

INTERDIGITAL COMMUNICATIONS CORP
Form 10-K/A
January 28, 2004
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

Amendment No. 1

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

For the fiscal year ended December 31, 2002

of

INTERDIGITAL COMMUNICATIONS CORPORATION

(Exact name of registrant as specified in its charter)

a Pennsylvania Corporation

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IRS Employer Identification No. 23-1882087

SEC File Number 1-11152

781 Third Avenue

King of Prussia, Pennsylvania 19406-1409

(610) 878-7800

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

Common Stock (Par Value \$0.01 Per Share)
Series B Junior Participating Preferred Stock Rights
\$2.50 Cumulative Convertible (Par Value \$0.10 Per Share)

The registrant does not have any securities registered pursuant to Section 12(b) of the Act.

The registrant's Common Stock is listed on the Nasdaq Stock Market.

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

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

The registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter: \$487,860,042 as of June 28, 2002.

On March 20, 2003, the registrant had 54,831,402 shares of Common Stock outstanding.

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EXPLANATORY NOTE

In accordance with Exchange Act Rule 12b-15, this Form 10-K/A, Amendment No. 1 amends certain items of the Annual Report on Form 10-K of InterDigital Communications Corporation (the Registrant) for the year ended December 31, 2002 filed with the Securities and Exchange Commission on March 31, 2003, and presents the complete text of the items amended, as amended. These amended items do not restate the Registrant's consolidated financial statements previously filed in the Form 10-K. This Form 10-K/A, Amendment No. 1 does not reflect events occurring after the filing of the original Form 10-K or modify or update those disclosures affected by subsequent events.

The change reflected by this Form 10-K/A, Amendment No. 1 is a revision to the report of independent accountants in Item 8, to include the city and state where the report was issued. The Exhibit Index in Item 15 is also amended to reflect the inclusion of updated certifications of certain executive officers. </R

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InterDigital® and SmartRRMSM are trademarks and service marks of InterDigital Communications Corporation. All other trademarks, service marks and/or trade names appearing in this Form 10-K/A, Amendment No. 1 are the property of their respective holders.

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In this document, the words we, our, ours, and us refer only to InterDigital Communications Corporation collectively with its subsidiaries.

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PART II

Item 8. INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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All other schedules are omitted because they are either not required or applicable or equivalent information has been included in the financial statements and notes thereto.</R

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PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Two Commerce Square, Suite 1700
2001 Market Street
Philadelphia, PA 19103-7042
Telephone (267) 330 3000
Facsimile (267) 330 3300

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors
of InterDigital Communications Corporation

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of InterDigital Communications Corporation and its subsidiaries at December 31, 2002 and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index present fairly, in all material respects, the information set forth therein for the year ended December 31, 2002 when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion. The financial statements and financial statement schedule of InterDigital Communications Corporation and its subsidiaries as of December 31, 2001, and for each of the two years in the period ended December 31, 2001, were audited by other independent accountants who have ceased operations. Those independent accountants expressed an unqualified opinion on those financial statements and financial statement schedule in their report dated February 14, 2002.

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/s/ PricewaterhouseCoopers LLP

PRICEWATERHOUSECOOPERS LLP

March 14, 2003</R

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THE FOLLOWING IS A COPY OF A REPORT PREVIOUSLY ISSUED BY ARTHUR ANDERSEN LLP (ANDERSEN). THIS REPORT HAS NOT BEEN REISSUED BY ANDERSEN AND ANDERSEN DID NOT CONSENT TO THE INCORPORATION BY REFERENCE OF THIS REPORT (AS INCLUDED IN THIS FORM 10-K/A, AMENDMENT NO. 1) INTO ANY OF THE COMPANY'S REGISTRATION STATEMENTS.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To InterDigital Communications Corporation:

We have audited the accompanying consolidated balance sheets of InterDigital Communications Corporation (a Pennsylvania corporation) and subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2001. These financial statements and the schedule referred to below are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of InterDigital Communications Corporation and subsidiaries as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

As explained in Note 2 to the consolidated financial statements, effective January 1, 2000, the Company changed its method of recognizing revenue.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule listed in the index of financial statements is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly states in all material aspects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

Arthur Andersen LLP

Philadelphia, Pennsylvania

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February 14, 2002

The consolidated financial statements for the year ended December 31, 1999 are not required to be presented in this Form 10-K/A, Amendment No. 1.

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REPORT OF MANAGEMENT

Management is responsible for the consolidated financial statements and the other financial information contained in this Annual Report. The financial statements have been prepared in accordance with accounting principles generally accepted in the United States considered appropriate in the circumstances to present fairly the company's financial position, results of operations and cash flows. The financial statements include some amounts that are based on management's best estimates and judgments.

To provide reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition and accounting records are reliable for preparing financial statements, management maintains a system of accounting and other internal controls. Even an effective system of internal controls, no matter how well designed, has inherent limitations, including the possibility of human error and the circumvention or overriding of controls, and therefore can provide only reasonable assurance with respect to financial statement preparation and safeguarding of assets. The system of accounting and other internal controls is continually assessed, modified and improved, where appropriate and cost effective, in response to both changes in business conditions and operations and recommendations made by the independent accountants.

The Audit Committee of the Board of Directors, which is composed of independent directors, meets periodically with management and the independent accountants to review the manner in which these groups are performing their responsibilities and to carry out the Audit Committee's oversight role with respect to corporate accounting, financial reporting practices and integrity of financial reports, as well as legal and regulatory compliance therewith. Both management and the independent accountants periodically meet privately with the Audit Committee and have access to its individual members.

The financial statements as of and for the year ended December 31, 2002, have been audited by the company's independent accountants, PricewaterhouseCoopers LLP, in accordance with auditing standards generally accepted in the United States. Their report is presented herein.

Howard E. Goldberg

President and Chief Executive Officer

Richard J. Fagan

Executive Vice President and Chief Financial Officer

King of Prussia, Pennsylvania

March 31, 2003

Table of Contents**FINANCIAL STATEMENTS****INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(in thousands, except per share data)**

| | DECEMBER 31, 2002 | DECEMBER 31, 2001 |
|---|------------------------------|------------------------------|
| | <u> </u> | <u> </u> |
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | \$ 22,337 | \$ 17,892 |
| Short-term investments | 65,229 | 72,471 |
| Accounts receivable | 53,486 | 14,479 |
| Prepaid and other current assets | 7,627 | 6,385 |
| | <u> </u> | <u> </u> |
| Total current assets | 148,679 | 111,227 |
| | <u> </u> | <u> </u> |
| PROPERTY AND EQUIPMENT, NET | 14,091 | 14,402 |
| PATENTS, NET | 15,016 | 11,334 |
| OTHER NON-CURRENT ASSETS | 13,392 | 11,418 |
| | <u> </u> | <u> </u> |
| | 42,499 | 37,154 |
| | <u> </u> | <u> </u> |
| TOTAL ASSETS | \$ 191,178 | \$ 148,381 |
| | <u> </u> | <u> </u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| CURRENT LIABILITIES: | | |
| Current portion of long-term debt | \$ 189 | \$ 184 |
| Accounts payable | 5,412 | 4,412 |
| Accrued compensation and related expenses | 5,886 | 5,985 |
| Deferred revenue | 17,087 | 10,490 |
| Foreign and domestic taxes payable | 5,434 | 907 |
| Other accrued expenses | 2,826 | 1,553 |
| | <u> </u> | <u> </u> |
| Total current liabilities | 36,834 | 23,531 |
| LONG-TERM DEBT | 1,970 | 2,158 |
| LONG-TERM DEFERRED REVENUE | 73,583 | 62,418 |
| | <u> </u> | <u> </u> |
| TOTAL LIABILITIES | 112,387 | 88,107 |
| | <u> </u> | <u> </u> |
| COMMITMENTS AND CONTINGENCIES (NOTES 7 AND 8) | | |
| SHAREHOLDERS' EQUITY: | | |
| Preferred Stock, \$.10 par value, 14,399 shares authorized-\$2.50 Convertible Preferred, 54 shares issued and outstanding, liquidation value of \$1,375 | 5 | 5 |
| Common Stock, \$.01 par value, 100,000 shares authorized, 56,267 shares and 54,391 shares issued and outstanding | 563 | 544 |
| Additional paid-in capital | 285,869 | 271,461 |

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| | | |
|---|-------------------|-------------------|
| Accumulated deficit | (198,945) | (201,320) |
| Accumulated other comprehensive income | 210 | 221 |
| Unearned compensation | (838) | (2,564) |
| | <u>86,864</u> | <u>68,347</u> |
| Treasury stock, 1,500 shares of common held at cost | 8,073 | 8,073 |
| | <u>78,791</u> | <u>60,274</u> |
| Total shareholders' equity | 78,791 | 60,274 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | \$ 191,178 | \$ 148,381 |

The accompanying notes are an integral part of these statements.

