products and ongoing royalties based on its sales of PoE products. \$2,000,000 of the license initiation fee will be paid within 30 days and the balance will be paid in three annual installments of \$1,000,000 beginning in October, 2017. Payments due in October 2018 and October 2019 need not be paid by Polycom if all asserted claims of the Remote Power Patent have been found invalid.

As a result of the aforementioned settlements, the remaining four defendants in the litigation pending in the United States District Court for the Eastern District of Texas are Avaya Inc., AXIS Communications Inc., Hewlett Packard Company, Inc. and Juniper Networks, Inc. On June 2, 2016, a Markman hearing on claim construction was held and oral argument also took place on defendants' motion for summary judgment that all asserted claims of our Remote Power Patent are invalid under 35 U.S.C. §325 for improper broadening. On November 2, 2016, the Court issued its ruling on the Markman hearing and defendants' motion for summary judgment asserting that all claims of the Remote Power Patent were invalid for improper claim broadening. The Court found that all of the original asserted claims of the Remote Power Patent survived the challenge and only one claim (Claim 23 obtained during a Reexamination of the Remote Power Patent at the USPTO in 2014) was invalid due to improper claim broadening. The litigation is scheduled for trial in March 2017.

#### **ITEM 1A. Risk Factors.**

Our operations and financial results are subject to various risks and uncertainties that could adversely affect our business, financial condition, results of operations and trading price of our common stock. In addition to the risks described in this quarterly report, our Annual Report on Form 10-K for the year ended December 31, 2015 (pages 14-25) filed with the Securities and Exchange Commission on March 30, 2016 includes a discussion of our risk factors and should be carefully considered by investors.

#### **ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

##### Recent Issuances of Unregistered Securities

There were no such issuances during the three month period ended September 30, 2016.

##### Stock Repurchases

On August 22, 2011, we announced that our Board of Directors approved a share repurchase program to repurchase up to \$2,000,000 of shares of our common stock over the next 12 months ("Share Repurchase Program"). On June 17, 2015, our Board of Directors authorized its fifth increase to our Share Repurchase Program authorizing the repurchase of up to an additional \$2,000,000 of shares of our common stock over the subsequent 12 month period (for a total of up to \$14,000,000 since inception of the Share Repurchase Program in August 2011). On June 9, 2016, our Board of Directors authorized the extension of the Share Repurchase Program to repurchase up to \$2,654,000 of shares of our common stock over the subsequent 12 month period. The common stock may be repurchased from time to time in open market transactions or privately negotiated transactions in our discretion. The timing and amount of the shares repurchased is determined by management based on its evaluation of market conditions and other factors. The Share Repurchase Program may be increased, suspended or discontinued at any time. Since inception of the Share Repurchase Program in August 2011 through September 30, 2016, we have repurchased an aggregate of 6,883,104 shares of our common stock at an average per share price of \$1.65 or an aggregate cost of \$11,345,803 (exclusive of commissions). During the nine month period ended September 30, 2016, we purchased 500 shares of our common stock at \$1.95 per share. During the three month period ended September 30, 2016, we did not purchase any shares of our common stock.

### ITEM 3. Defaults Upon Senior Securities.

None.

### ITEM 5. Other Information.

#### *Amendment to By-laws*

(a) On November 7, 2016, the Board of Directors (the "**Board**") of the Company adopted the Second Amended and Restated Bylaws (the "**By-laws**") of the Company. The By-laws were effective immediately and include, among other things, the following changes:

- Clarifying the Board's power to cancel, postpone or reschedule a meeting of stockholders;
- Resolving an inconsistency regarding the eligibility requirements for stockholders to call special meetings and providing for procedural requirements in connection therewith;
- Providing for an advance notice requirement for director nominations and stockholder proposals;
- Clarifying the power of the Chairman of a stockholder meeting to regulate the conduct of the meeting;
- Clarifying the power to fill director vacancies;
- Modifying the requirements on removing directors from office;
- Removing an obsolete provision with respect to the Company's ability to make loans to officers; and
- Designating the Court of Chancery of the State of Delaware as the sole and exclusive forum for certain legal action, unless the Company consents in writing to the selection of an alternative forum.

The foregoing description of the By-laws is not complete and is qualified in its entirety by reference to the complete text of the By-laws, a copy of which is filed as Exhibit 3.1 to this Quarterly Report on Form 10-Q and incorporated by reference herein.



## ITEM 6. Exhibits

### (a) Exhibits

- 3.1 Second Amended and Restated By-laws of the Company adopted on November 7, 2016.
- 31.1 Controls and Procedure Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 31.2 Controls and Procedure Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*
- 101 Interactive data files:\*\*
- 101.INS XBRL Instance Document
- 101.SCH XBRL Scheme Document
- 101.CAL XBRL Calculation Linkbase Document
- 101.DEF XBRL Definition Linkbase Document
- 101.LAB XBRL Label Linkbase Document
- 101.PRE XBRL Presentation Linkbase Document

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\* Filed herewith

\*\* Furnished herewith

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**NETWORK-1 TECHNOLOGIES, INC.**

Date: November 10, 2016

By: /s/ Corey M. Horowitz  
Corey M. Horowitz  
Chairman and Chief Executive Officer

Date: November 10, 2016

By: /s/ David C. Kahn  
David C. Kahn  
Chief Financial Officer

**SECOND AMENDED AND RESTATED  
BY-LAWS  
OF  
NETWORK-1 TECHNOLOGIES, INC.**

**A DELAWARE CORPORATION**

**ARTICLE I**

**OFFICES**

**Section 1. REGISTERED OFFICE.** The registered office of the Corporation shall be established and maintained at 32 Loockerman Square, Suite L-100, City of Dover 19901, County of Kent, in the State of Delaware.

**Section 2. OTHER OFFICES.** The Corporation may have offices at such other places both within and without the State of Delaware as the Board of Directors may from time to time determine or the business of the Corporation may require.

**ARTICLE II**

**CORPORATE SEAL**

**Section 3. CORPORATE SEAL.** The corporate seal shall be circular and shall consist of a die bearing the name of the Corporation, the year of its creation and the words "Corporate Seal Delaware." Said seal may be used by causing it, or a facsimile thereof, to be impressed or affixed or otherwise reproduced.

**ARTICLE III**

**STOCKHOLDERS' MEETINGS**

**Section 4. PLACE OF MEETINGS.** Meetings of the stockholders of the Corporation shall be held at such place, either within or without the State of Delaware, as may be designated from time to time by the Board of Directors, or, if not so designated, then at the office of the Corporation required to be maintained pursuant to Section 2 hereof. The Board of Directors may, at any time prior to the holding of a meeting of stockholders (annual or special), and for any reason, cancel, postpone or reschedule such meeting upon public notice given prior to the time previously scheduled for such meeting of stockholders. The meeting may be postponed or rescheduled to such time and place as is specified in the notice of postponement or rescheduling of such meeting.

**Section 5. ANNUAL MEETING.** Annual meetings of stockholders for the election of Directors and for such other business as may be stated in the notice of the meeting, shall be held at such place, either within or without the State of Delaware, and at such time and date as the Board of Directors, by resolution, shall determine and as set forth in the notice of the meeting. If the date of the annual meeting shall fall upon a legal holiday, the meeting shall be held on the next succeeding business day. At each annual meeting, the stockholders entitled to vote shall elect a Board of Directors and may transact such other corporate business as shall be stated in the notice of the meeting.

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**Section 6. SPECIAL MEETINGS.**

(a) Special meetings of the stockholders of the Corporation may be called, for any purpose or purposes, unless otherwise prescribed by law or by the Certificate of Incorporation (as the same may be amended or restated, the "Certificate of Incorporation"), by (i) the Chairman of the Board of Directors, (ii) Chief Executive Officer, or (iii) the Board of Directors, and shall be called by the President or Secretary at the request in writing of holders of a majority of the voting power of all the shares of the Corporation entitled to vote thereat.

