INTERMOLECULAR INC
Form 10-Q
November 06, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2015

Or

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

For the transition period from to

Commission File Number 001-35348

Intermolecular, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	20-1616267 (I.R.S. Employer Identification No.)
3011 N. First Street San Jose, California (Address of Principal Executive Offices)	95134 (Zip Code)

(408) 582-5700

(Registrant's Telephone Number, Including Area Code)

N/A

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

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

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

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

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

Shares outstanding of the registrant's common stock:

Class	Outstanding as of November 2, 2015
Common stock, $0.001 par value	48,920,754

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INTERMOLECULAR, INC.

FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2015

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PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

INTERMOLECULAR, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(In thousands, except share and per share data)

(Unaudited)

	September 30, 2015	December 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 3,301	$ 21,765
Short-term investments	31,193	43,304
Accounts receivable, net of allowance for doubtful accounts of $0 as of September 30, 2015 and December 31, 2014	7,841	5,321
Accounts receivable, due from related parties	23	—
Inventory, current portion	—	34
Prepaid expenses and other current assets	1,177	1,784
Total current assets	43,535	72,208
Inventory, net of current portion	4,180	5,894
Property and equipment, net	16,088	19,106
Intangible assets, net	7,316	7,941
Other assets	513	288
Total assets	$ 71,632	$ 105,437
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 1,764	$ 862
Accrued liabilities	2,320	2,101
Accrued compensation and employee benefits	4,342	1,628
Deferred revenue	1,864	2,709
Related party deferred revenue	208	831
Note payable	—	2,000
Total current liabilities	10,498	10,131
Deferred revenue, net of current portion	130	1,103
Deferred rent, net of current portion	3,324	2,810
Note payable, net of current portion	—	21,000
Other long-term liabilities	234	128
Total liabilities	14,186	35,172
Commitments and contingencies (note 5)		
Stockholders' equity:		

Preferred stock, $0.001 par value, 5,000,000 shares authorized, no shares issued and outstanding as of September 30, 2015 and December 31, 2014		—		—
Common stock, par value $0.001 per share—200,000,000 shares authorized; 48,851,166 and 47,614,150 shares issued and outstanding as of September 30, 2015 and December 31, 2014, respectively		49		48
Additional paid-in capital		207,788		202,139
Accumulated other comprehensive loss		(9)		(37)
Accumulated deficit		(150,382)		(131,885)
Total stockholders' equity		57,446		70,265
Total liabilities and stockholders' equity	$	71,632	$	105,437

See accompanying notes to unaudited condensed consolidated financial statements

INTERMOLECULAR, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

(In thousands, except share and per share data)

(Unaudited)

	Three Months Ended September 30, 2015	2014	Nine Months Ended September 30, 2015	2014
Revenue:				
Program revenue	$ 8,684	$ 7,699	$ 22,958	$ 23,450
Product revenue	—	—	75	—
Licensing and royalty revenue	2,844	3,156	9,334	13,244
Total revenue	11,528	10,855	32,367	36,694
Cost of revenue:				
Cost of development program and services revenue	4,984	6,090	14,884	18,044
Cost of product revenue	—	—	55	—
Cost of licensing and royalty revenue	64	77	216	327
Total cost of revenue	5,048	6,167	15,155	18,371
Gross profit	6,480	4,688	17,212	18,323
Operating expenses:				
Research and development	7,422	5,023	21,082	18,191
Sales and marketing	1,639	1,321	4,535	4,348
General and administrative	3,171	3,134	9,767	9,544
Restructuring charges	—	—	—	1,361
Total operating expenses	12,232	9,478	35,384	33,444
Loss from operations	(5,752)	(4,790)	(18,172)	(15,121)
Other income (expense):				
Interest expense, net	(52)	(159)	(307)	(532)
Other income (expense), net	(18)	(13)	(11)	(13)
Total other income (expense), net	(70)	(172)	(318)	(545)
Loss before provision for income taxes	(5,822)	(4,962)	(18,490)	(15,666)
Provision for income taxes	2	1	7	7
Net loss	$ (5,824)	$ (4,963)	$ (18,497)	$ (15,673)
Net loss per share of common stock, basic and diluted	$ (0.12)	$ (0.11)	$ (0.38)	$ (0.34)
Weighted-average number of shares used in computing net loss per share of common stock, basic and diluted	48,620,503	46,842,055	48,055,409	46,655,187

Related Party Transactions

The Condensed Consolidated Statements of Operations include the following related party transactions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Revenue:				
Program revenue	$ 26	$ 3	$ 32	$ 1,111
Licensing and royalty revenue	915	1,147	2,343	2,647
Total revenue	$ 941	$ 1,150	$ 2,375	$ 3,758

See accompanying notes to unaudited condensed consolidated financial statements

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Condensed Consolidated Statements of Comprehensive Loss

(In thousands)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net loss	$ (5,824)	$ (4,963)	$ (18,497)	$ (15,673)
Unrealized losses on available-for-sale-securities	41	(12)	28	(30)
Other comprehensive loss	41	(12)	28	(30)
Comprehensive loss, net of income tax	$ (5,783)	$ (4,975)	$ (18,469)	$ (15,703)

See accompanying notes to unaudited condensed consolidated financial statements

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INTERMOLECULAR, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Nine Months Ended September 30, 2015	2014
Cash flows from operating activities:		
Net loss	$ (18,497)	$ (15,673)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation, amortization, and accretion	7,468	8,149
Stock-based compensation	4,788	4,529
Changes in operating assets and liabilities:		
Prepaid expenses and other assets	(136)	656
Inventory	263	50
Accounts receivable	(2,543)	770
Accounts payable	745	(1,231)
Accrued and other liabilities	3,542	(440)
Deferred revenue	(1,818)	1,166
Related party deferred revenue	(623)	430
Net cash (used in) provided by operating activities	(6,811)	(1,594)
Cash flows from investing activities:		
Purchase of short-term investments	(32,118)	(45,171)
Redemption of short-term investments	44,114	785
Purchase of property and equipment	(933)	(2,568)
Purchased and capitalized intangible assets	(577)	(1,160)
Net cash (used in) provided by investing activities	10,486	(48,114)
Cash flows from financing activities:		
Payment of debt	(23,000)	(1,500)
Proceeds from exercise of common stock options	861	1,175
Net cash (used in) provided by financing activities	(22,139)	(325)
Net decrease in cash and cash equivalents	(18,464)	(50,033)
Cash and cash equivalents at beginning of period	21,765	72,083
Cash and cash equivalents at end of period	$ 3,301	$ 22,050
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 652	$ 471
Cash paid for income taxes, net of refunds received	$ 5	$ 33
Noncash investing/operating activities:		
Transfer of property and equipment to inventory	$ 1,252	$ 999
Transfer of inventory to property and equipment	$ 2,737	$ —
Additions to property, equipment and intangible assets not paid at the end of the period	$ 528	$ 284

See accompanying notes to unaudited condensed consolidated financial statements

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INTERMOLECULAR, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements of Intermolecular, Inc. and subsidiaries (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission (SEC). Accordingly, certain information and disclosures normally included in complete financial statements prepared in accordance with GAAP have been condensed or omitted. The information in this report should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in its Annual Report on Form 10-K for the fiscal year ended December 31, 2014, as filed with the SEC on February 27, 2015.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the Company's financial position, results of operations and cash flows for the interim periods presented. The operating results for the three and nine months ended September 30, 2015 are not necessarily indicative of the results that may be expected for any other future interim period or full year. The condensed consolidated balance sheet as of December 31, 2014 is derived from the audited consolidated financial statements as of the year then ended.

