INTERLINK ELECTRONICS INC
Form S-1
August 13, 2007
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As filed with the Securities and Exchange Commission on August 13, 2007

Registration No. 333-

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM S-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

Interlink Electronics, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	**5045**	**77-0056625**
(State or Other Jurisdiction of	**(Primary Standard Industrial**	**(I.R.S. Employer**
Incorporation or Organization)	**Classification Code Number)**	**Identification No.)**

Interlink Electronics, Inc.

546 Flynn Road

Camarillo, California 93012

(805) 484-8855

(Address, including zip code, and telephone number, including area code, of Registrant s executive offices)

E. Michael Thoben, III

Chief Executive Officer

Interlink Electronics, Inc.

546 Flynn Road

Camarillo, California 93012

(805) 484-8855

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Please send copies of all communications to:

John Halle, Esq.

Stoel Rives, LLP

900 S.W. Fifth Avenue

Suite 2600

Portland, Oregon 97204

(503) 224-3380

(503) 220-2480 Facsimile

Approximate date of commencement of proposed sale to the public: from time to time after the effective date of this registration statement.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended (the "Securities Act"), check the following box. x

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered[1]	Proposed Maximum Offering Price Per Share[4]	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common Stock, par value $.00001	4,129,630[2]	$1.12	$4,625,184	$142
Common Stock, par value $.00001	1,984,127[3]	1.12	2,222,220	68
Total	6,113,757	$1.12	$6,847,404	$210

(1) In accordance with Rule 416(a), the Registrant is also registering hereunder an indeterminate number of shares that may be issued and resold resulting from stock splits, stock dividends and similar transactions and anti-dilution provisions.
(2) Represents shares of Common Stock underlying the 8% Convertible Notes (the Notes) held by selling securityholders, issuable upon conversion of the principal amount of, and accrued and unpaid cash interest on, the Notes. The number of shares issuable upon conversion of the principal amount of the Notes was calculated by dividing the principal amount of $5,000,000 by the conversion price of $1.26, for a total of 3,968,254 shares. The number of shares issuable upon conversion of accrued and unpaid cash interest on the Notes was calculated by multiplying the principal amount of $5,000,000 by the fixed rate of 8% for one 6-month interest period, and dividing the result by the conversion price of $1.26, for a total of 161,376 shares.
(3) Represents shares of Common Stock underlying warrants held by selling securityholders.
(4) Estimated pursuant to Rule 457(c) of the Securities Act of 1933 solely for the purpose of computing the amount of the registration fee based on the high and low prices reported on the Over The Counter market trading system on August 8, 2007.

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(a) OF THE SECURITIES ACT OF 1933 OR UNTIL THIS REGISTRATION STATEMENT SHALL BECOME EFFECTIVE ON SUCH DATE AS THE SECURITIES AND EXCHANGE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(a), MAY DETERMINE.

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SUBJECT TO COMPLETION, dated August 13, 2007

PROSPECTUS

6,113,757 Shares of Common Stock

This prospectus relates to the sale or other disposition by the selling securityholders named herein or their transferees of up to 6,113,757 shares of the Common Stock of Interlink Electronics, Inc., a Delaware corporation, issuable upon conversion of Interlink s 8% Convertible Notes and upon exercise of certain warrants issued, in each case to the selling securityholders in a private placement. These dispositions may be at fixed prices, at prevailing market prices at the time of sale, at prices related to the prevailing market price, at varying prices determined at the time of sale, or at negotiated prices. See "Plan of Distribution" below.

As of April 10, 2006, our Common Stock trades through the Over The Counter ("*OTC*") market trading system under the symbol "LINK.PK." Prior to April 10, 2006, our Common Stock traded on the NASDAQ National Market under the symbol "LINK." The closing price of our Common Stock on August 9, 2007 was $0.94.