Table of Contents**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS**

(in thousands, except per share data)

| | FOR THE YEAR ENDED DECEMBER 31, | | |
|--|------------------------------------|--------------------|--------------------|
| | 2002 | 2001 | 2000 |
| REVENUES: | | | |
| Licensing and alliance | \$ 87,895 | \$ 52,562 | \$ 51,244 |
| Product revenues | | | 5,634 |
| | <u>87,895</u> | <u>52,562</u> | <u>56,878</u> |
| COST OF PRODUCT AND OPERATING EXPENSES: | | | |
| Cost of product | | | 5,200 |
| Sales and marketing | 4,330 | 4,698 | 3,919 |
| General and administrative | 14,477 | 14,898 | 13,408 |
| Patents administration and licensing | 13,162 | 8,959 | 5,095 |
| Development | 46,686 | 44,500 | 26,013 |
| | <u>78,655</u> | <u>73,055</u> | <u>53,635</u> |
| Income (loss) from operations | 9,240 | (20,493) | 3,243 |
| OTHER INCOME (EXPENSE): | | | |
| Interest income | 2,276 | 4,885 | 6,300 |
| Interest and financing expenses | (257) | (258) | (244) |
| | <u>11,259</u> | <u>(15,866)</u> | <u>9,299</u> |
| Income (loss) before income taxes | 11,259 | (15,866) | 9,299 |
| INCOME TAX PROVISION | (8,748) | (3,418) | (3,607) |
| | <u>2,511</u> | <u>(19,284)</u> | <u>5,692</u> |
| Net income (loss) before cumulative effect of change in accounting principle | 2,511 | (19,284) | 5,692 |
| CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET | | | (53,875) |
| | <u>2,511</u> | <u>(19,284)</u> | <u>(48,183)</u> |
| NET INCOME (LOSS) | 2,511 | (19,284) | (48,183) |
| PREFERRED STOCK DIVIDENDS | (136) | (137) | (128) |
| | <u>\$ 2,375</u> | <u>\$ (19,421)</u> | <u>\$ (48,311)</u> |
| Net income (loss) applicable to common shareholders | \$ 2,375 | \$ (19,421) | \$ (48,311) |
| NET INCOME (LOSS) PER COMMON SHARE BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE - BASIC | | | |
| | \$ 0.04 | \$ (0.36) | \$ 0.11 |
| NET INCOME (LOSS) PER COMMON SHARE - BASIC | | | |
| | \$ 0.04 | \$ (0.36) | \$ (0.91) |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING BASIC | | | |
| | 52,981 | 53,446 | 52,855 |
| NET INCOME (LOSS) PER COMMON SHARE BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE DILUTED | | | |
| | \$ 0.04 | \$ (0.36) | \$ 0.10 |

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| | | | |
|--|----------------|------------------|------------------|
| NET INCOME (LOSS) PER COMMON SHARE - DILUTED | <u>\$ 0.04</u> | <u>\$ (0.36)</u> | <u>\$ (0.91)</u> |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING DILUTED | <u>56,099</u> | <u>53,446</u> | <u>57,306</u> |

The accompanying notes are an integral part of these statements.

Table of Contents**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY**

(in thousands, except per share data)

| | <u>\$2.50 Convertible Preferred Stock</u> | <u>Common Stock</u> | <u>Additional Paid-In Capital</u> | <u>Accumulated Deficit</u> | <u>Accumulated Other Comprehensive Income(Loss)</u> | <u>Unearned Compensation</u> | <u>Treasury Stock</u> | <u>Total Stockholder Equity</u> | <u>Total Comprehensive Income</u> |
|--|---|-------------------------|---|--------------------------------|---|----------------------------------|---------------------------|---|---|
| BALANCE, DECEMBER 31, 1999 | 10 | 510 | 249,976 | (133,588) | | (1,769) | (5,632) | 109,507 | |
| Net loss | | | | (48,183) | | | | (48,183) | \$ (48,183) |
| Total Comprehensive Income | | | | | | | | | \$ (48,183) |
| Exercise of Common Stock options | | 7 | 3,706 | | | | | 3,713 | |
| Tax benefit related to Stock options | | | 604 | | | | | 604 | |
| Exercise of Common Stock warrants | | 16 | 8,012 | | | | | 8,028 | |
| Dividend of Common Stock and cash to \$2.50 Preferred shareholders | | | 53 | (128) | | | | (75) | |
| Conversion of Preferred Stock to Common Stock | (5) | 1 | 4 | | | | | | |
| Sale of Common Stock under Employee Stock Purchase Plan | | 1 | 508 | | | | | 509 | |
| Issuance of Restricted Common Stock | | 3 | 5,073 | | | (5,076) | | | |
| Amortization of unearned compensation | | | | | | 2,248 | | 2,248 | |
| Treasury Stock acquired | | | | | | | (2,441) | (2,441) | |
| BALANCE, DECEMBER 31, 2000 | 5 | 538 | 267,936 | (181,899) | | (4,597) | (8,073) | 73,910 | |
| Net loss | | | | (19,284) | | | | (19,284) | \$ (19,284) |
| Net unrealized gain on Short-term investments | | | | | 221 | | | 221 | 221 |
| Total Comprehensive Income | | | | | | | | | \$ (19,063) |
| Exercise of Common Stock options | | 2 | 1,249 | | | | | 1,251 | |
| Exercise of Common Stock warrants | | 1 | 335 | | | | | 336 | |
| Dividend of Common Stock and cash to \$2.50 Preferred shareholders | | | 44 | (137) | | | | (93) | |

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| | | | | | | | | | |
|--|------|--------|------------|--------------|--------|----------|------------|-----------|----------|
| Sale of Common Stock under Employee Stock Purchase Plan | 1 | 802 | | | | | | 803 | |
| Issuance of Restricted Common Stock | 2 | 1,095 | | | | (930) | | 167 | |
| Amortization of unearned compensation | | | | | | 2,963 | | 2,963 | |
| <hr/> | | | | | | | | | |
| BALANCE, DECEMBER 31, 2001 | 5 | 544 | 271,461 | (201,320) | 221 | (2,564) | (8,073) | 60,274 | |
| Net income | | | | 2,511 | | | | 2,511 | \$ 2,511 |
| Net unrealized loss on Short-term investments | | | | | (11) | | | (11) | (11) |
| <hr/> | | | | | | | | | |
| Total Comprehensive Income | | | | | | | | | \$ 2,500 |
| <hr/> | | | | | | | | | |
| Exercise of Common Stock options | 7 | 5,865 | | | | | | 5,872 | |
| Exercise of Common Stock warrants | 9 | 4,731 | | | | | | 4,740 | |
| Dividend of Common Stock and cash to \$2.50 Preferred shareholders | | | 44 | (136) | | | | (92) | |
| Sale of Common Stock under Employee Stock Purchase Plan | 2 | 1,253 | | | | | | 1,255 | |
| Issuance of Common Stock options to a non-employee | | | 37 | | | | | 37 | |
| Issuance of Restricted Common Stock | 1 | 1,044 | | | | (635) | | 410 | |
| Tax benefit from exercise of stock options | | | 1,434 | | | | | 1,434 | |
| Amortization of unearned compensation | | | | | | 2,361 | | 2,361 | |
| <hr/> | | | | | | | | | |
| BALANCE, DECEMBER 31, 2002 | \$ 5 | \$ 563 | \$ 285,869 | \$ (198,945) | \$ 210 | \$ (838) | \$ (8,073) | \$ 78,791 | |
| <hr/> | | | | | | | | | |

The accompanying notes are an integral part of these statements

Table of Contents**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

| | FOR THE YEAR ENDED DECEMBER | | |
|---|------------------------------------|------------------|------------------|
| | 31, | | |
| | 2002 | 2001 | 2000 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income (loss) before preferred stock dividends | \$ 2,511 | \$ (19,284) | \$ (48,183) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | | |
| Depreciation and amortization | 9,268 | 6,375 | 4,491 |
| Deferred revenue recognized | (54,738) | (9,877) | (12,500) |
| Increase in deferred revenue | 72,500 | 30,611 | |
| Cumulative effect of change in accounting principle, net of tax | | | 53,875 |
| Amortization of unearned compensation | 2,361 | 2,963 | 2,248 |
| Decrease (increase) in deferred charges | (805) | (4,240) | 1,685 |
| Other | 53 | (49) | |
| Decrease (increase) in assets: | | | |
| Receivables | (39,007) | 2,449 | (6,044) |
| Inventories | | | 3,092 |
| Other current assets | (1,030) | 743 | 6,964 |
| Increase (decrease) in liabilities: | | | |
| Accounts payable | 550 | (70) | 2,028 |
| Accrued compensation | (99) | 2,243 | (584) |
| Other accrued expenses | 5,800 | (2,297) | (1,737) |
| Net cash (used) provided by operating activities | <u>(2,636)</u> | <u>9,567</u> | <u>5,335</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Purchases of short-term investments | (124,466) | (107,857) | (126,814) |
| Sales of short-term investments | 131,697 | 112,251 | 118,720 |
| Purchases of property and equipment | (6,519) | (7,616) | (6,806) |
| Patent costs | (5,475) | (2,974) | (1,973) |
| Net cash used by investing activities | <u>(4,763)</u> | <u>(6,196)</u> | <u>(16,873)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Net proceeds from exercise of stock options and warrants and employee stock purchase plan | 12,314 | 2,606 | 12,250 |
| Payments on long-term debt, including capital lease obligations | (378) | (335) | (445) |
| Cash Dividends on preferred stock | (92) | (93) | (75) |
| Purchase of treasury stock | | | (2,441) |
| Net cash provided by financing activities | <u>11,844</u> | <u>2,178</u> | <u>9,289</u> |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | 4,445 | 5,549 | (2,249) |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 17,892 | 12,343 | 14,592 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | <u>\$ 22,337</u> | <u>\$ 17,892</u> | <u>\$ 12,343</u> |

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| | <u> </u> | <u> </u> | <u> </u> |
|--|-------------------|-------------------|-------------------|
| SUPPLEMENTAL CASH FLOW INFORMATION: | | | |
| Accrued purchase of patent rights | \$ 450 | \$ | \$ |
| | <u> </u> | <u> </u> | <u> </u> |
| Leased asset additions and related obligation | \$ 195 | \$ 117 | \$ |
| | <u> </u> | <u> </u> | <u> </u> |
| Interest paid | \$ 229 | \$ 201 | \$ 235 |
| | <u> </u> | <u> </u> | <u> </u> |
| Income taxes paid, including foreign withholding taxes | \$ 5,592 | \$ 5,485 | \$ 1,202 |
| | <u> </u> | <u> </u> | <u> </u> |
| Non-cash dividends on preferred stock | \$ 44 | \$ 44 | \$ 53 |
| | <u> </u> | <u> </u> | <u> </u> |

The accompanying notes are an integral part of these statements.

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INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2002

1. BACKGROUND

InterDigital Communications Corporation (collectively with its subsidiaries referred to as InterDigital, the Company, we, us and our) develops advanced wireless technologies and products that facilitate voice and data communications. In conjunction with our technology development, we have assembled an extensive body of technical know-how, related product embodiments and a broad patent portfolio of Time Division Multiple Access (TDMA) and Code Division Multiple Access (CDMA) patents, which we license worldwide.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of InterDigital and its subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash, Cash Equivalents and Short-Term Investments

We consider all highly liquid investments purchased with initial maturities of three months or less to be cash equivalents. Investments are held at amortized cost, which approximates market value. At December 31, 2002 and 2001, all of our short-term investments were classified as available-for-sale with unrealized gains and losses included as a separate component of equity, net of any related tax effect. Gross unrealized gains on short-term investments were \$0.2 million at December 31, 2002 and 2001.

