

ACACIA RESEARCH CORP

Form 10-K

March 15, 2019

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2018

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM TO .

Commission File Number 001-37721

(Exact name of registrant as specified in its charter)

DELAWARE	95-4405754
(State or other jurisdiction of incorporation organization)	(I.R.S. Employer Identification No.)

120 NEWPORT CENTER DRIVE	
NEWPORT BEACH, CA	92660
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: **(949) 480-8300**

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, \$0.001 par value	The NASDAQ Stock Market, LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒ R

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒ R

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 filing requirements for the past 90 days. Yes ☒ R No ☐ £

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☐ No ☒

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

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

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐ (Do not check if a smaller reporting company)

Smaller reporting company ☒

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

The aggregate market value of the registrant's voting and non-voting common stock held by non-affiliates of the registrant on June 30, 2018, the last business day of the registrant's most recently completed second fiscal quarter, computed by reference to the last sale price of the registrant's common stock as reported by The Nasdaq Global Select Market on such date, was approximately \$203,206,000. This computation assumes that all executive officers and directors are affiliates of the registrant. Such assumption should not be deemed conclusive for any other purpose. As of March 11, 2019, 49,647,693 shares of common stock were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

In accordance with General Instruction G(3) to Form 10-K, portions of the registrant's Definitive Proxy Statement on Schedule 14A for its Annual Meeting of Stockholders to be filed with the Commission within 120 days after the close of the fiscal year covered by this Annual Report on Form 10-K are incorporated by reference into Part III of this Annual Report on Form 10-K. Only those portions of the proxy statement that are specifically incorporated by reference herein shall constitute a part of this Annual Report on Form 10-K.

**ACACIA RESEARCH CORPORATION
ANNUAL REPORT ON FORM 10-K
FISCAL YEAR ENDED DECEMBER 31, 2018
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PART I

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

As used in this Annual Report on Form 10-K, “we,” “us” and “our” refer to Acacia Research Corporation and/or its wholly and majority-owned operating subsidiaries. All patent portfolio investments, development, licensing and enforcement activities are conducted solely by certain of our wholly owned operating subsidiaries.

This Annual Report on Form 10-K, or the annual report, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, which include, without limitation, statements about our future business operations and results, our strategies and competition, and other forward-looking statements included in this annual report. Such statements may be identified by the use of forward-looking terminology such as “may,” “will,” “expect,” “believe,” “estimate,” “anticipate,” “intend,” “continue,” or similar terms, variations of such terms or the negative of terms. Such statements are based on management’s current expectations and are subject to a number of risks and uncertainties, which could cause actual results to differ materially from those described in the forward-looking statements. Such statements address future events and conditions concerning earnings, capital expenditures, litigation, competition, regulatory matters, stock price volatility, liquidity and capital resources, accounting matters and investments. Actual results in each case could differ materially from those anticipated in such statements by reason of factors such as future economic conditions, legislative, regulatory and competitive developments in markets in which we and our subsidiaries operate, and other circumstances affecting anticipated revenues and costs, as more fully disclosed in our discussion of “Risk Factors” in Item 1A of Part I of this annual report. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. Additional factors that could cause such results to differ materially from those described in the forward-looking statements are set forth in connection with the forward-looking statements.

ITEM 1. BUSINESS

General

We invest in intellectual property, or IP, and related absolute return assets and engage in the licensing and enforcement of patented technologies. We partner with inventors and patent owners, from small entities to large corporations, applying our legal and technology expertise to patent assets to unlock the financial value in their patented inventions. We are an intermediary in the patent marketplace, bridging the gap between invention and application, and facilitating efficiency in connection with the monetization of patent assets.

We generate revenues and related cash flows from the granting of IP rights for the use of patented technologies that our operating subsidiaries control or own. We assist patent owners with the prosecution and development of their patent portfolios, the protection of their patented inventions from unauthorized use, the generation of licensing revenue from users of their patented technologies and, where necessary, with the enforcement against unauthorized users of their patented technologies through the filing of patent infringement litigation. Currently, on a consolidated basis, our operating subsidiaries own or control the rights to multiple patent portfolios, which include U.S. patents and certain foreign counterparts, covering technologies used in a variety of industries.

We have established a proven track record of licensing and enforcement success with over 1,560 license agreements executed to date, across nearly 200 patent portfolio licensing and enforcement programs. To date, we have generated gross licensing revenue of approximately \$1.6 billion, and have returned more than \$767 million to our patent partners.

Corporate Information

We were originally incorporated in California in January 1993 and reincorporated in Delaware in December 1999. Our website address is www.acaciaresearch.com. Reference in this annual report to this website address does not constitute incorporation by reference of the information contained on or accessed through our website and references to our website address in this annual report are inactive textual references only. We make our filings with the Securities and Exchange Commission, or the SEC, including our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, other reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, and amendments to the foregoing reports, available free of charge on or through our website as soon as reasonably practicable after we file these reports with, or furnish such reports to, the SEC. In addition, we post the following information on our website:

- our code of conduct for chief executive officer and other senior financial officers;
- our code of conduct for employees and directors and our fraud policy;
- our insider trading policy; and
- charters for our audit committee, nominating and corporate governance committee and compensation committee.

Also, the SEC maintains an Internet website that contains reports, proxy and information statements, and other information regarding issuers, including us, that file electronically with the SEC. The public can obtain any documents that we file with the SEC at <http://www.sec.gov>.

Patent Licensing and Enforcement Business

Patents are an important asset class worldwide. Licensing and enforcing patents requires an experienced, well-capitalized, licensing partner. We have partnered with patent owners, including individual inventors, universities, small companies and large multi-national corporations in a variety of technology sectors. These patent owners may possess limited internal resources and/or expertise to effectively address the unauthorized use of their patented technologies, or may seek to effectively and efficiently monetize their portfolio of patented technologies on an outsourced basis.

Under U.S. law, a patent owner has the right to exclude others from making, selling or using their patented invention. A third-party infringes a patent by making, offering for sale, selling, or using a patented invention without a license from the patent owner. In the majority of cases, infringers are generally unwilling, at least initially, to negotiate or pay reasonable license fees for their unauthorized use of third-party patents and will typically indiscriminately challenge any allegations of patent infringement. Inventors and patent holders without sufficient legal, financial and expert technical resources to bring and continue the pursuit of costly and complex patent infringement actions are often effectively ignored.

As a result of the common reluctance of patent infringers to negotiate and ultimately enter into a patent license for the use of patented technologies without at least the threat of legal action, patent licensing and enforcement often begins with the filing of patent infringement litigation. However, in our experience, most patent infringement litigation settles out of court at amounts that are related to the strength of the patent portfolio and the value of the invention or inventions in the infringer's products or services. We execute agreements that grant rights in our patents to users of our patented technologies. Our agreements can be negotiated without the filing of patent litigation, or negotiated within the context of ongoing patent litigation, depending on the specific facts and circumstances.

We are a principal in the licensing and enforcement effort, with our operating subsidiaries obtaining control of the rights in the patent portfolio, or control of the patent portfolio outright. Our relationship with patent owners drives our corporate strategy. We assume all responsibility for advancing operational expenses while pursuing a patent licensing and enforcement program, and then, when applicable, share net licensing revenue with our patent partners as that program matures, on a pre-arranged and negotiated basis. We may also provide upfront capital to patent owners as an advance against future licensing revenue.

Patent Licensing Business Model and Strategy - Overview

We have the flexibility to structure arrangements in a number of ways to address the needs and specific sets of circumstances presented by each of our unique patent partners, ranging from outright purchases to various forms of partnering arrangements.

Generally, we maintain a 100% to 200% preferred rate of return until all deployed capital and advanced operational costs are recovered by us. After recovery of these costs, the net profit revenue share with patent partner commences, if applicable.

Key Elements of Business Strategy

Patent licensing and enforcement can be an effective and efficient way to maximize the profit potential of a patent, or patents, that are being practiced by third-parties without authorization. A patent license agreement grants a third-party user of an invention specific patent rights to the patented invention in exchange for patent license fees. Our patent licensing business provides patent holders with an opportunity to generate income from their patented inventions being practiced by third-parties without authorization and from third-parties that desire to practice their patented inventions with authorization. Our patent licensing and enforcement business strategy includes three fundamental elements, as follows:

- *Patent Discovery* - Discover potentially valuable patents or patent portfolios.

- *Assessment of Economic Value* - Work internally and with external experts to evaluate the use of the patented invention(s) in the relevant marketplace and assess a patent or patent portfolio's expected economic value.

- *Licensing and Enforcement* - License those users wanting to utilize the patented invention with authorization. For unauthorized users of the patented invention, enter into license negotiations and, if necessary, litigation to monetize the patent based on its assessed value.

Patent Discovery. The patent process breeds, encourages and sustains innovation and invention by granting a limited monopoly to the inventor in exchange for sharing the invention with the public. Certain technologies become core technologies in the way products and services are manufactured, sold or delivered by companies across a wide array of industries. Patent discovery involves identifying core, patented technologies that have been or are anticipated to be widely adopted by third-parties in connection with the manufacture, sale or use of products and services.

Assessment of Economic Value. Subsequent to the patent discovery process, our executives work internally and/or with external industry experts in the specific technology field, to evaluate the patented invention and its adoption and implementation in the marketplace. There are a number of factors to consider when analyzing a patent and determining a patent's value including, (i) infringement, (ii) validity, (iii) enforceability and (iv) extent of usage.

To determine infringement, we must first identify third-parties that are practicing the invention(s) covered by the patent without obtaining permission from the patent owner to do so. A key tool in determining whether or not a company is infringing a patent is a claim chart, which demonstrates how the manufacture, sale, or use of an existing product compares against the claims of the patent.

The three main factors analyzed to determine validity are: (1) anticipation, which occurs when the claims of the patent are entirely revealed within a single piece of prior art, (2) obviousness which considers whether the differences between prior art and the patented invention are so slight that they would have been obvious at the time of invention to one who is skilled in the subject matter being patented, and (3) the existence of non-patentable subject matter, which considers whether the subject matter includes naturally occurring things, abstract concepts, or algorithms that perform an ordinary function.

To determine enforceability, a number of factors are analyzed, including whether or not there has been patent misuse, or whether or not there are antitrust violations associated with the patent. Due to the inherently complex nature of patent law, only a court or specific administrative body, such as the International Trade Commission, can make a decision whether a patent is infringed, valid and enforceable; however, we employ our wealth of expertise to make the best assessment possible given a specific fact pattern and set of circumstances.

We estimate a patent's economic value by evaluating the expected value of the license revenue stream based on past, present and future revenue of infringing products or services, and the risk that a court will disagree with our infringement, validity or enforcement assessments of the patent. The processes and procedures employed in connection with the evaluation of a specific patent portfolio for future investment, licensing and enforcement are tailored and unique to each specific situation and can vary widely based on the specific facts and circumstances of a specific patent portfolio, such as the related technology, related industry and other factors.

Our business development efforts are geared toward maintaining those relationships and identifying and growing new relationships in order to generate new technology-based patent opportunities for sustainable revenue and /or revenue

growth.

Legislative and legal changes have increased the complexity of patent enforcement actions. We believe that this provides Acacia a competitive advantage, as many patent monetization entities have either given up or failed. Furthermore, the challenging legislative environment has kept patent asset acquisition prices low.

In fiscal year 2018, Acacia experienced a number of changes in the Company's outlook and leadership. With new management in place during the year, the focus was on capturing the value of remaining portfolio assets while starting to rebuild the new business pipeline. In addition, we began to pursue other business opportunities which complement our legacy licensing and enforcement business and leverage our IP expertise, as described below.

Licensing and Enforcement. The final step in the patent licensing and enforcement process is to seek to monetize the patent portfolio by securing license agreements based on the patents use in the marketplace and estimated value. While we prefer to convince unauthorized users of our patented inventions of the value of the patented invention and secure a license

agreement in a non-litigious manner, many infringers refuse to take such licenses even when confronted with substantial and persuasive evidence of infringement, validity, enforceability and significant economic value. As a result, often we must resort to litigation to demonstrate and prove infringement and ultimately induce infringers to take a license from us. We often negotiate licenses concurrently with litigation due to the fact that litigation necessitates and facilitates an information exchange that helps both sides assess the value of a patent and make informed decisions. Also, litigation eventually leads to a court's judgment. When a court agrees with our assessment of a patent, this judgment stops recalcitrant infringers from utilizing the patented technology indefinitely, without appropriate authorization.

We engage highly competent and experienced patent lawyers to prosecute our patent portfolio litigation. It is imperative for us to be persistent and patient throughout the litigation process as it typically takes 18-36 months from the filing date of a lawsuit to yield a license agreement from a potential licensee. Often, it takes longer to secure a final court judgment.

Patent license negotiations and litigation initiated by our operating subsidiaries usually lead to serious and thoughtful discussions with the unauthorized users of the patented inventions. The result can be quite favorable with the user being granted rights under the patents for the patented invention in its products and services in exchange for financial remuneration.

Investments

In August 2016, we entered into an investment agreement with Veritone, a cloud-based Artificial Intelligence technology company. In connection with this investment agreement, we provided a total of \$53.3 million in funding. Upon Veritone's consummation of its initial public offering on May 17, 2017, or IPO, our loans and accrued interest were automatically converted into shares of Veritone common stock, and we were issued an additional warrant to purchase additional shares of Veritone common stock as described elsewhere herein. As of December 31, 2018, the Company's investment in Veritone totaled \$7.5 million.

In June 2017, we made a \$2.25 million equity investment in Miso Robotics, Inc., or Miso Robotics, an innovative leader in robotics and Artificial Intelligence, or AI, solutions. The investment was part of Miso Robotics' closing of \$3.1 million in Series A funding. In addition, in February 2018, we made an additional equity investment totaling \$6.0 million in the Series B financing round for Miso Robotics, increasing our fully diluted ownership interest to approximately 30%. Miso Robotics will use the capital to expand its suite of collaborative, adaptable robotic kitchen assistants and to broaden applications for Miso AI, the company's machine learning cloud platform.

Patented Technologies

Currently, on a consolidated basis, our operating subsidiaries own or control the rights to patent portfolios with future patent expiration dates ranging from 2019 to approximately 2033, covering technologies used in a number of industries, including: transportation and automotive, telecommunications, semiconductor, consumer electronics, energy efficiency, wireless, video/imaging and medical devices.

Refer to Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview" for a summary of patent portfolios generating revenues for the applicable periods presented.

Competition

We encounter competition in the area of patent portfolio investment opportunities and enforcement. Existing non-practicing entities compete in acquiring rights to IP assets, and more entities may enter or leave the market in future periods.

We also compete with financial firms, corporate buyers and others acquiring IP and investing in other technology opportunities. Many of these competitors may have more financial and human resources than us. We may find more companies entering the market for similar technology opportunities, which may reduce our market share in one or more technology industries that we currently or in the future may rely upon to generate future revenue.

Companies or other entities may develop competing technologies that offer better or less expensive alternatives to our patented technologies or technology partnerships. Many potential competitors may have significantly greater resources than the resources that we or our operating subsidiaries possess. Such technological advances or entirely different approaches developed by one or more of our competitors could render certain of the technologies owned or controlled by us obsolete and/or uneconomical.

Employees

As of December 31, 2018, on a consolidated basis, we had 13 full-time employees. Neither we, nor any of our subsidiaries, are a party to any collective bargaining agreement. We believe we have good relations with our employees.

ITEM 1A. RISK FACTORS

An investment in our common stock involves risks. You should carefully consider the risks described below, together with all of the other information included in this annual report, as well as in our other filings with the SEC, in evaluating our business. The risks described below are not the only risks we face. Additional risks that we do not yet know of or that we currently believe are immaterial may also impair our business operations. If any of the following risks actually occur, our business, financial condition and results of operations could be materially adversely affected, and the trading price of our common stock could decline significantly. Certain statements below may be considered forward-looking statements. For additional information, see “Cautionary Note Regarding Forward-Looking Statements.”

Risks Related to Our Business

We have a history of losses and may incur additional losses in the future.