(b) Only such business (including nominations and elections of directors) shall be conducted at a special meeting of stockholders as shall have been brought before the meeting pursuant to the Corporation's notice of meeting. Nominations of persons for election to the Board of Directors may be made at a special meeting of stockholders at which directors are to be elected pursuant to the Corporation's notice of meeting (i) by or at the direction of the Board of Directors or (ii) provided that the Board of Directors has determined that directors shall be elected at such meeting, by any stockholder of the Corporation who (A) is a stockholder of record at the time of giving of notice provided for in these By-laws and at the time of the special meeting, (B) is entitled to vote at the meeting, and (C) complies with the notice procedures set forth in these By-laws. In the event the Corporation calls a special meeting of stockholders for the purpose of electing one or more directors to the Board of Directors, any such stockholder may nominate a person or persons (as the case may be) for election to such position(s) as specified in the Corporation's notice of meeting, if the stockholder's notice required by Section 8(b) of these By-laws with respect to any nomination shall be delivered to the Secretary at the principal executive offices of the Corporation not earlier than the close of business on the 120th day prior to the date of such special meeting and not later than the close of business on the later of the 90th day prior to the date of such special meeting; provided, however, in the event that less than 100 days notice or prior public disclosure of the date of such special meeting is given or made to stockholders, notice by the stockholder to be timely must be received no later than the 10<sup>th</sup> day following the earlier of (i) the day on which notice of the special meeting was mailed, or (ii) such public disclosure was first made of the date of the special meeting and of the nominees proposed by the Board of Directors to be elected at such meeting. In no event shall any adjournment or postponement of a special meeting or the announcement thereof commence a new time period for the giving of a stockholder's notice as described above.

**Section 7. NOTICE OF MEETINGS.** Except as otherwise provided by law or the Certificate of Incorporation, written notice of each meeting of stockholders shall be given not less than ten (10) nor more than sixty (60) days before the date of the meeting to each stockholder entitled to vote at such meeting, such notice to specify the place, date, time and purpose or purposes of the meeting. Notice of any meeting of stockholders may be waived in writing, signed by the person entitled to notice thereof, either before or after such meeting, and will be waived by any stockholder by his attendance thereat in person or by proxy, except when the stockholder attends a meeting for the express purpose of objecting, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened. Any stockholder so waiving notice of such meeting shall be bound by the proceedings of any such meeting in all respects as if due notice thereof had been given.

**Section 8. ADVANCE NOTICE PROCEDURES.**

(a) Nominations of persons for election to the Board of Directors and the proposal of other business to be considered by the stockholders may be made at an annual meeting of stockholders (i) as specified by the Corporation's notice of meeting by or at the direction of the Board of Directors, (ii) by or at the direction of the Board of Directors or (iii) by any stockholder of the Corporation who (A) was a stockholder of record at the time of giving of notice provided for in these By-laws and at the time of the annual meeting, (B) is entitled to vote at the meeting and (C) complies with the procedures set forth in these By-laws and applicable law. The foregoing clause (iii) of this Section 8(a) shall be the exclusive means for a stockholder to make nominations or submit other business (other than matters properly brought under Rule 14a-8 under the Securities Exchange Act of 1934, as amended (the "Exchange Act") and included in the Corporation's notice of meeting) before an annual meeting of stockholders.

(b) Without qualification, for any nominations or any other business to be properly brought before an annual meeting by a stockholder pursuant to Section 8(a)(iii) of these By-laws, the stockholder must have given timely notice thereof in writing to the Secretary and such other business must otherwise be a proper matter for stockholder action. To be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of the Corporation not earlier than the close of business on the 120th day and not later than the close of business on the 90th day prior to the first anniversary of the preceding year's annual meeting; provided, however, that in the event that the date of the annual meeting is more than 30 days before or more than 60 days after such anniversary date, notice by the stockholder to be timely must be so delivered not earlier than the close of business on the 120th day prior to the date of such annual meeting and not later than the close of business on the later of the 90th day prior to the date of such annual meeting provided, however, in the event that less than 100 days notice or prior public disclosure of the date of the annual meeting is given or made to stockholders, notice by the stockholder to be timely must be received no later than the 10<sup>th</sup> day following the earlier of (i) the day on which notice of the annual meeting was mailed, or (ii) such public disclosure was first made of the annual meeting. In no event shall any adjournment or postponement of an annual meeting or the announcement thereof commence a new time period for the given of a stockholder's notice as described above.

To be in proper form, a stockholder's notice (whether given pursuant to this paragraph (b) or Section 6(b)) to the Secretary must:

(i) set forth, as to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made (including any affiliate or associate (each within the meaning of Rule 12b-2 under the Exchange Act) of such stockholder or beneficial owner) (A) the name and address of such stockholder, as they appear on the Corporation's books, and of such beneficial owner, if any; (B) (1) the class or series and number of shares of the Corporation which are, directly or indirectly, owned beneficially or of record (within the meaning of Rule 13d-3 under the Exchange Act) by such stockholder and such beneficial owner, if any (except that any such person shall in all events be deemed to beneficially own any shares of any class or series of the Corporation as to which such person has a right to acquire beneficial ownership at any time in the future), (2) any option, warrant, convertible security, stock appreciation right, or similar right with an exercise or conversion privilege or a settlement payment or mechanism at a price related to any class or series of shares of the Corporation, whether or not such instrument or right shall be subject to settlement in the underlying class or series of capital stock of the Corporation or otherwise (a "Derivative Instrument") directly or indirectly owned beneficially by such stockholder and such beneficial owner, if any, any other direct or indirect opportunity to profit or share in any profit derived from any increase or decrease in the value of shares of the Corporation, (3) any proxy, contract, arrangement, understanding, or relationship pursuant to which such stockholder and such beneficial owner, if any, has a right to vote any shares of any security of the Corporation, (4) any short interest of such stockholder or beneficial owner, if any, in any security of the Corporation (for purposes of these By-laws a person shall be deemed to have a short interest in a security if such person directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, has the opportunity to profit or share in any profit derived from any decrease in the value of the subject security), (5) any rights to dividends on the shares of the Corporation owned beneficially by such stockholder or beneficial owner, if any, that are separated or separable from the underlying shares of the Corporation, (6) any proportionate interest in shares of the Corporation or Derivative Instruments held, directly or indirectly, by a general or limited partnership in which such stockholder or beneficial owner, if any, is a general partner or, directly or indirectly, beneficially owns an interest in a general partner and (7) any performance-related fees (other than an asset-based fee) that such stockholder or beneficial owner, if any, is entitled to based on any increase or decrease in the value of shares of the Corporation or Derivative Instruments, if any, as of the date of such notice, including without limitation any such interests held by members of such stockholder's or beneficial owner's immediate family sharing the same household; (C) any other information relating to such stockholder and beneficial owner, if any, that would be required to be disclosed in a proxy statement or other filings required to be made in connection with solicitations of proxies for, as applicable, the proposal and/or for the election of directors in a contested election pursuant to Section 14 of the Exchange Act and the rules and regulations promulgated thereunder; and (D) a representation (1) that the stockholder is a holder of record of stock of the Corporation entitled to vote at such annual meeting and intends to appear in person or by proxy at the annual meeting to propose such business or nomination and (2) whether the stockholder or the beneficial owner, if any, intends or is part of a group which intends (x) to deliver a proxy statement and/or form of proxy to holders of at least the percentage of the Corporation's outstanding capital stock required to approve or adopt the proposal or elect the nominee and/or (y) otherwise to solicit proxies from stockholders in support of such proposal or nomination;

(ii) if the notice relates to any business other than a nomination of a director or directors that the stockholder proposes to bring before the meeting, set forth (A) a brief description of the business desired to be brought before the meeting, the reasons for conducting such business at the meeting and any material interest of such stockholder and beneficial owner, if any, in such business; (B) the text of the proposal or business (including the text of any resolutions proposed for consideration); and (C) a complete and accurate description of all agreements, arrangements and understandings between or among such stockholder and such beneficial owner, if any, and any other person or persons (including their names and addresses) in connection with the proposal of such business by such stockholder; and