Cash and cash equivalents consist of the following (in thousands):

| | <u>December 31,</u> | |
|--|---------------------|------------------|
| | <u>2002</u> | <u>2001</u> |
| Money market funds and demand accounts | \$ 22,160 | \$ 16,231 |
| Repurchase agreements | 177 | 1,661 |
| | <u>\$ 22,337</u> | <u>\$ 17,892</u> |

The repurchase agreements are fully collateralized by United States Government securities and are stated at cost which approximates fair market value.

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Short-term investments consist of the following (in thousands):

| | December 31, | |
|----------------------------------|------------------|------------------|
| | 2002 | 2001 |
| US Government agency instruments | \$ 37,131 | \$ 38,857 |
| Corporate bonds | 28,098 | 33,614 |
| | <u>\$ 65,229</u> | <u>\$ 72,471</u> |

Other Assets

Other assets consist primarily of prepaid foreign withholding taxes and prepaid commissions. We often pay foreign withholding taxes and commissions at the beginning of our patent license relationships in connection with our collection of related up-front payments. We capitalize these foreign withholding tax and prepaid commissions payments and recognize them in the same period as the related revenue.

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization of property and equipment are provided using the straight-line method. The estimated useful lives for computer equipment, machinery and equipment, and furniture and fixtures are generally three to five years. Leasehold improvements are being amortized over their lease term, which is generally five-to-ten years. Buildings are being depreciated over twenty-five years. Expenditures for major improvements and betterments are capitalized and minor repairs and maintenance are charged to expense as incurred.

Internal-Use Software Costs

Under the provisions of the American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal-Use, we capitalize costs associated with software for internal-use. Capitalization begins when the preliminary project stage is complete and ceases when the project is substantially complete and ready for its intended purpose. During the years ended December 31, 2001 and 2000, we capitalized \$0.1 million and \$1.8 million, respectively, of costs associated with a new ERP system. These costs are included within property and equipment and are being amortized over three years. Amortization expense of these costs was \$0.6 million in 2002 and 2001, and \$0.1 million in 2000. Accumulated amortization related to these costs was \$1.4 million and \$0.7 million at December 31, 2002 and 2001, respectively.

Patents

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The costs to obtain patents and patent license rights have been capitalized. Capitalized costs associated with patents obtained directly by the Company are amortized on a straight-line basis over their estimated useful lives of 10 years. Capitalized costs associated with the acquisition of patent licensing rights are amortized on a straight-line basis over the life of the patent rights. Amortization expense was \$2.2 million, \$1.8 million and \$1.5 million in 2002, 2001 and 2000, respectively. Accumulated amortization was \$13.8 million and \$11.6 million at December 31, 2002 and 2001, respectively.

The estimated aggregate amortization expense for patents and patent rights as of December 31, 2002 is as follows (in thousands):

| | |
|------|----------|
| 2003 | \$ 2,831 |
| 2004 | 2,778 |
| 2005 | 2,502 |
| 2006 | 1,892 |
| 2007 | \$ 1,310 |

Development

All engineering development expenditures are charged to expense in the period incurred. In accordance with SFAS No. 86, Accounting for the Costs of Computer Software to Be Sold, Leased or Otherwise Marketed, all costs incurred related to the

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development of wireless software to be sold, embedded in our products or otherwise marketed are expensed as incurred because costs qualifying for capitalization under such pronouncement have not been significant.

Revenue Recognition

We derive revenue principally from patent licensing, know-how licensing and compensated development agreements. The timing of revenue recognition and the amount of revenue actually recognized from each source depends upon a variety of factors, including the specific terms of each agreement and the nature of the deliverables and obligations. Such agreements are often complex and multi-faceted. These agreements can include, without limitation, elements related to the settlement of past patent infringement liabilities, up-front, non-refundable license fees for the use of patents and/or know-how, patent and/or know-how licensing royalty rates on covered products sold by licensees, cross licensing terms between InterDigital and other parties, and the compensation structure and ownership of intellectual property rights associated with contractual technology development arrangements. Due to the combined nature of some agreements and the inherent difficulty in establishing reliable, verifiable and objectively determinable evidence of the fair value of the separate elements of these agreements, the total revenue resulting from such agreements may sometimes be recognized over the combined performance period of such agreements. In other circumstances, such as those agreements involving payments for past and expected future patent royalty obligations, the determining factors necessary to allocate revenue between past, current and future years may be difficult to establish. In such instances, after considering the facts and circumstances, we may apply judgment in deferring the appropriate recording of revenue between periods. Generally, we will not recognize revenue related to payments that are due greater than twelve months from the balance sheet date. In all cases, revenue is only recognized after all the following criteria are met: written agreements have been executed; delivery of technology or intellectual property rights has occurred or services have been rendered; fees are fixed and determinable; and collectability of fees is reasonably assured. When we determine that elements of an agreement represent a settlement of a litigation, we report the proceeds of the settlement as other income.

Patent licensing arrangements usually consist primarily of upfront, nonrefundable fees (including royalty prepayments that are exhausted through future sales of licensee products, payments related to past sales of licensee products or payments related to a paid-up license in which the licensee makes a single payment for a lifetime patent license) and recurring royalties. Prior to 2000, we recorded revenue from upfront, nonrefundable patent license fees as revenue upon the signing of the applicable license agreement because we had delivered the license and had no remaining obligations. Effective January 1, 2000, we modified our licensing revenue recognition policy in response to Staff Accounting Bulletin (SAB) No. 101, *Revenue Recognition in Financial Statements*. SAB No. 101 expresses the view of the SEC Staff in applying generally accepted accounting principles to various revenue transactions, including licensing agreements involving upfront, nonrefundable payments. These payments can represent either royalty prepayments that are exhausted through future sales of licensee products or payments related to paid-up licenses in which the licensee makes a single payment for a lifetime patent license. Following SAB No. 101 guidance, we reflected in our 2000 results a net after-tax cumulative effect of change in accounting principle of \$53.9 million to defer the net portion of upfront payments that represent amounts which either had not yet been exhausted through sales of covered products by licensees as of January 1, 2000 or were expected to be recognized in the future on a straight-line basis over the expected period of use by the licensee. In cases where we receive objective, verifiable evidence that a licensee has discontinued sales of covered products, we recognize the remaining deferred revenue balance related to the unexhausted prepayment in the period we receive such evidence. In the years 2002, 2001 and 2000, we recognized approximately \$21.4 million, \$9.9 million and \$12.5 million of revenue and \$17.8 million, \$8.1 million and \$10.4 million of earnings, respectively, related to the deferred amounts on a post-SAB No. 101 basis.

Royalty revenue is recognized as earned in accordance with the specified terms of each license agreement, most of which provide for quarterly or semi-annual reporting of royalties due InterDigital. We generally recognize royalty revenue as earned based on royalty reports provided by our licensees. In some cases, royalty revenue is accrued prior to formal reporting by licensees when reasonable estimates of such amounts can be made. These estimates are based on both the historical royalty data of the licensees involved and currently available third party forecasts of royalty related product sales in the applicable market. When our licensees formally report royalties for which we accrued revenues based on estimates, we adjust revenue for the period in which the reports are received.

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Revenue from agreements that may include patents, technology and know-how, and development components is recognized based on the fair value of the elements delivered, which generally include both services and intellectual property license rights. Due to the combined nature of some agreements, the total revenue from such agreements may be recognized over the combined period of the agreements.

We recognize revenues associated with compensated development arrangements on either a time and materials basis or under the percentage-of-completion method of accounting, depending on the terms of the agreement. The percentage-of-completion method relies on estimates of total contract revenue and costs. Revenues and profit are subject to revisions as the contract progresses to completion. Under the percentage-of-completion method, revenue is recognized based on the percentage that incurred contract costs to date bear to total estimated contract costs, after giving effect to the most recent estimates of total contract costs. The effect of changes to total estimated contract costs is recognized in the period such changes are determined. Estimated losses, if any, are recorded when the loss first becomes apparent.

Table of Contents**Stock-Based Compensation**

We account for stock-based employee compensation using the intrinsic value method and provide pro forma disclosures related to our stock-based compensation under the provisions of Statement No. 148, Accounting for Stock-Based Compensation Transition and Disclosure an amendment of FASB Statement No. 123 .

At December 31, 2002, the Company has three stock-based employee compensation plans which are described more fully in Note 10. The Company accounts for these plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees , and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans have an exercise price equal to the market value of the Company underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, Accounting for Stock-Based Compensation , to stock-based employee compensation:

(In Thousands, except per share data)

| Year Ended December 31, | 2002 | 2001 | 2000 |
|--|-------------|-------------|-------------|
| Net income (loss) applicable to Common Shareholders as reported | \$ 2,375 | \$ (19,421) | \$ (48,311) |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards ^(a) | (18,993) | (27,687) | (30,587) |
| Net loss applicable to Common Shareholders pro forma | \$ (16,618) | \$ (47,108) | \$ (78,898) |
| Net income (loss) per share as reported basic | 0.04 | (0.36) | (0.91) |
| Net income (loss) per share as reported diluted | 0.04 | (0.36) | (0.91) |
| Net (loss) per share pro forma basic | (0.31) | (0.88) | (1.49) |
| Net (loss) per share pro forma diluted | (0.31) | (0.88) | (1.49) |

^(a) No tax benefit has been recognized for the stock-based employee compensation expense since the Company is in an NOL carryforward position and the realization of such benefit cannot be assured.

Equity instruments issued to non-employees for services are accounted for at fair value and are marked to market until service is complete.

Concentration of Credit Risk and Fair Value of Financial Instruments

Financial instruments that potentially subject us to concentration of credit risk consist primarily of cash equivalents, short-term investments, and accounts receivable. We place our cash equivalents and short-term investments only in highly rated financial instruments and in United States Government instruments. Our accounts receivable are derived principally from patent license agreements and engineering services. At December 31, 2002 and 2001, two customers represented 95% and 93%, respectively, of our accounts receivable balance. We perform ongoing credit evaluations of our customers who generally include large multi-national wireless telecommunications equipment manufacturers. We believe that the book value of our financial instruments, which include cash and cash equivalents, short-term investments, accounts receivable, accounts payable, accrued expenses and debt, approximate their fair values.