We reported a net loss of \$105.0 million (includes \$59.1 million of unrealized equity investment losses), and a net income of \$22.2 million (including \$42.2 million of unrealized equity investment gains) for the years ended December 31, 2018 and 2017, respectively, and on a cumulative basis, we have sustained substantial losses since our inception. As of December 31, 2018, our accumulated deficit was \$422.5 million. As of December 31, 2018, we had approximately \$165.5 million in cash and cash equivalents and short-term investments and working capital of \$170.4 million. Although we believe that our current cash and cash equivalents and investments will be sufficient to finance our anticipated capital and operating requirements for at least the next twelve months, we expect to continue incurring significant legal, general and administrative expenses in connection with our operations. As a result, we anticipate that we may incur losses in the future. Additional increases in our expenses without commensurate increases in revenues could significantly increase our operating losses. Any additional operating losses may have a material adverse effect on our stockholders' equity and overall financial condition.

Recent U.S. tax legislation may adversely affect our financial condition, results of operations and cash flows, including the ability to use net operating losses and certain other tax attributes.

On December 22, 2017, new tax legislation was signed into law. Among other things, it reduced the maximum federal corporate income tax rate to 21% in future periods, limited interest deductions, adopted elements of a territorial tax system, imposed a one-time transition tax (or “repatriation tax”) on all undistributed earnings and profits of certain U.S.-owned foreign corporations, revised the rules governing net operating losses and the rules governing foreign tax credits, and introduced new anti-base erosion provisions. Many of these changes were effective immediately, without any transition periods or grandfathering for existing transactions. While some of the changes made by the tax legislation may adversely affect the Company in one or more reporting periods and prospectively, other changes may be beneficial on a going forward basis. The legislation is unclear in many respects and could be subject to potential amendments and technical corrections, as well as interpretations and implementing regulations by the U.S. Treasury and the IRS, any of which could lessen or increase certain adverse impacts of the legislation. In addition, it is not clear how these U.S. federal income tax changes will affect state and local taxation, which often uses federal taxable

income as a starting point for computing state and local tax liabilities. We continue to work with our tax advisors to determine the full impact that the recent tax legislation as a whole will have on us. We urge our investors to consult with their legal and tax advisors with respect to such legislation.

The value of the Company's deferred tax assets (including the value of our net operating loss carryforwards and our tax credit carryforwards for financial statement purposes) was reduced by approximately \$25.3 million in the fourth quarter of 2017 . We have provided for a full valuation allowance for net deferred tax assets as of December 31, 2018 and 2017, and we do not expect the change in tax law to have a material impact on our consolidated financial statements provided herein.

Our ability to use our federal and state net operating losses to offset potential future taxable income and related income taxes that would otherwise be due is dependent upon our generation of future taxable income before the expiration dates of the net operating losses, and we cannot predict with certainty when, or whether, we will generate sufficient taxable income to use all or any portion of our net operating losses. In addition, utilization of net operating losses to offset potential future taxable income and related income taxes that would otherwise be due is subject to annual limitations under the "ownership change" provisions of Sections 382 and 383 of the Internal Revenue Code of 1986, as amended, or the Code, and

similar state provisions, which may result in the expiration of net operating losses before future utilization. In general, under the Code, if a corporation undergoes an “ownership change,” generally defined as a greater than 50% change (by value) in its equity ownership over a three-year period, the corporation’s ability to use its pre-change net operating losses and other pre-change tax attributes (such as research and development credit carryforwards) to offset its post-change taxable income or taxes may be limited. Changes in our stock ownership, some of which may be outside of our control, could in the future result in an ownership change. Although we have completed studies to provide reasonable assurance that an ownership change limitation would not apply, we cannot be certain that a taxing authority would reach the same conclusion. If, after a review or audit, an ownership change limitation were to apply, utilization of our domestic net operating losses and tax credit carryforwards could be limited in future periods and a portion of the carryforwards could expire before being available to reduce future income tax liabilities.

If we encounter unforeseen difficulties with our business or operations in the future that require us to obtain additional working capital, and we cannot obtain additional working capital on favorable terms, or at all, our business may suffer.

Our consolidated cash and cash equivalents and short-term investments totaled \$165.5 million and \$136.6 million at December 31, 2018 and 2017, respectively. To date, we have relied primarily upon net cash flows from our operations and from the public and private sale of equity securities to generate the working capital needed to finance our operations. We may encounter unforeseen difficulties with our business or operations in the future that may deplete our capital resources more rapidly than anticipated. As a result, we may be required to obtain additional working capital in the future through bank credit facilities, public or private debt or equity financings, or otherwise. If we are required to raise additional working capital in the future, such financing may be unavailable to us on favorable terms, if at all, or may be dilutive to our existing stockholders. If we fail to obtain additional working capital, as and when needed, such failure could have a material adverse impact on our business, results of operations and financial condition.

Failure to effectively manage our operational changes could strain our managerial, operational and financial resources and could adversely affect our business and operating results.

Operational changes primarily relate to recent changes in our board of directors and senior management and the reductions in employee headcount across our licensing, business development and engineering functions during the two year period ended December 31, 2018. During 2018, we announced various changes to our board of directors and senior management, including a reconstituted board of directors and the terminations of our President, our Chief Financial Officer, Senior Vice President of Finance and Treasurer and our Executive Vice President, General Counsel and Secretary. We also announced in 2018 the appointment of our new Chief Intellectual Property Officer Marc W. Booth. Changes in leadership and key management positions have inherent risks, and there are no assurances that any of our recent changes will not affect our financial condition.

In addition, employee headcount has been reduced as a result of a decrease in patent portfolio intake during the two year period.

If we fail to manage our operational changes effectively or to develop, expand or otherwise modify our managerial, operational and financial resources and systems, our business and financial results will be materially harmed.

Patent portfolio investments may present risks, and we may be unable to achieve the financial or other goals intended at the time of any potential investment.

Our licensing and enforcement business has depended, in part, on our ability to invest in patented technologies, patent portfolios, or companies holding such patented technologies and patent portfolios. Accordingly, historically we have engaged in patent portfolio investments in an effort to expand our patent portfolio assets. Such investments and potential investments are subject to numerous risks, including the following:

- our inability to enter into a definitive agreement with respect to any potential patent portfolio investment, or if we are able to enter into such agreement, our inability to consummate the potential investment transaction;

- difficulty integrating the operations, technology and personnel of the acquired entity;

- our inability to achieve the anticipated financial and other benefits of the specific patent portfolio investment;

- our inability to retain key personnel from the acquired company, if necessary;

• difficulty in maintaining controls, procedures and policies during the transition and integration process;

- diversion of our management's attention from other business concerns; and

• failure of our due diligence process to identify significant issues, including issues with respect to patented technologies and patent portfolios, and other legal and financial contingencies.

If we are unable to manage these risks effectively as part of any patent portfolio investment, our business could be adversely affected.

Our revenues are unpredictable, and this may harm our financial condition.

Due to the nature of our licensing business and uncertainties regarding the amount and timing of the receipt of license and other fees from potential infringers, stemming primarily from uncertainties regarding the outcome of enforcement actions, rates of adoption of our patented technologies, the growth rates of our existing licensees and certain other factors, our revenues may vary significantly from quarter to quarter and period to period, which could make our business difficult to manage, adversely affect our business and operating results, cause our quarterly and periodic results to fall below market expectations and adversely affect the market price of our common stock.

Our operating subsidiaries depend upon relationships with others to provide technology-based opportunities that can develop into profitable royalty-bearing licenses, and if they are unable to maintain and generate new relationships, then they may not be able to sustain existing levels of revenue or increase revenue.

Neither we nor our operating subsidiaries invent new technologies or products; rather, we depend upon the identification and investment in patents, inventions and companies that own IP through our relationships with inventors, universities, research institutions, technology companies and others. If our operating subsidiaries are unable to maintain those relationships and identify and grow new relationships, then we may not be able to identify new technology-based patent opportunities for sustainable revenue and /or revenue growth.

Our current or future relationships may not provide the volume or quality of technologies necessary to sustain our licensing, enforcement and overall business. If we are unable to maintain current relationships and sources of technology or to secure new relationships and sources of technology, such inability may have a material adverse effect on our revenues, operating results, financial condition and ability to maintain our licensing and enforcement business.

The success of our operating subsidiaries depends in part upon their ability to retain the best legal counsel to represent them in patent enforcement litigation in order to achieve favorable outcomes from such litigation. The outcome of such litigation is uncertain, and any unfavorable outcomes may harm our financial condition.

The success of our licensing business depends upon our operating subsidiaries' ability to retain the best legal counsel to prosecute patent infringement litigation. As our operations evolve and industry conditions increase in complexity, it will become more difficult to find the best legal counsel to handle all of our cases. This is due in part to many of the best law firms having conflicts of interest that prevents their representation of our subsidiaries.

We spend a significant amount of our financial and management resources to pursue our current litigation matters. We believe that these litigation matters and others that we may in the future determine to pursue could continue for years and continue to consume significant financial and management resources. The counterparties to our litigation are sometimes large, well-financed companies with substantially greater resources than us. We cannot assure you that any

of our current or future litigation matters will result in a favorable outcome for us. In addition, in part due to the appeals process and other legal processes, even if we obtain favorable interim rulings or verdicts in particular litigation matters, they may not be predictive of the ultimate resolution of the dispute. Also, we cannot assure you that we will not be exposed to claims or sanctions against us which may be costly or impossible for us to defend. The inability to retain the best legal counsel to represent our operating subsidiaries in infringement actions may result in unfavorable or adverse outcomes, which may result in losses, exhaustion of financial resources or other adverse effects which could encumber our ability to effectively operate our business or execute our business strategy.

Our operating subsidiaries, in certain circumstances, rely on representations, warranties and opinions made by third-parties that, if determined to be false or inaccurate, may expose us and our operating subsidiaries to certain material liabilities.

From time to time, our operating subsidiaries may rely upon representations and warranties made by third-parties from whom our operating subsidiaries acquired patents or the exclusive rights to license and enforce patents. We also may rely upon the opinions of purported experts. In certain instances, we may not have the opportunity to independently investigate and verify the facts upon which such representations, warranties, and opinions are made. By relying on these representations, warranties and opinions, our operating subsidiaries may be exposed to liabilities in connection with the licensing and enforcement of certain patents and patent rights which could have a material adverse effect on our operating results and financial condition.

In connection with patent enforcement actions conducted by certain of our subsidiaries, a court may rule that we or our subsidiaries have violated certain statutory, regulatory, federal, local or governing rules or standards, which may expose us and our operating subsidiaries to certain material liabilities.

In connection with any of our patent enforcement actions, it is possible that a defendant may request and/or a court may rule that we have violated statutory authority, regulatory authority, federal rules, local court rules, or governing standards relating to the substantive or procedural aspects of such enforcement actions. In such event, a court may issue monetary sanctions against us or our operating subsidiaries or award attorney's fees and/or expenses to a defendant(s), which could be material, and if we or our operating subsidiaries are required to pay such monetary sanctions, attorneys' fees and/or expenses, such payment could materially harm our operating results and our financial position.

In connection with patent enforcement actions conducted by certain of our subsidiaries, a court may find the patents invalid, not infringed or unenforceable and/or the U.S. Patent and Trademark Office, or the USPTO, or other relevant patent office, may either invalidate the patents or materially narrow the scope of their claims during the course of a reexamination, opposition or other such proceeding.

Patent litigation is inherently risky and the outcome is uncertain. Some of the parties that we believe infringe on our patents are large and well-financed companies with substantially greater resources than ours. We believe that these parties would devote a substantial amount of resources in an attempt to avoid or limit a finding that they are liable for infringing on our patents or, in the event liability is found, to avoid or limit the amount of associated damages. In addition, there is a risk that these parties may file reexaminations or other proceedings with the USPTO or other government agencies in the United States or abroad in an attempt to invalidate, narrow the scope or render unenforceable the patents we own or control. If this were to occur, it may have a material adverse effect on our operations.

In addition, it is difficult to predict the outcome of patent enforcement litigation at any level. In the United States, there is a higher rate of appeals in patent enforcement litigation than standard business litigation. The defendant to any case we bring, may file as many appeals as allowed by right, including to the first, second and/or final courts of appeal (in the United States those courts would be the Federal Circuit and Supreme Court, respectively). Such appeals are expensive and time-consuming, and the outcomes of such appeals are sometimes unpredictable, resulting in increased costs and reduced or delayed revenue which could have a material adverse effect on our operating results and financial condition.

Our licensing cycle is lengthy and costly, and our legal and sales efforts may be unsuccessful.

We expect our operating subsidiaries to incur significant general and administrative and legal expenses prior to entering into license agreements and generating license revenues. We also spend considerable resources educating prospective licensees on the benefits of a license arrangement with us. As such, we may incur significant losses in any

particular period before any associated revenue stream begins.

If our efforts to educate prospective licensees on the benefits of a license arrangement are unsuccessful, we may need to pursue litigation or other enforcement action to protect our patent rights. We may also need to litigate to enforce the terms of our existing license agreements, protect our trade secrets, or determine the validity and scope of the proprietary rights of others. Enforcement proceedings are typically protracted and complex. The costs are typically substantial, and the outcomes are unpredictable. Enforcement actions will divert our managerial, technical, legal and financial resources from business operations and there are no assurances that such enforcement actions will result in favorable results for us.

Failure to maintain effective internal control over our financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act could cause our financial reports to be inaccurate.

We are required pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, or Section 404, to maintain internal control over financial reporting and to assess and report on the effectiveness of those controls. This assessment includes disclosure of any material weaknesses identified by our management in our internal control over financial reporting.

Our management concluded that our internal control over financial reporting was effective as of December 31, 2018. However, there are inherent limitations on effectiveness of controls. Our management, including our chief intellectual property officer and corporate controller, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of the effectiveness of controls to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

If we are not able to maintain effective internal control over financial reporting, our financial statements, including related disclosures, may be inaccurate, which could have a material adverse effect on our business. Refer to Item 9A. "Controls and Procedures" for additional information related to the current period.

Our equity investments are subject to risks and we may experience significant financial losses.

As described herein, in August 2016, we invested in Veritone. In connection with this investment, we entered into an investment agreement and bridge financing with Veritone, investing approximately \$53.3 million in Veritone, comprised of common stock and warrants. In fiscal year 2018, we realized a loss of \$19.1 million on the sale of 2,700,000 shares of Veritone common stock at a weighted average price of \$7.07. As of December 31, 2018, the Company's investment in Veritone totaled \$7.5 million.

In addition, in June 2017, we made a \$2.25 million investment in Miso Robotics, as part of Miso Robotics' closing of \$3.1 million in Series A funding. In February 2018, we made an additional strategic equity investment totaling \$6.0 million in the Series B financing round for Miso Robotics.

Our equity investments are subject to a high degree of risk and could diminish our financial condition. Currently, none of our investees are profitable and have limited financial resources. The overall sustained economic uncertainty, as well as financial, operational and other difficulties encountered by certain companies in which we have equity investments increases the risk that the actual amounts realized in the future on our debt and equity investments will differ significantly from the fair values currently assigned to them. In addition, the companies in which we have equity investments may not be able to compete effectively or there may be insufficient demand for the services and products offered by these companies. These investments could also expose us to significant financial losses and may limit alternative uses of our capital resources. If our investees suffer losses, our financial condition could be materially adversely affected. In addition, applicable securities law restrictions and other factors may result in an inability to liquidate any equity components of our equity investments.

Risks Related to Our Industry

Our exposure to uncontrollable outside influences, including new legislation, court rulings or actions by the USPTO, could adversely affect our licensing and enforcement business and results of operations.

Our licensing and enforcement business is subject to numerous risks from outside influences, including the following:

New legislation, regulations or rules related to obtaining patents or enforcing patents could significantly increase our operating costs and decrease our revenue.