Use of Estimates

The preparation of the accompanying condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions about future events. These estimates and the underlying assumptions affect the amounts of assets and liabilities reported, disclosures about contingent assets and liabilities, and reported amounts of revenue and expenses. Management uses estimates and judgments in determining recognition of revenues, valuations of accounts receivable, inventories, intangible assets, warrants and assumptions used in the calculation of income taxes and stock-based compensation, among others. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, and adjusts such estimates and assumptions when facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentration of credit risk consist of cash, cash equivalents, short-term investments and accounts receivable. The Company's cash, cash equivalents and short-term investments consist of demand deposits, money market accounts, certificates of deposit, corporate bonds and commercial paper maintained with high quality financial institutions. The Company's accounts receivable consist of non-interest bearing balances due from credit-worthy customers.

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Cash, Cash Equivalents and Short-Term Investments

The Company holds its cash and cash equivalents in checking, money market and investment accounts with high credit quality financial institutions. The Company considers all highly liquid investments with original maturities of three months or less when purchased to be cash equivalents.

Short-term investments consist principally of corporate debt securities and commercial paper. If applicable, the Company considers marketable securities with remaining time to maturity greater than one year and that are expected to be held to maturity to be classified as long-term, as it expects to hold them to maturity. As of September 30, 2015, the Company did not have any such securities. The Company considers all other marketable securities to be short-term marketable securities. The short-term marketable securities are classified as current assets because they can be readily converted into securities with a shorter remaining time to maturity or into cash. The Company determines the appropriate classification of its marketable securities at the time of purchase and re-evaluates such designations as of each balance sheet date. All marketable securities and cash equivalents in the portfolio are classified as available-for-sale and are stated at fair value, with all the associated unrealized gains and losses reported as a component of accumulated other comprehensive income (loss). Fair value is based on quoted market rates or direct and indirect observable markets for these investments. The amortized cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and accretion are included in interest income. The cost of securities sold and any gains and losses on sales are based on the specific identification method.

The Company reviews its investment portfolio periodically to assess for other-than-temporary impairment in order to determine the classification of the impairment as temporary or other-than-temporary, which involves considerable judgment regarding factors such as the length of the time and the extent to which the market value has been lower than the amortized cost, the nature of underlying assets, and the financial condition, credit rating, market liquidity conditions and near-term prospects of the issuer. If the fair value of a debt security is less than its amortized cost basis at the balance sheet date, an assessment would have to be made as to whether the impairment is other-than-temporary. If the Company considers it more likely than not that it will sell the security before it will recover its amortized cost basis, an other-than-temporary impairment will be considered to have occurred. An other-than-temporary impairment will also be considered to have occurred if the Company does not expect to recover the entire amortized cost basis of the security, even if it does not intend to sell the security. The Company has recognized no other-than-temporary impairments for its marketable securities.

Inventory

Inventories are stated at the lower of cost or market value, with cost determined on an average cost basis. Current inventories consist of work-in-process for products that are expected to be sold in the next twelve months. Noncurrent inventories consist of raw materials in the amount of $4.2 million and $5.9 million as of September 30, 2015 and December 31, 2014, respectively. Inventories in excess of salable or usable amounts and spare parts inventories that are considered obsolete are recorded as a cost of revenue in the period in which they occur. The Company recorded inventory impairments of $0.9 million and $0.3 million during the nine months ended September 30, 2015 and September 30, 2014, respectively.

Impairment of Long-Lived Assets

The Company evaluates its long-lived assets, which consist of property and equipment and intangible assets, for indicators of possible impairment when events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Impairment exists if the carrying amounts of such assets exceed the estimates of future net undiscounted cash flows expected to be generated by such assets. Should impairment exist, the impairment loss would be measured based on the excess carrying value of the asset over the estimated fair value of the asset. The Company had no

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impairment of property and equipment during the nine months ended September 30, 2015 and 2014. The company did write off $0.6 million and $0.2 million of pending patents in the nine months ending September 30, 2015 and 2014.

Revenue Recognition

The Company derives its revenue from two principal sources: research and development programs and other services, and technology licensing and royalty fees. Product sales have been made historically, but are not a principal source of revenue. Revenue is recognized when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services have been rendered;
- The fee is fixed or determinable; and
- Collectability of the fee is probable.

Persuasive evidence of the arrangement represents a written contract signed by both the Company and the customer, or a customer purchase order. The Company assesses whether a price is fixed or determinable by, among other things, reviewing contractual terms and conditions related to payment terms. The Company assesses collectability based on factors such as the customer's creditworthiness and past collection history, if applicable. If collection is not probable, revenue recognition is deferred until receipt of payment.

Programs and other services - The Company enters into development programs and other research and development service agreements with customers under which the Company conducts research and development activities with customers. The agreements specify minimum levels of research effort required to be performed by the Company. Payments received under the agreements are not refundable if the research effort is not successful. In some contracts, the Company retains rights to certain elements of technology developed in the course of its performance, which the customer has an option to license in the future under the terms defined in the agreement. Most arrangements with customers have fixed monthly fees and requirements to provide regular reporting of research and development activities performed, and revenue is recognized in a manner consistent with the fixed monthly fee. Payments received prior to performance are deferred and recognized as revenue when earned over future performance periods.

Product maintenance and support services - Included in program and other services revenue, these services entitle customers to receive product updates and enhancements or technical support and maintenance, depending on the offering. The related revenue is recognized ratably over the period the services are delivered.

Product revenue - The Company recognizes revenue from the sale of products once delivery has occurred (title and risk of loss have passed to the customer), and customer acceptance, if required, has been achieved.

Licensing and royalty revenue - The Company recognizes revenue for licenses to intellectual property when earned pursuant to the terms of the agreements. Time-based license revenue is recognized ratably over the license term. Licensing and royalty revenue that becomes triggered by specific customer actions, such as exercise of a license option or by sales volume, is recognized when it occurs based on royalty reports or other information received from the licensee. Minimum and prepaid royalties and license fees are recognized ratably over the related periods. Revenue on the sale of intellectual property is recognized in full when title transfers if there are no remaining deliverables related to the intellectual property purchase.

Multiple-element arrangements - Certain of the Company’s customer arrangements involve the delivery or performance of multiple products, services or licenses. Product sale arrangements include product maintenance and support. Development programs and other research and development services include licenses of technology and may also include sales of products. For multiple-element arrangements that include hardware products containing software essential to the hardware product's functionality, undelivered software elements that relate to the hardware product's

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essential software, and undelivered non-software services, the Company allocates revenue to all deliverables based on their relative selling prices.

The Company evaluates whether a delivered element has value to the customer without the remaining undelivered elements by determining whether the delivered element could be sold by the Company, or resold by the customer, on a stand-alone basis. The Company concluded that all of its products and services deliverables have value to the customers on a stand-alone basis, as all these deliverables have been or could be sold and used by customers on a stand-alone basis. Intellectual property license arrangements have value on a stand-alone basis if the customer could purchase and use them without the remaining elements of the arrangement. Essential and non-essential software deliverables used in conjunction with products are evaluated as to whether industry specific software accounting guidance applies to the product as well as the related software. In instances where software is considered non-essential to the functionality of the product, only the software portion and post contract support is evaluated under industry specific software accounting guidance. For purposes of classification in the consolidated statements of operations, revenue is allocated between development programs and services revenue, product revenue and licensing and royalty revenue based on objective and reliable evidence of fair value for any elements for which it exists or based on the relative stated invoice amount for elements for which objective and reliable evidence of fair value does not exist.