(iii) set forth or provide, as to each person, if any, whom the stockholder proposes to nominate for election or reelection to the Board of Directors (A) the name, age, business address and residence address of such person; (B) the principal occupation or employment of such person (present and for the past five (5) years); (C) the class or series and number of shares of capital stock of the Corporation which are owned beneficially and of record by such person; (D) a completed and signed questionnaire, and written representation and agreement, each as required by Section 8(c) of these By-laws; (E) all information relating to such person that would be required to be disclosed in a proxy statement or other filings required to be made in connection with solicitations of proxies for election of directors in a contested election pursuant to Section 14 of the Exchange Act and the rules and regulations promulgated thereunder (including such person's written consent to being named in the proxy statement as a nominee and to serve as a director if elected); and (F) a complete and accurate description of all direct and indirect compensation and other material monetary agreements, arrangements and understandings during the past three years, and any other material relationships, between or among such stockholder and beneficial owner, if any, and their respective affiliates and associates, or others acting in concert therewith, on the one hand, and each proposed nominee, and his or her respective affiliates and associates, or others acting in concert therewith, on the other hand, including, without limitation, all information that would be required to be disclosed pursuant to Rule 404 promulgated under Regulation S-K if the stockholder making the nomination and any beneficial owner on whose behalf the nomination is made, if any, or any affiliate or associate thereof or person acting in concert therewith, were the "registrant" for purposes of such rule and the nominee were a director or executive officer of such registrant.

The Corporation may require any proposed nominee to furnish such other information as may reasonably be required by the Corporation to determine the eligibility of such proposed nominee to serve as an independent director of the Corporation or that could be material to a reasonable stockholder's understanding of the independence, or lack thereof, of such nominee.

(c) To be eligible to be a nominee for election or reelection as a director of the Corporation (whether at an annual or special meeting), a proposed nominee must deliver (in accordance with the time periods prescribed for delivery of notice under these By-laws and applicable law) to the Secretary at the principal executive offices of the Corporation:

(i) a written questionnaire with respect to the background and qualification of such person and the background of any other person or entity on whose behalf the nomination is being made (which questionnaire shall be provided by the Secretary upon written request); and

(ii) a written representation and agreement (in the form provided by the Secretary upon written request) that such person (A) is not and will not become a party to (1) any agreement, arrangement or understanding with, and has not given any commitment or assurance to, any person or entity as to how such person, if elected as a director of the Corporation, will act or vote in such capacity on any issue or question (a "Voting Commitment") that has not been disclosed to the Corporation or (2) any Voting Commitment that could limit or interfere with such person's ability to comply, if elected as a director of the Corporation, with such person's fiduciary duties under applicable law; (B) is not and will not become a party to any agreement, arrangement or understanding with any person or entity other than the Corporation with respect to any direct or indirect compensation, reimbursement or indemnification in connection with service or action as a director of the Corporation that has not been disclosed to the Corporation; (C) if elected as a director of the Corporation, intends to serve a full term, and (D) in such person's individual capacity and on behalf of any person or entity on whose behalf the nomination is being made, would be in compliance, if elected as a director of the Corporation, and will comply with all applicable law and all applicable rules of the U.S. exchanges upon which the common stock of the Corporation is listed and all applicable publicly disclosed corporate governance, conflict of interest, confidentiality and stock ownership and trading policies and other guidelines of the Corporation duly adopted by its Board of Directors.

**Section 9. QUORUM.** At all meetings of stockholders, except where otherwise provided by statute or by the Certificate of Incorporation, or by these By-laws, the presence, in person or by proxy duly authorized, of the holders of a majority of the outstanding shares of stock entitled to vote shall constitute a quorum for the transaction of business. In the absence of a quorum, any meeting of stockholders may be adjourned, from time to time, either by the Chairman of the meeting or by vote of the holders of a majority of the shares represented thereat, but no other business shall be transacted at such meeting. The stockholders present at a duly called or convened meeting, at which a quorum is present, may continue to transact business until adjournment. When a quorum is once present to organize a meeting, it is not broken by the subsequent withdrawal of any stockholders. Except as otherwise provided by law, the Certificate of Incorporation or these By-laws, all action taken by the holders of a majority of the votes cast, excluding abstentions, at any meeting at which a quorum is present shall be valid and binding upon the Corporation; provided, however, that Directors shall be elected by a plurality of the votes of the shares present in person or represented by proxy at the meeting and entitled to vote on the election of Directors. Where a separate vote by a class or classes is required, a majority of the outstanding shares of such class or classes, present in person or represented by proxy, shall constitute a quorum entitled to take action with respect to that vote on that matter and the affirmative vote of the majority (plurality, in the case of the election of Directors) of shares of such class or classes present in person or represented by proxy at the meeting shall be the act of such class.



**Section 10. ADJOURNMENT AND NOTICE OF ADJOURNED MEETINGS .** Any meeting of stockholders, whether annual or special, may be adjourned from time to time either by the Board of Directors or by the Chairman of the meeting or by the vote of a majority of the shares casting votes, excluding abstentions. When a meeting is adjourned to another time or place, notice need not be given of the adjourned meeting if the time and place thereof are announced at the meeting at which the adjournment is taken. At the adjourned meeting, the Corporation may transact any business which might have been transacted at the original meeting. If the adjournment is for more than thirty (30) days or if after the adjournment a new record date is fixed for the adjourned meeting, a notice of the adjourned meeting shall be given to each stockholder of record entitled to vote at the meeting.

**Section 11. VOTING RIGHTS.** For the purpose of determining those stockholders entitled to vote at any meeting of the stockholders, except as otherwise provided by law, only persons in whose names shares stand on the stock records of the Corporation on the record date, as provided in Section 13 of these By-laws, shall be entitled to vote at any meeting of stockholders. Every person entitled to vote or execute consents shall have the right to do so either in person or by an agent or agents authorized by a written proxy executed by such person or his duly authorized agent, which proxy shall be filed with the Secretary at or before the meeting at which it is to be used. An agent so appointed need not be a stockholder. Elections of Directors need not be by written ballot, unless otherwise provided in the Certificate of Incorporation.

**Section 12. JOINT OWNERS OF STOCK.** If shares or other securities having voting power stand of record in the names of two (2) or more persons, whether fiduciaries, members of a partnership, joint tenants, tenants in common, tenants by the entirety, or otherwise, or if two (2) or more person share the same fiduciary relationship respecting the same shares, unless the Secretary is given written notice to the contrary and is furnished with a copy of the instrument or order appointing them or creating the relationship wherein it is so provided, their acts with respect to voting shall have the following effect: (a) if only one (1) votes, his act binds all; (b) if more than one (1) votes, the act of the majority so voting binds all; (c) if more than one (1) votes, but the vote is evenly split on any particular matter, each faction may vote the securities in question proportionally, or may apply to the Delaware Court of Chancery for relief as provided in Section 217(b) of the General Corporation Law of Delaware (the "Delaware General Corporation Law"). If the instrument filed with the Secretary shows that any such tenancy is held in unequal interests, a majority or even-split for the purpose of clause (c) shall be a majority or even-split in interest.

**Section 13. LIST OF STOCKHOLDERS.** The Secretary shall prepare and make, at least ten (10) days before every meeting of stockholders, a complete list of the stockholders entitled to vote at said meeting, arranged in alphabetical order, showing the address of each stockholder and the number of shares registered in the name of each stockholder. Such list shall be open to the examination of any stockholder, for any purpose germane to the meeting, during ordinary business hours, for a period of at least ten (10) days prior to the meeting, either at a place within the city where the meeting is to be held, which place shall be specified in the notice of the meeting, or, if not specified, at the place where the meeting is to be held. The list shall be produced and kept at the time and place of meeting during the whole time thereof and may be inspected by any stockholder who is present.