Our operating subsidiaries invest in patents with enforcement opportunities and spend a significant amount of resources to enforce those patents. If new legislation, regulations or rules are implemented by Congress, the USPTO or the courts that impact the patent application process, the patent enforcement process or the rights of patent holders, such changes could negatively affect our business. United States patent laws were amended with the enactment of the Leahy-Smith America Invents Act, or the America Invents Act, which took effect on March 16, 2013. The America Invents Act includes a number of significant changes to U.S. patent law. In general, the legislation attempts to address issues surrounding the enforceability of patents and the increase in patent litigation by, among other things, establishing new procedures for patent litigation. For example, the America Invents Act changes the way that parties may be joined in patent infringement actions, increasing the likelihood that such actions will need to be brought against individual allegedly-infringing parties by their respective individual

actions or activities. In addition, the America Invents Act enacted a new inter-partes review process, or IPR process, at the USPTO which can be, and often is, used by defendants, and other individuals and entities, to separately challenge the validity of any patent. The IPR process of the America Invents Act has in many instances increased costs for licensing and litigation and has resulted in the loss of certain portfolio patents which, in some cases, may have negatively impacted the value of those portfolios. The America Invents Act and its implementation has increased the uncertainties and costs surrounding the enforcement of our patented technologies, which in certain circumstances could have a material adverse effect on our business and financial condition.

The U.S. Department of Justice, or the DOJ, has conducted reviews of the patent system to evaluate the impact of patent assertion entities on industries in which those patents relate. It is possible that the findings and recommendations of the DOJ could impact the ability to effectively license and enforce standards-essential patents and could increase the uncertainties and costs surrounding the enforcement of any such patented technologies. Also, in 2014, the Federal Trade Commission, or FTC, initiated a study under Section 6(b) of the Federal Trade Commission Act to evaluate the patent assertion practice and market impact of Patent Assertion Entities, or PAEs. The FTC's initial notice and request for public comment relating to the PAE study appeared in the Federal Register on October 3, 2013. We received and responded to a request for information as part of this FTC study. The FTC study entitled, "Patent Assertion Entity Activity" was released in October 2016.

Finally, new rules regarding the burden of proof in patent enforcement actions could significantly increase the cost of our enforcement actions, and new standards or limitations on liability for patent infringement could negatively impact our revenue derived from such enforcement actions. In addition, recent federal court decisions have lowered the threshold for obtaining attorneys' fees in patent infringement cases and increased the level of deference given to a district court's fee-shifting determination. These decisions may make it easier for district courts to shift a prevailing party's attorneys' fees to a non-prevailing party if the district court believes that the case was weak or conducted in an abusive manner. As a result, defendants in patent infringement actions brought by non-practicing entities may elect not to settle because these decisions make it much easier for defendants to get attorneys' fees.

Changes in patent law could adversely impact our business.

Patent laws may continue to change, and may alter the historically consistent protections afforded to owners of patent rights. Such changes may not be advantageous for us and may make it more difficult to obtain adequate patent protection to enforce our patents against infringing parties. Increased focus on the growing number of patent-related lawsuits may result in legislative changes which increase our costs and related risks of asserting patent enforcement actions. For instance, the United States Congress has considered a bill that would require, among other things, non-practicing entities that bring patent infringement lawsuits to pay legal costs of the defendants, if the lawsuits are unsuccessful and certain standards are not met.

Trial judges and juries often find it difficult to understand complex patent enforcement litigation, and as a result, we may need to appeal adverse decisions by lower courts in order to successfully enforce our patents.

It is difficult to predict the outcome of patent enforcement litigation at the trial level. It is often difficult for juries and trial judges to understand complex, patented technologies, and as a result, there is a higher rate of successful appeals in patent enforcement litigation than more standard business litigation. Such appeals are expensive and time consuming, resulting in increased costs and delayed revenue. Although we diligently pursue enforcement litigation, we cannot predict with significant reliability the decisions made by juries and trial courts.

More patent applications are filed each year resulting in longer delays in getting patents issued by the USPTO.

Certain of our operating subsidiaries hold and continue to invest in pending patents. We have identified a trend of increasing patent applications each year, which we believe is resulting in longer delays in obtaining approval of pending patent applications. The application delays could cause delays in recognizing revenue from these patents and could cause us to miss opportunities to license patents before other competing technologies are developed or introduced into the market.

Federal courts are becoming more crowded, and as a result, patent enforcement litigation is taking longer.

Our patent enforcement actions are almost exclusively prosecuted in federal court. Federal trial courts that hear our patent enforcement actions also hear criminal cases. Criminal cases always take priority over our actions. As a result, it is difficult to predict the length of time it will take to complete an enforcement action. Moreover, we believe there is a trend in increasing numbers of civil lawsuits and criminal proceedings before federal judges and, as a result, we believe that the risk of delays in our patent enforcement actions will have a greater negative effect on our business in the future unless this trend changes.

Any reductions in the funding of the USPTO could have an adverse impact on the cost of processing pending patent applications and the value of those pending patent applications.

The assets of our operating subsidiaries consist of patent portfolios, including pending patent applications before the USPTO. The value of our patent portfolios is dependent upon the issuance of patents in a timely manner, and any reductions in the funding of the USPTO could negatively impact the value of our assets. Further, reductions in funding from Congress could result in higher patent application filing and maintenance fees charged by the USPTO, causing an increase in our expenses.

Competition is intense in the industries in which our subsidiaries do business and as a result, we may not be able to grow or maintain our market share for our technologies and patents.

We expect to encounter competition in the area of patent portfolio investments and enforcement. This includes competitors seeking to invest in the same or similar patents and technologies that we may seek to invest in. As new technological advances occur, many of our patented technologies may become obsolete before they are completely monetized. If we are unable to replace obsolete technologies with more technologically advanced patented technologies, then this obsolescence could have a negative effect on our ability to generate future revenues.

Our licensing business also competes with venture capital firms and various industry leaders for patent licensing opportunities. Many of these competitors may have more financial and human resources than we do. As we become more successful, we may find more companies entering the market for similar technology opportunities, which may reduce our market share in one or more technology industries that we currently rely upon to generate future revenue.

Our patented technologies face uncertain market value.

Our operating subsidiaries have invested in patents and technologies that may be in the early stages of adoption in the commercial and consumer markets. Demand for some of these technologies is untested and is subject to fluctuation based upon the rate at which our licensees will adopt our patents and technologies in their products and services.

Further, significant judgment is required in connection with estimates of the recoverability of the carrying value of our intangible patent assets, including estimates of market values, estimates of the amount and timing of future cash flows, and estimates of other factors that are used to determine the fair value and recoverability of the respective patent asset values. Developments with respect to ongoing patent litigation, patent challenges and re-exams, legislative and judicial decisions and other factors outside of our control, may unfavorably impact the validity, applicability, and enforceability of our patent assets, and therefore, negatively impact the future value of our patent portfolios. If certain of these unfavorable events occur, our estimates or related projections may change materially in future periods, and future intangible asset impairment tests may result in material charges to earnings.

As patent enforcement litigation becomes more prevalent, it may become more difficult for us to voluntarily license our patents.

We believe that the more prevalent patent enforcement actions become, the more difficult it will be for us to voluntarily license our patents. As a result, we may need to increase the number of our patent enforcement actions to cause infringing companies to license the patent or pay damages for lost royalties. This may increase the risks associated with an investment in our company.

Patent litigation trials and scheduled trial dates are subject to routine delay, and any such delays could adversely impact our business, results of operations and financial condition.

Patent infringement trials are components of our overall patent licensing process and are one of many factors that contribute to the existence of possible future revenue opportunities for us. Patent litigation schedules in general, and in particular trial dates, are subject to routine adjustment, and in most cases delay, as courts adjust their calendars or respond to requests from one or more parties. Trial dates often are rescheduled by the court for various reasons that are often unrelated to the underlying patent assets and typically for reasons that are beyond our control. As a result, to the extent such events are an indicator of possible future revenue opportunities for us, or other outcome determinative events, they may and often do change which can result in delay of the expected scheduled event. Any such delay could be significant and could affect the corresponding future revenue opportunities, thus adversely impacting our business, results of operations and financial condition.

The markets served by our operating subsidiaries are subject to rapid technological change, and if our operating subsidiaries are unable to develop and invest in new technologies and patents, our ability to generate revenues could be substantially impaired.

The markets served by our operating subsidiaries and their licensees frequently undergo transitions in which products rapidly incorporate new features and performance standards on an industry-wide basis. Products for communications applications and high-speed computing applications, as well as other applications covered by our operating subsidiaries' IP, are based on continually evolving industry standards. In addition, the communications industry is intensely competitive and has been impacted by price erosion, rapid technological change, short product life cycles, cyclical market patterns and increasing foreign and domestic competition. Our ability to compete in the future will depend on our ability to identify and ensure compliance with evolving industry standards. This will require our continued efforts and success in acquiring new patent portfolios with licensing and enforcement opportunities. If we are unable to invest in new patented technologies and patent portfolios, or to identify and ensure compliance with evolving industry standards, our ability to generate revenues could be substantially impaired and our business and financial condition could be materially harmed.

Uncertainty in global economic conditions could negatively affect our business, results of operations and financial condition.

Our revenue-generating opportunities depend on the use of our patented technologies by existing and prospective licensees, the overall demand for the products and services of our licensees, and on the overall economic and financial health of our licensees. If economic conditions do not continue to improve, or if they deteriorate, many of our licensees' customers, which may rely on credit financing, may delay or reduce their purchases of our licensees' products and services. In addition, the use or adoption of our patented technologies is often based on current and forecasted demand for our licensees' products and services in the marketplace and may require companies to make significant initial commitments of capital and other resources. If negative conditions in the global credit markets delay or prevent our licensees' and their customers' access to credit, overall consumer spending on the products and services of our licensees may decrease and the adoption or use of our patented technologies may slow, respectively. Further, if the markets in which our licensees' participate do not continue to improve, or deteriorate further, this could negatively impact our licensees' long-term sales and revenue generation, margins and operating expenses, which could in turn have an adverse effect on our business, results of operations and financial condition.

Risks Related to Our Common Stock

The availability of shares for sale in the future could reduce the market price of our common stock.

In the future, we may issue securities to raise cash for operations and patent portfolio investments. We may also pay for interests in additional subsidiary companies by using shares of our common stock or a combination of cash and shares of our common stock. We may also issue securities convertible into our common stock. Any of these events may dilute stockholders' ownership interests in our company and have an adverse impact on the price of our common stock.

In addition, sales of a substantial amount of our common stock in the public market, or the perception that these sales may occur, could reduce the market price of our common stock. This could also impair our ability to raise additional capital through the sale of our securities.

Delaware law and our charter documents contain provisions that could discourage or prevent a potential takeover of our company that might otherwise result in our stockholders receiving a premium over the market price of their shares.

Provisions of Delaware law and our certificate of incorporation and bylaws could make the acquisition of our company by means of a tender offer, proxy contest or otherwise, and the removal of incumbent officers and directors, more difficult. These provisions include:

Section 203 of the Delaware General Corporation Law, which prohibits a merger with a 15%-or-greater stockholder, such as a party that has completed a successful tender offer, until three years after that party became a 15%-or-greater stockholder;

amendment of our bylaws by the stockholders requires a two-thirds approval of the outstanding shares;

the authorization in our certificate of incorporation of undesignated preferred stock, which could be issued without stockholder approval in a manner designed to prevent or discourage a takeover;

provisions in our bylaws eliminating stockholders' rights to call a special meeting of stockholders, which could make it more difficult for stockholders to wage a proxy contest for control of our board of directors or to vote to repeal any of the anti-takeover provisions contained in our certificate of incorporation and bylaws; and

the division of our board of directors into three classes with staggered terms for each class, which could make it more difficult for an outsider to gain control of our board of directors.

Together, these provisions may make the removal of management more difficult and may discourage transactions that could otherwise involve payment of a premium over prevailing market prices for our common stock.

We may fail to meet market expectations because of fluctuations in quarterly operating results, which could cause the price of our common stock to decline.

Our reported revenues and operating results have fluctuated in the past and may continue to fluctuate significantly from quarter to quarter in the future. It is possible that in future periods, revenues could fall below the expectations of securities analysts or investors, which could cause the market price of our common stock to decline. The following are among the factors that could cause our operating results to fluctuate significantly from period to period:

the dollar amount of agreements executed in each period, which is primarily driven by the nature and characteristics of the technology being licensed and the magnitude of infringement associated with a specific licensee;

the specific terms and conditions of agreements executed in each period and the periods of infringement contemplated by the respective payments;

fluctuations in the total number of agreements executed;

fluctuations in the sales results or other royalty-per-unit activities of our licensees that impact the calculation of license fees due;

the timing of the receipt of periodic license fee payments and/or reports from licensees;

fluctuations in the net number of active licensees period to period;

costs related to investments, alliances, licenses and other efforts to expand our operations;

the timing of payments under the terms of any customer or license agreements into which our operating subsidiaries may enter;

we may elect to account for equity investments in companies where our investment gives us the ability to exercise significant influence over the operating and financial policies of the investee at fair value, which may result in significant fluctuations in operating results (unrealized gains and losses) each period based on fluctuations in the stock price of our investments and the requirement to mark such investments to market at each balance sheet date;

- expenses related to, and the timing and results of, patent filings and other enforcement proceedings relating to IP rights, as more fully described in this section; and

new litigation or developments in current litigation and the unpredictability of litigation results or settlements or appeals.

Technology company stock prices are especially volatile, and this volatility may depress the price of our common stock.

The stock market has experienced significant price and volume fluctuations, and the market prices of technology companies have been highly volatile. We believe that various factors may cause the market price of our common stock to fluctuate, perhaps substantially, including, among others, the following:

• announcements of developments in our patent enforcement actions;

• developments or disputes concerning our patents;

our or our competitors' technological innovations;

- developments in relationships with licensees;

variations in our quarterly operating results;

our failure to meet or exceed securities analysts' expectations of our financial results;

a change in financial estimates or securities analysts' recommendations;

changes in management's or securities analysts' estimates of our financial performance;

changes in market valuations of similar companies;

concerns about sovereign debt of the United States and the European Union;

announcements by us or our competitors of significant contracts, investments, partnerships, joint ventures, capital commitments, new technologies, or patents; and

failure to complete significant transactions.

For example, the NASDAQ-100 Technology Sector Index (NDXT) had a range of \$3,451.91 - \$4,544.46 during the 52-weeks ended December 31, 2018 and the NASDAQ Composite Index (IXIC) had a range of \$6,190.17-\$8,133.30 over the same period. Over the same period, our common stock fluctuated within a range of \$2.75 - \$4.40.

As noted above, our stock price, like many others, has fluctuated significantly in recent periods and if investors have concerns that our business, operating results and financial condition will be negatively impacted by industry, global economic or other negative conditions, our stock price could continue to fluctuate significantly in future periods.

In addition, we believe that fluctuations in our stock price during applicable periods can also be impacted by court rulings and/or other developments in our patent licensing and enforcement actions. Court rulings in patent enforcement actions are often difficult to understand, even when favorable or neutral to the value of our patents and our overall business, and we believe that investors in the market may overreact, causing fluctuations in our stock prices that may not accurately reflect the impact of court rulings on our business operations and assets.

In the past, companies that have experienced volatility in the market price of their stock have been the objects of securities class action litigation. If our common stock was the object of securities class action litigation, it could result in substantial costs and a diversion of management's attention and resources, which could materially harm our business and financial results.

We do not currently intend to pay dividends on our common stock in the foreseeable future, and consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.

On February 23, 2016, our board of directors eliminated our dividend policy that provided for the discretionary payment of a total annual cash dividend of \$0.50 per common share, payable in the amount of \$0.125 per share per quarter, effective as of February 23, 2016. As a result, we do not anticipate paying any cash dividends to holders of

our common stock in the foreseeable future. Consequently, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments. There is no guarantee that shares of our common stock will appreciate in value or even maintain the price at which our stockholders have purchased their shares.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our principal executive, corporate and administrative offices are located in Newport Beach, California, where we lease approximately 2,075 square feet of office space, under a lease agreement that expires in 2019. Our primary operating subsidiary, Acacia Research Group, LLC, and its subsidiaries, are headquartered in Frisco, Texas, where we lease office space under a lease agreement that expires in 2020. Certain of our operating subsidiaries also maintain additional office space in New York and Munich, Germany. We believe that our facilities are adequate, suitable and of sufficient capacity to support our immediate needs.