Impairment of Long-Lived Assets

Pursuant to Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, we evaluate long-lived assets and intangible assets for impairment when factors indicate that the carrying amount of an asset may not be recoverable. When factors indicate that such assets should be evaluated for possible impairment, we review the realizability of our long-lived assets by analyzing the projected undiscounted cash flows in measuring whether the asset is recoverable. No such adjustments were recorded in 2002, 2001 or 2000.

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Income Taxes

Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the Consolidated Statement of Operations in the period that includes the enactment date. A valuation allowance is recorded to reduce the carrying amounts of deferred tax assets if it is more likely than not that such assets will not be realized.

Table of Contents**Net Income (Loss) Per Common Share**

Basic earnings per share (EPS) are calculated by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if options, warrants or other securities with features that could result in the issuance of Common Stock were exercised or converted to Common Stock. The following tables reconcile the numerator and the denominator of the basic and diluted net income (loss) per share computation (in thousands, except for per share data):

(In thousands, except per share data)

| Year Ended December 31, 2002 | Income (Numerator) | Shares (Denominator) | Per-Share Amount |
|---|-------------------------------|---------------------------------|-----------------------------|
| Income per Share Basic: | | | |
| Income available to common shareholders | \$ 2,375 | 52,981 | \$ 0.04 |
| Dilutive effect of options, warrants and convertible preferred stock | | 3,118 | |
| Income per Share Diluted: | | | |
| Income available to common shareholders + dilutive effects of options, warrants and convertible preferred stock | \$ 2,375 | 56,099 | \$ 0.04 |

(In thousands, except per share data)

| Year Ended December 31, 2001 | Income (Numerator) | Shares (Denominator) | Per-Share Amount |
|---|-------------------------------|---------------------------------|-----------------------------|
| Loss per Share Basic: | | | |
| Loss available to common shareholders | \$ (19,421) | 53,446 | \$ (0.36) |
| Dilutive effect of options, warrants and convertible preferred stock | | | |
| Loss per Share Diluted: | | | |
| Loss available to common shareholders + dilutive effects of options, warrants and convertible preferred stock | \$ (19,421) | 53,446 | \$ (0.36) |

(In thousands, except per share data)

| Year Ended December 31, 2000 | Income (Numerator) | Shares (Denominator) | Per-Share Amount |
|--|-------------------------------|---------------------------------|-----------------------------|
| Income per Share Basic: | | | |
| Income before cumulative effect of change in accounting principle | \$ 5,692 | | \$ |
| Preferred stock dividend | (128) | | |
| Income available to common shareholders before cumulative effect of change in accounting principle | 5,564 | 52,855 | 0.11 |
| Dilutive effect of options, warrants and convertible preferred stock | | 4,451 | (0.01) |
| Income per Share Diluted: | | | |

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| | | | |
|--|-------------|--------|-----------|
| Income available to common shareholders before cumulative effect of change in accounting principle + dilutive effects of options, warrants and convertible preferred stock | 5,564 | 57,306 | 0.10 |
| Cumulative effect of change in accounting principle | (53,875) | | |
| Loss per Share Basic: | | | |
| Loss available to common shareholders | (48,311) | 52,855 | (0.91) |
| Dilutive effect of options, warrants and convertible preferred stock | | | |
| Loss per Share Diluted: | | | |
| Loss available to common shareholders + dilutive effects of options, warrants and convertible preferred stock | \$ (48,311) | 52,855 | \$ (0.91) |

For the year ended December 31, 2002, options and warrants to purchase approximately 3.6 million shares of Common Stock were excluded from the computation of diluted EPS because the exercise prices of the options were greater than the weighted average market price of our common stock during the period and, therefore, their effect would have been anti-dilutive. For the years ended December 31, 2001 and 2000, the effects of all options, warrants and convertible preferred stock were excluded from the computation of diluted earnings per share (EPS) as a result of a net loss reported in each period. For the year ended December 31, 2000, options to purchase 1.0 million shares were excluded from the calculation of diluted EPS before the

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cumulative effect of change in accounting principle, because the exercise prices of the options were greater than the weighted-average market price of our Common Stock during the period and, therefore, their effect would have been anti-dilutive.

Recent Accounting Pronouncements

In June 2002, the Financial Accounting Standards Board (FASB) issued Statement No. 146, Accounting for Costs Associated with Exit or Disposal Activities (SFAS No. 146). SFAS No. 146 addresses financial accounting and reporting for costs associated with exit or disposal activities. SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of commitment to an exit or disposal plan. This statement is effective for exit or disposal activities initiated after December 31, 2002. We will adopt SFAS No. 146 as of January 1, 2003 for any exit or disposal activities after that date.

In December 2002, the FASB issued Statement No. 148, Accounting for Stock-Based Compensation Transition and Disclosure an amendment of FASB Statement No. 123 (SFAS No. 148). SFAS No. 148 amends Statement No. 123 Accounting for Stock-Based Compensation (SFAS No. 123) to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this Statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. This statement is effective for financial statements for fiscal years ending after December 15, 2002. We account for stock-based compensation using the intrinsic value method and provide disclosures as required under SFAS No. 148.

In November 2002, the FASB issued FASB Interpretation No. 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others (FIN 45). FIN 45 elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and measurement provisions of FIN 45 apply on a prospective basis to guarantees issued or modified after December 31, 2002. We do not believe the impact of adopting FIN 45 will have a material impact on our financial statements.

Reclassification

Certain prior period amounts have been reclassified to conform to the current year presentation.

3. GEOGRAPHIC/CUSTOMER CONCENTRATION

We have one operating segment. Substantially all of our revenue is derived from a limited number of customers based outside of the United States (primarily Japan and Europe). These revenues are paid in U.S. dollars and are not subject to any substantial foreign exchange transaction risk. During 2002, 2001, and 2000, revenue from our Japan based licensees comprised 94%, 50%, and 51% of total revenues, respectively. Revenue from a customer based in Finland, represented 5%, 42% and 31% of total revenues in 2002, 2001 and 2000, respectively.

During 2002, 2001, and 2000, the following customers accounted for 10% or more of revenues:

| | <u>2002</u> | <u>2001</u> | <u>2000</u> |
|-------|-------------|-------------|-------------|
| NEC | 35% | | |
| Sharp | 30% | 30% | 32% |
| Denso | 11% | 2% | 3% |
| Nokia | 5 % | 42% | 31% |

4. SIGNIFICANT AGREEMENTS

In addition to the following significant agreements, in March 2003, we entered into worldwide royalty-bearing license agreements with Telefonaktiebolaget LM Ericsson and Ericsson Inc. (Ericsson) and Sony Ericsson Mobile Communications AB (Sony Ericsson) for sales of terminal units and infrastructure products compliant with 2G GSM/TDMA and 2.5G GSM/GPRS/TDMA standards. These agreements are described in greater detail in Note 14 Subsequent Event below.

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NEC

In 2002, we entered into a worldwide royalty-bearing license agreement (3G Agreement) with NEC Corporation (NEC) for sales of wireless products compliant with all 3G and narrowband CDMA standards. We also concurrently reached an amicable settlement of a Second Generation (2G) patent licensing dispute (2G Dispute) with NEC in connection with a 1995 2G patent license agreement (2G Agreement).

In connection with the 3G Agreement, we received a non-refundable advance royalty of \$19.5 million in April 2002 and recognized revenue of approximately \$18.3 million related to that advance royalty in 2002. We will continue to recognize additional revenue as licensed products are sold. Once the initial advance is exhausted, NEC will be obligated to pay us additional royalties as it sells licensed products. We will continue to recognize additional revenue if and as products covered under the 3G Agreement are sold.

In connection with the settlement of the 2G Dispute, we received \$13.25 million in April 2002, as the first of four equal nonrefundable installments totaling \$53 million. The second installment was received in January 2003. The remaining two installments are payable in the second and fourth quarters of 2003. In connection with the \$53 million settlement, we are recognizing revenue on a straight-line basis from the January 2002 agreement date until February 2006, which is the expected period of use by NEC. In 2002, we recognized approximately \$12.3 million of revenue related to this settlement. At December 31, 2002, our balance sheet included \$39.8 million in accounts receivable due under the 1995 Agreement. Our deferred revenue balance contained approximately \$40.7 million related to these receivables and the \$13.25 million in cash previously collected under this agreement.

Tantivy

In 2002, we acquired global patent rights associated with mobile wireless technology from Tantivy Communications, Inc. (Tantivy). These rights include an exclusive license (subject to certain rights retained by Tantivy), with the right to sublicense, under a number of Tantivy's patents applicable to, among other products, CDMA2000 products manufactured, used or sold in the United States and other countries where Tantivy's patents have been filed. These rights also include a non-exclusive license under Tantivy's smart antenna patents, generally, to manufacture and sell TDD products. We are obligated to pay Tantivy a minimum, of \$1.5 million, plus a share of patent license royalties collected on CDMA2000 product sales from newly entered into agreements that, in effect, include a sub-license under Tantivy's patents. In addition, we expect to incur costs in connection with the prosecution of certain of the patent rights. The \$1.5 million minimum will secure our rights under the agreement for an initial period (Initial Period) of three years and is to be paid in three installments. Payments of \$1.05 million were made in 2002 and an additional installment of \$0.45 million was paid in the first quarter 2003. Our maximum payment obligation to Tantivy associated with the sublicenses entered into during the Initial Period, inclusive of the \$1.5 million, is \$19.0 million. The \$1.5 million has been capitalized as a patent cost and is being amortized over the initial three-year period. Commencing in 2005, certain adjustments to the maximum amount payable, alone or in combination with additional installments, are required to be made in order to maintain certain of the patent rights under the agreement beyond the Initial Period. Our maximum payment obligation to Tantivy for all license rights received under the agreement, inclusive of the \$1.5 million, is \$24.0 million. Should we choose not to maintain our rights, previously entered into sublicenses with third parties shall not be affected.