**Section 14. ACTION WITHOUT MEETING.** Unless otherwise provided in the Certificate of Incorporation, any action required to be taken at any annual or special meeting of stockholders of the Corporation, or any action that may be taken at any annual or special meeting of such stockholders, may be taken without a meeting, without prior notice and without a vote, if a consent in writing, setting forth the action so taken, shall be signed by the holders of outstanding stock having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all shares entitled to vote thereon were present and voted and shall be delivered to the Corporation by delivery in a manner permitted by applicable law.

**Section 15. ORGANIZATION.**

(a) At every meeting of stockholders, the Chairman of the Board of Directors, or, if a Chairman has not been appointed, is absent, or designates the next senior officer present to so act, the President, or, if the President is absent, the most senior Vice President present, or, in the absence of any such officer, a Chairman of the meeting chosen by a majority in interest of the stockholders entitled to vote, present in person or by proxy, shall act as Chairman. The Secretary, or, in his absence, an Assistant Secretary directed to do so by the President, shall act as Secretary of the meeting.

(b) The Board of Directors of the Corporation shall be entitled to make such rules or regulations for the conduct of meetings of stockholders as it shall deem necessary, appropriate or convenient. Subject to such rules and regulations of the Board of Directors, if any, the Chairman of the meeting shall have the right and authority to prescribe such rules, regulations and procedures and to do all such acts as, in the judgment of such Chairman, are necessary, appropriate or convenient for the proper conduct of the meeting, including, without limitation, (i) to prescribe an agenda for the meeting, (ii) to adjourn or recess the meeting, (iii) to silence or expel persons to ensure the orderly conduct of the meeting, (iv) to declare motions or persons out of order, (v) to impose reasonable time limits on questions and remarks by any stockholder, (vi) to limit the number of questions a stockholder may ask, (vii) to limit the nature of questions and comments to one subject matter at a time as dictated by any agenda for the meeting, (viii) to limit the number of speakers or persons addressing the chairman of the meeting or the meeting, (ix) to determine when the polls shall be closed, (x) to limit the attendance at the meeting to stockholders of record, beneficial owners of stock who present letters from the record holders confirming their status as beneficial owners, and the proxies of such record and beneficial holders, (xi) to restrict the use of audio or video recording devices at the meeting, and (xii) to prescribe any other rules and procedures for maintaining order at the meeting and the safety of those present. Unless and to the extent determined by the Board of Directors or the Chairman of the meeting, meetings of stockholders shall not be required to be held in accordance with rules of parliamentary procedure.

**ARTICLE IV**

**DIRECTORS**

**Section 16. NUMBER AND TERM OF OFFICE.** The number of Directors which shall constitute the whole of the Board of Directors shall be no less than three (3). The number of Directors shall be determined from time to time by resolution adopted by the Board of Directors. At each annual meeting of stockholders, directors of the Corporation shall be elected to hold office until the expiration of the term for which they are elected, and until their successors have been duly elected and qualified; except that if any such election shall not be so held, such election shall take place at a stockholders' meeting called and held in accordance with the Delaware General Corporation Law.

The number of Directors which constitute the whole Board of Directors of the Corporation shall be designated in the By-laws of the Corporation or by resolution adopted by the Board of Directors. Vacancies occurring on the Board of Directors for any reason may be filled solely by vote of a majority of the remaining members of the Board of Directors, although less than a quorum, at any meeting of the Board of Directors. A person so elected by the Board of Directors to fill a vacancy shall hold office until the next succeeding annual meeting of stockholders of the Corporation and until his or her successor shall have been duly elected and qualified. Directors need not be stockholders unless so required by the Certificate of Incorporation. If, for any reason, the Directors shall not have been elected at an annual meeting, they may be elected as soon thereafter as convenient at a special meeting of the stockholders called for that purpose in the manner provided in these By-laws.

**Section 17. POWERS.** The powers of the Corporation shall be exercised, its business conducted and its property controlled by the Board of Directors, except as may be otherwise provided by statute or by the Certificate of Incorporation.

**Section 18. VACANCIES.** Unless otherwise provided in the Certificate of Incorporation, vacancies and newly created directorships resulting from any increase in the authorized number of Directors may be filled solely by a majority of the Directors then in office, although less than a quorum, or by a sole remaining Director, and each Director so elected shall hold office for the unexpired portion of the term of the Director whose place shall be vacant and until his or her successor shall have been duly elected and qualified. A vacancy in the Board of Directors shall be deemed to exist under this Section 18 in the case of the death, removal or resignation of any Director, or if the stockholders fail at any meeting of stockholders at which Directors are to be elected to elect the number of Directors then constituting the whole Board of Directors.

**Section 19. RESIGNATION.** Any Director may resign at any time by delivering his or her written resignation to the Secretary, such resignation to specify whether it will be effective at a particular time, upon receipt by the Secretary or at the pleasure of the Board of Directors. If no such specification is made, it shall be deemed effective upon delivery to the Corporation. When one or more Directors shall resign from the Board of Directors, effective at a future date, a majority of the Directors then in office, including those who have so resigned, shall have power to fill such vacancy or vacancies, the vote thereon to take effect when such resignation or resignations shall become effective, and each Director so chosen shall hold office for the unexpired portion of the term of the Director whose place shall be vacated and until his successor shall have been duly elected and qualified.

**Section 20. REMOVAL.** Subject to any limitations imposed by law or the Certificate of Incorporation, the Board of Directors, or any individual Director, may be removed from office, with or without cause.

**Section 21. MEETINGS.**

(a) Annual Meetings. The annual meeting of the Board of Directors shall be held immediately before or after the annual meeting of stockholders and at the place where such meeting is held. No notice of an annual meeting of the Board of Directors shall be necessary and such meeting shall be held for the purpose of electing officers and transacting such other business as may lawfully come before it.

(b) Regular Meetings. Unless otherwise restricted by the Certificate of Incorporation, regular meetings of the Board of Directors may be held at any place within or without the State of Delaware as may be designated from time to time by the Board of Directors.

(c) Special Meetings. Unless otherwise restricted by the Certificate of Incorporation, special meetings of the Board of Directors may be held at any time and place within or without the State of Delaware whenever called by the Chairman of the Board, the Chief Executive Officer or any two of the Directors.

(d) Telephone Meetings. Any member of the Board of Directors, or of any committee thereof, may participate in a meeting by means of conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other, and participation in a meeting by such means shall constitute presence in person at such meeting.

(e) Notice of Meetings. Written notice of the time and place of all special meetings of the Board of Directors shall be given at least one (1) day before the date of the meeting. Notice of any meeting may be waived in writing at any time before or after the meeting and will be waived by any Director by attendance thereat, except when the Director attends the meeting for the express purpose of objecting, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened.

(f) Waiver of Notice. The transaction of all business at any meeting of the Board of Directors, or any committee thereof, however called or noticed, or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice, if a quorum be present and if, either before or after meeting, each of the Directors not present shall sign a written waiver of notice, or a consent to holding such meeting, or an approval of the minutes thereof. All such waivers, consents or approvals shall be filed with the corporate records or made a part of the minutes of the meeting.

**Section 22. QUORUM AND VOTING.**

(a) A quorum of the Board of Directors shall consist of a majority of the exact number of directors fixed from time to time in accordance with Section 16 of these By-laws, but not less than one (1); provided, however, at any meeting whether a quorum be present or otherwise, a majority of the Directors present may adjourn from time to time until the time fixed for the next regular meeting of the Board of Directors, without notice other than by announcement at the meeting.

(b) At each meeting of the Board of Directors at which a quorum is present, all questions and business shall be determined by a vote of the majority of the Directors present, unless a different vote is required by law, the Certificate of Incorporation or these By-laws.

**Section 23. ACTION WITHOUT MEETING.** Unless otherwise restricted by the Certificate of Incorporation or these By-laws, any action required or permitted to be taken at any meeting of the Board of Directors or of any committee thereof may be taken without a meeting, if all members of the Board of Directors or committee, as the case may be, consent thereto in writing, and such writing or writings are filed with the minutes of proceedings of the Board of Directors or committee.