Interlink will not receive any proceeds from the sale or other disposition of the shares covered hereby. Interlink will, however, receive proceeds from any cash exercise of warrants by the selling securityholders. Interlink has agreed to pay all of the costs of this offering, excluding commissions and discounts regarding the sale or other disposition of the shares covered hereby.

Brokers or dealers effecting transactions in the shares should confirm the registration of these securities under the securities laws of the states in which transactions occur or the existence of an exemption from registration.

Investing in these the Common Stock of Interlink Electronics, Inc. involves significant risks. See " Risk Factors" beginning on page 6.

The information in this prospectus is not complete and may be changed. These securities may not be sold or otherwise transferred until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of the disclosures in this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is , 2007

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PROSPECTUS SUMMARY

This summary provides a brief overview of key aspects of the offering. However, it is a summary and may not contain all of the information that is important to you. For a more complete understanding of this offering, we encourage you to read this entire prospectus, including our financial statements and the notes to those statements. As used in this prospectus, the terms we, our, us or Interlink refer to Interlink Electronics, Inc. and its subsidiaries, taken as a whole, as well as any predecessor entities, unless the context otherwise indicates.

The Company

We are a global leader in the design, development and manufacture of human interface products and technologies. Our products include electronic signature and E-notarization products, advanced remotes controls and consumer electronics interface solutions. Our signature and pen input pads record and bind signatures to contracts or other legally significant documents and also record various identity-defining factors such as signature biometrics and fingerprints. Our Specialty Components technologies, such as *MicroNav* , support full mouse functionality and file navigation using miniaturized sensors and supporting systems that consume relatively little power, thereby making them particularly attractive to manufacturers of handheld devices. Our remote control input devices enable a user to control and communicate with electronic products, such as computers, digital projection systems and digital televisions, by providing an intuitive device on which the user can remotely input a variety of commands. Our products benefit from a diverse technology portfolio based on trade secrets, patented inventions and proprietary software. These technologies include our force sensing resistor (FSR) technology, wireless communication technologies and unique or patented product design features. Alone and in collaboration with our industry partners, we have developed numerous technologies that support various product applications.

We currently sell our products in four principal markets that we refer to as our E-transactions, Specialty Components, OEM Remotes and Branded Products markets. We serve a global customer base from our corporate headquarters in Camarillo, California, where we also manufacture all of the components incorporating our FSR technology. We have sales offices in Tokyo and Taiwan and production logistics centers and subsidiaries in Hong Kong and Schenzen, China. Customers who buy our products through our OEM channel include Acer, Bose, BenQ, Dell, Hewlett-Packard, Hitachi, Lenovo (IBM), Mitsubishi, Panasonic, Sanyo, Sharp, Sony and Toshiba.

Competitive Strengths

We believe that our industry leadership is based on the following competitive strengths:

- *Proprietary and Patented Intuitive Interface Technologies*: Our strong technology portfolio, including our proprietary and patented technologies and trade secrets, has enabled us to position ourselves as the solution of choice for demanding applications in our markets.

- *Technology Leadership for Intuitive Interface Designs*: Our suite of proprietary interface technologies and design patents enables users to address complex requirements in an efficient and cost-effective manner. We have developed a wide range of technologies including software, wireless protocols and advanced packaging that enable us to deliver additional value to our customers.

- *Strong Strategic Relationships with Industry Leading OEMs*: We have established a strong customer base with leading OEMs and work with a wide range of partners including customers, suppliers, software and hardware developers and integrators that enable us to offer a wide range of applications.

- *Proven Supplier to First-Tier Global Companies*: We have several years of experience as a supplier of electronic products and solutions to many of the world s most knowledgeable and demanding OEMs.

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Our Strategy

Our overall objective is to be the leading provider of advanced intuitive interface devices to business and consumer markets by implementing the following key strategies:

Leverage our momentum in the E-transactions market. We have evolved from a simple signature pad provider to a complete solutions provider offering a signature software platform, a broad set of signature capture options and professional services to address the unique needs of the E-transactions market. Our technologies, solutions, and approach have enabled us to secure the largest implementations in the industries in which we focus including banking, insurance, auto finance, brokerage, and healthcare.