By separate agreement in 2002, we obtained the right to market the licensing of Tantivy's smart antenna technology and patents for certain 2G and 3G products in Japan, China, Korea and Taiwan. We expect to market Tantivy's smart antenna patents and technology in connection with our patent licensing activities. With respect to certain agreements arranged by us on Tantivy's behalf that are entered concurrently with new InterDigital licenses to the same party, Tantivy could be entitled either to a pre-determined lump sum amount and/or an amount equivalent to a percentage of patent license royalties collected by us on 2G CDMA product sales under such transactions. With respect to certain other agreements arranged by us on Tantivy's behalf, we would be entitled to a commission for arranging the transaction.

Matsushita

In 2001, we entered into a worldwide royalty-bearing license agreement with Matsushita Communications Industrial Co., Ltd. (Matsushita) of Japan under our patent portfolio for Matsushita to manufacture, sell, and distribute 3G products. We received a non-refundable advance royalty payment of \$19.5 million related to this agreement that will be recognized as revenue when Matsushita sells covered product. No revenue was recognized under this agreement in 2002 or 2001.

Sharp

In 2001, we entered into a worldwide royalty-bearing license agreement with Sharp Corporation (Sharp) under our patent portfolio for Sharp to manufacture, sell, and distribute GSM, narrowband CDMA and 3G products. We received a nonrefundable advance royalty payment of \$11.1 million related to these agreements that is being recognized as Sharp sells covered product. We recognized revenue of approximately \$2.7 million against that advance in 2002. No revenue was recognized under this agreement in 2001.

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We are currently in negotiations with Sharp to renew a patent license covering sales of PHS and PDC products that expired in the first quarter 2003.

Nokia

In February 1999, we entered into a multi-year arrangement with Nokia Corporation (Nokia) for development of new technology for 3G wireless telecommunications products. Under the multi-year arrangement, we are providing specialized engineering services and technology and know-how development and we will retain ownership rights of all of the technology we develop thereunder. Additionally, in February 1999, we entered into a patent license agreement with Nokia related to our TDMA and CDMA patents. In the third quarter of 2001, Nokia and the Company amended the agreement by refining the pace and scope of the development arrangement and Nokia committed to increase funding to a maximum of approximately \$58 million, up from the original estimate of \$40 million. We will be responsible for costs not covered by the maximum funding amount. This modification was treated as a new contract for accounting purposes and as a result, we changed the method of reporting revenue related to the remainder of the program to the percentage-of-completion accounting basis. Prior to the change, revenue had been reported on a time and materials basis and we had billed Nokia approximately \$46 million under the contract, leaving approximately \$12 million of revenue to be recognized on the percentage of completion basis. Of the \$12 million, approximately \$4.6 million and \$6.2 million were recognized in 2002 and 2001, respectively. During 2002, we accrued a loss of \$1.2 million on the modified contract based on our estimates of cost to complete the contract. The final \$1.0 million payment associated with this contract will be withheld until final delivery of the remaining technology required under the agreement has been made. We currently expect final delivery to occur in the second half of 2003 and will defer the recognition of the final \$1.0 million of specialized engineering services revenue associated with the agreement until that time. For the years ended December 31, 2002, 2001 and 2000, we recognized specialized engineering service revenue related to this development arrangement of \$4.6 million, \$21.8 million, and \$17.2 million, respectively.

Table of Contents**5. PROPERTY AND EQUIPMENT**

| | December 31, | |
|---------------------------------|-----------------------|------------------|
| | 2002 | 2001 |
| | (In thousands) | |
| Land, building and improvements | \$ 6,303 | \$ 5,446 |
| Machinery and equipment | 10,080 | 8,630 |
| Computer equipment and software | 22,730 | 18,743 |
| Furniture and fixtures | 3,702 | 3,498 |
| Leasehold improvements | 1,849 | 1,633 |
| | <u>44,664</u> | <u>37,950</u> |
| Less: Accumulated depreciation | (30,573) | (23,548) |
| | <u>\$ 14,091</u> | <u>\$ 14,402</u> |

Depreciation expense was \$7.0 million, \$5.0 million and \$3.0 million in 2002, 2001 and 2000, respectively.

6. LONG-TERM DEBT OBLIGATIONS

| | December 31, | |
|----------------------------------|-----------------------|-----------------|
| | 2002 | 2001 |
| | (In thousands) | |
| Mortgage debt | \$ 2,088 | \$ 2,225 |
| Capitalized leases | 71 | 117 |
| | <u>2,159</u> | <u>2,342</u> |
| Total long-term debt obligations | 2,159 | 2,342 |
| Less: Current portion | (189) | (184) |
| | <u>\$ 1,970</u> | <u>\$ 2,158</u> |

During 1996, we purchased our King of Prussia, Pennsylvania facility for \$3.7 million, including cash of \$0.9 million and a 16-year mortgage of \$2.8 million with interest payable at a rate of 8.28% per annum.

Capitalized lease obligations are payable in monthly installments at an average rate of 4.6%, through 2004. The net book value of equipment under capitalized lease obligations was \$0.1 million at December 31, 2002 and 2001.

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Maturities of principal of the long-term debt obligations as of December 31, 2002 are as follows (in thousands):

| | |
|------------|----------|
| 2003 | \$ 189 |
| 2004 | 192 |
| 2005 | 176 |
| 2006 | 191 |
| 2007 | 207 |
| Thereafter | \$ 1,204 |

Table of Contents**7. COMMITMENTS AND CONTINGENCIES***Leases*

We have entered into various operating lease agreements. Total rent expense primarily for office space, was \$2.4 million, \$2.4 million and \$1.9 million in 2002, 2001 and 2000, respectively. Minimum future rental payments for operating leases as of December 31, 2002 are as follows (in thousands):

| | |
|------------|----------|
| 2003 | \$ 2,345 |
| 2004 | 1,560 |
| 2005 | 1,514 |
| 2006 | 1,470 |
| 2007 | 238 |
| Thereafter | \$ -0- |

Employment Agreements

We have entered into agreements with certain employees that provide for the payment of severance pay (in the aggregate, approximately \$3.3 million at December 31, 2002), among other things, in certain events of termination of employment. All but one of these agreements generally provide for the payment of severance up to a maximum of one year of salary and up to a maximum of one year of continued medical and dental benefits. The other agreement generally provides for the payment of severance up to a maximum of eighteen months of salary and up to a maximum of eighteen months of continued medical and dental benefits. In all of these agreements, in the event of a termination or resignation within one year following a change of control, which is defined to include the acquisition (including by merger or consolidation, or by the issuance by the Company of our securities) by one or more persons in one transaction or a series of related transactions of more than fifty percent (50%) of the voting power represented by the outstanding stock of the Company, the employee would generally receive two years of salary (approximately \$6.3 million at December 31, 2002) and the immediate vesting of all stock options.

8. LITIGATION*Ericsson*

In March 2003, we entered into an agreement with Ericsson to settle a longstanding patent infringement lawsuit between us. In connection with the settlement, we entered into worldwide royalty-bearing license agreements with Telefonaktiebolaget LM Ericsson and Ericsson and Sony Ericsson for sales of terminal units and infrastructure products compliant with Second Generation (2G) GSM/TDMA and 2.5G GSM/GPRS/TDMA standards. These agreements are described in greater detail in Note 14 "Subsequent Event" below.

As part of the settlement of the litigation, the parties requested, and the Court signed, a Stipulation and Order of Dismissal dismissing the case with prejudice.

Samsung

In February 2002, we filed a Complaint against Samsung Electronics Co. Ltd. (Samsung) with the International Chamber of Commerce (ICC), International Court of Arbitration. The dispute involved the applicability of the Most Favored Licensee (MFL) clause contained in our patent license agreement with Samsung and Samsung's alleged underreporting of, failure to report, and failure to pay royalties on its more recent covered sales. MFL clauses typically permit a licensee to elect to apply the terms of a subsequently executed license agreement that are more favorable than those of the licensee's agreement. In particular, the dispute related to the manner in which our patent license agreement with Nokia should apply to Samsung under Samsung's MFL rights included in its 1996 patent license agreement with us. The dispute dealt with specific contractual terms in the Samsung patent license agreement and did not involve any issue of validity or infringement of our patents.

In December 2002, the ICC rendered a decision, under which, Samsung's MFL rights were applied retroactively until January 29, 1999, the date of the Nokia patent license agreement. The ICC decision also determined Samsung's royalty obligation on sales of licensed TDMA products for the period commencing January 29, 1999 through December 31, 2001 to be approximately \$4.4 million, reducing Samsung's prior royalty credit of \$18.7 million (\$11.5 million of which had previously been recognized as revenue by the Company) to \$6.7 million. As a result of the ICC decision, we recognized approximately \$0.5 million of revenue in the fourth quarter 2002 related to Samsung's royalty obligations through December 31, 2001.

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Also, pursuant to Samsung's election regarding the Nokia patent license agreement under its MFL rights, Samsung's royalty obligations (against which the \$6.7 million credit would apply) for sales of 2G and 2.5G TDMA wireless communications products commencing January 1, 2002 will be determined in accordance with the terms of the Nokia patent license agreement, including its MFL provision. By reference to the Nokia patent license agreement, Samsung's royalty obligations for sales of 2G and 2.5G TDMA wireless communications products commencing January 1, 2002 will be defined by the relevant licensing terms between us and Ericsson and us and Sony Ericsson.

Other

We are a party to legal actions arising in the ordinary course of our business. Based upon information presently available to us, we believe that the ultimate outcome of these other actions will not have a material effect on our results of operations or financial condition.

9. RELATED PARTY TRANSACTIONS

In 2000, we engaged L.E.K. Consulting, a shareholder value consulting firm and paid approximately \$0.5 million for their services. One of our outside directors is Chairman of the Advisory Board to L.E.K. Consulting. Our board member did not receive any compensation or commissions related to the engagement.

10. PREFERRED STOCK

The holders of the \$2.50 Convertible Preferred Stock are entitled to receive, when and as declared by our Board of Directors, cumulative annual dividends of \$2.50 per share payable in cash or Common Stock at the Company's election (subject to a cash election right of the holder), if legally available. Such dividends are payable semi-annually on June 1 and December 1. In the event we fail to pay two consecutive semi-annual dividends within the required time period, certain penalties may be imposed. The \$2.50 Convertible Preferred Stock is convertible into Common Stock at any time prior to redemption at a conversion rate of 2.08 shares of Common Stock for each share of preferred. In 2002, 2001 and 2000, InterDigital declared and paid dividends on the \$2.50 Preferred Convertible Stock of \$136,000, \$137,000 and \$128,000, respectively. These dividends were paid with both cash of \$92,000, \$93,000 and \$75,000, in 2002, 2001 and 2000, respectively, and with 3,113, 3,260, and 5,141 shares of Common Stock in 2002, 2001 and 2000, respectively.