**Section 24. FEES AND COMPENSATION.** Directors shall be entitled to such compensation for their services as may be approved by the Board of Directors, including, if so approved, by resolution of the Board of Directors, a fixed sum and expenses of attendance, if any, for attendance at each regular or special meeting of the Board of Directors and at any meeting of a committee of the Board of Directors. Nothing herein contained shall be construed to preclude any Director from serving the Corporation in any other capacity as an officer, agent, employee, or otherwise and receiving compensation therefor.

**Section 25. COMMITTEES.**

(a) Executive Committee. The Board of Directors may by resolution passed by a majority of the whole Board of Directors appoint an Executive Committee to consist of one (1) or more members of the Board of Directors. The Executive Committee, to the extent permitted by law and specifically granted by the Board of Directors, shall have, and may exercise when the Board of Directors is not in session, all powers of the Board of Directors in the management of the business and affairs of the Corporation, including, without limitation, the power and authority to declare a dividend or to authorize the issuance of stock, except such committee shall not have the power or authority to amend the Certificate of Incorporation, to adopt an agreement of merger or consolidation, to recommend to the stockholders the sale, lease or exchange of all or substantially all of the Corporation's property and assets, to recommend to the stockholders of the Corporation a dissolution of the Corporation or a revocation of a dissolution or to amend these By-laws.

(b) Other Committees. The Board of Directors may, by resolution passed by a majority of the whole Board of Directors, from time to time appoint such other committees as may be permitted by law. Such other committees appointed by the Board of Directors shall consist of one (1) or more members of the Board of Directors and shall have such powers and perform such duties as may be prescribed by the resolution or resolutions creating such committees, but in no event shall such committee have the powers denied to the Executive Committee in these By-laws.

(c) Term. Each member of a committee of the Board of Directors shall serve a term on the committee coexistent with such member's term on the Board of Directors. The Board of Directors, subject to the provisions of subsections (a) or (b) of this By-law may at any time increase or decrease the number of members of a committee or terminate the existence of a committee. The membership of a committee member shall terminate on the date of his or her death or voluntary resignation from the committee or from the Board of Directors. The Board of Directors may at any time for any reason remove any individual committee member and the Board of Directors may fill any committee vacancy created by death, resignation, removal or increase in the number of members of the committee. The Board of Directors may designate one or more Directors as alternate members of any committee, who may replace any absent or disqualified member at any meeting of the committee, and, in addition, in the absence or disqualification of any member of a committee, the member or members thereof present at any meeting and not disqualified from voting, whether or not he or they constitute a quorum, may unanimously appoint another member of the Board of Directors to act at the meeting in the place of any such absent or disqualified member.

(d) Meetings. Unless the Board of Directors shall otherwise provide, regular meetings of the Executive Committee or any other committee appointed pursuant to this Section 25 shall be held at such times and place as are determined by the Board of Directors, or by any such committee and when notice thereof has been given to each member of such committee, no further notice of such regular meetings need be given thereafter. Special meetings of any such committee may be held at any place which has been determined from time to time by such committee, and may be called by any Director who is a member of such committee, upon written notice to the members of such committee of the time and place of such special meeting given in the manner provided for the giving of written notice to members of the Board of Directors of the time and place of special meetings of the Board of Directors. Notice of any special meeting of any committee may be waived in writing at any time before or after the meeting and will be waived by any Director by attendance thereat, except when the Director attends such special meeting for the express purpose of objecting, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened. A majority of the authorized number of members of any such committee shall constitute a quorum for the transaction of business, and the act of a majority of those present at any meeting at which a quorum is present shall be the act of such committee.

**Section 26. ORGANIZATION.** The Chairman of the Board shall preside at every meeting of the Board of Directors, if present. In the case of any meeting, if there is no Chairman of the Board or if the Chairman is not present, a Chairman chosen by a majority of the directors present shall act as Chair of such meeting. The Secretary of the Corporation or, in the absence of the Secretary, any person appointed by the Chairman shall act as Secretary of the meeting.

## ARTICLE V

### OFFICERS

**Section 27. OFFICERS DESIGNATED.** The officers of the Corporation shall include, if and when designated by the Board of Directors, the Chief Executive Officer, the President, one or more Vice Presidents, the Secretary, the Chief Financial Officer and the Treasurer, all of whom shall be elected at the annual organizational meeting of the Board of Directors. The Board of Directors may also appoint one or more Assistant Secretaries, Assistant Treasurers and such other officers and agents with such powers and duties as it shall deem necessary. The Board of Directors may assign such additional titles to one or more of the officers as it shall deem appropriate. Any one person may hold any number of offices of the Corporation at any one time unless specifically prohibited therefrom by law. The salaries and other compensation of the officers of the Corporation shall be fixed by or in the manner designated by the Board of Directors.

**Section 28. TENURE AND DUTIES OF OFFICERS.**

( a ) General. All officers shall hold office at the pleasure of the Board of Directors and until their successors shall have been duly elected and qualified, unless sooner removed. Any officer elected or appointed by the Board of Directors may be removed at any time by the Board of Directors. If the office of any officer becomes vacant for any reason, the vacancy may be filled by the Board of Directors.

( b ) Duties of the Chief Executive and Chief Operating Officers. Subject to the control of the Board of Directors, the Chief Executive Officer shall have general executive charge, management and control, of the properties, business and operations of the Corporation with all such powers as may be reasonably incident to such responsibilities; and subject to the control of the Chief Executive Officer, the Chief Operating Officer (if designated) shall have general operating charge, management and control, of the properties, business and operations of the Corporation with all such powers as may be reasonably incident to such responsibilities. The Chief Executive Officer and, if and to the extent designated by the Chief Executive Officer, the Chief Operating Officer, may agree upon and execute all leases, contracts, evidences of indebtedness and other obligations in the name of the Corporation and may sign all certificates for shares of capital stock of the Corporation, and each shall have such other powers and duties as are designated in accordance with these By-laws and as from time to time may be assigned to each by the Board of Directors.

( c ) Duties of President. Unless the Board of Directors otherwise determines, subject to the control of the Chief Executive Officer, the President shall have the authority to agree upon and execute all leases, contracts, evidences of indebtedness and other obligations in the name of the Corporation; and, unless the Board of Directors otherwise determines, he shall, in the absence of the Chairman of the Board or if there be no Chairman of the Board, preside at all meetings of the stockholders and (should he be a Director) of the Board of Directors, and the President shall have such other powers and duties as designated in accordance with these By-laws and as from time to time may be assigned to him by the Board of Directors.

( d ) Duties of Vice Presidents. If and to the extent determined by the Board of Directors, the Vice Presidents, in the order of their seniority, may assume and perform the duties of the President in the absence or disability of the President or whenever the office of President is vacant. The Vice Presidents shall perform other duties commonly incident to their office and shall also perform such other duties and have such other powers as the Board of Directors or the President shall designate from time to time.

(e) Duties of Secretary. The Secretary shall attend all meetings of the stockholders and of the Board of Directors and shall record all acts and proceedings thereof in the minute book of the Corporation. The Secretary shall give notice in conformity with these By-laws of all meetings of the stockholders and of all meetings of the Board of Directors and any committee thereof requiring notice. The Secretary shall perform all other duties given in these By-laws and other duties commonly incident to such office and shall also perform such other duties and have such other powers as the Board of Directors shall designate from time to time. The President may direct any Assistant Secretary to assume and perform the duties of the Secretary in the absence or disability of the Secretary, and each Assistant Secretary shall perform other duties commonly incident to such office and shall also perform such other duties and have such other powers as the Board of Directors or the President, shall designate from time to time.