Use our core sensor technology and innovative new applications to support integrated micro-input devices such as our MicroNav family of products. The advent and increasing complexity of a wide range of miniaturized consumer electronics products have greatly increased demand for small, low-power-consuming input devices that can provide full mouse functionality, including cursor control. Our patented *MicroNav* technologies are well suited for these applications and we have invested considerable effort in the development of this technology and its markets. We are developing a broad range of applications for our *MicroNav* products targeted at the tasks that today s complex handheld devices accomplish.

Identify fundamental changes in consumer or business practices resulting from technological change and develop technologies and products that facilitate this change. We remain alert to technological changes that alter the basic processes that businesses and consumers rely upon. We are working aggressively to identify new technologies as they develop and to design products and solutions appropriate to these technologies. We believe that by applying a disciplined approach to the identification and selection of our target markets and technologies, we can achieve a leading position in those markets based on our strong intellectual property position and market relationships.

Maintain and develop new strategic relationships with software developers and other integrator that address our target markets in order to deliver turnkey solutions. We work with software and hardware developers, integrators and other companies to provide turnkey solutions that address our customers evolving requirements. We believe that, by coupling our proprietary technologies with our partners expertise, we can deliver solutions that uniquely address our customers requirements.

Leverage and extend our strong intellectual property position. We have significant expertise in the design and manufacture of intuitive interface technologies and products. We intend to continue to broaden our intellectual property position through internal development to enhance the competitiveness and size of our current businesses and diversify into markets and technologies that complement our current product portfolio.

Opportunistically acquire and divest technologies and businesses that deepen our penetration into our target markets. We may evaluate acquisition and divestiture opportunities that we believe will, among other things, increase our market share in our target markets, improve our portfolio of intellectual property or strengthen our customer base.

Corporate Information

We were incorporated in California in February 1985. In July 1996, we reincorporated in Delaware. Our principal executive office is located at 546 Flynn Road, Camarillo, California 93012 and our telephone number is (805) 484-8855. Our website address is http://www.interlinkelectronics.com. None of the information on our website is part of this prospectus.

OFFERING SUMMARY

Common Stock Covered Hereby:	6,113,757 shares.
Common Stock Outstanding as of August 9, 2007:	13,749,310 shares.
Common Stock Outstanding Assuming the Conversion or Exercise of all Convertible Notes and Warrants Described Below:	19,701,691 shares.(1)
Use of Proceeds:	We will not receive any of the proceeds from the sale or other disposition of the shares covered hereby. We will receive proceeds from the cash exercise of the warrants upon exercise, if they are exercised.
Trading Symbol:	LINK.PK

GENERAL

The shares of Common Stock covered hereby are issuable to the selling securityholders upon the conversion of principal and accrued and unpaid interest on certain convertible notes and/or the exercise of certain warrants that we issued in the transaction discussed below under Convertible Note and Warrant Placement. The shares registered pursuant to the registration statement, of which this prospectus is a part, may be sold or disposed of from time to time.

CONVERTIBLE NOTE AND WARRANT PLACEMENT

On July 20, 2007, we issued 8% Convertible Notes, in an aggregate principal amount of $5,000,000, and warrants exercisable for up to 1,984,125 shares of Common Stock in a private placement pursuant to an exemption from registration provided by Regulation D under the Securities Act, as amended (the *Securities Act*), and Rule 506 thereunder. The notes mature on July 19, 2010, and some or all of the outstanding principal balance and unpaid interest may be converted into Common Stock at any time before the maturity date at a conversion price of $1.26 per share (subject to adjustment). Interest on the Notes accrues and is payable semiannually on January 15th or July 15th of each year. The warrants expire on July 19, 2012, and may be exercised at any time prior to expiration on a cash or cashless basis at an exercise price of $1.51 per share (subject to adjustment).