The Company recognizes revenue using estimated selling prices of the delivered goods and services based on a hierarchy of methods as required by GAAP. The Company has not established vendor-specific objective evidence for the determination of estimated selling price of elements, and since third-party evidence is not available for those elements where vendor-specific objective evidence of selling price cannot be determined, the Company evaluates factors to determine its estimated selling prices for all other elements. In multiple-element arrangements where hardware and software are sold as part of the solution, revenue is allocated to the hardware and software as a group using the relative selling prices of each of the deliverables in the arrangement based upon the aforementioned selling price hierarchy.

Deferred Revenue - Deferred revenue represents amounts collected from customers for which the related revenue has not been recognized, because one or more of the revenue recognition criteria have not been met, net of the associated costs. The current portion of deferred revenue represents the amount that is expected to be recognized as revenue within one year from the balance sheet date. When deferred revenues are recognized as revenues, the associated deferred costs are also recognized as cost of revenues.

Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at invoiced amounts and unbilled contractually obligated amounts. Trade accounts receivable are presented net of allowances for doubtful accounts, if applicable, and do not bear interest. The allowance for doubtful accounts is based on the Company's assessment of the collectability of its customer accounts. The Company reviews the allowance by considering certain factors such as historical experience, industry data, credit quality, age of balances and current economic conditions that may affect customers' ability to pay.

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Concentration of Revenue and Accounts Receivable

Significant customers are those that represent more than 10% of the Company’s total revenue or accounts receivable. For each significant customer, including related parties, revenue as a percentage of total revenue and accounts receivable as a percentage of total accounts receivable are as follows:

	Revenue				Accounts Receivable	
	Three Months Ended September 30,		Nine Months Ended September 30,		As of September 30,	As of December 31,
	2015	2014	2015	2014	2015	2014
Customer A	34 %	38 %	39 %	34 %	46 %	54 %
Customer B	10 %	22 %	11 %	16 %	*	14 %
Customer D	-	*	*	*	-	11 %
Customer E	-	-	-	14 %	-	-
Customer G	12 %	-	16 %	-	17 %	-
Customer H	12 %	-	*	-	18 %	-

* less than 10%

Stock-Based Compensation

The Company applies the fair value recognition and measurement provisions of ASC 718 Compensation — Stock Compensation. The Company measures and recognizes compensation expense for all stock-based payment awards issued to employees and directors including employee stock options and restricted stock units based on estimated fair values. The Company uses the grant-date fair value of its common stock to determine the fair value of restricted stock units. The Company uses the Black-Scholes option pricing model to determine the fair value of stock options. Stock-based compensation cost is recorded net of estimated forfeitures on a straight-line basis over the requisite service period (generally the vesting period).

The Company accounts for stock options issued to nonemployees based on the fair value of the options determined using the Black-Scholes option-pricing model. The fair value of stock options granted to nonemployees is remeasured each reporting period as the stock options vest and the resulting change in value, if any, is recognized in the Company’s consolidated statements of operations during the period the related services are rendered.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2014-09 (ASU 2014-09) "Revenue from Contracts with Customers." ASU 2014-09 supersedes the revenue recognition requirements in “Revenue Recognition (Topic 605)”, and requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. As currently issued, the standard is effective beginning in the first quarter of fiscal year 2018. The Company is currently in the process of evaluating the impact of the adoption of ASU 2014-09 on the consolidated financial statements.

In July 2015, the FASB issued Accounting Standards Update No. 2015-11 (ASU 2015-11) “Simplifying the Measurement of Inventory.” ASU 2015-11 changes the measurement principle for inventory from the lower of cost or market to the lower of cost and net realizable value and will be effective for annual reporting periods beginning after December 15, 2016. Early adoption is permitted and the Company does not expect the adoption of ASU 2015-11 to have a material effect on the consolidated financial statements.

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2. Fair Value of Financial Instruments

The Company measures and reports its cash equivalents and short-term investments at fair value on a recurring basis. There have been no transfers between fair values during the nine months ended September 30, 2015 and 2014. The Company does not have any financial liabilities that are measured and reported at fair value.

The following tables set forth the fair value of the Company's cash equivalents by level within the fair value hierarchy (in thousands):

	As of September 30, 2015			
	Fair Value	Level I	Level II	Level III
Assets:				
Money market funds	$ 234	$ 234	$ —	$ —
Corporate debt securities and commercial paper	31,193	—	31,193	—
Total assets measured at fair value	$ 31,427	$ 234	$ 31,193	$ —

	As of December 31, 2014			
	Fair Value	Level I	Level II	Level III
Assets:				
Money market funds	$ 16,376	$ 16,376	$ —	$ —
Corporate debt securities and commercial paper	43,304	—	43,304	—
Total assets measured at fair value	$ 59,680	$ 16,376	$ 43,304	$ —

Short-term investments are classified as "available-for-sale" and are carried at fair value based on quoted markets or other readily available market information. The Company's investment policy requires investments less than twenty four months and a minimum credit rating of A-. Unrealized gains and losses, net of taxes, are included in accumulated other comprehensive loss. Gains and losses are determined using the specific identification method. Cash, cash equivalents, and short-term investments consisted of the following as of September 30, 2015 (in thousands):

	As of September 30, 2015			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Assets:				
Cash	$ 3,067	$ —	$ —	$ 3,067
Money market funds	234	—	—	234
Corporate debt securities and commercial paper	31,202	—	(9)	31,193

Total cash, cash equivalents and short-term investments	$ 34,503	$ —	$ (9)	$ 34,494

As of December 31, 2014 the Company had $37,000 of unrealized losses.

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3. Property and Equipment

Property and equipment consist of the following (in thousands):

	As of September 30, 2015	As of December 31, 2014
Lab equipment and machinery	$ 55,077	$ 53,412
Leasehold improvements	6,116	5,892
Computer equipment and software	4,270	3,774
Furniture and fixtures	203	197
Construction in progress	984	847
Total property and equipment	66,650	64,122
Less accumulated depreciation	(50,562)	(45,016)
Property and equipment, net	$ 16,088	$ 19,106

The following table presents depreciation expense included in the Condensed Consolidated Statement of Operations and includes amortization of leasehold improvements (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Depreciation expense	$ 1,674	$ 2,433	$ 5,664	$ 7,267

4. Intangible Assets

Intangible assets consist of the following (in thousands):

	As of September 30, 2015	As of December 31, 2014
Patents issued	$ 7,460	$ 6,518
Patents pending	2,351	3,373
Trademarks	40	40
Total intangible assets	9,851	9,931
Less patent amortization	(2,535)	(1,990)
Intangible assets, net	$ 7,316	$ 7,941

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Amortization commences upon patent issuance. The useful life of the patents, once issued, will not exceed 20 years, and will depend on the nature of the patent. The average estimated amortization period of the Company's current portfolio is approximately 17 years from the date of patent issuance. The average estimated remaining amortization period of patents acquired as part of an asset purchase from Symyx Technologies, Inc. (Symyx) in 2011 is approximately 3 years.

The following table presents patent amortization expense included in the Condensed Consolidated Statement of Operations (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Amortization expense	$ 182	$ 175	$ 545	$ 505

5. Commitments and Contingencies

Leases

The Company entered into an operating lease agreement in October 2013 that expires in June 2025. Rent expense is being recognized on a straight-line basis over the lease term.

The following table presents rent expense included in the Condensed Consolidated Statement of Operations (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Rent expense	$ 567	$ 567	$ 1,701	$ 1,701

Future commitments and obligations under this operating lease to be satisfied as they become due over the term are as follows (in thousands):

As of September 30, 2015:	
Three months ending December 31, 2015	$ 490
The years ending December 31,	
2016	2,350
2017	2,399
2018	2,459
2019	2,521
Thereafter	15,037
Total	$ 25,256

During 2015, the Company has made payments of $1.2 million related to this operating lease.