ITEM 3. LEGAL PROCEEDINGS

In the ordinary course of business, we are the subject of, or party to, various pending or threatened legal actions, including various counterclaims in connection with our patent enforcement activities. We believe that any liability arising from these actions will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

Our operating subsidiaries are often required to engage in litigation to enforce their patents and patent rights. Certain of our operating subsidiaries are parties to ongoing patent enforcement related litigation, alleging infringement by third-parties of certain of the patented technologies owned or controlled by our operating subsidiaries.

In connection with any of our patent enforcement actions, it is possible that a defendant may claim and/or a court may rule that we have violated statutory authority, regulatory authority, federal rules, local court rules, or governing standards relating to the substantive or procedural aspects of such enforcement actions. In such event, a court may issue monetary sanctions against us or our operating subsidiaries or award attorney's fees and/or expenses to a defendant(s), which could be material, and if required to be paid by us or our operating subsidiaries, could materially harm our operating results and our financial position.

We spend a significant amount of our financial and management resources to pursue our current litigation matters. We believe that these litigation matters and others that we may in the future determine to pursue could continue for years and continue to consume significant financial and management resources. The counterparties to our litigation are sometimes large, well-financed companies with substantially greater resources than us. We cannot assure you that any of our current or future litigation matters will result in a favorable outcome for us. In addition, in part due to the appeals process and other legal processes, even if we obtain favorable interim rulings or verdicts in particular litigation matters, they may not be predictive of the ultimate resolution of the dispute. Also, we cannot assure you that we will not be exposed to claims or sanctions against us which may be costly or impossible for us to defend. Unfavorable or adverse outcomes may result in losses, exhaustion of financial resources or other adverse effects which could encumber our ability to effectively and efficiently monetize our assets.

On June 17, 2015, Celltrace Communications Ltd., or Celltrace, filed a lawsuit against Acacia in U.S. District Court for the Southern District of New York, Case No. 1:15-cv-04746, alleging, among other things, significant damages for alleged breach of contract, unjust enrichment and fraud. Acacia disputes the allegations and does not believe that Celltrace is entitled to any damages. Acacia successfully moved to compel arbitration of the dispute, and the District Court stayed the litigation pending arbitration before the International Court of Arbitration for the International Chamber of Commerce, or the ICC. Celltrace appealed the decision to the U.S. Court of Appeals for the Second Circuit, which denied the appeal. Celltrace filed its request for arbitration of the claims with the ICC on November 28, 2016. Acacia filed an answer denying all allegations of wrongdoing and asserting affirmative defenses. A

tribunal was appointed to preside over the arbitration and conducted its first case management conference on June 26, 2017. The parties conducted discovery and submitted their cases in chief to the tribunal in a series of written submissions per the tribunal's orders between January 2018 and December 2018. The tribunal held an evidentiary hearing with live witness testimony in New York City between February 4, 2019 and February 13, 2019. At the end of the hearing, the tribunal set a schedule for post-hearing briefing by the parties, which is currently scheduled to conclude in April 2019, after which the tribunal will render a decision. Acacia continues to vigorously contest all allegations of wrongdoing.

ITEM 4. MINE SAFETY DISCLOSURES

None.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

General

Our common stock trades on The NASDAQ Global Select Market under the symbol "ACTG."

Dividend Policy

On April 23, 2013, we announced that our Board of Directors approved the adoption of a cash dividend policy that called for the payment of an expected total annual cash dividend of \$0.50 per common share, payable in the amount of \$0.125 per share per quarter. On February 23, 2016, our Board of Directors terminated the company's dividend policy due to a number of factors, including our financial performance, our available cash resources, our cash requirements and alternative uses of capital that our Board of Directors concluded would represent an opportunity to generate a greater return on investment for us and our stockholders.

The current policy of our Board of Directors is to retain earnings, if any, to provide for our growth. Consequently, we do not expect to pay any cash dividends in the foreseeable future. Further, there can be no assurance that our proposed operations will generate revenues and cash flow needed to declare any future cash dividends or that we will have legally available funds to pay future dividends.

Recent Sales of Unregistered Securities

None.

Stock Repurchase Program

In February 2018, our Board of Directors authorized a stock repurchase program, or the Program, to repurchase up to \$20 million of our outstanding common stock in open market purchases or private purchases, from time to time, in amounts and at prices to be determined by the Board of Directors at its discretion. In determining whether or not to repurchase any shares of our common stock, our Board of Directors will consider such factors as the impact of the repurchase on our cash position, as well as our capital needs and whether there is a better alternative use of our capital. In fiscal year 2018, we repurchased 1,190,420 shares of common stock at an average price of \$3.89 for \$4,634,000. All of these shares were repurchased during the second quarter of fiscal year 2018. The Program expired on February 28, 2019.

Holders of Common Stock

On March 11, 2019, there were approximately 49 owners of record of our common stock. The majority of the outstanding shares of our common stock are held by a nominee holder on behalf of an indeterminable number of ultimate beneficial owners.

ITEM 6. SELECTED FINANCIAL DATA

Not required for "smaller reporting companies."

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our consolidated financial statements included elsewhere in this Annual Report on Form 10-K. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors including the risks we discuss in Item 1A, "Risk Factors," and elsewhere herein.

General

We invest in intellectual property, or IP, and related absolute return assets and engage in the licensing and enforcement of patented technologies. We partner with inventors and patent owners, applying our legal and technology expertise to patent assets to unlock the financial value in their patented inventions. We generate revenues and related cash flows from the granting of patent rights for the use of patented technologies that our operating subsidiaries control or own. We assist patent owners with the prosecution and development of their patent portfolios, the protection of their patented inventions from unauthorized use, the generation of licensing revenue from users of their patented technologies and, where necessary, with the enforcement against unauthorized users of their patented technologies through the filing of patent infringement litigation. We are principals in the licensing and enforcement effort, obtaining control of the rights in the patent portfolio, or control of the patent portfolio outright.

We have a proven track record of licensing and enforcement success with over 1,560 license agreements executed to date, across nearly 200 patent portfolio licensing and enforcement programs. Currently, on a consolidated basis, our operating subsidiaries own or control the rights to multiple patent portfolios, which include U.S. patents and certain foreign counterparts, covering technologies used in a variety of industries. To date, we have generated gross licensing revenue of approximately \$1.6 billion, and have returned more than \$767 million to our patent partners.

Our business is described more fully in Item 1. "Business," of this annual report.

Executive Overview

For the years ended December 31, 2018 and 2017, we reported revenues of \$131.5 million and \$65.4 million. Cash and short-term investments totaled \$165.5 million as of December 31, 2018, as compared to \$136.6 million as of December 31, 2017. Our operating activities during the periods presented were focused on the continued operation of our patent licensing and enforcement business, including the continued pursuit of our ongoing patent licensing and enforcement programs. During 2018 and 2017, we also focused on cost reduction and optimization efforts, including reductions in headcount, renegotiation of certain existing arrangements, termination of certain patent licensing programs to maximize resource allocation, and reducing facilities costs.

Our team's expertise in identifying and evaluating complex IP, and in developing and cultivating long-term business relationships, provides us a unique window into innovation and technological advancement. We are increasing our efforts to leverage our expertise and experience to create new avenues and monetize our existing IP assets, which we believe will lead to increased shareholder value. We will leverage our experience, expertise, data and relationships developed as a leader in the IP industry to pursue these opportunities.

Enforcement Activities. As previously reported, in March 2017, our subsidiary, Saint Lawrence Communications, LLC, or Saint Lawrence, received a jury verdict in its case against Motorola, Inc. in the United States District Court for the Eastern District of Texas, or District Court. The jury returned a verdict that five U.S. patents were valid and

infringed. The jury found that the infringement was willful and returned a damages award of nearly \$9.2 million for past infringement. In addition, our German subsidiary, Saint Lawrence Communications GmbH, was granted injunctions by the German court in enforcement proceedings against Motorola, Inc. In the fourth quarter of 2018, Saint Lawrence and Saint Lawrence Communications GmbH entered into an agreement with Motorola, Inc. to resolve the patent litigation.

During the second quarter of 2017, Saint Lawrence resolved its enforcement actions against ZTE including the U.S. lawsuit. In February 2018, Saint Lawrence and Saint Lawrence Communications GmbH entered into an agreement with Apple Inc. to resolve all outstanding litigation.

As previously reported, in September 2016, our subsidiary Cellular Communications Equipment LLC, or CCE, received a jury verdict of infringement by Apple, Inc. In the third quarter of 2017, CCE entered into an agreement with Apple Inc. to resolve the patent litigation.

Investment in Veritone. In connection with its previous investment in Veritone in August 2016, Acacia received an aggregate total of 4,119,521 shares and 1,120,432 warrants of Veritone. In fiscal year 2018, Acacia sold 2,700,000 shares of Veritone common stock at a weighted average price of \$7.07 and recorded a realized loss of \$19.1 million on the sale. Refer to Note 6 to the consolidated financial statements elsewhere herein for additional information regarding our investment in Veritone.

Investment in Miso Robotics. In June 2017, Acacia made a \$2.25 million equity investment in Miso Robotics, as part of Miso Robotics' closing of \$3.1 million in Series A funding. In February 2018, we made an additional strategic equity investment totaling \$6.0 million in the Series B financing round for Miso Robotics. Refer to Note 6 to the consolidated financial statements elsewhere herein for additional information regarding our investment in Miso Robotics.

Patent Portfolio Intake. In fiscal year 2018, Acacia underwent a number of changes, including the establishment of a new IP team that is working to refill the patent portfolio intake pipeline. In addition, the Company has experienced substantial deal flow and is currently considering many late stage opportunities.

Operating activities during the periods presented included the following:

	2018	2017
Revenues (in thousands)	\$ 131,506	\$ 65,402
New agreements executed	12	20
Licensing and enforcement programs generating revenues - during the respective period	8	13
Licensing and enforcement programs with initial revenues	—	1
New patent portfolios	—	1
Year-end cash, cash equivalents and short-term investments	\$ 165,463	\$ 136,604

Our revenues historically have fluctuated period to period, and can vary significantly, based on a number of factors including the following:

- the dollar amount of agreements executed each period, which can be driven by the nature and characteristics of the technology or technologies being licensed and the magnitude of infringement associated with a specific licensee;
- the specific terms and conditions of agreements executed each period including the nature and characteristics of rights granted, and the periods of infringement or term of use contemplated by the respective payments;
- fluctuations in the total number of agreements executed each period;
- the number of, timing, results and uncertainties associated with patent licensing negotiations, mediations, patent infringement actions, trial dates and other enforcement proceedings relating to our patent licensing and enforcement programs;
- the relative maturity of licensing programs during the applicable periods;
- other external factors, including the periodic status or results of ongoing negotiations, the status or results of ongoing litigations and appeals, actual or perceived shifts in the regulatory environment, impact of unrelated patent related judicial proceedings and other macroeconomic factors;
- the willingness of prospective licensees to settle significant patent infringement cases and pay reasonable license fees for the use of our patented technology, as such infringement cases approached a court determined trial date; and
- fluctuations in overall patent portfolio related enforcement activities which are impacted by the portfolio intake challenges discussed above.

Our management does not attempt to manage for smooth sequential periodic growth in revenues period to period, and therefore, periodic results can be uneven. Unlike most operating businesses and industries, licensing revenues not generated in a current period are not necessarily foregone but, depending on whether negotiations, litigation or both continue into subsequent periods, and depending on a number of other factors, such potential revenues may be pushed into subsequent fiscal periods.

Summary of Results of Operations - For Fiscal Years 2018 and 2017
(In thousands, except percentage change values)

	Fiscal Year		%
	2018	2017	Change 2018 vs. 2017
Revenues	\$ 131,506	\$ 65,402	101 %
Inventor royalties and contingent legal fees	66,669	21,634	208 %
Litigation and licensing expenses - patents	8,866	18,219	(51)%
Amortization expense	27,120	22,154	22 %
Impairment of patent-related intangible assets	28,210	2,248	*
Other operating costs and expenses ⁽¹⁾	25,452	28,419	(10)%
Operating loss	(24,811)	(27,272)	(9)%
Total other income (expense)	(78,858)	51,911	(252)%
Provision for income taxes	(1,179)	(2,955)	(60)%
Net (income) loss attributable to noncontrolling interests in subsidiaries	(181)	496	(136)%
Net income (loss) attributable to Acacia Research Corporation	(105,029)	22,180	*

* Percentage change in excess of 300%

⁽¹⁾ Includes non-cash stock compensation charges (credits) of \$(317,000) and \$8.9 million in fiscal years 2018 and 2017, respectively, included in general and administrative expense in the consolidated statements of operations.

Overview - Fiscal Year 2018 compared with Fiscal Year 2017

Revenues increased \$66.1 million, or 101% to \$131.5 million, due primarily to an increase in average revenue per agreement. Refer to “*Investments in Patent Portfolios*” below for additional information regarding the impact of portfolio acquisition trends on current and future licensing and enforcement related revenues.

Loss before provision for income taxes was \$103.7 million for fiscal year 2018, as compared to income before provision for income taxes of \$24.6 million for fiscal year 2017. The net change was primarily comprised of the change in revenues described above, a net \$59.1 million unrealized loss on our equity investment in Veritone in fiscal year 2018, as compared to a net \$49.5 million gain in fiscal year 2017, and a net increase in operating expenses, as follows:

Inventor royalties and contingent legal fees, on a combined basis, increased \$45.0 million, or 208%. Contingent legal fees increased \$14.8 million, or 89%, as compared to a 101% increase in revenue due to lower average contingent legal fee rates for the portfolios generating revenues in fiscal year 2018. Inventor royalties increased \$30.2 million, or 610%, as compared to the 101% increase in revenue, primarily due to lower average inventor royalty rates for the portfolios generating revenues during fiscal year 2017.

Litigation and licensing expenses-patents decreased \$9.4 million, or 51%, to \$8.9 million, due primarily to a net decrease in litigation support and third-party technical consulting expenses associated with ongoing licensing and enforcement programs and an overall decrease in portfolio related enforcement activities. Refer to “*Investments in Patent Portfolios*” below for additional information regarding the impact of portfolio acquisition trends on licensing and enforcement activities and current and future licensing and enforcement related revenues.

Amortization expense increased \$5.0 million, or 22%, to \$27.1 million, due to accelerated amortization related to patent portfolio sales or dispositions during fiscal year 2018.

Impairment of patent-related intangible asset charges increased \$26.0 million. Impairment charges reflect the impact of reductions in expected estimated future net cash flows for certain patent portfolios and/or the impairment of certain portfolios that management determined it would no longer allocate resources to in future periods.

General and administrative expenses decreased \$8.4 million, or 31%, to \$18.9 million, due primarily to a decrease in non-cash stock compensation, a reduction in personnel costs in fiscal years 2018 and 2017, and a decrease in variable performance based compensation costs.

Excluding profits interests related non-cash stock compensation, non-cash stock compensation expense decreased \$3.7 million, or 64% due primarily to 2017 non-cash stock compensation expense including amounts related to the August 2016 grant of options with market-based vesting conditions which were fully expensed in fiscal year 2017. Profits interests related non-cash stock compensation expense decreased \$5.5 million, primarily due to the decrease in the fair value of our Veritone related profits interest units, consistent with the decrease in underlying Veritone stock price since December 31, 2017.

Other income (expense) for fiscal year 2018 included an unrealized loss on our investment in Veritone totaling \$59.1 million and a realized loss on the sale of Veritone totaling \$19.1 million. Other income (expense) for fiscal year 2017 comprised of an unrealized gain on conversion of our Veritone loans to equity of \$2.7 million and an unrealized gain on the exercise of our Primary Warrant of \$4.6 million, both as of May 2017, and an unrealized gain related to the change in fair value of our equity investment in Veritone through December 31, 2017 of \$42.2 million.

Tax expense for fiscal years 2018 and 2017 primarily reflects the impact of state taxes and foreign withholding taxes incurred on revenue agreements executed with third-party licensees domiciled in foreign jurisdictions.