(f) Duties of Chief Financial Officer. The Chief Financial Officer shall keep or cause to be kept the books of account of the Corporation in a thorough and proper manner and shall render statements of the financial affairs of the Corporation in such form and as often as required by the Board of Directors, the Chairman of the Board or the President. The Chief Financial Officer, subject to the order of the Board of Directors, shall have the custody of all funds and securities of the Corporation. The Chief Financial Officer shall perform other duties commonly incident to such office and shall also perform such other duties and have such other powers as the Board of Directors, the Chairman of the Board or the President shall designate from time to time. The Chairman of the Board or the President may direct the Treasurer or any Assistant Treasurer to assume and perform the duties of the Chief Financial Officer in the absence or disability of the Chief Financial Officer, and each Assistant Treasurer shall perform other duties commonly incident to such office and shall also perform such other duties and have such other powers as the Board of Directors, the Chairman of the Board or the President shall designate from time to time.

**Section 29. DELEGATION OF AUTHORITY.** The Board of Directors may from time to time delegate the powers or duties of any officer to any other officer or agent, notwithstanding any provision hereof.

**Section 30. RESIGNATIONS.** Any officer may resign at any time by giving written notice to the Board of Directors or to the President or to the Secretary. Any such resignation shall be effective when received by the person or persons to whom such notice is given, unless a later time is specified therein, in which event the resignation shall become effective at such later time. Unless otherwise specified in such notice, the acceptance of any such resignation shall not be necessary to make it effective. Any resignation shall be without prejudice to the rights, if any, of the Corporation under any contract with the resigning officer.

**Section 31. REMOVAL.** Any officer may be removed from office at any time, either with or without cause, by the vote or written consent of all of the Directors in office at the time, or by any committee or superior officers upon whom such power of removal may have been conferred by the Board of Directors.



## ARTICLE VI

### EXECUTION OF CORPORATE INSTRUMENTS AND VOTING OF SECURITIES OWNED BY THE CORPORATION

**Section 32. EXECUTION OF CORPORATE INSTRUMENTS.** The Board of Directors may, in its discretion, determine the method and designate the signatory officer or officers, or other person or persons, to execute on behalf of the Corporation any corporate instrument or document, or to sign on behalf of the Corporation the corporate name without limitation, or to enter into contracts on behalf of the Corporation, except where otherwise provided by law or these By-laws, and such execution or signature shall be binding upon the Corporation.

Unless otherwise specifically determined by the Board of Directors or otherwise required by law, promissory notes, deeds of trust, mortgages and other evidences of indebtedness of the Corporation, and other corporate instruments or documents requiring the corporate seal, and certificates of shares of stock owned by the Corporation, shall be executed, signed or endorsed by the Chief Executive Officer, or the President or any Vice President, and by the Secretary or Chief Financial Officer or Treasurer or any Assistant Secretary or Assistant Treasurer. All other instruments and documents requiring the corporate signature, but not requiring the corporate seal, may be executed as aforesaid or in such other manner as may be directed by the Board of Directors.

All checks and drafts drawn on banks or other depositories on funds to the credit of the Corporation or in special accounts of the Corporation shall be signed by such person or persons as the Board of Directors shall authorize so to do.

Unless authorized or ratified by the Board of Directors or within the agency power of an officer, no officer, agent or employee shall have any power or authority to bind the Corporation by any contract or engagement or to pledge its credit or to render it liable for any purpose or for any amount.

**Section 33. VOTING OF SECURITIES OWNED BY THE CORPORATION.** All stock and other securities of other corporations owned or held by the Corporation for itself, or for other parties in any capacity, shall be voted, and all proxies with respect thereto shall be executed, by the person authorized so to do by resolution of the Board of Directors, or, in the absence of such authorization, by the Chairman of the Board of Directors, Chief Executive Officer, or any Vice President.

## ARTICLE VII

### SHARES OF STOCK

**Section 34. FORM AND EXECUTION OF CERTIFICATES.** Certificates for the shares of stock of the Corporation shall be in such form as is consistent with the Certificate of Incorporation and applicable law. Every holder of stock in the Corporation shall be entitled to have a certificate signed by or in the name of the Corporation by the Chief Executive Officer, or the President or any Vice President and by the Secretary or Chief Financial Officer or Treasurer or any Assistant Treasurer or Assistant Secretary, certifying the number of shares owned by him in the Corporation. Where such certificate is countersigned by a transfer agent other than the Corporation or its employee, or by a registrar other than the Corporation or its employee, any other signature on the certificate may be a facsimile. In case any officer, transfer agent, or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent, or registrar before such certificate is issued, it may be issued with the same effect as if he were such officer, transfer agent, or registrar at the date of issue. Each certificate shall state upon the face or back thereof, in full or in summary, all of the designations, preferences, limitations, restrictions on transfer and relative rights of the shares authorized to be issued.

**Section 35. LOST CERTIFICATES.** A new certificate or certificates shall be issued in place of any certificate or certificates theretofore issued by the Corporation alleged to have been lost, stolen, or destroyed, upon the making of an affidavit of that fact by the person claiming the certificate of stock to be lost, stolen, or destroyed. The Corporation may require, as a condition precedent to the issuance of a new certificate or certificates, the owner of such lost, stolen, or destroyed certificate or certificates, or his legal representative, to advertise the same in such manner as it shall require or to give the Corporation a surety bond in such form and amount as it may direct as indemnity against any claim that may be made against the Corporation with respect to the certificate alleged to have been lost, stolen or destroyed.

**Section 36. TRANSFERS.**

(a) Transfers of record of shares of stock of the Corporation shall be made only on its books by the holders thereof, in person or by attorney duly authorized and upon the surrender of a properly endorsed certificate or certificates for a like number of shares.

(b) The Corporation shall have power to enter into and perform any agreement with any number of stockholders of any one or more classes of stock of the Corporation to restrict the transfer of shares of stock of the Corporation of any one or more classes owned by such stockholders in any manner not prohibited by the Delaware General Corporation Law.

**Section 37. FIXING RECORD DATES.**

(a) In order that the Corporation may determine the stockholders entitled to notice of or to vote at any meeting of stockholders or any adjournment thereof, the Board of Directors may fix, in advance, a record date, which record date shall not precede the date upon which the resolution fixing the record date is adopted by the Board of Directors, and which record date shall not be more than sixty (60) nor less than ten (10) days before the date of such meeting. If no record date is fixed by the Board of Directors, the record date for determining stockholders entitled to notice of or to vote at a meeting of stockholders shall be at the close of business on the day next preceding the day on which notice is given, or if notice is waived, at the close of business on the day next preceding the day on which the meeting is held. A determination of stockholders of record entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the Board of Directors may fix a new record date for the adjourned meeting.

(b) In order that the Corporation may determine the stockholders entitled to receive payment of any dividend or other distribution or allotment of any rights or the stockholders entitled to exercise any rights in respect of any change, conversion or exchange of stock, or for the purpose of any other lawful action, the Board of Directors may fix, in advance, a record date, which record date shall not precede the date upon which the resolution fixing the record date is adopted, and which record date shall be not more than sixty (60) days prior to such action. If no record date is fixed by the Board of Directors, the record date for determining stockholders for any such purpose shall be at the close of business on the day on which the Board of Directors adopts the resolution relating thereto.

**Section 38. REGISTERED STOCKHOLDERS.** The Corporation shall be entitled to recognize the exclusive right of a person registered on its books as the owner of shares to receive dividends, and to vote as such owner, and shall not be bound to recognize any equitable or other claim to or interest in such share or shares on the part of any other person whether or not it shall have express or other notice thereof, except as otherwise provided by the laws of Delaware.