The following table presents payments made during 2015 for interest and principal owed under the terms of the Loan Agreement (in thousands):

	Three Months Ended September 30, 2015			Nine Months Ended September 30, 2015		
	Principal	Interest	Total	Principal	Interest	Total
SVB payments	$ 22,000	$ 278	$ 22,278	$ 23,000	$ 652	$ 23,652

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6. Stockholders' Equity

Stock-Based Compensation

The fair value of the employee stock options granted during the period was estimated on the respective grant date using a Black-Scholes option-pricing model with the following weighted-average assumptions:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
Expected term (in years)	6.1		6.1		5.9		5.8	
Risk-free interest rate	1.8	%	1.9	%	1.6	%	1.9	%
Expected volatility	49	%	57	%	50	%	57	%
Expected dividend rate	—	%	—	%	—	%	—	%

Stock-based compensation expense, net of estimated forfeitures, was included in the following line items on the Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Cost of revenue	$ 172	$ 407	$ 956	$ 955
Research and development	320	296	1,338	876
Sales and marketing	157	412	680	1,072
General and administrative	496	621	1,814	1,626
Total stock-based compensation	$ 1,145	$ 1,736	$ 4,788	$ 4,529

The following table presents stock-based compensation expense, net of estimated forfeitures, by grant type (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Stock options	$ 1,052	$ 874	$ 3,513	$ 2,672
Restricted stock awards and restricted stock units (RSUs)	93	862	1,275	1,857
Total stock-based compensation	$ 1,145	$ 1,736	$ 4,788	$ 4,529

The following table presents unrecognized compensation expense, net of estimated forfeitures, related to the Company's equity compensation plans as of September 30, 2015, which is expected to be recognized over the following weighted-average periods (in thousands, except for weighted-average period):

	Unrecognized Compensation Expense	Weighted-Average Period (in years)
Stock options	$ 6,522	2.8
RSUs	$ 1,124	2.2

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The following table presents details on grants made by the Company for the following periods:

	Nine Months Ended September 30, 2015		Nine Months Ended September 30, 2014	
	Shares Granted	Weighted-Average Grant Date Fair Value	Shares Granted	Weighted-Average Grant Date Fair Value
Stock options	3,479,313	$ 0.86	1,922,600	$ 1.47
RSUs	40,000	$ 1.66	1,410,450	$ 2.78

The total intrinsic value of stock options exercised during the nine months ended September 30, 2015 and 2014 was $0.8 million and $0.7 million, respectively.

RSUs that vested during the nine months ended September 30, 2015 and 2014 had fair values of $2.8 million and $1.7 million, respectively, as of the vesting date.

Common Stock Warrants

As of December 31, 2014, the Company had 90,000 outstanding and exercisable warrants to purchase shares of common stock. All of these warrants expired unexercised as of June 30, 2015.

Common Stock

As of September 30, 2015 and December 31, 2014, the Company had reserved shares of common stock for issuance as follows:

	As of September 30, 2015	As of December 31, 2014
Number of stock options outstanding	11,667,660	10,441,562
Number of RSUs outstanding	415,241	1,583,801
Shares available for future grant	2,799,694	1,770,411
Number of warrants outstanding	—	90,000
Total shares reserved	14,882,595	13,885,774

7. Net Loss per Share of Common Stock

The following table sets forth the computation of the Company’s basic and diluted net loss per share of common stock during the three and nine months ended September 30, 2015 and 2014 (in thousands, except for share and per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net loss attributable to common stockholders	$ (5,824)	$ (4,963)	$ (18,497)	$ (15,673)
Shares used in computing net loss per share of common stock, basic and diluted	48,620,503	46,842,055	48,055,409	46,655,187
Net loss per share of common stock, basic and diluted	$ (0.12)	$ (0.11)	$ (0.38)	$ (0.34)

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The following outstanding shares of common stock equivalents were excluded from the computation of diluted net loss per share of common stock for the periods presented because including them would have been antidilutive:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Stock options to purchase common stock	11,667,660	6,699,670	11,667,660	6,699,670
RSUs	415,241	1,830,805	415,241	1,830,805
Common stock warrants	—	90,000	—	90,000

8. Income Taxes

Income tax expense for the nine months ended September 30, 2015 was $7,000, or 0.0%, on a pre-tax loss of $18.5 million. The difference between the Company's effective tax rate and the federal statutory rate of 35% is primarily attributable to the differential in foreign taxes, non-deductible stock-based compensation expense, other currently non-deductible items and movement in its valuation allowance. The Company maintained a valuation allowance as of September 30, 2015 against all of its deferred tax assets.

The Company intends to maintain a full valuation allowance until sufficient positive evidence exists to support its reduction.

9. Related Party Transactions

In March 2013, the Company amended the program agreement that it had entered into in March 2010 with a related party and that it and the related party had amended in March 2012. Under the amended agreement, the two companies agreed to work together to conduct research and development and other activities. The program development between the parties ended during the year ended December 31, 2014, although certain licensing and royalty elements continue. The other party and the Company each have an independent board member that serves on both companies’ boards of directors and the independent board member is also a managing member of a significant stockholder of the Company. As of September 30, 2015, this stockholder was a beneficial owner of approximately 8.8% of the Company’s common stock. The following table presents related party revenue included in the Condensed Consolidated Statement of Operations from this amended agreement (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Related party revenue	$ 336	$ 313	$ 961	$ 1,570

In November 2006, the Company entered into an Alliance Agreement with a related party that was a beneficial owner of less than 5% of the Company's common stock as of September 30, 2015. The other party and the Company each have an independent board member that serves on both companies' boards of directors. Since November 2006, the agreement has been amended numerous times with the last amendment signed in December 2013.

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As of September 30, 2015 and December 31, 2014, the Company had an immaterial accounts receivable balance, and had a deferred revenue balance in the amount of $0.2 million and $0.8 million, respectively, related to the amended agreement. The following table presents related party revenue included in the Condensed Consolidated Statement of Operations from the amended agreement (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Related party revenue	$ 605	$ 837	$ 1,414	$ 2,188

10. Information about Geographic Areas

Revenue

Revenue by geography is based on the billing address of the customer. The following table sets forth revenue by geographic area (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
United States	$ 7,206	$ 9,626	$ 21,835	$ 32,897
Japan	913	685	2,208	1,942
APAC other	3,115	407	7,599	1,338
Europe and Middle East	294	137	725	517
Total	$ 11,528	$ 10,855	$ 32,367	$ 36,694

Long-Lived Assets

Substantially all of the Company’s long-lived assets are located in the U.S. An insignificant amount of long-lived assets reside in the Company’s foreign subsidiaries and branches in Hong Kong, Japan and Taiwan.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Our Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is provided in addition to the accompanying consolidated condensed financial statements and notes to assist readers in understanding our results of operations, financial condition, and cash flows. Our MD&A is organized as follows:

- Overview. Discussion of our business and overall analysis of financial and other highlights affecting the Company in order to provide context for the remainder of MD&A.
- Strategy. Our overall strategy.
- Basis of Presentation. A summary of the primary elements of our financial results.
- Critical Accounting Estimates. Accounting estimates that we believe are most important to understanding the assumptions and judgments incorporated in our reported financial results and forecasts.
- Results of Operations. An analysis of our financial results comparing the three and nine months ended September 30, 2015 to the three and nine months ended September 30, 2014.
- Liquidity and Capital Resources. An analysis of changes in our balance sheets and cash flows, and discussion of our financial condition and potential sources of liquidity.