Revenues for the periods presented included fees from the following licensing and enforcement programs:

Bone Wedge technology ⁽¹⁾⁽²⁾	Semiconductor Testing technology ⁽¹⁾
Cardiology and Vascular Device technology ⁽¹⁾⁽²⁾	Semiconductor and Memory-Related technology ⁽²⁾
DisplayPort and MIPI DSI technology ⁽²⁾	Shared Memory for Multimedia Processing ⁽²⁾
Electronic Access Control technology ⁽²⁾	Speech codes used in wireless and wireline systems technology ⁽¹⁾⁽²⁾
Innovative Display technology ⁽²⁾	Super Resolutions Microscopy technology ⁽¹⁾⁽²⁾
Online Auction Guarantee technology ⁽¹⁾⁽²⁾	Video Conferencing technology ⁽¹⁾⁽²⁾
Optical Networking technology ⁽²⁾	Wireless Infrastructure and User Equipment technology ⁽¹⁾⁽²⁾

⁽¹⁾ Licensing and enforcement program generating revenue in fiscal year 2018.

⁽²⁾ Licensing and enforcement program generating revenue in fiscal year 2017.

Revenues from one or more of our patents or patent portfolios may be significant in a specific reporting period, and may be significant to our licensing and enforcement business as a whole.

Patent Licensing and Enforcement

Patent Litigation Trial Dates and Related Trials. As of the date of this report, our operating subsidiaries have two pending patent infringement cases with a scheduled trial date in the next twelve months. Patent infringement trials are components of our overall patent licensing process and are one of many factors that contribute to possible future revenue generating opportunities for us. Scheduled trial dates, as promulgated by the respective court, merely provide an indication of when, in future periods, the trials may occur according to the court's scheduling calendar at a specific point in time. A court may change previously scheduled trial dates. In fact, courts often reschedule trial dates for various reasons that are unrelated to the underlying patent assets and typically for reasons that are beyond our control. While scheduled trial dates provide an indication of the timing of possible future revenue generating opportunities for us, the trials themselves and the immediately preceding periods represent the possible future revenue generating opportunities. These future opportunities can result in varying outcomes. In fact, it is difficult to predict the outcome of patent enforcement litigation at the trial level and outcomes can be unfavorable. It can be difficult to understand complex patented technologies, and as a result, this may lead to a higher rate of unfavorable litigation outcomes. Moreover, in the event of a favorable outcome, there is, in our experience, a higher rate of successful

appeals in patent enforcement litigation than more standard business litigation. Such appeals are expensive and time consuming, resulting in increased costs and a potential for delayed or foregone revenue opportunities in the event of modification or reversal of favorable outcomes. Although we diligently pursue enforcement litigation, we cannot predict with reliability the decisions made by juries and trial courts. Please refer to Item 1A. "Risk Factors" for additional information regarding trials, patent litigation and related risks.

Litigation and Licensing Expense. We expect patent-related legal expenses to continue to fluctuate from period to period based on the factors summarized herein, in connection with future trial dates, international enforcement, strategic patent

portfolio prosecution and our current and future patent portfolio investment, prosecution, licensing and enforcement activities. The pursuit of enforcement actions in connection with our licensing and enforcement programs can involve certain risks and uncertainties, including the following:

Increases in patent-related legal expenses associated with patent infringement litigation, including, but not limited to, increases in costs billed by outside legal counsel for discovery, depositions, economic analyses, damages assessments, expert witnesses and other consultants, re-exam and inter partes review costs, case-related audio/video presentations and other litigation support and administrative costs could increase our operating costs and decrease our profit generating opportunities;

Our patented technologies and enforcement actions are complex and, as a result, we may be required to appeal adverse decisions by trial courts in order to successfully enforce our patents. Moreover, such appeals may not be successful;

New legislation, regulations or rules related to enforcement actions, including any fee or cost shifting provisions, could significantly increase our operating costs and decrease our profit generating opportunities. Increased focus on the growing number of patent-related lawsuits may result in legislative changes which increase our costs and related risks of asserting patent enforcement actions. For instance, the United States House of Representatives passed a bill that would require non-practicing entities that bring patent infringement lawsuits to pay legal costs of the defendants, if the lawsuits are unsuccessful and certain standards are not met;

Courts may rule that our subsidiaries have violated certain statutory, regulatory, federal, local or governing rules or standards by pursuing such enforcement actions, which may expose us and our operating subsidiaries to material liabilities, which could harm our operating results and our financial position;

The complexity of negotiations and potential magnitude of exposure for potential infringers associated with higher quality patent portfolios may lead to increased intervals of time between the filing of litigation and potential revenue events (i.e. markman dates, trial dates), which may lead to increased legal expenses, consistent with the higher revenue potential of such portfolios; and

Fluctuations in overall patent portfolio related enforcement activities which are impacted by the portfolio intake challenges discussed above could harm our operating results and our financial position.

Investments in Patent Portfolios

One of the significant challenges in our industry continues to be quality patent intake due to the challenges and complexity associated with the current patent environment. In fiscal year 2018 we did not acquire any patent portfolios, compared to one portfolio during fiscal year 2017.

With respect to our licensing, enforcement and overall business, neither we nor our operating subsidiaries invent new technologies or products; rather, we depend upon the identification and investment in patents, inventions and companies that own intellectual property through our relationships with inventors, universities, research institutions, technology companies and others. If our operating subsidiaries are unable to maintain those relationships and identify and grow new relationships, then we may not be able to identify new technology-based patent opportunities for sustainable revenue and /or revenue growth.

Our current or future relationships may not provide the volume or quality of technologies necessary to sustain our licensing, enforcement and overall business. In some cases, universities and other technology sources compete against us as they seek to develop and commercialize technologies. Universities may receive financing for basic research in exchange for the exclusive right to commercialize resulting inventions. These and other strategies employed by potential partners may reduce the number of technology sources and potential clients to whom we can market our solutions. If we are unable to maintain current relationships and sources of technology or to secure new relationships and sources of technology, such inability may have a material adverse effect on our revenues, operating results, financial condition and ability to maintain our licensing and enforcement business.

Critical Accounting Policies

Our consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. In preparing these financial statements, we make assumptions, judgments and estimates that can have a significant impact on amounts reported in our consolidated financial statements. We base our assumptions, judgments and

estimates on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results could differ materially from these estimates under different assumptions or conditions. On a regular basis, we evaluate our assumptions, judgments and estimates and make changes accordingly.

We believe that, of the significant accounting policies discussed in Note 2 to our notes to consolidated financial statements, the following accounting policies require our most difficult, subjective or complex judgments:

- revenue recognition;
- stock-based compensation expense, including valuation of profits interests;
- valuation of long-lived and intangible assets including goodwill;
- valuation of investments; and
- accounting for income taxes.

We discuss below the critical accounting assumptions, judgments and estimates associated with these policies. Historically, our assumptions, judgments and estimates relative to our critical accounting policies have not differed materially from actual results. For further information on our critical accounting policies, refer to Note 2 to the notes to consolidated financial statements included herein.

Revenue Recognition

As described below, significant management judgment must be made and used in connection with the revenue recognized in any accounting period. Material differences may result in the amount and timing of revenue recognized or deferred for any period, if management made different judgments.

Revenue is recognized upon transfer of control of promised bundled IP rights and other contractual performance obligations to licensees in an amount that reflects the consideration we expect to receive in exchange for those IP Rights. Revenue contracts that provide promises to grant the right to use IP Rights as they exist at the point in time at which the IP Rights are granted, are accounted for as performance obligations satisfied at a point in time and revenue is recognized at the point in time that the applicable performance obligations are satisfied and all other revenue recognition criteria have been met.

For the periods presented, revenue contracts executed by the Company primarily provided for the payment of contractually determined, one-time, paid-up license fees in consideration for the grant of certain IP Rights for patented technologies owned or controlled by Acacia ("Paid-up Revenue Agreements"). Revenues also included license fees from sales-based revenue contracts, the majority of which were originally executed in prior periods, which provide for the payment of quarterly license fees based on quarterly sales of applicable product units by licensees ("Recurring Revenue Agreements"). Revenues may also include court ordered settlements or awards related to our patent portfolio ("Other Settlements") or sales of our patent portfolio ("Sales"). IP Rights granted included the following, as applicable: (i) the grant of a non-exclusive, retroactive and future license to manufacture and/or sell products covered by patented technologies, (ii) a covenant-not-to-sue, (iii) the release of the licensee from certain claims, and (iv) the dismissal of any pending litigation. The IP Rights granted were perpetual in nature, extending until the legal expiration date of the related patents. The individual IP Rights are not accounted for as separate performance obligations, as (i) the nature of the promise, within the context of the contract, is to transfer combined items to which the promised IP Rights are inputs and (ii) the Company's promise to transfer each individual IP right described above to the customer is not separately identifiable from other promises to transfer IP Rights in the contract.

Since the promised IP Rights are not individually distinct, the Company combined each individual IP right in the contract into a bundle of IP rights that is distinct, and accounted for all of the IP Rights promised in the contract as a single performance obligation. The IP Rights granted were “functional IP rights” that have significant standalone functionality. Acacia's subsequent activities do not substantively change that functionality and do not significantly affect the utility of the IP to which the licensee has rights. Acacia's operating subsidiaries have no further obligation with respect to the grant of IP Rights, including no express or implied obligation to maintain or upgrade the technology, or provide future support or services. The contracts provide for the grant (i.e., transfer of control) of the licenses, covenants-not-to-sue, releases, and other significant deliverables upon execution of the contract. Licensees legally obtain control of the IP Rights upon execution of the contract. As such, the earnings process is complete and revenue is recognized upon the execution of the contract, when collectability is probable and all other revenue recognition criteria have been met. Revenue contracts generally provide for payment of contractual amounts with 30-90 days of execution of the contract, or the end of the quarter in which the sale or usage occurs for Recurring Revenue Agreements. Contractual payments made by licensees are generally non-refundable.

For sales-based royalties, the Company includes in the transaction price some or all of an amount of estimated variable consideration to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not

occur when the uncertainty associated with the variable consideration is subsequently resolved. Notwithstanding, revenue is recognized for a sales-based royalty promised in exchange for a license of IP Rights when the later of (i) the subsequent sale or usage occurs, or (ii) the performance obligation to which some or all of the sales-based royalty has been allocated has been satisfied. Estimates are generally based on historical levels of activity, if available.

Revenues from contracts with significant financing components (either explicit or implicit) are recognized at an amount that reflects the price that a licensee would have paid if the licensee had paid cash for the IP Rights when they transfer to the licensee. In determining the transaction price, the Company adjusts the promised amount of consideration for the effects of the time value of money. As a practical expedient, the Company does not adjust the promised amount of consideration for the effects of a significant financing component if the Company expects, at contract inception, that the period between when the entity transfers promised IP Rights to a customer and when the customer pays for the IP Rights will be one year or less.

In general, the Company is required to make certain judgments and estimates in connection with the accounting for revenue contracts with customers. Such areas may include identifying performance obligations in the contract, estimating the timing of satisfaction of performance obligations, determining whether a promise to grant a license is distinct from other promised goods or services, evaluating whether a license transfers to a customer at a point in time or over time, allocating the transaction price to separate performance obligations, determining whether contracts contain a significant financing component, and estimating revenues recognized at a point in time for sales-based royalties.

For fiscal years 2018 and 2017, the majority of our revenue agreements provided for the payment to us of one-time, paid-up license fees in consideration for the grant of certain IP rights for patented technology rights owned by our operating subsidiaries. These rights were primarily granted on a perpetual basis, extending until the expiration of the underlying patents. Pursuant to the terms of these agreements, our operating subsidiaries have no further obligation with respect to the grant of the non-exclusive licenses, covenants-not-to-sue, releases, and other deliverables, including no express or implied obligation on our operating subsidiaries' part to maintain or upgrade the technology, or provide future support or services. The agreements provided for the grant of the licenses, covenants-not-to-sue, releases, and other significant contractual performance obligations upon execution of the agreement. As such, the earnings process was determined to be complete and revenue was recognized upon the execution of the agreements. Historically, term license agreements have not been a material component of our operating revenues, with the majority of license agreements being paid-up, perpetual license agreements.

Stock-based Compensation Expense

Equity Based Awards. Stock-based compensation payments to employees and non-employee directors are recognized as expense in the statements of operations. The compensation cost for all stock-based awards is measured at the grant date, based on the fair value of the award (determined using a Black-Scholes option pricing model for stock options and intrinsic value on the date of grant for nonvested restricted stock), and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award). Determining the fair value of stock-based awards at the grant date requires significant estimates and judgments, including estimating the market price volatility of our common stock, future employee stock option exercise behavior and requisite service periods.

The Financial Accounting Standards Board issued a new standard, effective January 1, 2017, that changes the accounting for certain aspects of share-based payments to employees, including allowing an employer to make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current generally accepted

accounting principles in the United States, or GAAP) or account for forfeitures when they occur. Effective January 1, 2017, we elected to account for forfeitures of awards as they occur. The prior standard required us to estimate the number of awards for which the requisite service period is expected to be rendered and base the accruals of compensation cost on the estimated number of awards that will vest. The adoption of this standard did not have a material impact on our consolidated financial statements.

During the year ended December 31, 2016, the Company granted stock options with market-based vesting conditions. The options with market-based vesting conditions vest based upon the Company achieving specified stock price targets over a four-year period. The effect of a market-based vesting condition is reflected in the estimate of the grant-date fair value of the options utilizing a Monte Carlo valuation technique. Compensation cost is recognized for an option with a market-based vesting condition provided that the requisite service is rendered, regardless of when, if ever, the market condition is satisfied. The service period for options with a market-based vesting condition is inferred from the application of the Monte Carlo valuation technique. The derived service period represents the duration of the median of the distribution of share price paths on which the market condition is satisfied. The duration is the period of time from the service inception date to the expected date of satisfaction, as determined from the valuation technique.

Profits Interests Units. In February 2017, AIP Operation LLC, or AIP, an indirect subsidiary of ours, adopted a Profits Interests Plan, or the Profits Interests Plan, that provides for the grant of AIP membership interests in the form of profits interests to certain members of management and the Board of Directors of Acacia Research Corporation as compensation for services rendered. As of December 31, 2018 and 2017, AIP held the Veritone 10% Warrant described in Note 6.

For the year ended December 31, 2018, the fair value of the Units was estimated at 40% of the fair value of the 10% Warrant, based on the Black-Scholes option-pricing model (Level 2). For the year ended December 31, 2017, the fair value of the Units was estimated based on probable vesting dates and values for the applicable instruments (i.e. common stock and warrants related to Acacia's Veritone investment described at Note 6) underlying or associated with the Units (Level 3).

Valuation of Long-lived and Intangible Assets

Patent Portfolio Impairment Testing. We review long-lived assets and intangible assets for potential impairment annually (quarterly for patents) and when events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. In the event the expected undiscounted future cash flows resulting from the use of the asset is less than the carrying amount of the asset, an impairment loss is recorded equal to the excess of the asset's carrying value over its fair value. If an asset is determined to be impaired, the loss is measured based on quoted market prices in active markets, if available. If quoted market prices are not available, the estimate of fair value is based on various valuation techniques, including a discounted value of estimated future cash flows.

For the fiscal year ended December 31, 2018 and 2017, we recorded \$28.2 million and \$2.2 million, respectively of patent portfolio impairment charges. The impairment charges were recorded in the periods due to adverse litigation outcomes, a reduction in expected estimated future net cash flows and certain patent portfolios that management determined it would no longer allocate future resources to in connection with the licensing and enforcement of such portfolios. The impairment charges consisted of the excess of the asset's carrying value over its estimated fair value as of the applicable measurement date. Estimated fair value was determined based on estimates of future cash flows and estimates of probabilities of realization given adverse litigation outcomes and resource allocation decisions.

Investments

Investment in Veritone. We have elected to account for equity investments in companies with readily determinable fair values, where our investment gives us the ability to exercise significant influence over the operating and financial policies of the investee, at fair value. If the fair value option is applied to an investment that would otherwise be accounted for under the equity method of accounting, it is applied to all of the financial interests in the same entity that are eligible items (i.e. common stock and warrants). Refer to Note 6 for information regarding our investment in Veritone.

Determination of whether we possess the ability to exercise significant influence requires significant judgment, including consideration of the extent to which our voting interests, board representation, financial arrangements and other factors provide us with the ability to exercise significant influence with respect to an investee. A change in facts or judgments resulting in the determination that control exists would result in consolidation of the investment and recognition of related revenues and expenses with a corresponding non-controlling interest.