The conversion price under the notes and the exercise price under the warrants are subject to adjustment upon the occurrence of certain events including the issuance of stock dividends to existing Common Stockholders, or a stock split. Also, the holders of notes and warrants are entitled to receive the economic benefit of any reorganization, consolidation or merger of Interlink which results in a payment in shares, other securities

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(1) Represents the sum of shares of Common Stock outstanding as of August 9, 2007 plus the number of shares issuable upon conversion of the principal amount of the notes and exercise of the warrants. This calculation of shares outstanding does not include shares of Common Stock issuable upon the conversion of accrued and unpaid cash interest on the notes because it is not possible to predict with certainty the timing of any conversion and the related amount of accrued and unpaid interest on the notes.

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or property to our Common Stockholders. In connection with the placement of these notes and warrants, we entered into a registration rights agreement dated July 19, 2007 with the selling securityholders under which we agreed to register with the Securities and Exchange Commission (the *SEC*) the Common Stock underlying the notes and warrants for resale to the public.

The registration rights agreement also provides for payment of liquidated damages by Interlink if (i) the registration statement covering the shares to be registered pursuant to the registration rights agreement is not filed by August 20, 2007, or (ii) after a registration statement is filed with the SEC such registration statement is not declared effective on or prior to October 18, 2007 or (iii) after such registration statement has been declared effective, sales of Common Stock cannot be made pursuant to the registration statement, then in any of these and certain other circumstances enumerated in registration rights agreement, Interlink must pay to each holder of the notes, warrants or shares of Common Stock required to be registered an amount equal to 1.5% of the aggregate amount invested by each such investor for each 30 day period (or pro rata portion of such 30 day period) of such delinquency.

For more information concerning the convertible note and warrant placement discussed above, please see the Company s Current Report on Form 8-K dated July 23, 2007, which is incorporated herein by reference.

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SUMMARY CONSOLIDATED FINANCIAL DATA

(In thousands, except per share data)

(unaudited)

The following table presents our summary consolidated financial data and should be read in conjunction with our audited financial statements, our unaudited consolidated financial statements, the accompanying notes, "Management s Discussion and Analysis of Financial Condition and Results of Operations," each of which is incorporated by reference in this prospectus.

The summary consolidated statement of operations data for the years ended December 31, 2002, 2003, 2004, 2005 and 2006 has been derived from our audited consolidated financial statements incorporated by reference into this prospectus. The summary balance sheet data at March 31, 2006 and 2007 and the summary statement of operations data for the three months ended March 31, 2006 and 2007 have been derived from our unaudited consolidated financial statement for the three-month periods then ended, which statements are incorporated by reference into this prospectus and which, in the opinion of our management, contain all adjustments, including normal recurring adjustments, necessary for the fair presentation of our financial position and results of operations at and for such periods. The results of operations for any interim period are not necessarily indicative of the results of operations to be expected for the full year.

	Year Ended December 31,					Three Months Ended March 31,	
	2006	2005	2004	2003	2002	2007	2006
Consolidated Statements of							
Operations Data:							
Revenue	$ 36,238	$ 38,239	$ 35,406	$ 31,042	$ 25,042	$ 8,885	$ 8,531
Cost of Revenues	25,966	30,181	24,811	19,676	16,959	6,215	4,489
Gross Profit	10,272	8,058	10,595	11,366	8,083	2,670	3,682
Operating expenses	22,169	16,319	14,396	11,590	10,793	5,131	6,315
Operating loss	(11,897)	(8,261)	(3,801)	(224)	(2,710)	(2,461)	(2,633)
Other income (expense)	267	67	32	4	(87)	(6)	111
Net loss	(11,756)	(8,305)	(3,769)	(248)	(4,098)	(2,519)	(2,593)
Loss per share-basic and diluted	$ (0.85)	$ (0.61)	$ (0.31)	$ (0.02)	$ (0.42)	$ (0.18)	$ (0.19)