The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q (Form 10-Q) and in our Annual Report on Form 10-K (2014 Form 10-K), as filed with the Securities and Exchange Commission. This Form 10-Q contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements are often identified by the use of words such as, but not limited to, "may," "will," "expect," "believe," "anticipate," "intend," "could," "should," "esti "continue," and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" in Part II, Item 1A of this Form 10-Q and in our 2014 Form 10-K. Furthermore, such forward-looking statements speak only as of the date of this Form 10-Q. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We provide solutions for the evaluation and development of engineered thin-film materials for next generation technology products. Our customers manufacture products by depositing thin films of advanced materials using customized processes to create structures that must meet increasingly rigorous optical, mechanical or electrical specifications. Developing advanced thin film structures capable of addressing the specifications of particular applications increasingly requires the evaluation of a wider range of materials, as well as the development of a broader range of processes. Intermolecular utilizes proprietary methods to accelerate a broad and deep understanding of the characteristics of thin-film engineered materials. Due to our flexibility, speed and materials focus, we are able to assist

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our customers by more quickly evaluating candidate materials and combining them into thin film solutions that meet their specific needs.

We were founded in 2004 and are headquartered in San Jose, California. Our total revenue increased to $11.5 million for the three months ended September 30, 2015 and decreased to $32.4 million for the nine months ended September 30, 2015 from $10.9 million and $36.7 million for the three and nine months ended September 30, 2014. Our net loss increased to $5.8 million for the three months ended September 30, 2015 and $18.5 million for the nine months ended September 30, 2015, from a net loss of $5.0 million and $15.7 million for the three and nine months ended September 30, 2014. Since inception, we have incurred net losses leading to an accumulated deficit of $150.4 million as of September 30, 2015.

Strategy

Our mission is to become the leader in engineered materials solutions for complex technologies that differentiate our customers' products, allowing them to derive a competitive advantage from the interaction of materials science, processes, integration and device architecture that Intermolecular brings to bear. The company's products and services consist of information products, tools, and materials formulations that enable its customers' R&D departments to efficiently evaluate, develop and integrate materials that are critical to their next generation products. Intermolecular's product solutions create significant economic value for its customers by enabling them to rapidly discover and create new options for mission-critical materials decisions. We currently target semiconductor markets, including memory, logic and embedded memory, flat glass coatings and glass-based devices, light-emitting diodes (LEDs), displays, advanced alloys and other applications and markets that rely on multinary thin films for differentiation. To date, we have received the majority of our revenue from customers in DRAM, stand-alone non-volatile memory, complex logic, solar cells, and energy-efficiency applications in flat glass coatings and glass-based devices, and we have not yet received a material amount of revenue from customers in embedded memory, LEDs, displays and other technologies.

Basis of Presentation

How We Generate Revenue

Our customer engagement process generates revenue in three ways: program revenue; licensing and royalty revenue, and product revenue. Programs are our primary engagement model with customers and are structured to result in program fees, and in some cases licensing and/or royalty revenue arrangements. Program revenue may include payments for research services, milestone payments, and subscription payments for dedicated and shared workflow tools used in the programs and reimbursed payments for consumables and outside services from third parties. Individual programs typically range from six months up to three years. Services revenue outside of programs are substantially comprised of support and maintenance fees and extended warranty agreements. Program revenue is recognized in a manner consistent with activities performed. As we engage new customers and negotiate extensions for existing customer agreements that are nearing completion, we expect program revenue to continue to fluctuate.

· Program revenue. Program revenue may include payments for research services, milestone payments, and subscription payments for dedicated and shared workflow tools used in the programs and reimbursed payments for consumables and outside services from third parties. Individual programs typically range from six months up to three years. Services revenue outside of programs are substantially comprised of support and maintenance fees and extended warranty agreements. Program revenue is recognized in a manner consistent with activities performed. As we engage new customers and negotiate extensions for existing customer agreements that are nearing completion, we expect program revenue to continue to fluctuate.

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- Licensing and royalty revenue. Licensing and royalty revenue consists of licensing fees and royalties for granting our customers rights to our proprietary technology and intellectual property (IP). Specifically, this includes licensing the HPC capabilities of our workflows, licensing our informatics and analysis software, and licensing fees and royalties on products commercialized by our customers that incorporate technology developed through our programs. In certain instances, minimum license fees and royalties may be guaranteed by customer contracts and are recognized as revenue ratably over the related periods. We anticipate our licensing and royalty revenue to continue to fluctuate based on the timing and amount of minimum license fees guaranteed by certain customer contracts and the timing of customer reported volume-based royalties.
- Product revenue. Product revenue consists of sales of our workflow hardware and embedded software. In support of our business strategy, we selectively sell our proprietary tools to increase opportunities for programs and licensing fees and royalties. As our other revenue streams increase we expect our product revenue to continue to decrease as a percentage of our overall revenue. Product revenue is recognized upon shipment (when title and risk of loss have passed to the customer), and customer acceptance, if required, is achieved.

Cost of Revenue

Our cost of revenue is variable and depends on the product mix and type of revenue earned in each period relating to our customer programs.

- Cost of program revenue. Our cost of program revenue is primarily comprised of salaries and other personnel-related expenses (including stock-based compensation) for our research and development scientists, engineers and development fab process operations employees. Additionally, our cost of revenue includes costs of wafers, targets, materials, program-related supplies, third-party professional fees and depreciation of equipment used in programs. Inventory obsolescence and customer related asset impairments are included in cost of program revenue.
- Cost of licensing and royalty revenue. Our cost of licensing and royalty revenue has been, and we expect will continue to be, primarily comprised of the amortization of acquired patents, which were acquired as part of our completion of the Symyx asset purchase transaction in November 2011, and licensing obligations.
- Cost of product revenue. Our cost of product revenue primarily includes our cost of products sold, which we expect to continue to decrease as a percentage of overall cost of revenue. Cost of product revenue is recognized upon product shipment (when title and risk of loss transfer) and customer acceptance, if required. The cost of product revenue as a percentage of revenue is related to the quantity and configuration of products sold during the period.

Research and Development

Our R&D expenses consist of costs incurred for development and continuous improvement of our HPC platform, expansion of software capabilities and application research and development that are not associated with customer programs. R&D costs include personnel-related expenses (including stock-based compensation expenses) for our technical staff as well as consultant costs, parts and prototypes, wafers, chemicals, supply costs, facilities costs,

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utilities costs related to laboratories and offices occupied by technical staff, depreciation on equipment used by technical staff, and outside services, such as machining and third-party R&D costs. R&D overhead costs that are not allocated to a customer program are recognized as expenses within R&D. We expect our R&D expense to increase modestly in absolute dollars in the near-term periods as resources are reallocated from customer programs to R&D and as we continue to develop and improve our HPC platform and extend the applicability of our platform to a broader set of applications within the industries we serve.

Sales and Marketing

Our sales and marketing expenses consist primarily of personnel-related costs (including stock-based compensation) for our sales and marketing employees, as well as payments of commissions to our sales employees, facility costs and professional expenses. Professional expenses consist of external website and marketing communication consulting costs and market research. We expect sales and marketing expense to increase in the near-term periods as we develop new business opportunities.

General and Administrative

General and administrative expenses consist primarily of personnel-related costs (including stock-based compensation) as well as professional services and facilities costs related to our executive, finance, legal, human resources, management information systems and information technology functions. Professional services consist of outside accounting, information technology, consulting and legal costs. We also incur significant accounting and legal costs related to compliance with rules and regulations enacted by the Securities and Exchange Commission, including the costs maintaining compliance with Section 404 of the Sarbanes-Oxley Act, as well as insurance, investor relations and other costs associated with being a public company. We expect that general and administrative expense will increase modestly in absolute dollars in the near-term periods.