U.S. GAAP defines fair value as the price that would be received for an asset or the exit price that would be paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants

on the measurement date, and also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs, where available. The three-level hierarchy of valuation techniques established to measure fair value includes: Level 1 - Observable Inputs; Level 2 - Pricing Models with Significant Observable Inputs; and Level 3 - Unobservable Inputs. Refer to Note 2 to the consolidated financial statements elsewhere herein for additional information.

Whenever possible, we are required to use observable market inputs (Level 1 - quoted market prices) when measuring fair value. Our Veritone common stock is reported at fair value, based on the applicable NASDAQ Global Select Market stock price as of the applicable valuation date, as adjusted for an estimated DLOM (2017 only) associated with the restricted nature of the common stock acquired (Level 3 input). Acacia's investment in Veritone warrants is recorded at fair value, based on the Black-Scholes option-pricing model, as adjusted for an estimated DLOM (2017 only). A one percent increase in the DLOM assumptions utilized at December 31, 2017 would result in a \$1.1million decrease in the fair value of our investment in Veritone at December 31, 2017, and a corresponding decrease in the net unrealized investment gain reflected in the consolidated statements of operations for the year ended December 31, 2017.

Investment in Miso Robotics. In June 2017, we made an investment in the Series A Preferred financing round for Miso Robotics, an innovative leader in robotics and AI solutions, totaling \$2,250,000, acquiring a 22.6% ownership interest in Series A preferred stock of Miso Robotics, and one board seat. In February 2018, we made an additional equity investment in the Series B Preferred financing round for Miso Robotics totaling \$6,000,000, increasing our ownership interest (Series B preferred stock) in Miso Robotics to approximately 30%, and acquiring an additional board seat. As of February 2018, the preferred stock was not deemed to be in-substance common stock due to the substantive liquidation preference associated with the preferred stock. As such, as of February 2018, our investment in Miso Robotics is recorded at cost and assessed for any impairment at each balance sheet date. Prior to February 2018, the equity method of accounting was applied.

Equity investments in common stock and in-substance common stock without readily determinable fair values in companies over which we have the ability to exercise significant influence, are accounted for using the equity method of accounting. In-substance common stock is an investment in an entity that has risk and reward characteristics that are substantially similar to that entity's common stock. An investment in preferred stock with substantive liquidation preferences over common stock, are not substantially similar to the common stock, and therefore is not considered in-substance common stock. A liquidation preference is substantive if the investment has a stated liquidation preference that is significant, from a fair value perspective, in relation to the purchase price of the investment. A liquidation preference in an investee that has sufficient subordinated equity from a fair value perspective is substantive because, in the event of liquidation, the investment will not participate in substantially all of the investee's losses. Investments in preferred stock with substantive liquidation preferences, and therefore not deemed to be in-substance common stock, are accounted for at cost (subject to impairment considerations, if any), as adjusted for the impact of changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer.

Determination of whether an equity investment is in-substance common stock requires significant judgment, including an estimation of the fair value of the equity investments in relation to the fair value of subordinated equity of the investee, if any. A change in estimates or judgments resulting in the determination that an equity investment is or is not in-substance common stock would result in the application of either the equity method of accounting, or the cost method of accounting to the investment.

The fair value of subordinated equity (i.e., common stock) and preferred stock for purposes of determining whether a liquidation preference is substantive was determined utilizing an option pricing methodology, including a discount for lack of marketability. A one percent change in the DLOM assumptions utilized to estimate the fair value of common stock would not have a material impact on the analysis.

We review investments quarterly for indicators of other-than-temporary impairment. This determination requires significant judgment. In making this judgment, we consider available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds its fair value, we evaluate, among other factors, general market conditions and the duration and extent to which the fair value is less than cost. We also consider specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, and operational and financing cash flow factors. Once a decline in fair value is determined to be other-than-temporary, an impairment charge is recorded to other income (expense) and a new cost basis in the investment is established. If market, industry, and/or investee conditions deteriorate, we may incur future impairments.

Accounting for Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves the estimating of our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the consolidated statements of operations.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and our valuation allowance. Due to uncertainties related to our ability to utilize certain deferred tax assets in future periods, we have recorded a full valuation allowance against our net deferred tax assets as of December 31, 2018 and 2017. These assets primarily consist of foreign tax credits, capital loss carryforwards and net operating loss carryforwards.

In assessing the need for a valuation allowance, management has considered both the positive and negative evidence available, including but not limited to, estimates of future taxable income and related probabilities, estimates surrounding the

character of future income and the timing of realization, consideration of the period over which our deferred tax assets may be recoverable, our recent history of net income and prior history of losses, projected future outcomes, industry and market trends and the nature of existing deferred tax assets. In management's estimate, any positive indicators, including forecasts of potential future profitability of our businesses, are outweighed by the uncertainties surrounding our estimates and judgments of potential future taxable income, primarily due to uncertainties surrounding the timing of realization of future taxable income and the character of such income in particular future periods (i.e. foreign or domestic). In the event that actual results differ from these estimates or we adjust these estimates should we believe we would be able to realize these deferred tax assets in the future, an adjustment to the valuation allowance would increase income in the period such determination was made.

In fiscal years 2018 and 2017, based on management's assessment, a full valuation allowance was recorded against the company's net deferred tax assets generated during the periods and the balances as of the end of each of the periods, due to uncertainty regarding future realization of such tax assets pursuant to guidance set forth in ASC 740, "Income Taxes." In future periods, if we determine that the company will more likely than not be able to realize certain of these amounts, the applicable portion of the benefit from the release of the valuation allowance will generally be recognized in the statements of operations in the period the determination is recorded.

Any changes in the judgments, assumptions and estimates associated with our analysis of the need for a valuation allowance in any future periods could materially impact our financial position and results of operations in the periods in which those determinations are made.

Consolidated Results of Operations

Comparison of the Results of Operations for Fiscal Years 2018 and 2017

Revenues

			2018 vs. 2017	
	2018	2017	\$	%
			Change	Change
	(in thousands, except percentage change values and number of agreements)			
Revenues	\$131,506	\$65,402	\$66,104	101 %
New revenue agreements executed	12	20		
Average revenue per agreement	\$10,959	\$3,270		

A reconciliation of the change in revenues (based on average revenue per agreement) for the periods presented, in relation to the revenues reported for the comparable prior year period, is as follows:

	2018 vs. 2017 (in thousands)
Decrease in number of agreements executed	\$ (26,160)
Increase in average revenue per agreement executed	92,267
Total	\$ 66,107

Three licensees individually accounted for 45%, 17% and 17%, respectively, of revenues recognized during the year ended December 31, 2018. Three licensees individually accounted for 54%, 21% and 10%, respectively, of revenues

recognized during the year ended December 31, 2017.

For the periods presented herein, the majority of the revenue agreements executed provided for the payment of one-time, paid-up license fees in consideration for the grant of certain IP rights for patented technology rights owned by our operating subsidiaries. These rights were primarily granted on a perpetual basis, extending until the expiration of the underlying patents. Refer to “*Investments in Patent Portfolios*” above for information regarding the impact of portfolio acquisition trends on current and future licensing and enforcement related revenues.

Net Income (Loss)

			2018 vs. 2017	
	2018	2017	\$ Change	% Change
	(in thousands, except percentages)			
Net income (loss) attributable to Acacia Research Corporation	\$(105,029)	\$22,180	\$(127,209)	(574)%

A reconciliation of the change in net income (loss) for the periods presented is as follows:

	2018 vs. 2017	
	(in thousands, except percentage values)	%
Increase in revenues	\$66,104	(52)%
Increase in inventor royalties and contingent legal fees combined	(45,035)	35 %
Decrease in general and administrative expenses	8,369	(7)%
Decrease in litigation and licensing expenses	9,353	(7)%
Increase in patent amortization expenses	(4,966)	4 %
Increase in impairment of patent-related intangible assets	(25,962)	20 %
Change in provision for income taxes	1,776	(1)%
Unrealized gain (loss) and change in fair value of investment	(108,629)	85 %
Loss on sale of investment	(19,095)	15 %
Other	(9,124)	8 %
Net change in net income (loss)	\$(127,209)	100 %

Cost of Revenues

			2018 vs. 2017	
	2018	2017	\$ Change	% Change
	(in thousands, except percentages)			
Inventor royalties	\$35,168	\$4,952	\$30,216	610 %
Contingent legal fees	31,501	16,682	14,819	89 %
Patent acquisition expenses	4,000	—	4,000	— %
Litigation and licensing expenses - patents	8,866	18,219	(9,353)	(51)%
Amortization of patents	27,120	22,154	4,966	22 %

Inventor Royalties, Contingent Legal Fees Expense and Other Patent Acquisition Costs. The economic terms of patent portfolio related partnering agreements and contingent legal fee arrangements, if any, including royalty obligations, if any, royalty rates, contingent fee rates and other terms and conditions, vary across the patent portfolios owned or controlled by our operating subsidiaries. In certain instances, we have invested in certain patent portfolios without future inventor royalty obligations. These costs fluctuate period to period, based on the amount of revenues recognized each period, the terms and conditions of revenue agreements executed each period and the mix of specific patent portfolios with varying economic terms, conditions and obligations generating revenues each period. Fiscal year 2018 included \$4.0 million in other direct costs of revenues related to patent rights acquired and licensed in 2018.

Litigation and Licensing Expenses - Patents. Litigation and licensing expenses-patents include patent-related litigation, enforcement and prosecution costs incurred by external patent attorneys engaged on an hourly basis and the

out-of-pocket expenses incurred by law firms engaged on a contingent fee basis. Litigation and licensing expenses-patents also includes third-party patent research, development, prosecution, re-exam and inter partes reviews, consulting, and other costs incurred in connection with the licensing and enforcement of patent portfolios.

Litigation and licensing expenses-patents decreased for the periods presented due to a net decrease in litigation support, patent prosecution and litigation expenses associated with ongoing licensing and enforcement programs and an overall decrease in portfolio related enforcement activities. We expect patent-related legal expenses to continue to decrease based upon

the overall decrease in portfolio related enforcement activities as we continue monetizing our existing patent assets. Refer to “*Investments in Patent Portfolios*” above for additional information regarding the impact of portfolio acquisition trends on licensing and enforcement activities and current and future licensing and enforcement related revenues.

Amortization of Patents. The change in amortization expense for the comparable periods presented was due to the following:

	2018 vs. 2017 (in thousands)
Scheduled amortization related to patent portfolios owned or controlled as of the end of the prior year	\$ (3,341)
Patent portfolio sales and dispositions	8,307
Total change in patent amortization expense	\$ 4,966

Impairment Charges

	2018	2017	2018 vs. 2017 \$ % Change Change
	(in thousands, except percentages)		
Impairment of patent-related intangible assets	\$28,210	\$2,248	\$25,962 1,155 %

Patent Impairment Charges

Impairment charges for fiscal year 2018 and 2017 primarily reflect reductions in expected estimated future net cash flows for certain patent portfolios to which management determined it would no longer allocate resources in future periods. Impairment charges consisted of the excess of the asset’s carrying value over its estimated fair value as of the applicable measurement date.

Operating Expenses

	2018	2017	2018 vs. 2017 \$ % Change Change
	(in thousands, except percentages)		
General and administrative	\$19,167	\$18,334	\$833 5 %
Non-cash stock compensation expense - G&A	2,133	5,844	(3,711) (64)%
Non-cash stock compensation expense - Veritone Profits Interests	(2,450)	3,041	(5,491) (181)%
Total general and administrative expenses	\$18,850	\$27,219	\$(8,369) (31)%

General and Administrative Expenses. General and administrative expenses include employee compensation and related personnel costs, including variable performance based compensation and non-cash stock compensation expenses, office and facilities costs, legal and accounting professional fees, public relations, marketing, stock administration, business development, state taxes based on gross receipts and other corporate costs. A summary of the main drivers of the change in

general and administrative expenses for the periods presented is as follows (in thousands):

2018 vs. 2017		
(in thousands)		
Net change in personnel costs	\$ (1,102)
Variable performance-based compensation expense	(278)
Corporate, general and administrative expense	2,194	
Business development expense	(412)
Non-cash stock compensation expense - general and administrative ⁽¹⁾	(3,711)
Non-cash stock compensation expense - Veritone related profits interests ⁽¹⁾	(5,491)
Employee severance costs	431	
Total change in general and administrative expenses	\$ (8,369)

(1) - Refer to Note 9 in the accompany consolidated financial statements

General and administrative non-cash stock compensation expense for fiscal year 2018, excluding profits interests related non-cash compensation, decreased due to reductions in headcount and a \$2.4 million reduction in scheduled non-cash stock compensation expense related to options with market-based performance conditions with graded vesting features that resulted in higher non-cash stock compensation expense in fiscal year 2017, as compared to fiscal year 2018.

Profits interests are classified as liability awards, which are measured at fair value on the grant date and re-measured each reporting period at fair value until the award is settled. Compensation expense (included in “non-cash stock compensation expense - Veritone related profits interests” above) is adjusted each reporting period for increases or decreases in the estimated fair value, which is primarily impacted by changes in the fair value of the underlying Veritone common stock and warrants related to the liability. Upon vesting of the units, which occurred in September 2017, any previously unrecognized compensation expense was immediately recognized for any changes in fair value. The fair value of the Veritone related profits interests Units totaled \$591,000 and \$3.0 million as of December 31, 2018 and 2017, respectively. Refer to Note 9 in the condensed consolidated financial statements elsewhere herein for additional information.

Other Operating Income (Expense)

Change in Fair Value of Investment, net. Our equity investment in Veritone is recorded at fair value, and therefore, is marked to market at each balance sheet date. Results for fiscal year 2018 included a net unrealized loss on our equity investment in Veritone totaling \$59.1 million and a realized loss of \$19.1 million on the sale of 2,700,000 shares of Veritone common stock at a weighted average price of \$7.07. Results for fiscal year 2017 included a net unrealized gain on our equity investment in Veritone totaling \$49.5 million, comprised of an unrealized gain on conversion of our Veritone loans to equity of \$2.7 million and an unrealized gain on the exercise of our Primary Warrant of \$4.6 million, both as of May 2017, and an unrealized gain related to the change in fair value of our equity investment in Veritone through December 31, 2017 of \$42.2 million.

Other. Fiscal year 2018 and 2017 operating expenses included expenses for court ordered attorney fees and settlement and contingency accruals totaling \$2.6 million and \$1.2 million, respectively.

Income Taxes

	2018	2017
Provision for income taxes (in thousands)	\$(1,179)	\$(2,955)
Effective tax rate	1 %	12 %

Our effective tax rates for fiscal year 2018 and 2017, were primarily comprised of foreign taxes withheld on revenue agreements with licensees in foreign jurisdictions, state taxes, and the impact of full valuation allowances recorded for net operating loss (2018 and 2017) and foreign tax credit related tax assets generated in those periods due to uncertainty regarding future realization. Foreign taxes withheld related to revenue agreements executed with third-party licensees domiciled in certain foreign jurisdictions for fiscal year 2018 and 2017 totaled \$1.1 million and \$2.9 million, respectively. Results for fiscal year 2017 included an unrealized gain on our equity investment in Veritone which created a deferred tax liability totaling approximately \$10.6 million. The future anticipated reversal of this deferred tax liability provides for a source of taxable

income that allows for the realizability of existing deferred tax assets that have been reduced by a valuation allowance for the periods presented. The effective tax rate reflects both the recognition of the deferred tax liability and the reversal of valuation allowance.

Inflation

Inflation has not had a significant impact on us or any of our subsidiaries in the current or prior periods.