	December 31,					March 31,	
	2006	2005	2004	2003	2002	2007	2006
Consolidated Balance Sheet Data:							
Cash and short term investments, available for sale	$ 2,944	$ 13,938	$ 19,067	$ 6,061	$ 7,906	$ 5,177	$ 11,741
Working capital	14,753	22,952	30,455	18,873	16,414	13,277	21,490
Total assets	24,355	33,171	39,948	25,582	21,766	24,463	30,668
Current portion of long-term debt	152	154	491	706	933	153	154
Long-term debt (net)		154	405	1,010	1,401		154
Total liabilities	7,491	8,745	7,452	6,212	5,466	9,143	7,741
Stockholders equity	16,864	24,272	32,091	19,370	16,300	15,320	22,773

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RISK FACTORS

This offering and an investment in our securities involves a high degree of risk. You should carefully consider the risks described below and the other information in this prospectus, including our financial statements and the notes to those statements, before you purchase any securities. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us, or that we currently deem immaterial, could negatively affect our business, results of operations or financial condition in the future. If any of the following risks and uncertainties develops into actual events, our business, results of operations or financial condition could be adversely affected. In those cases, the trading price of our securities could decline, and you may lose all or part of your investment.

We have incurred net losses and negative cash flow from operations for the past twelve fiscal quarters and will experience future quarterly losses. Continued losses and negative cash flow would reduce our internal resources, limit our growth options, require additional cash infusions and could ultimately place our continued viability in question.

We have incurred losses and negative cash flow from operations in each of the previous three years 2004, 2005 and 2006 and for the first two quarters of 2007 as a result of various factors, including declining gross profit margins in our OEM Remotes business segment, increases in operating costs, inventory reserve adjustments, increased compliance and regulatory costs, and internal investigation costs. We will continue to incur net quarterly losses and negative cash flow from operations as we continue to invest in new technology and emerging markets. We are incurring these losses in part to develop lines of business that we believe to be promising but that may fall short of our expectations. Accordingly, we cannot assure you that we will achieve or sustain profitability or positive cash flow. If we do not achieve profitability and positive cash flow, our financial resources will be adversely affected and we may be forced to curtail or discontinue certain operations which could result in the allocation of fixed costs over a smaller revenue base or affect our future competitiveness. Continued negative cash flow from operations could also require us to seek financing, which could prove dilutive to the interests of existing investors, or to divest certain aspects of our business, including through the sale of operating assets. The Company s independent registered public accounting firm has informed the Company that it may include in its report on the Company s financial statements for the year ending December 31, 2007 an explanatory paragraph expressing substantial doubt about the Company s ability to continue as a going concern if the Company fails to successfully fund its current operations.

Our existing capital resources and credit availability may not be sufficient to pursue our business plan and our auditors have expressed doubt as to our ability to continue as a going concern. The failure to secure the necessary resources would require us to limit operations, which could have an adverse impact on our ability to develop our business as currently planned.

On July 20, 2007, the Company raised $5 million through a private placement of convertible notes and warrants with certain institutional stockholders. We may require additional financing for the remainder of 2007 to fund our continuing operations. We cannot assure you that we will be successful in obtaining additional required capital. Any financing arrangements that we may enter into may increase future costs, involve restrictions on our financing and operating activities or be dilutive to existing stockholders. If we are unable to obtain additional financing as needed, which may include commercial or securitized debt, sales of equity securities or other alternatives, we may be required to reduce the scope of, or curtail, our operations. If our revenues fall short of, or our costs exceed, our expectations, any financing that we do secure may be inadequate to meet our cash requirements.

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We are facing litigation based on our restatements of historical financial statements, which may have a material adverse impact on our cash reserves and may impair our ability to achieve our business objectives.