Restructuring Expenses

In 2014, after experiencing a reduced level of program activity, we initiated reductions in force in February 2014 and May 2014 with respect to approximately 18% and 10% of our workforce at such times, respectively. These reductions in force were part of an overall plan to reduce our cost structure and were completed during 2014. Restructuring expenses consisted of personnel-related costs.

Interest Expense, net

Interest expense consisted primarily of interest accrued on our three year note payable with Silicon Valley Bank. Interest income represents interest earned on our cash, cash equivalents and short-term investments. We expect interest income will vary each reporting period depending on our average investment balances during the period and market interest rates.

Critical Accounting Estimates

Our condensed consolidated financial statements have been prepared in conformity with generally accepted accounting principles in the United States and include our accounts and the accounts of our wholly-owned subsidiaries. The preparation of our condensed consolidated financial statements requires our management to make estimates, assumptions and judgments that affect the reported amounts of assets and liabilities and disclosures for contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenue and expenses during the applicable periods. Management bases its estimates, assumptions and judgments on historical experience and on various other factors that management believed were reasonable under the circumstances. Different assumptions and judgments would change the estimates used in the preparation of our consolidated financial statements which, in turn, could change

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the results from those reported. Our management evaluates its estimates, assumptions and judgments on an ongoing basis.

There have been no material changes in the matters for which we make critical accounting estimates in the preparation of our condensed consolidated financial statements during the three and nine months ended September 30, 2015 as compared to those disclosed in our 2014 Form 10-K. For further information on our critical and other significant accounting policies, see our 2014 Form 10-K.

Recent Accounting Pronouncements

See Note 1 of the Notes to Condensed Consolidated Financial Statements included in this Form 10-Q for recent accounting pronouncements that could have an effect on us.

Results of Operations

Comparison of the Three and Nine Months Ended September 30, 2015 and 2014

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015	2014	$ Change	% Change	2015	2014	$ Change	% Change
	(in thousands)				(in thousands)			
Revenue:								
Program revenue	$ 8,684	$ 7,699	$ 985	13 %	$ 22,958	$ 23,450	$ (492)	(2) %
Product revenue	—	—	—	100 %	75	—	75	100 %
Licensing and royalty revenue	2,844	3,156	(312)	(10) %	9,334	13,244	(3,910)	(30) %
Total revenue	11,528	10,855	673	6 %	32,367	36,694	(4,327)	(12) %
Cost of revenue:	5,048	6,167	(1,119)	(18) %	15,155	18,371	(3,216)	(18) %
Gross profit	6,480	4,688	1,792	38 %	17,212	18,323	(1,111)	(6) %
Operating expenses:								
Research and development	7,422	5,023	2,399	48 %	21,082	18,191	2,891	16 %
Sales and marketing	1,639	1,321	318	24 %	4,535	4,348	187	4 %
General and administrative	3,171	3,134	37	1 %	9,767	9,544	223	2 %
Restructuring charges	—	—	—	— %	—	1,361	(1,361)	(100) %
Total operating expenses	12,232	9,478	2,754	29 %	35,384	33,444	1,940	6 %

Loss from operations	(5,752)	(4,790)	(962)	(18,172)	(15,121)	(3,051)
Other income (expense):						
Interest expense, net	(52)	(159)	107	(307)	(532)	225
Other income (expense), net	(18)	(13)	(5)	(11)	(13)	2
Total other income (expense), net	(70)	(172)	102	(318)	(545)	227
Loss before provision for income taxes	(5,822)	(4,962)	(860)	(18,490)	(15,666)	(2,824)
Provision for income taxes	2	1	1	7	7	—
Net loss	$ (5,824)	$ (4,963)	$ (861)	$ (18,497)	$ (15,673)	$ (2,824)

Revenue

Our revenue increased by $0.7 million, or 6%, to $11.5 million during the three months ended September 30, 2015, from $10.9 million during the three months ended September 30, 2014, due to increases in program revenue, partially offset by decreases in licensing and royalty revenue.

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Our revenue decreased by $4.3 million, or 12%, to $32.4 million during the nine months ended September 30, 2015, from $36.7 million during the nine months ended September 30, 2014, due to decreases in program revenue and licensing and royalty revenue.

Program revenue increased by $1.0 million, or 13%, to $8.7 million during the three months ended September 30, 2015, from $7.7 million during the three months ended September 30, 2014. This increase was primarily attributable to a $3.2 million increase in revenue from new customer engagements. This is partially offset by $2.4 million decrease in revenue related to scheduled completion and reduction of program agreements.

Program revenue decreased by $0.5 million, or 2%, to $23.0 million during the nine months ended September 30, 2015, from $23.5 million during the nine months ended September 30, 2014. This decrease was primarily attributable to $8.6 million decrease in revenue from the scheduled completion and reduction of program agreements. This was partially offset by $8.0 million in revenue derived from new customer engagements.

Product revenue increased by $0.1 million during the nine months ended September 30, 2015. There were no product revenues during the three and nine months ended September 30, 2014.

Licensing and royalty revenue decreased by $0.3 million, or 10%, to $2.8 million during the three months ended September 30, 2015, from $3.2 million during the three months ended September 30, 2014. This decrease was primarily attributable to lower end-market sales of products subject to royalties.

Licensing and royalty revenue decreased by $3.9 million, or 30%, to $9.3 million during the nine months ended September 30, 2015, from $13.2 million during the nine months ended September 30, 2014. This decrease was primarily attributable to $4.2 million in accelerated payments from a customer in connection with the suspension of program activities during the nine months ended September 30, 2014 that did not reoccur in 2015. This was partially offset by a non-recurring success fee of $0.9 million and $0.1 million increase in scheduled minimum license fees guaranteed by other customer contracts.

The following table presents revenue by geographic region (based on invoiced locations) during the three and nine months ended September 30, 2015 and 2014 in dollars (in thousands) and as a percentage of revenue for the periods presented:

	Three Months Ended September 30,						Nine Months Ended September 30,					
	2015			2014			2015			2014		
	Revenues	% of Revenues		Revenues	% of Revenues		Revenues	% of Revenues		Revenues	% of Revenues	
United States	$ 7,206	62	%	$ 9,626	89	%	$ 21,835	68	%	$ 32,897	90	%
Japan	913	8	%	685	6	%	2,208	7	%	1,942	5	%
APAC other	3,115	27	%	407	4	%	7,599	23	%	1,338	4	%
Europe and Middle	294	3	%	137	1	%	725	2	%	517	1	%

East																
Total	$	11,528	100	%	$	10,855	100	%	$	32,367	100	%	$	36,694	100	%

Cost of Revenue

Cost of revenue decreased by $1.1 million, or 18%, to $5.0 million during the three months ended September 30, 2015, from $6.2 million during the three months ended September 30, 2014. This change is a result of decreases in direct labor, materials and other costs associated with programs.

Cost of revenue decreased by $3.2 million, or 18%, to $15.2 million during the nine months ended September 30, 2015, from $18.4 million during the nine months ended September 30, 2014. This change is a result of a $3.2 million decrease in direct labor, materials and other costs associated programs consistent with the decrease in program revenue.

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Gross Margin

Our gross profit as a percentage of net revenues, or gross margin, has been and will continue to be affected by a variety of factors, including the mix of program revenue, product revenue, and licensing and royalty revenue recognized during the period. We achieve a higher gross margin on licensing and royalty revenue as compared to program and product revenue.