## ARTICLE VIII

### OTHER SECURITIES OF THE CORPORATION

**Section 39. EXECUTION OF OTHER SECURITIES.** All bonds, debentures and other corporate securities of the Corporation, other than stock certificates (covered in Section 34), may be signed by the Chief Executive Officer, the President or any Vice President, or such other person as may be authorized by the Board of Directors, and the corporate seal impressed thereon or a facsimile of such seal imprinted thereon and attested by the signature of the Secretary or an Assistant Secretary, or the Chief Financial Officer or Treasurer or an Assistant Treasurer; provided, however, that where any such bond, debenture or other corporate security shall be authenticated by the manual signature of a trustee under an indenture pursuant to which such bond, debenture or other corporate security shall be issued, the signatures of the persons signing and attesting the corporate seal on such bond, debenture or other corporate security may be the imprinted facsimile of the signatures of such persons. Interest coupons appertaining to any such bond, debenture or other corporate security, authenticated by a trustee as aforesaid, shall be signed by the Chief Financial Officer or Treasurer of the Corporation or such other person as may be authorized by the Board of Directors, or bear imprinted thereon the facsimile signature of such person. In case any officer who shall have signed or attested any bond, debenture or other corporate security, or whose facsimile signature shall appear thereon or on any such interest coupon, shall have ceased to be such officer before any bond, debenture or other corporate security so signed or attested shall have been delivered, such bond, debenture or other corporate security nevertheless may be adopted by the Corporation and issued and delivered as though the person who signed the same or whose facsimile signature shall have been used thereon had not ceased to be such officer of the Corporation.

## ARTICLE IX

### DIVIDENDS

**Section 40. DECLARATION OF DIVIDENDS.** Dividends upon the capital stock of the Corporation, subject to the provisions of the Certificate of Incorporation, if any, may be declared by the Board of Directors pursuant to law at any regular or special meeting. Dividends may be paid in cash, in property, or in shares of the capital stock, subject to the provisions of the Certificate of Incorporation.

**Section 41. DIVIDEND RESERVE.** Before payment of any dividend, there may be set aside out of any funds of the Corporation available for dividends such sum or sums as the Board of Directors from time to time, in their absolute discretion, think proper as a reserve or reserves to meet contingencies, or for equalizing dividends, or for repairing or maintaining any property of the Corporation, or for such other purpose as the Board of Directors shall think conducive to the interests of the Corporation, and the Board of Directors may modify or abolish any such reserve in the manner in which it was created.

## ARTICLE X

### FISCAL YEAR

**Section 42. FISCAL YEAR.** The fiscal year of the Corporation shall be fixed by resolution of the Board of Directors.

## ARTICLE XI

### INDEMNIFICATION

**Section 43. INDEMNIFICATION OF DIRECTORS, OFFICERS, EMPLOYEES AND OTHER AGENTS.**

(a) Directors and Executive Officers. The Corporation shall indemnify its Directors and executive officers to the fullest extent not prohibited by the Delaware General Corporation Law; provided, however, that the Corporation may limit the extent of such indemnification by individual contracts with its Directors and executive officers; and, provided, further, that the Corporation shall not be required to indemnify any Director or executive officer in connection with any proceeding (or part thereof) initiated by such person or any proceeding by such person against the Corporation or its Directors, officers, employees or other agents unless (1) such indemnification is expressly required to be made by law, (2) the proceeding was authorized by the Board of Directors of the Corporation or (3) such indemnification is provided by the Corporation, in its sole discretion, pursuant to the powers vested in the Corporation under the Delaware General Corporation Law.

(b) Other Officers, Employees and Other Agents. The Corporation shall have power to indemnify its other officers, employees and other agents as set forth in the Delaware General Corporation Law.

(c) Good Faith.

(1) The termination of any proceeding by judgment, order, settlement, conviction or upon a plea of nolo contendere or its equivalent shall not, of itself, create a presumption that the person did not act in good faith and in a manner which such person reasonably believed to be in or not opposed to the best interests of the Corporation, and, with respect to any criminal proceeding, that such person had reasonable cause to believe that his conduct was unlawful.

(2) The provisions of this paragraph (c) shall not be deemed to be exclusive or to limit in any way the circumstances in which a person may be deemed to have met the applicable standard of conduct set forth by the Delaware General Corporation Law.

(d) Expenses. The Corporation shall advance, prior to the final disposition of any proceeding, promptly following request therefor, all expenses incurred by any Director or executive officer in connection with such proceeding upon receipt of an undertaking by or on behalf of such person to repay said amounts if it should be determined ultimately that such person is not entitled to be indemnified under this By-law or otherwise.

Notwithstanding the foregoing, unless otherwise determined pursuant to paragraph (e) of this By-law, no advance shall be made by the Corporation if a determination is reasonably and promptly made (1) by the Board of Directors by a majority vote of a quorum consisting of Directors who were not parties to the proceeding, or (2) if such quorum is not obtainable, or, even if obtainable, a quorum of disinterested directors so directs, by independent legal counsel in a written opinion, that the facts known to the decision-making party at the time such determination is made demonstrate clearly and convincingly that such person acted in bad faith or in a manner that such person did not believe to be in or not opposed to the best interests of the Corporation.

(e) Enforcement. Without the necessity of entering into an express contract, all rights to indemnification and advances to Directors and executive officers under this By-law shall be deemed to be contractual rights and be effective to the same extent and as if provided for in a contract between the Corporation and the Director or executive officer. Any right to indemnification or advances granted by this By-law to a Director or executive officer shall be enforceable by or on behalf of the person holding such right in any court of competent jurisdiction if (1) the claim for indemnification or advances is denied, in whole or in part, or (2) no disposition of such claim is made within ninety (90) days of request therefor. The claimant in such enforcement action, if successful in whole or in part, shall be entitled to be paid also the expense of prosecuting his or her claim to the fullest extent permitted by law. The Corporation shall be entitled to raise as a defense to any such action that the claimant has not met the standards of conduct that make it permissible under the Delaware General Corporation Law for the Corporation to indemnify the claimant for the amount claimed. Neither the failure of the Corporation (including its Board of Directors, independent legal counsel or its stockholders) to have made a determination prior to the commencement of such action that indemnification of the claimant is proper in the circumstances because such person has met the applicable standard of conduct set forth in the Delaware General Corporation Law, nor an actual determination by the Corporation (including its Board of Directors, independent legal counsel or its stockholders) that the claimant has not met such applicable standard of conduct, shall be a defense to the action or create a presumption that claimant has not met the applicable standard of conduct.

(f) Non-Exclusivity of Rights. The rights conferred on any person by this By-law shall not be exclusive of any other right which such person may have or hereafter acquire under any statute, provision of the Certificate of Incorporation, By-laws, agreement, vote of stockholders or disinterested Directors or otherwise, both as to action in his official capacity and as to action in another capacity while holding office. The Corporation is specifically authorized to enter into individual contracts with any or all of its Directors, officers, employees or agents respecting indemnification and advances, to the fullest extent not prohibited by the Delaware General Corporation Law.

(g) Survival of Rights. The rights conferred on any person by this By-law shall continue as to a person who has ceased to be a Director, officer, employee or other agent and shall inure to the benefit of the heirs, executors and administrators of such a person.

(h) Insurance. To the fullest extent permitted by the Delaware General Corporation Law, the Corporation, upon approval by the Board of Directors, may purchase insurance on behalf of any person required or permitted to be indemnified pursuant to this By-law.

(i) Amendments. Any repeal or modification of this By-law shall only be prospective and shall not affect the rights under this By-law in effect at the time of the alleged occurrence of any action or omission to act that is the cause of any proceeding against any agent of the Corporation.

(j) Saving Clause. If this By-law or any portion hereof shall be invalidated on any ground by any court of competent jurisdiction, then the Corporation shall nevertheless indemnify each Director and executive officer to the full extent not prohibited by any applicable portion of this By-law that shall not have been invalidated, or by any other applicable law.

(k) Certain Definitions. For the purposes of this By-law, the following definitions shall apply:

(1) The term "**proceeding**" shall be broadly construed and shall include, without limitation, the investigation, preparation, prosecution, defense, settlement, arbitration and appeal of, and the giving of testimony in, any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative.

(2) The term "**expenses**" shall be broadly construed and shall include, without limitation, court costs, attorneys' fees, witness fees, fines, amounts paid in settlement or judgment and any other costs and expenses of any nature or kind incurred in connection with any proceeding.