Liquidity and Capital Resources

General

Our primary sources of liquidity are cash and cash equivalents on hand generated from our operating activities. Our management believes that our cash and cash equivalent balances and anticipated cash flows from operations will be sufficient to meet our cash requirements through at least March 2020 and for the foreseeable future. We may, however, encounter unforeseen difficulties that may deplete our capital resources more rapidly than anticipated, including those set forth under Item 1A, “Risk Factors”, above. Any efforts to seek additional funding could be made through issuances of equity or debt, or other external financing. However, additional funding may not be available on favorable terms, or at all. The capital and credit markets have experienced extreme volatility and disruption in recent years, and the volatility and impact of the disruption may continue. At times during this period, the volatility and disruption has reached unprecedented levels. In several cases, the markets have exerted downward pressure on stock prices and credit capacity for certain issuers, and the commercial paper markets may not be a reliable source of short-term financing for us. If we fail to obtain additional financing when needed, we may not be able to execute our business plans and our business, conducted by our operating subsidiaries, may suffer.

Certain of our operating subsidiaries are often required to engage in litigation to enforce their patents and patent rights. In connection with any of our operating subsidiaries’ patent enforcement actions, it is possible that a defendant may request and/or a court may rule that an operating subsidiary has violated statutory authority, regulatory authority, federal rules, local court rules, or governing standards relating to the substantive or procedural aspects of such enforcement actions. In such event, a court may issue monetary sanctions against us or our operating subsidiaries or award attorney’s fees and/or expenses to a defendant(s), which could be material.

Cash, Cash Equivalents and Investments

Our consolidated cash and cash equivalents and short-term investments totaled \$165.5 million at December 31, 2018, compared to \$136.6 million at December 31, 2017. The net change in cash and cash equivalents for the periods presented was comprised of the following (in thousands):

	2018	2017
Net cash provided by (used in):		
Operating activities	\$20,877	\$12,966
Investing activities	(24,066)	(16,114)
Financing activities	(4,606)	700
	\$(7,795)	\$(2,448)

Cash Flows from Operating Activities. Cash receipts from licensees totaled \$103.4 million and \$91.2 million in fiscal years 2018 and 2017, respectively. The fluctuations in cash receipts for the periods presented primarily reflects the

corresponding fluctuations in revenues recognized during the same periods, as described above, and the related timing of payments received from licensees. Cash outflows from operations totaled \$82.5 million and \$66.8 million in fiscal years 2018 and 2017, respectively. The fluctuations in cash outflows for the periods presented reflects the fluctuations in revenue-related inventor royalties and contingent legal fees and other operating costs and expenses during the same periods, as discussed above, and the impact of the timing of payments to inventors, attorneys and other vendors.

Cash Flows from Investing Activities. Cash flows from investing activities and related changes were comprised of the following for the periods presented (in thousands):

	2018	2017
Investment in Investees ⁽¹⁾	\$(7,000)	\$(31,514)
Sale of investment ⁽¹⁾	19,097	—
Advances to Investee ⁽¹⁾	—	(4,000)
Purchases of property and equipment	(34)	(2)
Net sale (purchase) of available-for-sale investments	(36,129)	19,402
Net cash used in investing activities	\$(24,066)	\$(16,114)

(1) - Refer to Note 6 in the accompany consolidated financial statements

Investment in Veritone. In connection with its previous investment agreement with Veritone in August 2016, in fiscal year 2017 Acacia entered into an additional secured convertible promissory note with Veritone and advanced \$4.0 million. In addition, upon the consummation of Veritone's IPO, Acacia exercised its option to purchase an additional 2,150,335 shares of Veritone common stock, at an aggregate purchase price of \$29.3 million. Acacia received an aggregate total of 4,119,521 shares of common stock and 1,120,432 warrants of Veritone. In fiscal year 2018, Acacia sold 2,700,000 shares of Veritone common stock at a weighted average price of \$7.07 and recorded a realized loss of \$19.1 million on the sale. Refer to Note 6 to the consolidated financial statements elsewhere herein for additional information regarding our investment with Veritone.

Investment in Miso Robotics. In June 2017, Acacia made a \$2.25 million equity investment in Miso Robotics, as part of Miso Robotics' closing of \$3.1 million in Series A funding. In February 2018, we made an additional strategic equity investment totaling \$6.0 million in the Series B financing round for Miso Robotics. Refer to Note 6 to the consolidated financial statements elsewhere herein for additional information regarding our investment in Miso.

Cash Flows from Financing Activities. Cash flows from financing activities and related changes included the following for the periods presented (in thousands):

	2018	2017
Repurchase of common stock	\$(4,634)	\$—
Proceeds from the exercise of stock options	257	745
Repurchases of common stock	(229)	(45)
Net cash provided by financing activities	\$(4,606)	\$700

Stock Repurchase Program. In February 2018, our Board of Directors authorized the Program to repurchase up to \$20 million of our outstanding common stock in open market purchases or private purchases, from time to time, in amounts and at prices to be determined by the Board of Directors at its discretion. In determining whether or not to repurchase any shares of our common stock, our Board of Directors will consider such factors as the impact of the repurchase on our cash position, as well as our capital needs and whether there is a better alternative use of our capital. We have no obligation to repurchase any amount of our common stock under the Program. In fiscal year 2018, we repurchased 1,190,420 shares at an average price of \$3.89 for \$4,634,000. The Program expired on February 28, 2019.

Working Capital

The primary components of working capital are cash and cash equivalents, short-term investments, accounts receivable, prepaid expenses, accounts payable, accrued expenses, and royalties and contingent legal fees payable. Working capital at December 31, 2018 was \$170.4 million, compared to \$130.1 million at December 31, 2017.

Consolidated accounts receivable from licensees increased to \$32.9 million at December 31, 2018, compared to \$153,000 at December 31, 2017. Accounts receivable balances fluctuate based on the timing, magnitude and payment terms associated with revenue agreements executed during the year, and the timing of cash receipts on accounts receivable balances recorded in previous periods. Four licensees individually represented approximately 38%, 36%, 12% and 11%, respectively, of accounts receivable at December 31, 2018. One licensee accounted for 100% of accounts receivable at December 31, 2017.

Accounts payable and accrued expenses increased slightly to \$8.3 million at December 31, 2018, from \$8.0 million at December 31, 2017.

Consolidated royalties and contingent legal fees payable increased to \$22.7 million at December 31, 2018, compared to \$1.6 million at December 31, 2017. Royalties and contingent legal fees payable balances fluctuate based on the magnitude and timing of the execution of related license agreements, the timing of cash receipts for the related license agreements, and the timing of payment of current and prior period royalties and contingent legal fees payable to inventor and outside attorneys, respectively.

All of accounts receivable from licensees at December 31, 2018 are scheduled to be collected in the first and second quarter of 2019, in accordance with the terms of the related underlying license agreements. The majority of royalties and contingent legal fees payable are scheduled to be paid through the third quarter of 2019 in accordance with the underlying contractual arrangements.

Off-Balance Sheet Arrangements

We have not entered into off-balance sheet financing arrangements, other than operating leases.

Uncertain Tax Positions. At December 31, 2018, we had total unrecognized tax benefits of approximately \$808,000 million, including a recorded noncurrent liability of \$85,000 related to unrecognized tax benefits primarily associated with state taxes. No interest and penalties have been recorded for the unrecognized tax benefits as of December 31, 2018. If recognized, approximately \$1.4 million would impact our effective tax rate. We do not expect that the liability for unrecognized tax benefits will change significantly within the next 12 months.

Recent Accounting Pronouncements

Refer to Note 2 to our notes to consolidated financial statements included elsewhere herein.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The primary objective of our short-term investment activities is to preserve principal while concurrently maximizing the income we receive from our short-term investments without significantly increasing risk. Some of the securities that we invest in may be subject to interest rate risk and/or market risk. This means that a change in prevailing interest rates, with respect to interest rate risk, or a change in the value of the United States equity markets, with respect to market risk, may cause the principal amount or market value of the short-term investments to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the current value of the principal amount of our investment may decline. To minimize these risks in the future, we intend to maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, money market funds, high-grade corporate bonds, government and non-government debt securities and certificates of deposit.

At December 31, 2018, our short-term investments were comprised of AAA rated money market funds that invest in first-tier only securities, which primarily include domestic commercial paper, securities issued or guaranteed by the U.S. government or its agencies, U.S. bank obligations, and fully collateralized repurchase agreements (included in cash and cash equivalents in the accompanying consolidated balance sheets), and direct investments in short term, highly liquid, investment grade, U.S. government and corporate securities (included in short-term investments in the accompanying consolidated balance sheets). Short-term investment balances were zero at December 31, 2017.

In general, money market funds are not subject to market risk because the interest paid on such funds fluctuates with the prevailing interest rate. Accordingly, a 100 basis point increase in interest rates or a 10% decline in the value of the United States equity markets would not be expected to have a material impact on the value of such money market funds. Investments in U.S. government fixed income securities are subject to interest rate risk and will decline in value if interest rates increase. However, due to the relatively short duration of our short-term investment portfolio, an immediate 10% change in interest rates would have no material impact on our financial condition, results of operations or cash flows. Declines in interest rates over time will, however, reduce our interest income.

Investment Risk. We are exposed to investment risks related to changes in the underlying financial condition of certain of our equity investments in these technology companies. The fair value of these investments can be significantly impacted by the risk of adverse changes in securities markets generally, as well as risks related to the performance of the companies whose securities we have invested in, risks associated with specific industries, and other factors. These investments are subject to significant fluctuations in fair value due to the volatility of the securities markets and of the underlying businesses. As of

December 31, 2018 and 2017, the carrying value of our common stock and warrants in public and private companies was \$18.7 million and \$107.0 million, respectively. We record our common stock and warrant investments in publicly traded companies at fair value, which is subject to market price volatility, and represents \$10.5 million and \$104.8 million of our assets as of December 31, 2018 and 2017, respectively. As of December 31, 2018, a hypothetical 10% adverse change in the market price of Veritone's publicly traded common stock would have resulted in a decrease of approximately \$540,000 in the fair value of our equity and equity warrant investments in Veritone and a decrease of approximately \$301,000 in our other equity investments. As of December 31, 2017, a hypothetical 10% adverse change in the market price of Veritone's publicly traded common stock would have resulted in a decrease of approximately \$11.1 million in the fair value of our equity and equity warrant investments in Veritone. We evaluate our equity and equity warrant investments in private companies for impairment when events and circumstances indicate that the decline in fair value of such assets below the carrying value is other-than temporary. Our analysis includes a review of recent operating results and trends, recent sales/acquisitions of the investee securities, and other publicly available data. The current global economic climate provides additional uncertainty. Valuations of private companies are inherently more complex due to the lack of readily available market data. As such, we believe that market sensitivities are not practicable for our private company equity investments.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and related financial information required to be filed hereunder are indexed under Item 15 of this report and are incorporated herein by reference.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Intellectual Property Officer and Corporate Controller, we conducted an evaluation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based on this evaluation, our Chief Intellectual Property Officer and Corporate Controller concluded that, as of December 31, 2018, our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Intellectual Property Officer and Corporate Controller, as appropriate to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized and reported within the time periods prescribed by the SEC.

(b) Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Under the supervision and with the participation of

our management, including our Chief Intellectual Property Officer and Corporate Controller, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the 2013 framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control - Integrated Framework*, our management concluded that our internal control over financial reporting was effective as of December 31, 2018.

Grant Thornton LLP, the independent registered public accounting firm who audited our consolidated financial statements included in this Annual Report on Form 10-K, has issued an attestation report on the effectiveness of our internal control over financial reporting as of December 31, 2018, which is included herein.

Changes in Internal Controls. There were no changes in our internal control over financial reporting during the fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls. Our management, including our Chief Intellectual Property Officer and Corporate Controller, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of the effectiveness of controls to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

ITEM 9B. OTHER INFORMATION

On March 12, 2019, Acacia's Board of Directors unanimously approved the adoption of a Tax Benefits Preservation Plan, or the 2019 Plan, with Computershare Trust Company, N.A., as Rights Agent, or the Rights Agent. The 2019 Plan replaces the Company's Tax Benefits Preservation Plan dated March 15, 2016, or the 2016 Plan, which expires on March 15, 2019, and is substantially similar to 2016 Plan. While the 2019 Plan was effective upon adoption by the Board, and while not required by the Company's governing documents or by applicable law, as a matter of good corporate governance, the Company intends to submit the 2019 Plan for stockholder ratification at its next annual meeting of stockholders.

The purpose of the 2019 Plan is to protect the Company's ability to utilize potential tax assets, such as net operating loss carryforwards, or NOLs, and tax credits, or Tax Benefits, to offset potential future taxable income. As of December 31, 2018, the Company had U.S. federal income tax NOLs totaling approximately \$222,860,808 and U.S. state income tax NOLs totaling approximately \$19,470,755. The Internal Revenue Code of 1986, as amended, or the Code, limits the ability of a company to use its NOLs if it experiences an "ownership change," as defined in Section 382 of the Code. A company generally experiences such an ownership change if the percentage of its stock owned by its "5-percent shareholders," as defined in Section 382 of the Code, increases by more than 50 percentage points over a rolling three-year period.

The 2019 Plan is designed to reduce the likelihood that the Company will experience an ownership change by discouraging any (i) person or group from acquiring beneficial ownership of 4.9% or more of the Company's outstanding common stock and (ii) any existing shareholders who, as of the time of the first public announcement of the adoption of the 2019 Plan, beneficially own more than 4.9% of the Company's then-outstanding shares of the Company's common stock from acquiring additional shares of the Company's common stock (subject to certain exceptions). There is no guarantee, however, that the 2019 Plan will prevent the Company from experiencing an ownership change.

A company that experiences an ownership change generally will be subject to an annual limitation on certain of its pre-ownership change tax assets equal to the value of the corporation immediately before the ownership change, multiplied by the long-term-tax-exempt rate (subject to certain adjustments), provided that the annual limitation will be increased each year to the extent that there is an unused limitation in a prior year. The limitation arising from an ownership change on the Company's ability to utilize the Tax Benefits depends on the value of the Company's stock at the time of the ownership change.

In connection with the adoption of the 2019 Plan, the board of directors of the Company authorized and declared a dividend distribution of one right, or a Right, for each outstanding share of the common stock of the Company, to

shareholders of record at the close of business on March 16, 2019.

Summary Description of the 2019 Plan

The following summary of the 2019 Plan does not purport to be complete and is qualified in its entirety by the full text of the 2019 Plan, a copy of which is filed as Exhibit 4.1 and is incorporated herein by reference.

Distribution Date. Subject to certain exceptions, Rights would separate from the common stock and become exercisable apart from the common stock only following the earlier of (i) the close of business on the tenth (10th) business day after public announcement that a person has become an “Acquiring Person” or (ii) the close of business on the tenth (10th) business day (or such later date as the Board shall determine) after a third party makes a tender or exchange offer which, if consummated, would result in such third party becoming an Acquiring Person.

Exercise of Rights. On or after the Distribution Date, each Right would initially entitle the holder to purchase one one-thousandth of a share of the Company's Series B Junior Participating Preferred Stock, \$0.001 par value, or the Series B Preferred Stock, for a purchase price of \$12.00 (subject to adjustment), or the Exercise Price. Under certain circumstances set forth in the 2019 Plan, the Company may suspend the exercisability of the Rights.

Definition of Acquiring Person. An "Acquiring Person" is a person or group that, together with affiliates and associates of such person or group, acquires beneficial ownership of 4.9% or more of the common stock, other than: (i) the Company, its subsidiaries and their respective employee benefit plans; (ii) any shareholder that, as of the time of the first public announcement of adoption of the 2019 Plan, beneficially owns 4.9% or more of the common stock (unless and until such person thereafter acquires any additional shares of common stock, subject to certain exceptions); (iii) a person who becomes an Acquiring Person solely as a result of the Company repurchasing shares of common stock or a stock dividend, stock split, reverse stock split or similar transaction effected by the Company (unless and until such person acquires additional shares, other than in certain specified exempt transactions) and (iv) certain shareholders who, inadvertently or without knowledge of the terms of the Rights, buy shares in excess of 4.899% of the common stock and who thereafter reduce the percentage of shares owned below 4.9%. Prior to the Distribution Date, the Board has sole discretion to make an affirmative determination, taking into account the intent and purposes of the 2019 Plan or other circumstances facing the Company, that a Person is not an Acquiring Person (even if such Person satisfies the requirements of any of subclauses (i), (ii), (iii) or (iv) if and for so long as such Person complies with any limitations or conditions required by the Board in making such determination).