Certain former Interlink stockholders have filed a class action lawsuit claiming damages under various federal securities laws based on our restatement of historical financial statements. Other stockholders have brought a derivative action against our Chief Executive Officer and our former Chief Financial Officer that alleges, among other things, securities-related violations of the California Corporations Code. These actions will require a vigorous defense and could result in a settlement or adverse award that is not covered by insurance or that exceeds applicable insurance limits. The time and expense required to defend these claims may also affect our ability to pursue our business strategy. There is also no assurance that additional lawsuits will not be filed or that the ultimate resolution of these matters will not result in a material adverse effect on our financial condition or results of operations.

We have identified material weaknesses in our internal control over financial reporting and have been required to restate our historical financial statements.

In our Annual Reports for the years ended December 31, 2005 and 2006, we reported material weaknesses in our internal control over financial reporting. As a result of these material weaknesses, we were required to restate our historical financial statements for the fiscal years 2001 through 2004, as well as for the first and second quarters of fiscal 2005. We have taken significant measures to improve our financial reporting process and as of June 30, 2007, no material weaknesses remain to be remediated. As of December 31, 2006, our disclosure controls and procedures were effective, though there can be no assurances that future material weaknesses will be discovered. These measures are more fully described in the Company s Quarterly Report on Form 10-Q for the period ended March 31, 2007 under the caption "Item 4 Controls and Procedures."

Despite our substantial efforts to ensure the integrity of our financial reporting process, we cannot guarantee that we will not identify additional weaknesses as we continue to work with the new systems that we have implemented over the past year. Any continuing material weaknesses in our internal control over financial reporting could result in errors in our financial statements. Such errors could cause our internal planning and assessment of our business to be based on false information and could cause our published financial statements to fail to fairly present our financial condition and results of operations, which could erode market confidence in our company, cause the price of our stock to be based on false or misleading information and result in litigation based on such false or misleading information.

Business acquisitions, divestitures or partnering arrangements may disrupt our business, dilute stockholder value and distract management s attention.

As part of our business strategy, we may consider acquisitions of, or significant investments in, businesses with services, products or technologies that we believe could complement or expand our business. Such acquisitions or investments involve numerous risks, including:

- unanticipated costs and liabilities;
- difficulty of integrating the operations, products and personnel of the acquired business;
- difficulties in managing the financial and strategic position of acquired or developed products and technologies;
- difficulties in maintaining customer relationships;
- diversion of management s attention;
- inability to maintain uniform standards, controls, policies and procedures;

impairment of relationships with acquired employees and customers occurring as a result of integration of the acquired business; and

accounting results that are unrelated to the performance of either business.

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Acquisitions also frequently result in recording of goodwill and other intangible assets that are subject to potential impairments in the future. Additionally, if we finance acquisitions by using convertible debt or stock, our existing stockholders may be diluted which could affect the market price of our stock. If we fail to properly evaluate and execute acquisitions or investments, we may not achieve the anticipated additional benefit to our business, and we may incur costs in excess of what we anticipate.

We may also from time to time consider the divestiture or discontinuance of aspects of our business, which may involve many of the risks identified above, including significant internal adjustments and management distractions. Any such changes could require us to amortize fixed costs over a smaller revenue base and could require other changes that could consume resources and management attention. Additionally, we may fail to replace divested operations with new business segments that contribute to our financial health and strategic objectives. Failure to successfully implement acquisition or divestiture plans could damage the viability of our ongoing operations.

We are emphasizing new markets and if we fail to accurately predict the growth of these new markets, we may suffer reduced earnings.