(3) The term the "**Corporation**" shall include, in addition to the resulting corporation, any constituent corporation (including any constituent of a constituent) absorbed in a consolidation or merger which, if its separate existence had continued, would have had power and authority to indemnify its directors, officers, and employees or agents, so that any person who is or was a director, officer, employee or agent of such constituent corporation, or is or was serving at the request of such constituent corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, shall stand in the same position under the provisions of this By-law with respect to the resulting or surviving corporation as he would have with respect to such constituent corporation if its separate existence had continued.

(4) References to a "Director", "officer", "employee", or "agent" of the Corporation shall include without limitation, situations where such person is serving at the request of the Corporation as a director, officer, employee, trustee or agent of another corporation, partnership, joint venture, trust or other enterprise.

(5) References to "other enterprises" shall include employee benefit plans; references to "fines" shall include any excise taxes assessed on a person with respect to an employee benefit plan; and references to "serving at the request of the Corporation" shall include any service as a director, officer, employee or agent of the Corporation which imposes duties on, or involves services by, such director, officer, employee, or agent with respect to an employee benefit plan, its participants, or beneficiaries; and a person who acted in good faith and in a manner he reasonably believed to be in the interest of the participants and beneficiaries of an employee benefit plan shall be deemed to have acted in a manner "not opposed to the best interests of the Corporation" as referred to in this By-law.

## ARTICLE XII

### NOTICES

#### Section 44. NOTICES.

(a) Notice to Stockholders. Whenever, under any provisions of these By-laws, notice is required to be given to any stockholder, it shall be given in writing, timely and duly deposited in the United States mail, postage prepaid, and addressed to such stockholder's last known post office address as shown by the stock record of the Corporation or its transfer agent.

(b) Notice to Directors. Any notice required to be given to any Director may be given by the method stated in subsection (a), or by facsimile, telex or telegram, except that such notice other than one which is delivered personally shall be sent to such address as such Director shall have filed in writing with the Secretary, or, in the absence of such filing, to the last known post office address of such Director.

(c) Address Unknown. If no address of a stockholder or Director be known, notice may be sent to the office of the Corporation required be maintained pursuant to Section 2 hereof.

(d) Affidavit of Mailing. An affidavit of mailing, executed by a duly authorized and competent employee of the Corporation or its transfer agent appointed with respect to the class of stock affected, specifying the name and address or the names and addresses of the stockholder or stockholders, or Director or Directors, to whom any such notice or notices was or were given, and the time and method of giving the same, shall be conclusive evidence of the statements therein contained.

(e) Time Notices Deemed Given. All notices given by mail, as above provided, shall be deemed to have been given as at the time of mailing, and all notices given by facsimile, telex or telegram shall be deemed to have been given as of the sending time recorded at the time of transmission.

(f) Methods of Notices. It shall not be necessary that the same method of giving notice be employed in respect of all Directors, but one permissible method may be employed in respect of any one or more, and any other permissible method or methods may be employed in respect of any other or others.

(g) Failure to Receive Notice. The period or limitation of time within which any stockholder may exercise any option or right, or enjoy any privilege or benefit, or be required to act, or within which any Director may exercise any power or right, or enjoy any privilege, pursuant to any notice sent such person in the manner above provided, shall not be affected or extended in any manner by the failure of such stockholder or such Director to receive such notice.

(h) Notice to Person with Whom Communication Is Unlawful. Whenever notice is required to be given, under any provision of law or of the Certificate of Incorporation or By-laws of the Corporation, to any person with whom communication is unlawful, the giving of such notice to such person shall not be required and there shall be no duty to apply to any governmental authority or agency for a license or permit to give such notice to such person. Any action or meeting which shall be taken or held without notice to any such person with whom communication is unlawful shall have the same force and effect as if such notice had been duly given. In the event that the action taken by the Corporation is such as to require the filing of a certificate under any provision of the Delaware General Corporation Law, the certificate shall state, if such is the fact and if notice is required, that notice was given to all persons entitled to receive notice except such persons with whom communication is unlawful.

(i) Notice to Person with Undeliverable Address. Whenever notice is required to be given, under any provision of law or the Certificate of Incorporation or By-laws of the Corporation, to any stockholder to whom (1) notice of two consecutive annual meetings, and all notices of meetings to such person during the period between such two consecutive annual meetings, or (2) all, and at least two, payments (if sent by first class mail) of dividends or interest on securities during a twelve-month period, have been mailed addressed to such person at such person's address as shown on the records of the Corporation and have been returned undeliverable, the giving of such notice to such person shall not be required. Any action or meeting which shall be taken or held without notice to such person shall have the same force and effect as if such notice had been duly given. If any such person shall deliver to the Corporation a written notice setting forth such person's then current address, the requirement that notice be given to such person shall be reinstated. In the event that the action taken by the Corporation is such as to require the filing of a certificate under any provision of the Delaware General Corporation Law, the certificate need not state that notice was not given to persons to whom notice was not required to be given pursuant to this paragraph.



## **ARTICLE XIII**

### **AMENDMENTS**

**Section 45. AMENDMENTS.** Except as otherwise set forth in paragraph (i) of Section 43 of these By-laws, or as provided in the Certificate of Incorporation, the Board of Directors shall have power to make, alter, amend and repeal these By-laws (except so far as the By-laws adopted by the stockholders shall otherwise provide). Any By-laws made by the Board of Directors under the powers conferred hereby may be altered, amended or repealed by the directors or by the stockholders. Notwithstanding the foregoing, these By-laws shall not be altered, amended or repealed by action of the stockholders and no provision inconsistent therewith shall be adopted by the stockholders without the affirmative vote of the holders of a majority of the voting power of all the shares of the Corporation entitled to vote thereon, voting together as a single class.

## **ARTICLE XIV**

### **FORUM FOR ADJUDICATION OF DISPUTES**

**Section 46. FORUM FOR ADJUDICATION OF DISPUTES.** To the fullest extent provided by law, and unless the Corporation consents in writing to the selection of an alternative forum, Internal Corporate Claims shall be brought solely and exclusively in the courts of the State of Delaware; provided, however, that an Internal Corporate Claim may be brought in another forum if the courts of the State of Delaware cannot exercise personal jurisdiction over all necessary parties or lack subject matter jurisdiction over the claim. Internal Corporate Claims: means claims, including claims in the right of the corporation, (i) that are based upon a violation of a duty by a current or former director or officer or stockholder in such capacity, or (ii) as to which the General Corporation Law of Delaware confers jurisdiction upon the Court of Chancery of the State of Delaware.

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C.ss.1350)**

I, Corey M. Horowitz, Chairman and Chief Executive Officer of Network-1 Technologies, Inc. (the "Registrant"), certify that:

1. I have reviewed this report on Form 10-Q of the Registrant;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (that Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: November 10, 2016

By: /s/ Corey M. Horowitz

Corey M. Horowitz  
Chairman and Chief Executive Officer

**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C.ss.1350)**

I, David C. Kahn, Chief Financial Officer of Network-1 Technologies, Inc. (the "Registrant"), certify that:

1. I have reviewed this report on Form 10-Q of the Registrant;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: November 10, 2016

By: /s/ David C. Kahn

David C. Kahn  
Chief Financial Officer

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER**

**Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. ss. 1350)**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. ss. 1350), the undersigned, Corey M. Horowitz, Chief Executive Officer and Chairman of Network-1 Technologies, Inc., a Delaware corporation (the "Company"), does hereby certify to his knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended September 30, 2016 of the Company (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Act of 1934, and the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Corey M. Horowitz  
Chief Executive Officer and Chairman  
November 10, 2016

**CERTIFICATION OF CHIEF FINANCIAL OFFICER**

**Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. ss. 1350)**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. ss. 1350), the undersigned, David C. Kahn, Chief Financial Officer of Network-1 Technologies, Inc., a Delaware corporation (the "Company"), does hereby certify to his knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended September 30, 2016 of the Company (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Act of 1934, and the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David C. Kahn  
Chief Financial Officer  
November 10, 2016