Upon any liquidations, dissolution or winding up of the Company, the holders of the \$2.50 Convertible Preferred Stock will be entitled to receive, from the Company's assets available for distribution to shareholders, \$25 per share plus all dividends accrued, before any distribution is made to Common shareholders. After such payments, the holders of the \$2.50 Convertible Preferred Stock would not be entitled to any other payments. The redemption price for each share of the \$2.50 Convertible Preferred Stock is \$25 per share. The \$2.50 Convertible Preferred Stock is redeemable at our option.

The holders of the \$2.50 Convertible Preferred Stock do not have any voting rights except on those amendments to the Company's Articles of Incorporation which would adversely affect their rights, create any class or series of stock ranking senior to or not at parity with the \$2.50 Convertible Preferred Stock, as to either dividend or liquidation rights, or increase the authorized number of shares of any senior stock. In addition, if two or more consecutive semi-annual dividends on the \$2.50 Convertible Preferred Stock are not paid by the Company, the holders of the \$2.50 Convertible Preferred Stock, separately voting as a class, will be entitled to elect one additional director of the Company.

11. COMMON STOCK COMPENSATION PLANS

Stock Compensation Plans

We have stock-based compensation plans under which, depending on the plan, directors, employees, consultants and advisors can receive stock options, stock appreciation rights, restricted stock awards and other stock unit awards.

Common Stock Option Plans

We have granted options under two incentive stock option plans, three non-qualified stock option plans and two plans which provide for grants of both incentive and non-qualified stock options (Pre-existing Plans) to non-employee directors, officers and employees of the Company and certain others, depending on the plan. No further grants are allowed under the Pre-existing Plans. In 2000, the shareholders approved the 2000 Stock Award and Incentive Plan (2000 Plan) that allows for the granting of incentive and non-qualified options, as well as certain other securities. The 2000 Plan authorizes the offer and sale of up to approximately 7.4 million shares of common stock. The Board of Directors or the Compensation and Stock Option Committee of the Board determine the number of options to be granted. Under the terms of the 2000 Plan, the option price cannot be less than 100% of fair market value of the Common Stock at the date of grant.

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In 2002, the Board of Directors approved the 2002 Stock Award and Incentive Plan (2002 Plan) that allows for the granting of incentive and non-qualified options, as well as certain other securities to Company employees who are not subject to the reporting requirements of Section 16 of the Securities Act of 1934 or an affiliate for purposes of Rule 144 of the Securities Act of 1933. The 2002 Plan authorizes the offer and sale of up to 1.5 million shares of common stock. The Board of Directors or the Compensation and Stock Option Committee of the Board determine the number of options to be granted.

Under the terms of the 2002 Plan, the option price cannot be less than 100% of fair market value of the Common Stock at the date of grant. In addition, unless otherwise modified, no awards may be granted under the 2002 Plan after the close of business on the date of the Company's 2003 Annual Meeting of Shareholders.

Under all of these plans, options are generally exercisable for a period of 10 years from the date of grant and may vest on the grant date, another specified date or over a period of time. However, under plans which provide for both incentive and non-qualified stock options, grants most commonly vest in six semi-annual installments.

SFAS No. 123 Disclosure

We have adopted the disclosure-only provisions of SFAS No. 123, Accounting for Stock-Based Compensation. Accordingly, no compensation cost has been recognized in the Statements of Operations for our stock option plans. Had compensation cost been calculated based on the fair value at the grant date for awards in 2002, 2001 and 2000, consistent with the provisions of SFAS No. 123, our net income (loss) and net income (loss) per share would change to the following pro forma amounts (in thousands, except per share amounts):

| | <u>2002</u> | <u>2001</u> | <u>2000</u> |
|---|-------------|-------------|-------------|
| Net income (loss) applicable to Common Shareholders as reported | \$ 2,375 | \$ (19,421) | \$ (48,311) |
| Net (loss) applicable to Common Shareholders pro forma | (16,618) | (47,108) | (78,898) |
| Net income (loss) per share as reported basic | 0.04 | (0.36) | (0.91) |
| Net income (loss) per share as reported diluted | 0.04 | (0.36) | (0.91) |
| Net (loss) per share pro forma basic | (0.31) | (0.88) | (1.49) |
| Net (loss) per share pro forma diluted | (0.31) | (0.88) | (1.49) |

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants in 2002, 2001 and 2000; no dividend yield; expected volatility of 72% for 2002, 97% for 2001 and 130% for 2000, risk-free interest rates of 3.83%, 4.59% and 6.33% for 2002, 2001 and 2000, respectively, and an expected option life of 4.32 years for 2002, 4.21 years for 2001 and 3.93 years for 2000. The weighted-average fair value at the date of grant for options granted during 2002, 2001 and 2000 is estimated as \$8.51, \$8.16 and \$21.23 per share, respectively.

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Information with respect to stock options under the above plans is summarized as follows (in thousands, except per share amounts):

| | <u>Available</u> | <u>Outstanding Options</u> | | <u>Price</u> | Weighted Average Exercise |
|------------------------------|------------------|----------------------------|---------------|--------------|--|
| BALANCE AT DECEMBER 31, 1999 | 5,722 | 4,483 | \$ 0.01-11.65 | \$ 6.26 | |
| Granted | (2,514) | 2,514 | \$ 5.19-39.00 | \$ 23.90 | |
| Canceled | 392 | (392) | \$ 4.50-39.00 | \$ 23.01 | |
| Exercised | | (686) | \$ 0.10-11.63 | \$ 5.41 | |
| 2000 Plan Authorization | 2,200 | | | | |
| BALANCE AT DECEMBER 31, 2000 | 5,800 | 5,919 | \$ 5.19-39.00 | \$ 12.90 | |
| Granted | (5,109) | 5,109 | \$ 5.38-15.10 | \$ 10.47 | |
| Canceled | 280 | (280) | \$ 5.38-39.00 | \$ 17.30 | |
| Exercised | | (184) | \$ 6.80-15.38 | \$ 11.61 | |
| BALANCE AT DECEMBER 31, 2001 | 971 | 10,564 | \$ 0.01-39.00 | \$ 11.67 | |
| Granted | (1,056) | 1,056 | \$ 6.32-19.10 | \$ 12.46 | |
| Canceled | 463 | (463) | \$ 0.01-39.00 | \$ 13.80 | |
| Exercised | | (695) | \$ 0.01-17.13 | \$ 8.45 | |
| 2002 Plan Authorization | 1,500 | | | | |
| BALANCE AT DECEMBER 31, 2002 | 1,878 | 10,462 | \$ 0.01-39.00 | \$ 11.86 | |

The following table summarizes information regarding the stock options outstanding at December 31, 2002 (in thousands, except for per share amounts):

| <u>Range of Exercise Prices</u> | <u>Number Outstanding</u> | <u>Weighted Average Remaining Contractual Life</u> | <u>Weighted Average Exercise Price</u> | <u>Number Exercisable</u> | <u>Weighted Average Exercise Price</u> |
|-------------------------------------|-------------------------------|--|--|-------------------------------|--|
| \$ 0.01 - 5.38 | 791 | 6.64 | \$ 4.83 | 732 | \$ 4.80 |
| \$ 5.41 - 5.44 | 1,168 | 4.73 | 5.44 | 1,168 | 5.44 |
| \$ 5.50 - 7.81 | 1,241 | 5.83 | 6.71 | 1,163 | 6.68 |
| \$ 7.81 - 9.19 | 446 | 14.64 | 8.57 | 304 | 8.55 |
| \$ 9.23 - 9.60 | 1,792 | 8.97 | 9.59 | 828 | 9.59 |
| \$ 9.63 - 10.75 | 1,132 | 8.51 | 10.36 | 801 | 10.33 |
| \$10.81 - 12.40 | 1,428 | 12.39 | 11.85 | 788 | 11.81 |
| \$12.43 - 17.13 | 1,320 | 8.48 | 15.03 | 826 | 15.22 |
| \$17.26 - 34.13 | 533 | 7.62 | 23.12 | 481 | 23.61 |
| \$39.00 - 39.00 | 611 | 7.04 | 39.00 | 611 | 39.00 |
| \$ 0.01 - 39.00 | 10,462 | 8.36 | \$ 11.86 | 7,702 | \$ 12.14 |

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Common Stock Warrants

As of December 31, 2002, we had warrants outstanding to purchase 222,000 shares of Common Stock at exercise prices ranging from \$2.50 to \$7.63 per share, with a weighted average exercise price of \$6.22 per share. As of December 31, 2002, all of these warrants were currently exercisable. 30,000 warrants will expire in 2003 and the remaining warrants will expire through 2006. The exercise price and number of shares of Common Stock to be obtained upon exercise of these warrants are subject to adjustment under certain conditions.

Restricted Stock

In 1999, we adopted the 1999 Restricted Stock Plan, amended April 13, 2000 under which we can issue up to 3,500,000 shares of restricted common stock and restricted stock units to directors, employees, consultants and advisors. The restrictions on issued shares lapse over periods generally ranging from 1 to 5 years from the date of the grant. As of December 31, 2002 and 2001, we had 915,064 and 812,658 shares of restricted stock and restricted stock units, respectively, issued under the plan. The balance of unearned compensation at December 31, 2002 was \$0.8 million, which will be amortized over vesting periods that are generally from one to three years.