Gross margin was 56.2% during the three months ended September 30, 2015 compared to 43.2% for the three months ended September 30, 2014. This increase is primarily attributable to the increased revenue and decreased direct labor, materials and other costs associated with programs.

Gross margin was 53.2% during the nine months ended September 30, 2015 compared to 49.9% for the nine months ended September 30, 2014. This increase was primarily attributable to a decrease in direct labor, materials and other costs associated with programs.

Research and Development

R&D expenses increased by $2.4 million, or 48%, to $7.4 million during the three months ended September 30, 2015, from $5.0 million during the three months ended September 30, 2014. The change is primarily attributable to an increase of $1.9 million in personnel costs related to increased headcount, wages, stock-based compensation and other related benefits, an increase of $0.4 million in engineering parts and other expenses and an increase of $0.5 million in professional services. These increases were partially offset by a $0.2 million decrease in administrative expenses and a $0.1 million decrease in depreciation and amortization expenses. Research and development expense included stock-based compensation of $0.3 million during the three months ended September 30, 2015 and 2014.

R&D expenses increased by $2.9 million, or 16%, to $21.0 million during the nine months ended September 30, 2015, from $18.2 million during the nine months ended September 30, 2014. The change was primarily attributable to an increase of $1.9 million in personnel costs, a $1.2 million increase in professional services and a $0.1 million increase in facility and depreciation expense. These increases were partially offset by $0.2 million decrease in engineering parts and other expenses associated with new application development. Research and development expense included stock-based compensation of $1.3 million and $0.9 million during the nine months ended September 30, 2015 and 2014, respectively.

Sales and Marketing

Sales and marketing expenses increased by $0.3 million, or 24%, to $1.6 million during the three months ended September 30, 2015, from $1.3 million during the three months ended September 30, 2014. This increase is attributable to $0.3 million in higher personnel costs related to increased headcount, wages, stock-based compensation and other related benefits. Sales and marketing expense included stock-based compensation of $0.2 million and $0.4 million during the three months ended September 30, 2015 and 2014, respectively.

Sales and marketing expenses increased by $0.2 million, or 4%, to $4.5 million during the nine months ended September 30, 2015, from $4.3 million during the nine months ended September 30, 2014. This increase is primarily attributable to $0.4 million in higher personnel costs, partially offset by a $0.1 million decline in professional services related costs. Sales and marketing expense included stock-based compensation of $0.7 million and $1.1 million during the nine months ended September 30, 2015 and 2014, respectively.

General and Administrative

General and administrative expenses increased by $0.1 million, or 1%, to $3.2 million during the three months ended September 30, 2015, from $3.1 million during the three months ended September 30, 2014. This increase is primarily attributable to $0.3 million in higher personnel costs related to increased headcount, wages, stock-based

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compensation and other related benefits. This is partially offset by a $0.2 million decrease in professional fees. General and administrative expense included stock-based compensation of $0.5 million and $0.6 million during the three months ended September 30, 2015 and 2014, respectively.

General and administrative expenses increased by $0.2 million, or 2%, to $9.7 million during the nine months ended September 30, 2015, from $9.5 million during the nine months ended September 30, 2014. This increase is primarily attributable to $0.7 million in higher personnel costs related to increased wages, stock-based compensation and other related benefits. This is partially offset by a $0.4 million decrease in professional fees and a $0.1 million decrease in depreciation and amortization expense. General and administrative expense included stock-based compensation of $1.8 million and $0.6 million during the nine months ended September 30, 2015 and 2014, respectively.

Restructuring Charges

There were no restructuring charges for the three months ended September 30, 2015 and September 30, 2014.

There were no restructuring charges for the nine months ended September 30, 2015 compared to $1.4 million during the nine months ended September 30, 2014. In January and May 2014, our Board of Directors authorized restructuring plans to reduce our workforce by 18% and 10%, respectively, pursuant to which charges of $1.1 million and $0.3 million were incurred for severance and other personnel related costs.

Loss from Operations

Our operating loss increased by $1.0 million, to an operating loss of $5.8 million during the three months ended September 30, 2015, from an operating loss of $4.8 million during the three months ended September 30, 2014. Our operating expenses increased by $2.8 million to $12.2 million during the three months ended September 30, 2015, from $9.5 million during the three months ended September 30, 2014.

Our operating loss increased by $3.1 million, to an operating loss of $18.2 million during the nine months ended September 30, 2015, from an operating loss of $15.1 million during the nine months ended September 30, 2014. Our operating expenses increased by $1.9 million to $35.4 million during the nine months ended September 30, 2015, from $33.4 million which includes $1.4 million in restructuring related expenses, during the nine months ended September 30, 2014.

Interest Expense, net

Interest expense, net decreased by $0.1 million to $0.1 million during the three months ended September 30, 2015, from $0.2 million during the three months ended September 30, 2014, and is primarily comprised of interest expense associated with the Loan Agreement with SVB during the three months ended September 30, 2015 and September 30, 2014.

Interest expense, net, decreased by $0.2 million to $0.3 million during the nine months ended September 30, 2015, from $0.5 million during the nine months ended September 30, 2014 and is primarily comprised of interest expense associated with the Loan Agreement with SVB during the nine months ended September 30, 2015 and June 30, 2014.

Other Income (Expense), net

Other income (expense), net, for the three and nine months ended September 30, 2015 and 2014 consisted of foreign exchange gains and losses that were not significant during these periods.

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Provision for Income Taxes

Provision for income taxes during the three and nine months ended September 30, 2015 and 2014 consisted of income taxes on our foreign entities and were not significant during these periods.

Net Loss

Our net loss increased by $0.9 million, to a net loss of $5.8 million during the three months ended September 30, 2015, from a net loss of $4.9 million during the three months ended September 30, 2014. The difference between operating loss and net loss during the three months ended September 30, 2015 and September 30, 2014 was primarily related to interest expense associated with the Loan Agreement with SVB.

Our net loss increased by $2.8 million, to a net loss of $18.5 million during the nine months ended September 30, 2015, from a net loss of $15.7 million during the nine months ended September 30, 2014. The difference between operating loss and net loss during the nine months ended September 30, 2015 and 2014 was primarily related to interest expense associated with the Loan Agreement with SVB.

Liquidity and Capital Resources

Prior to our initial public offering in November 2011, we substantially satisfied our capital and liquidity needs through private placements of redeemable convertible preferred stock and, to a lesser extent, cash flow from operations. As of September 30, 2015 we had $34.5 million of cash, cash equivalents and short-term investments and $33.0 million of net working capital.

To date, we have incurred significant losses. During the nine months ended September 30, 2015 and 2014, we incurred net losses of $18.5 million and $15.7 million, respectively. As of September 30, 2015, our accumulated deficit was $150.3 million.

We believe that we have the financial resources needed to meet business requirements for the next 12 months. However, our forecast of the period of time through which our financial resources will be adequate to meet business requirements are forward-looking statements and involve risks and uncertainties. Our future capital requirements will depend on many factors, many of which are set forth in greater detail under the caption “Risk Factors,” but generally include without limitation our rate of revenue growth, our expansion of our sales and marketing activities and overhead expenses, the timing and extent of our spending to support our R&D efforts and our ability to expand programs in the semiconductor and clean energy industries, whether we are successful in obtaining payments from customers, the financial stability of our customers, whether we can enter into additional contracts in our target industries, the progress and scope of R&D projects performed by us and our customers, the effect of any acquisitions of other businesses or technologies that we may make in the future, the filing, prosecution and enforcement of patent claims, how much funding we may need to develop or enhance our solutions or HPC platform and any necessary responses to competitive pressures. To the extent that existing cash, cash equivalents, short-term investments and cash from operations are insufficient to fund our operations and repay our outstanding debt when it may become due, we may need to raise additional funds through public or private equity or debt financing. We may also seek to invest in or acquire complementary businesses, applications or technologies, any of which could also require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all. We maintain almost all of our cash and investments in the United States and therefore are not subject to restrictions or tax obligations as we access the cash.