Historically, the largest contributor to our consolidated sales was from our OEM Remotes business segment. In late 2005, we deemphasized and reorganized certain segments of this market. As a result, OEM Remotes sales in these segments have declined. At the same time, we have devoted significant resources to the development of products and the support of marketing and sales efforts in new markets, such as our *MicroNav* family of products, the E-transactions market and selected aspects of the OEM Remotes market. We expect to continue to identify and develop products for new markets. These markets change rapidly and we cannot assure you that they will grow or that we will be able to accurately forecast market demand in time to respond appropriately. Our investment of resources in these markets may either be insufficient to meet actual demand or result in expenses that are excessive in light of actual sales volumes. Failure to accurately predict growth and demand in new markets may cause us to suffer substantial losses or reduced earnings.

Our OEM Remotes business is focused on consumer markets that are intensely price competitive. If we cannot generate volume and related manufacturing efficiencies required to compete in these markets, our results of operations will be adversely affected.

Historically, our OEM Remotes business was primarily focused on selling remote devices in the presentation projector market. As a specialty market, this sector generated relatively low sales volumes with correspondingly high margins. However the presentation projector market has become more consumer-oriented and price competition has increased. We have shifted our OEM Remotes business toward sales to manufacturers of advanced viewing devices which is also very consumer oriented and price competitive but which offers the potential for higher volumes. If we cannot increase production and sales volume, or if we otherwise fail to achieve production efficiencies, our results of operations and financial position will be adversely affected.

Failure to maintain, develop and expand our OEM relationships could cause demand for our products to decrease.

Sales to OEMs in our OEM Remotes and Specialty Components markets constituted 53% of our total sales for 2006. If we fail to maintain, develop and expand our relationships with significant OEMs, or if those OEMs are not successful in their marketing and sales efforts, demand for our products may decrease. If our OEM customers experience a significant reduction in demand for advanced viewing devices, televisions or presentation systems, it will significantly decrease demand for our remote devices.

Our ability to generate increased revenues also depends significantly on the extent to which our OEM customers develop, promote and sell products that incorporate our technology and products. If our OEM customers do not successfully develop and market products that incorporate our products, sales of our products to our OEM customers would be adversely affected. The extent to which our OEM customers develop, promote and sell our products is based on a number of factors that are largely beyond our ability to control.

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The loss of any significant customer or any cancellation, reduction or delay of a large purchase by a significant customer could reduce our revenue and require us to write down inventory.

Our five largest OEM customers accounted for approximately 14% of our total 2006 sales. Although we have been deemphasizing segments of our OEM business, the loss of any key OEM customer, or a significant reduction in sales to any such customer, could significantly reduce our revenue below anticipated levels. OEM sales tend to be related to specific products offered by our OEM customers and therefore fluctuate significantly as such products are introduced and discontinued. From time to time, we expect to lose significant revenue streams as the result of OEM product discontinuances and will be required constantly to seek new opportunities with new and existing customers in those segments that we choose to continue to pursue. Because our expense levels are based on our expectations as to future revenue and are, to a large extent, fixed in the short term, a substantial reduction or delay in sales of our products to an OEM customer, the unexpected loss of any significant OEM or other customer, or unexpected returns from customers, could harm our business.

Failure to increase market awareness and acceptance of E-transactions and our E-transaction products may cause our revenues in this market to fall short of our expectations.

We are focusing considerable resources on developing our E-transactions market. The prospects for growth of our E-transactions business depend in part on the acceptance by our target markets of electronic signatures as a replacement for traditional pen and ink signatures. The market for E-transactions is new and emerging and we cannot be certain that it will continue to develop or grow or that businesses will elect to adopt our products rather than continuing to rely on traditional pen and ink signatures. Businesses that have invested substantial resources in traditional infrastructures may be reluctant to adopt an electronic approach to replace their existing systems. Concerns about privacy and fraud may cause businesses not to adopt E-transactions or our e-transaction products. We expect that we will need to continue to pursue intensive marketing and sales efforts to educate prospective customers about the benefits of E-transactions and our E-transaction products. If market awareness and acceptance of E-transactions do not occur, our revenues and profitability in this market will fall short of our expectations.