12. SHAREHOLDER RIGHTS PLAN

In December 1996, our Board of Directors declared a distribution under its Shareholder Rights Plan (the Rights Plan) of one right for each outstanding common share of the Company to shareholders of record as the close of business on January 3, 1997. In addition, any new common shares issued after January 4, 1997 will receive one right for each common share. The Rights Plan was amended in a number of respects in March 2000. As amended, each right entitles shareholders to buy one-thousandth of a share of Series B Junior Participating Preferred Stock at a purchase price of \$250 per share, subject to adjustment. Ordinarily, the rights will not be exercisable until 10 business days after any of the following events (each, a *Triggering Event*): (i) a non-exempt person or group owns or acquires more than 10% of the Company's outstanding Common Stock, or (ii) a nonexempt person or group publicly commences an offer for 10% or more of the Company's outstanding Common Stock, or (iii) a nonexempt person or group publicly announces an intention to acquire control over the Company and proposes in a proxy or consent solicitation to elect such a number of directors, who if elected, would represent a majority of the directors when compared with the Independent Directors on the Board. If the Company's Board of Directors has consented to the occurrence of a particular Triggering Event, then the occurrence of such Triggering Event will not give rise to the exercisability of the rights. In general, upon the occurrence of a Triggering Event without Board approval, each holder of a right will have the right to receive, upon exercise, Units of Preferred Stock (or, in certain circumstances, Company Common Stock, cash, property, or other securities of the Company) having a current market value equal to two times the exercise price of the Right, or if the Company is acquired in a merger or other business combination, each holder of a right will have the right to receive stock of the acquiring person equal to twice the exercise price of that Right.

Table of Contents**13. TAXES**

Income tax expense/(benefit) consists of the following components for 2002, 2001, and 2000:

| | Year Ended December 31, | | |
|--|-------------------------|-----------------|-----------------|
| | 2002 | 2001 | 2000 |
| Current | | | |
| Federal | \$ 1,434 | \$ 200 | \$ 200 |
| State | | | |
| Foreign | 8,348 | 3,218 | 3,407 |
| Alternative Minimum Tax | 400 | | |
| | <u>10,182</u> | <u>3,418</u> | <u>3,607</u> |
| Deferred | | | |
| Federal | (165) | (6,621) | (16,148) |
| State | (4,095) | (3,363) | (2,944) |
| Foreign | | | |
| Increase/(Decrease) in Valuation Allowance | 2,826 | 9,984 | 19,092 |
| | <u>(1,434)</u> | | |
| Total | <u>\$ 8,748</u> | <u>\$ 3,418</u> | <u>\$ 3,607</u> |

The deferred tax assets and liabilities are comprised of the following at December 31, 2001, and 2002:

| | 2002 | | 2001 | |
|---|-----------|-----------------|-----------|-------------|
| | Current | Non-Current | Current | Non-Current |
| Depreciation | \$ | \$ 1,141 | \$ | \$ 913 |
| Patent Amortization | | 1,762 | | 1,540 |
| Other Employee Benefits | 564 | | 608 | |
| Other Accrued Liabilities | 542 | | 231 | |
| Other | | 34 | | 299 |
| Restricted Stock Compensation | 417 | | 1,937 | |
| Deferred Revenue | 28,966 | | 22,686 | |
| Alternative Minimum Tax Credit Carryforward | | 1,434 | | 1,434 |
| R&E Credits | | 2,657 | | 2,657 |
| Net Operating Losses | | 31,689 | | 32,641 |
| Less: Valuation Allowance | (30,489) | (37,283) | (25,462) | (39,484) |
| Net Deferred Tax Asset | <u>\$</u> | <u>\$ 1,434</u> | <u>\$</u> | <u>\$</u> |

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The following is a reconciliation of income taxes at the federal statutory rate with income taxes recorded by the Company for the years ended December 31, 2002, 2001 and 2000:

| | <u>2002</u> | <u>2001</u> | <u>2000</u> |
|--|-----------------|-----------------|-----------------|
| Tax at U.S. Statutory Rate | \$ 3,828 | \$ (5,394) | \$ 3,162 |
| Foreign withholding tax, with no US foreign tax credit | 5,502 | 2,124 | 2,249 |
| Change in Federal Valuation Allowance | (1,269) | 6,621 | 16,148 |
| Cumulative Effect of Accounting Change | | | (18,318) |
| Other | 687 | 67 | 366 |
| | <u> </u> | <u> </u> | <u> </u> |
| Total Tax Provision | \$ 8,748 | \$ 3,418 | \$ 3,607 |
| | <u> </u> | <u> </u> | <u> </u> |

At December 31, 2002, the Company had an unused R&E credit of approximately \$2.7 million which if unused will expire in the year 2020.

At December 31, 2002, the Company has a federal net operating loss carryforward of approximately \$137.6 million, which will expire, if unused, in the years 2005 through 2021.

At December 31, 2002 approximately \$67.1 million of benefits associated with the exercise of non-qualified stock options are included in the net operating loss carryforward. However, these benefits have been deferred because the Company is in a net operating loss position. Such benefits will be credited to additional paid-in capital in the year in which the benefits are realized.

Under the Tax Reform Act of 1986, the utilization of a corporation's net operating loss carryforwards is limited following a change in ownership of greater than 50% within a three-year period. If it is determined that prior equity transactions limit the Company's net operating loss carryforwards, the annual limitation will be determined by multiplying the market value on the date of ownership by the federal long-term tax-exempt rate. Any amount exceeding the annual limitation may be carried forward to future years for the balance of the net operating loss carryforward period.

14. SUBSEQUENT EVENT

In March 2003, we entered into worldwide royalty-bearing license agreements with Telefonaktiebolaget LM Ericsson and Ericsson and Sony Ericsson for sales of terminal units and infrastructure products compliant with Second Generation (2G) GSM/TDMA and 2.5G GSM/GPRS/TDMA standards. These agreements resolved a patent infringement lawsuit with Ericsson that was scheduled for trial in May 2003. We also were granted an option for a Reference Design License and Support Agreement for Ericsson's GSM/GPRS/UMTS Platform.

We are due to receive aggregate payments currently estimated to be approximately \$34 million from Ericsson and Sony Ericsson related to sales of terminal and infrastructure products through December 31, 2002. These payments are due over four quarters, commencing in the second quarter 2003, including approximately \$16 million in 2003. We will recognize the aggregate expected payments as other income in the first quarter 2003.

For the period January 1, 2003 through December 31, 2006, Sony Ericsson will be obligated to pay us a royalty on each licensed product sold. In return for advance royalty payments covering projected sales of covered products for discrete twenty-four month periods, Sony Ericsson will receive certain prepayment discounts and credits. The initial advance royalty payments for the first twenty-four month period are mandatory and Sony Ericsson is obligated to make these payments in the second and third quarters of 2003. Once the initial prepayments are exhausted, Sony Ericsson would have the option to make additional advance royalty payments (net of related prepayment discounts and any applicable credits) or, pay royalties on an ongoing basis at undiscounted base royalty rates. The advance royalty payments will be recorded as deferred revenue and recognized as revenue in the periods in which Sony Ericsson exhausts such prepayments through the sale of covered product.

Ericsson also is obligated to pay us an annual license fee of \$6 million per year for sales of covered infrastructure products for each of the years 2003 through 2006. The annual license fee will be recognized as revenue on a straight-line basis each year.

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We believe the license agreements with Ericsson and Sony Ericsson establish the financial terms necessary to define the royalty obligations of Nokia and Samsung on sales of 2G GSM/TDMA and 2.5G GSM/GPRS/TDMA products under their existing agreements with us. Under the MFL provision applicable to their respective patent licenses, we believe both companies are obligated to pay royalties to us on sales of covered products from January 1, 2002 by reference to the terms of the Ericsson and Sony Ericsson licenses. The MFL terms include provisions for a period of review, negotiation, and dispute resolution with regard to the determination of the royalty obligations of both Nokia and Samsung. We will not record revenue associated with the Nokia and Samsung license agreements until all elements required for revenue recognition are met.

15. SELECTED QUARTERLY RESULTS (Unaudited)

The table below presents quarterly data for the years ended December 31, 2002 and 2001:

| | 2002 | | | | |
|---|------------|------------|------------|------------|-------------|
| | First | Second | Third | Fourth | Full Year |
| Selected Quarterly Results (in thousands, except per share amounts, unaudited) | | | | | |
| Revenues | \$ 20,949 | \$ 25,149 | \$ 14,706 | \$ 27,091 | \$ 87,895 |
| Net income (loss) applicable to common shareholders | \$ 16 | \$ 2,444 | \$ (5,833) | \$ 5,748 | \$ 2,375 |
| Net income (loss) per share - diluted | \$ 0.00 | \$ 0.04 | \$ (0.11) | \$ 0.10 | \$ 0.04 |
| | | | | | |
| | 2001 | | | | |
| Revenues | \$ 14,687 | \$ 14,953 | \$ 14,543 | \$ 8,379 | \$ 52,562 |
| Net loss applicable to common shareholders | \$ (2,155) | \$ (2,459) | \$ (5,012) | \$ (9,795) | \$ (19,421) |
| Net loss per share - diluted | \$ (0.04) | \$ (0.05) | \$ (0.09) | \$ (0.18) | \$ (0.36) |

Table of Contents**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES****SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS****(in thousands)**

| Description | Balance, Beginning of Period | Charged to Costs and Expenses | Deductions | Balance, End of Period |
|--------------------------------------|---|--|-------------------|-----------------------------------|
| 2002 | | | | |
| Allowance for uncollectible accounts | -0- | | | -0- |
| 2001 | | | | |
| Allowance for uncollectible accounts | \$ 73 | | \$ 73 | -0- |
| 2000 | | | | |
| Allowance for uncollectible accounts | \$ 975 | | \$ 902 | \$ 73 |

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PART IV

Item 15. EXHIBITS, FINANCIAL STATEMENT OF SCHEDULES, AND REPORTS ON FORM 8-K

(a) The following documents are filed as part of this Form 10-K/A, Amendment No. 1:

- (1) Financial Statements.
- (2) Financial Statement Schedules.
- (3) The Index to Financial Statements and Schedules and the Financial Statements begin on page 1.
- *3.1 Restated Articles of Incorporation (Exhibit 3.1 to InterDigital's Quarterly Report on Form 10-Q for the quarter ended September 30, 1996).
- *3.2 By-laws, as amended March 21, 2002 (Exhibit 3.2 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 2001 (the 2001 Form 10-K)).
- *4.1 Rights Agreement between InterDigital and American Stock Transfer & Trust Co., (AST) (Exhibit 4 to InterDigital's Current Report on Form 8-K filed on January 2, 1997).
- *4.2 Amendment No. 1 to the Rights Agreement between InterDigital and AST (Exhibit 4.2 to InterDigital's Quarterly Report on Form 10-Q for the quarter ended June 30, 1997 (the June 1997 Form 10-Q)).
- *4.3 Amendment No. 2 to the Rights Agreement between InterDigital and AST (Exhibit 4.3 to the June 1997 Form 10-Q).
- *4.4 Amendment No. 3 to the Rights Agreement between InterDigital and AST (Exhibit 4.4 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 1999 (the 1999 Form 10-K)).
- *10.1 Intellectual Property License Agreement between InterDigital and Hughes Network Systems, Inc. (Exhibit 10.39 to InterDigital's Registration Statement No. 33-28253 filed on April 18, 1989).
- *10.2 1992 License Agreement dated February 29, 1992 between InterDigital and Hughes Network Systems, Inc. (Exhibit 10.3 to InterDigital's Current Report on Form 8-K dated February 29, 1992 (the February 1992 Form 8-K)).
- *10.3 E-TDMA License Agreement dated February 29, 1992 between InterDigital and Hughes Network Systems, Inc. (Exhibit 10.4 to the February 1992 Form 8-K).
- *10.4 Non-Qualified Stock Option Plan, as amended (Exhibit 10.4 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 1991).
- *10.5 Amendment to Non-Qualified Stock Option Plan (Exhibit 10.31 to InterDigital's Quarterly Report on Form 10-Q for the quarter ended June 30, 2000 (the June 2000 Form 10-Q)).
- *10.6 Amendment to Non-Qualified Stock Option Plan, effective October 24, 2001 (Exhibit 10.6 to the 2001 Form 10-K).
- *10.7 1992 Non-Qualified Stock Option Plan (Exhibit 10.1 to InterDigital's Current Report on Form 8-K dated October 21, 1992).
- *10.8 Amendment to 1992 Non-Qualified Stock Option Plan (Exhibit 10.32 to the June 2000 Form 10-Q).
- *10.9 1992 Employee Stock Option Plan (Exhibit 10.71 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 1992).
- *10.10 Amendment to 1992 Employee Stock Option Plan (Exhibit 10.29 to the June 2000 Form 10-Q).
- *10.11 Amendment to 1992 Employee Stock Option Plan, effective October 24, 2001 (Exhibit 10.11 to the 2001 Form 10-K).
- *10.12 1995 Stock Option Plan for Employees and Outside Directors, as amended (Exhibit 10.7 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 1997 (the 1997 Form 10-K)).
- *10.13 Amendment to the 1995 Stock Option Plan for Employees and Outside Directors (Exhibit 10.25 to the 1999 Form 10-K).

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- *10.14 Amendment to 1995 Stock Option Plan for Employees and Outside Directors (Exhibit 10.33 to the June 2000 Form 10-Q).
- *10.15 Amendment to 1995 Stock Option Plan for Employees and Outside Directors, effective October 24, 2001 (Exhibit 10.15 to the 2001 Form 10-K).
- *10.16 1997 Stock Option Plan for Non-Employee Directors (Exhibit 10.34 to InterDigital's Quarterly Report on Form 10-Q for the quarter ended September 30, 1997).
- *10.17 1997 Stock Option Plan for Non-Employee Directors, as amended March 30, 2000 (Exhibit 10.42 to the June 2000 Form 10-Q).
- *10.18 Amendment to 1997 Stock Option Plan for Non-Employee Directors (Exhibit 10.34 to the June 2000 Form 10-Q).
- *10.19 Amendment to 1997 Stock Option Plan for Non-Employee Directors, effective October 24, 2001 (Exhibit 10.19 to the 2001 Form 10-K).
- *10.20 2000 Stock Award and Incentive Plan (Exhibit 10.28 to the June 2000 Form 10-Q).
- *10.21 1999 Restricted Stock Plan, as amended April 13, 2000 (Exhibit 10.43 to the June 2000 Form 10-Q).
- *10.22 Amended and Restated Employment Agreement dated as of November 20, 2000 by and between InterDigital Communications Corporation and Howard E. Goldberg (Exhibit 10.12 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 2000 (the 2000 Form 10-K)).
- *10.23 Employment Agreement dated November 18, 1996 by and between InterDigital Communications Corporation and Charles R. Tilden (Exhibit 10.26 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 1996).
- *10.24 Amendment dated as of April 6, 2000 by and between InterDigital and Charles R. Tilden (Exhibit 10.39 to the June 2000 Form 10-Q).
- *10.25 Employment Agreement dated May 7, 1997 by and between InterDigital and Mark A. Lemmo (Exhibit 10.32 to InterDigital's Quarterly Report on Form 10-Q for the quarter ended March 31, 1997).
- *10.26 Amendment dated as of April 6, 2000 by and between InterDigital and Mark A. Lemmo (Exhibit 10.37 to the June 2000 Form 10-Q).
- *10.27 Employment Agreement dated September 3, 1998 by and between InterDigital and William J. Merritt (Exhibit 10.23 to InterDigital's Annual Report on Form 10-K for the year ended December 31, 1998 (the 1998 Form 10-K)).
- *10.28 Amendment dated as of April 6, 2000 by and between InterDigital and William J. Merritt (Exhibit 10.38 to the June 2000 Form 10-Q).
- *10.29 Employment Agreement dated November 16, 1998 by and between InterDigital and Richard J. Fagan (Exhibit 10.24 to the 1998 Form 10-K).
- *10.30 Amendment dated as of April 6, 2000 by and between InterDigital and Richard J. Fagan (Exhibit 10.36 to the June 2000 Form 10-Q).
- *10.31 Employment Agreement dated November 19, 1996 by and between InterDigital and Brian G. Kiernan (Exhibit 10.37 to the 2000 Form 10-K).
- *10.32 Amendment dated as of April 6, 2000 by and between InterDigital and Brian G. Kiernan (Exhibit 10.38 to the 2000 Form 10-K).
- *10.33 Employment Agreement dated July 24, 2000 by and between InterDigital and William C. Miller (Exhibit 10.39 to the 2000 Form 10-K).
- *10.34 Agreement dated January 2, 2001, by and between InterDigital and Alain C. Briancon (Exhibit 10.41 to the 2000 Form 10-K).
- *10.35 Employment Agreement dated as of November 12, 2001 by and between InterDigital and Lawrence F. Shay (Exhibit 10.38 to the 2001 Form 10-K).

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| | |
|---------|---|
| *10.36 | Employment Agreement dated as of December 3, 2001 by and between InterDigital and Guy M. Hicks (Exhibit 10.39 to the 2001 Form 10-K). |
| *10.37 | Agreement of Lease dated November 25, 1996 by and between InterDigital and We re Associates Company (Exhibit 10.42 to the 2000 Form 10-K). |
| *10.38 | Modification of Lease Agreement dated December 28, 2000 by and between InterDigital and We re Associates Company (Exhibit 10.43 to the 2000 Form 10-K). |
| *10.39 | 2002 Stock Award and Incentive Plan (Exhibit 10.50 to InterDigital s Quarterly Report on Form 10-Q for the quarter ended March 31, 2002). |
| *10.40 | Patent License Agreement dated May 8, 1995 between ITC and NEC (Exhibit 10.51 to InterDigital s Current Report on Form 8-K dated February 21, 2003 (the 2003 Form 8-K)). |
| *10.41 | Amendment to the Patent License Agreement of May 8, 1995 between ITC and NEC (Exhibit 10.52 to the 2003 Form 8-K). |
| *10.42 | Narrowband CDMA and Third Generation Patent License Agreement dated January 15, 2002 between ITC and NEC (Exhibit 10.53 to the 2003 Form 8-K). |
| *10.43 | Settlement Agreement dated January 15, 2002 between ITC and NEC (Exhibit 10.54 to the 2003 Form 8-K). |
| *10.44 | The TDD Development Agreement between and among InterDigital, ITC and NEC (Exhibit 10.55 to the 2003 Form 8-K). |
| *10.45 | Amendment No. 1 to the TDD Development Agreement dated September 30, 2001 between and among InterDigital, ITC and NEC (Exhibit 10.56 to the 2003 Form 8-K). |
| *10.46 | PHS and PDC Subscriber Unit Patent License Agreement dated March 19, 1998 between ITC and NEC (Exhibit 10.57 to the 2003 Form 8-K). |
| *21 | Subsidiaries of InterDigital (Exhibit 21 to InterDigital s Annual Report on Form 10-K for the year ended December 31, 2002). |
| <R*23.1 | Consent of PricewaterhouseCoopers LLP. (Exhibit 23.1 to InterDigital s Annual Report on Form 10-K for the year ended December 31, 2002). |
| 31.1 | Certification of the President and Chief Executive Officer. |
| 31.2 | Certification of the Chief Financial Officer. |
| 32.1 | Certification of the President and Chief Executive Officer. |
| 32.2 | Certification of the Chief Financial Officer.</R |

* Incorporated by reference to the previous filing indicated.

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(b) The following is a list of Current Reports filed on Form 8-K during the last quarter of 2002:

We filed a Current Report on Form 8-K dated December 16, 2002 under Item 5 Other Events relating to the Company's announcement that on December 12, 2002, the Federal District Court Judge presiding over the patent infringement lawsuit involving the Company, ITC and Ericsson ordered the case be transferred to Judge Barbara M. G. Lynn in the same Federal District Court. The order further specified that the case remain on its current pretrial and trial schedule subject to any modifications that Judge Lynn may direct with the commencement date for the trial to remain at February 10, 2003.

We filed a Current Report on Form 8-K dated December 26, 2002 under Item 5 Other Events relating to the Company's announcement that on December 23, 2002, the International Chamber of Commerce (ICC) rendered a decision in the arbitration proceeding involving the Company, ITC and Samsung regarding the application of most favored licensee (MFL) rights under the parties' patent license agreement, and Samsung's royalty obligations for sales of covered products.

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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.

INTERDIGITAL COMMUNICATIONS CORPORATION

Date: January 28, 2004

/s/ Howard E. Goldberg

Howard E. Goldberg
President and Chief Executive Officer

Date: January 28, 2004

/s/ R. J. Fagan

Richard J. Fagan
Executive Vice President and Chief Financial Officer