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Cash Flows

The following summary of our cash flows for the periods indicated has been derived from our condensed consolidated financial statements included elsewhere in this filing (in thousands):

	Nine Months Ended September 30,	
	2015	2014
Net cash (used in) provided by operating activities	$ (6,811)	$ (1,594)
Net cash (used in) provided by investing activities	$ 10,486	$ (48,114)
Net cash (used in) provided by financing activities	$ (22,139)	$ (325)

Cash Flows from Operating Activities

We experienced negative cash flows from operating activities during the nine months ended September 30, 2015 in the amount of $6.8 million as compared to negative cash flows for the same period ending 2014 in the amount of $1.6 million.

Net cash used in operating activities during the nine months ended September 30, 2015 of $6.8 million was primarily attributable to our net loss of $18.5 million, offset by non-cash charges of $7.5 million for depreciation, amortization, and accretion and $4.8 million for stock-based compensation. The net decrease in cash flow from operating assets and liabilities of $0.6 million was primarily a result of a $3.5 million increase in accrued and other liabilities, offset by a decrease in deferred revenue of $1.8 million due to the earn out of advance customer payments and increase in accounts receivable of $2.5 million.

Cash Flows from Investing Activities

Our investing activities consist primarily of purchases and maturities of short-term investments, capital expenditures to purchase property and equipment, and our investments in intangible assets relating to our patents and trademarks. In the future, we expect we will continue to make modest capital expenditures to support our operations, and to incur costs to protect our investment in our developed technology and IP.

During the nine months ended September 30, 2015, cash provided by investing activities was $10.5 million, a result of $12.0 million in the net redemptions of short-term investments, $0.9 million in capital expenditures, and $0.6 million in capitalized patent and trademark costs.

Cash Flows from Financing Activities

To date, we have financed our operations primarily with proceeds from the sale of our redeemable convertible preferred stock and proceeds received from our initial public offering.

During the nine months ended September 30, 2015, cash used in financing activities of $22.1 million primarily related to the repayment of our SVB term loan in the amount of $23.0 million, which was offset by proceeds from common stock option exercises in the amount of $0.9 million.

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Contractual Obligations and Commitments

The following summarizes our contractual obligations as of September 30, 2015 (in thousands):

	Payments Due by Period				
	Total	Less Than One Year	1 - 3 Years	3 - 5 Years	More Than 5 Years
Operating lease obligations	$ 25,256	$ 490	$ 7,209	$ 5,104	$ 12,453
Purchase obligations (1)	425	425	—	—	—
Total	$ 25,681	$ 915	$ 7,209	$ 5,104	$ 12,453

(1) Purchase obligations consist of firm, non-cancelable agreements to purchase property and equipment and inventory related items.

Operating lease agreements represent our obligations to make payments under our non-cancelable lease agreement for our facility in San Jose, California. During the nine months ended September 30, 2015, we made regular lease payments of $1.2 million under this operating lease agreement.

During 2013 we entered into a term loan pursuant to the Loan Agreement with SVB in the amount of $25.0 million that bore interest at a fixed rate equal to 3.25%. As of September 30, 2015, the remaining principal on the term loan was paid back in full.

Off-Balance Sheet Arrangements

As of September 30, 2015, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risks in the ordinary course of our business. Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of fluctuations in interest rates and foreign currency exchange rates. We do not hold or issue financial instruments for trading purposes.

Interest Rate Sensitivity

The primary objectives of our investment activities are to preserve principal, provide liquidity and maximize income without exposing us to significant risk of loss. The securities we invest in are subject to market risk and a change in prevailing interest rates may cause the principal amount of our investments to fluctuate. We maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, corporate debt securities and money market funds. As of September 30, 2015, our investments were primarily in commercial paper, corporate notes and bonds and money market funds. If overall interest rates fell 10% for the three months ended September 30, 2015, our interest income would have decreased by an immaterial amount, assuming consistent investment levels.

Foreign Currency Exchange Risk

As we expand internationally, our consolidated results of operations and cash flows will become increasingly subject to fluctuations due to changes in foreign currency exchange rates. Our revenue is denominated in U.S. dollars. Our expenses are generally denominated in the currencies in which our operations are located, which is primarily in the

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United States, with an insignificant portion of expenses incurred in the local currencies of our wholly-owned subsidiaries in Hong Kong and Japan and our wholly-owned branch in Taiwan. The effect of a hypothetical 10% change in foreign currency exchange rates applicable to our business would not have a material impact on our consolidated financial statements. To date, we have not entered into any material foreign currency hedging contracts, although we may do so in the future.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2015. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Based on the evaluation of our disclosure controls and procedures as of September 30, 2015, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes to our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including our Chief Executive Officer and Chief Financial Officer, believes that our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance of achieving their objectives and are effective at the reasonable assurance level. However, our management does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Because of the inherent limitations in a cost effective control system, misstatements due to error or fraud may occur and not be detected.

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PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we may become involved in legal proceedings and claims arising in the ordinary course of our business, including but not limited to legal proceedings and claims brought by employees or former employees relating to working conditions or other issues. We are not currently a party to any legal proceedings the outcome of which, if determined adversely to us, we believe would individually or in the aggregate have a material adverse effect on our business, operating results, financial condition or cash flows.

ITEM 1A. RISK FACTORS

The risks described in Part I, Item 1A, "Risk Factors," in our Annual Report on Form 10-K for the year ended December 31, 2014, could materially and adversely affect our business, financial condition or future results. These risk factors are not the only risks facing our company. Risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and operating results. The Risk Factors section of our 2014 Annual Report on Form 10-K remains current in all material respects.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Recent Sales of Unregistered Securities

None.

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ITEM 6. EXHIBITS

Exhibit Number	Exhibit Description	Incorporated by Reference Form	Date	Number	Filed Herewith
2.1	Asset Purchase Agreement by and between Intermolecular, Inc. and Symyx Technologies, Inc. dated as of July 28, 2011. (1)	S-1/A	09/09/11	2.1	
3.1	Amended and Restated Certificate of Incorporation of Intermolecular, Inc.	10-K	03/16/12	3.1	
3.2	Amended and Restated Bylaws of Intermolecular, Inc.	10-K	03/16/12	3.2	
4.1	Specimen Common Stock Certificate.	S-1/A	11/07/11	4.1	
4.2	Warrant to purchase shares of common stock issued to Timane S.a.r.l. dated June 20, 2008.	S-1	07/29/11	4.2	
4.3	Fourth Amended and Restated Investor Rights Agreement dated as of March 4, 2011, by and among Intermolecular, Inc. and certain stockholders named therein, as amended by Amendment No. 1 to Fourth Amended and Restated Investor Rights Agreement dated as of June 14, 2011.	S-1	07/29/11	10.1	
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
101.INS	XBRL Instance Document				X
101.SCH	XBRL Taxonomy Extension Schema Document				X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document				X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document				X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document				X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document				X

(1) All exhibits, schedules and similar attachments to this exhibit have been omitted. Copies of such exhibits, schedules and similar attachments will be furnished supplementally to the SEC upon request.

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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.

	INTERMOLECULAR, INC.
	(Registrant)
Date: November 6, 2015	By: /s/ C. Richard Neely, Jr.
	C. Richard Neely, Jr.
	Chief Financial Officer