Sales of simple signature capture devices are growing rapidly and the manufacturers of these devices could broaden their product range to include products that compete with our ePad.

Simple signature capture devices have recently become a common sight at retail checkout counters and a number of companies manufacture and sell these devices. While our ePad product is targeted at a more demanding market, signature capture device manufacturers could elect to upgrade their existing products in an effort to compete in our markets. Such competition could reduce margins or otherwise adversely affect our prospects in our E-transactions market.

If we are unable to keep pace with rapid technological change and gain market acceptance of new products, we may not be able to compete effectively.

Technology, both in our markets and in our customers markets, is undergoing rapid change. In order to maintain our leadership position in our existing markets and to emerge as a leader in new markets, we will have to maintain a leadership position in the technologies supporting those markets. Doing so will require, among other things, that we accomplish the following:

- accurately predict the evolving needs of our customers and develop, in a timely manner, the technology required to support those needs;
- provide products that are not only technologically sophisticated and well supported but are also available at a price within market tolerances and competitive with comparable products;
- establish and effectively defend our ownership of the intellectual property supporting our products; and
- enter into relationships with other companies that have developed complementary technology on which our products also depend.

We cannot assure you that we will be able to achieve any of these objectives.

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If our products do not support evolving industry standards, they may not achieve or maintain market acceptance and our revenues may decline.

Our wireless communication products must communicate using whatever communication protocol is chosen by the customer. Supporting a particular communication protocol requires specific technical expertise and we expect that we will be required to establish and maintain such expertise with respect to each commonly used communication protocol. New communication protocols are constantly under development and we may fail to acquire the necessary experience to support a popular new protocol or to respond to changes in an existing protocol. In our E-transactions business, our customers will expect that our products will enable them to comply with applicable requirements relating to electronic signatures, such as the Electronic Signatures in Global Commerce Act and procedures adopted by the National Notary Association. If our products do not support these requirements, sales of our E-transactions products would be adversely affected.

If we fail to manage change successfully, our operations could be adversely impacted and our business could be impaired.

The ability to operate our business in rapidly evolving markets requires an effective planning and management process. We expect that responding to changes in our business will place a significant strain on our personnel, management systems, infrastructure and other resources. Our ability to manage change effectively will require us to attract, train, motivate and manage new employees, to reallocate human and other resources to support new undertakings and to restructure our operations to manage a restructured business effectively. If we are unable to respond effectively to change, our operations could be adversely affected and our business could be impaired.

Most of our OEM and major retail customers order from us on a just in time basis, which requires us to estimate demand for particular products, and many of these products are customer specific.

The agreements or understandings that we reach with most of our OEM customers specify various terms such as product design and price, but do not constitute firm purchase orders for a specific number of products or components. Our OEM and major retail customers typically place firm purchase orders on a just in time basis and expect products or components to be shipped to them as soon as they can be made. Accordingly, our backlog of firm orders is typically quite small in relation to the volume of our sales. In anticipation of customer demand, we are often required to purchase raw materials and components based on estimates of customer demand derived from non-binding information furnished by the customer. If customer purchase orders differ substantially from our estimates, we may accumulate excess inventory that has to be written off. If we underestimate demand, we may be unable to meet customer needs, which could harm our relationship with the customer.

We rely on third parties for the materials that we use to manufacture our products and a shortage of supply could adversely affect our revenues, operating results and customer relationships.

We rely on third-party suppliers for the raw material components of our products. We cannot assure you that our suppliers will be able to maintain an adequate supply of these raw materials to enable us to fulfill all of our customers orders on a timely basis. A failure to obtain an adequate supply of the materials for our products could increase our costs of goods sold, cause us to fail to meet delivery commitments and cause our customers to purchase from our competitors, which could adversely affect our operating results and customer relationships. In some situations, we rely on a single supplier for raw material components of our products. Any disruption in these supplier relationships could prevent us from maintaining an adequate supply of materials and could adversely affect our results of operation and financial position.