"Flip-in" Feature. If any person or group of affiliated or associated persons becomes an Acquiring Person, then each Right (other than Rights owned by an Acquiring Person, its affiliates, associates or certain transferees, which will become void) will entitle the holder to purchase, at the then current exercise price, common stock (or, in certain circumstances, a combination of common stock, other securities, cash or other property) having a value of twice the exercise price of the Right, in effect enabling a purchase at half-price. However, Rights are not exercisable following such an event until such time as the Rights are no longer redeemable by the Company as described below.

"Flip-over" Feature. If, at any time after a person or group of affiliated or associated persons becomes an Acquiring Person, the Company engages in a merger or other business combination transaction or series of related transactions in which the Company is not the surviving corporation, the common stock is changed or exchanged, or fifty percent (50%) or more of its assets, cash flow or earning power is sold, then each Right (not previously voided by the occurrence of a Flip-in Event) will entitle the holder to purchase, at the Right's then current exercise price, common stock of such Acquiring Person having a value of twice the Right's then current exercise price, in effect enabling a purchase at half-price.

Exchange Option. At any time after a person or group of affiliated or associated persons becomes an Acquiring Person and prior to the acquisition by such person or group of fifty percent (50%) or more of the then outstanding common stock, the Board may, in lieu of allowing Rights to be exercised, cause each outstanding Right (other than Rights owned by an Acquiring Person, its affiliates, associates or certain transferees, which will become void) to be exchanged for one share of common stock or one one-thousandth of a share of Series B Preferred Stock, in each case as adjusted to reflect stock splits or similar transactions.

Redemption. The Rights may be redeemed by the Board, at a price of \$0.001 per Right at any time prior to the earlier of (i) the tenth (10th) business day following a public announcement that a person or group of affiliated or associated persons has become an Acquiring Person or (ii) the final expiration of the Rights.

Power to Amend. Prior to a Distribution Date, the Company may amend the 2019 Plan in any respect without shareholder approval, other than to extend the final expiration date of the Rights. From and after a Distribution Date, the Company may amend the 2019 Plan without the approval of holders of certificates representing Rights in order to (i) cure any ambiguity, (ii) correct or supplement any provision which may be defective or inconsistent with any other provisions, (iii) shorten or lengthen any time period (other than to lengthen the final expiration date of the Rights), or (iv) change or supplement the provisions in any manner which the Company may deem necessary or desirable and which does not adversely affect the interests of the holders of certificates representing Rights. The 2019 Plan,

however, may not be amended at such time as the Rights are not redeemable (other than certain limited technical amendments).

Expiration. The Rights will expire on the earliest of (i) 5:00 P.M., New York, New York time, on March 15, 2021, (ii) the time at which the rights are redeemed or exchanged pursuant to the 2019 Plan, (iii) the close of business on the effective date of the repeal of Section 382 or any successor statute if the Board determines that the 2019 Plan is no longer necessary or desirable for the preservation of Tax Benefits or (iv) the close of business on the first day of a taxable year of the Company to which the Board determines that Tax Benefits may not be carried forward.

Rights Certificates. Prior to a Distribution Date, the Rights will be evidenced by, and trade with, the common stock and will not be exercisable or transferable apart from the common stock. After a Distribution Date, the Rights Agent will send certificates representing Rights to shareholders and the Rights will trade independent of the common stock. *No Rights as a Shareholder; Other Matters.* Until a Right is exercised, the holder of Rights, as such, is not entitled to any separate rights as a shareholder of the Company (such as voting or dividend rights). Although the distribution of the Rights will not be taxable to shareholders or to the Company for U.S. federal income tax purposes, shareholders may, depending upon the circumstances, recognize taxable income in the event that the Rights become exercisable for common stock (or other consideration) or for common stock of the acquiring company or in the event of the redemption of the Rights as set forth above.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Except as provided below, in accordance with General Instruction G(3) to Form 10-K, certain information required by this Item is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders to be filed with the SEC no later than April 30, 2019.

Code of Conduct.

We have adopted a Code of Conduct that applies to all employees, including our chief intellectual property officer and corporate controller and any persons performing similar functions. Our Code of Conduct is provided on our internet website at www.acaciaresearch.com.

ITEM 11. EXECUTIVE COMPENSATION

In accordance with General Instruction G(3) to Form 10-K, the information required by this Item is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders to be filed with the SEC no later than April 30, 2019.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

In accordance with General Instruction G(3) to Form 10-K, certain information required by this Item is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders to be filed with the SEC no later than April 30, 2019.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

In accordance with General Instruction G(3) to Form 10-K, the information required by this Item is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders to be filed with the SEC no later than April 30, 2019.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

In accordance with General Instruction G(3) to Form 10-K, the information required by this Item is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders to be filed with the SEC no later than April 30, 2019.

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PART IV**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

(a) The following documents are filed as part of this report.

(1) Financial Statements

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Acacia Research Corporation Consolidated Financial Statements

Reports of Independent Registered Public Accounting Firm

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Consolidated Balance Sheets as of December 31, 2018 and 2017

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Consolidated Statements of Operations for the Years Ended December 31, 2018 and 2017

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Consolidated Statements of Comprehensive Income (Loss) for the Years Ended December 31, 2018 and 2017

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Consolidated Statements of Stockholders' Equity for the Years Ended December 31, 2018 and 2017

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Consolidated Statements of Cash Flows for the Years Ended December 31, 2018 and 2017

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Notes to Consolidated Financial Statements

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(2) Financial Statement Schedules

Financial statement schedules are omitted because they are not applicable or the required information is shown in the Financial Statements or the Notes thereto.

(3) Exhibits

Refer to Item 15(b) below.

(b) Exhibits. The following exhibits are either filed herewith or incorporated herein by reference:

<u>Exhibit Number</u>	<u>Description</u>
2.1	<u>Agreement and Plan of Merger, dated November 22, 2011, by and among Acacia Research Group LLC, Apollo Patent Corp., Adaptix, Inc., and Baker Communications Fund II (QP), L.P., solely in its capacity as representative for the shareholders of Adaptix, Inc.(15)</u>
3.1	<u>Amended and Restated Certificate of Incorporation (1)</u>
3.2	<u>Amended and Restated Bylaws (20)</u>
4.1	<u>Tax Benefits Preservation Plan, dated as of March 16, 2019, by and between Acacia Research Corporation and Computershare Inc., as Rights Agent, which includes the form of Certificate of Designation of Series A Cumulative Participating Preferred Stock as Exhibit A, the Form of Right Certificate as Exhibit B and the Summary of Terms as Exhibit C</u>
10.9	<u>Form of Indemnification Agreement</u>
10.17*	<u>Acacia Research Corporation Amended and Restated Executive Severance Policy (12)</u>
10.19	<u>Form of Purchase Agreement (16)</u>
10.20*	<u>2013 Acacia Research Corporation Stock Incentive Plan (17)</u>
10.21*	<u>Form of Stock Issuance Agreement under the 2013 Acacia Research Corporation Stock Incentive Plan (18)</u>
10.23*	<u>2016 Acacia Research Corporation Stock Incentive Plan (21)</u>
10.24*	<u>Form of Stock Option Agreement under the 2016 Acacia Research Corporation Stock Incentive Plan (24)</u>
10.25*	

Form of Stock Issuance Agreement under the 2016 Acacia Research Corporation Stock Incentive Plan (24)

10.27*

Employment Agreement, dated September 18, 2017, by and between Acacia Research Group LLC and Robert Stewart (25)

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- 10.28* Form of Profits Interest Agreement Under AIP Operation LLC Profits Interest Plan (26)
- 10.29 Investment Agreement dated August 15, 2016, by and between Acacia Research Corporation and Veritone, Inc. (27)
- 10.30 Secured Promissory Note dated August 15, 2016, issued by Veritone, Inc. to Acacia Research Corporation (27)
- 10.31 Primary Common Stock Purchase Warrant dated August 15, 2016, issued by Veritone, Inc. to Acacia Research Corporation, together with form of 10% Warrant to Purchase Common Stock (27)
- 10.32 Common Stock Purchase Warrant dated August 15, 2016, issued by Veritone, Inc. to Acacia Research Corporation (27)
- 10.33 Common Stock Purchase Warrant dated November 25, 2016, issued by Veritone, Inc. to Acacia Research Corporation (27)
- 10.34 Common Stock Purchase Warrant dated November 25, 2016, issued by Veritone, Inc. to Acacia Research Corporation (27)
- 10.35* Employment Agreement, effective August 13, 2018, by and between Acacia Research Group, LLC and Marc Booth (29)
- 10.36* Separation Agreement and General Release of Claims, effective August 10, 2018, by and between Acacia Research Group, LLC and Clayton J. Haynes (29)
- 10.37* Consulting Agreement, effective August 10, 2018, by and between Acacia Research Corporation and Clayton J. Haynes (29)
- 10.38* Separation Agreement and General Release of Claims, effective August 10, 2018, by and between Acacia Research Group, LLC and Edward J. Treska (29)
- 10.39* Consulting Agreement, effective August 10, 2018, by and between Acacia Research Corporation and Edward J. Treska (29)
- 10.40* Separation Agreement and General Release of Claims, dated February 12, 2019, by and between Acacia Research Group, LLC and Kirsten Hoover (30)
- 21.1 List of Subsidiaries
- 23.1 Consent of Independent Registered Public Accounting Firm
- 24.1 Power of Attorney (included in the signature page hereto).
- 31.1† Certification of Chief Intellectual Property Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934
- 31.2† Certification of Corporate Controller Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934
- 32.1 Certification of Chief Intellectual Property Officer Pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350
- 32.2 Certification of Corporate Controller Pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350
- 101 Interactive Data Files Pursuant to Rule 405 of Regulation S-T.

* The referenced exhibit is a management contract, compensatory plan or arrangement required to be filed as an exhibit to this Annual Report on Form 10-K pursuant to Item 15(c) of Form 10-K.

The certifications attached as Exhibits 32.1 and 32.2 that accompany this Annual Report on Form 10-K are not deemed filed with the SEC and are not to be incorporated by reference into any filing of Acacia Research Corporation under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Annual Report on Form 10-K, regardless of any general incorporation language contained in any filing.

(1) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on June 5, 2008 (File No. 000-26068).

(2)

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Incorporated by reference to Appendix A to Acacia Research Corporation's Definitive Proxy Statement on Schedule 14A filed on April 20, 2000 (File No. 000-26068).

(3) Incorporated by reference to Appendix A to Acacia Research Corporation's Definitive Proxy Statement on Schedule 14A filed on April 26, 1996 (File No. 000-26068).

- Incorporated by reference to Annex E to the Proxy Statement/Prospectus which formed part of Acacia Research Corporation's Registration Statement on Form S-4 (File No. 333-87654) which became effective on November 8, 2002.
- (5) Incorporated by reference to Acacia Research Corporation's Registration Statement on Form S-8 (File No. 333-144754) which became effective on July 20, 2007.
- (6) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended September 30, 2007, filed on November 2, 2007 (File No. 000-26068).
- (7) Incorporated by reference to Acacia Research Corporation's Annual Report on Form 10-K for the year ended December 31, 2001, filed on March 27, 2002 (File No. 000-26068).
- (8) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended June 30, 2012, filed on July 30, 2012 (File No. 000-26068).
- (9) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended March 31, 2006, filed on May 10, 2006 (File No. 000-26068).
- (10) Incorporated by reference to Acacia Research Corporation's Annual Report on Form 10-K for the year ended December 31, 2007, filed on March 14, 2008 (File No. 000-26068).
- (11) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on April 2, 2008 (File No. 000-26068).
- (12) Incorporated by reference to Acacia Research Corporation's Annual Report on Form 10-K for the year ended December 31, 2008, filed on February 26, 2009 (File No. 000-26068).
- (13) Incorporated by reference to Acacia Research Corporation's Annual Report on Form 10-K for the year ended December 31, 2009, filed on February 26, 2010, as amended on March 1, 2010 (File No. 000-26068).
- (14) Incorporated by reference to Acacia Research Corporation's Annual Report on Form 10-K for the year ended December 31, 2010, filed on February 28, 2011, as amended on March 24, 2011 (File No. 000-26068).
- (15) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K/A filed on January 19, 2012 (File No. 000-26068). Portions of this exhibit have been omitted pursuant to a request for confidential treatment under Rule 24-b-2 of the Securities Exchange Act of 1934, as amended. The omitted material has been separately filed with the Securities and Exchange Commission.
- (16) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on February 16, 2012 (File No. 000-26068).
- (17) Incorporated by reference to Appendix A to Acacia Research Corporation's Definitive Proxy Statement on Schedule 14A filed on April 24, 2013 (File No. 000-26068).
- (18) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on May 22, 2013 (File No. 000-26068).
- (19) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended September 30, 2015, filed on November 9, 2015 (File No. 000-26068).
- (20) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on March 28, 2016 (File No. 001-37721).
- (21) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended June 30, 2016, filed on August 9, 2016 (File No. 001-37721).
- (22) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on March 4, 2016 (File No. 000-26068).

- (23) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on March 21, 2016 (File No. 000-26068).
- (24) Incorporated by reference to Acacia Research Corporation's Annual Report on Form 10-K for the year ended December 31, 2016, filed on March 10, 2017 (File No. 001-37721).
- (25) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended September 30, 2017, filed on November 7, 2017 (File No. 001-37721).
- (26) Incorporated by reference to Acacia Research Corporation's Quarterly Report on Form 10-Q for the period ended March 31, 2017, filed on May 10, 2017 (File No. 001-37721).
- (27) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on March 16, 2017 (File No. 001-37721).
- (28) Incorporated by reference to Annex A to Acacia Research Corporation's Definitive Proxy Statement on Schedule 14A filed on May 3, 2018 (File No. 001-37721).

- (29) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on August 16, 2018 (File No. 001-37721).

- (30) Incorporated by reference to Acacia Research Corporation's Current Report on Form 8-K filed on February 13, 2019 (File No. 001-37721).

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

ACACIA RESEARCH CORPORATION

Dated: March 15, 2019 By: /s/ Marc W. Booth
 Marc W. Booth
Chief IP Officer
(Authorized Signatory)

POWER OF ATTORNEY

We, the undersigned directors and officers of Acacia Research Corporation, do hereby constitute and appoint Marc W. Booth and Kirsten L. Hoover, and each of them, as our true and lawful attorneys-in-fact and agents with power of substitution, to do any and all acts and things in our name and behalf in our capacities as directors and officers and to execute any and all instruments for us and in our names in the capacities indicated below, which said attorney-in-fact and agent may deem necessary or advisable to enable said corporation to comply with the Securities Exchange Act of 1934, as amended, and any rules, regulations and requirements of the Securities and Exchange Commission, in connection with this Annual Report on Form 10-K, including specifically but without limitation, power and authority to sign for us or any of us in our names in the capacities indicated below, any and all amendments hereto; and we do hereby ratify and confirm all that said attorney-in-fact and agent, shall do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
/s/Marc W. Booth Marc W. Booth	Chief Intellectual Property Officer (Principal Executive Officer)	March 15, 2019
/s/Kirsten L. Hoover Kirsten L. Hoover	Corporate Controller (Principal Financial Officer)	March 15, 2019
/s/Allen Bradley Allen Bradley	Director	March 15, 2019
/s/Maureen O'Connell Maureen O'Connell	Director	March 15, 2019
/s/Clifford Press Clifford Press	Director	March 15, 2019
/s/Alfred V. Tobia, Jr. Alfred V. Tobia, Jr.	Director	March 15, 2019
/s/Katharine Wolanyk Katharine Wolanyk	Director	March 15, 2019

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
Acacia Research Corporation

Opinion on the financial statements

We have audited the accompanying consolidated balance sheets of Acacia Research Corporation and subsidiaries (the “Company”) as of December 31, 2018 and 2017, the related consolidated statements of operations, comprehensive income (loss), stockholders’ equity, and cash flows for each of the two years in the period ended December 31, 2018, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”), the Company’s internal control over financial reporting as of December 31, 2018, based on criteria established in the 2013 Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”), and our report dated March 15, 2019 expressed an unqualified opinion.

Change in accounting principle

As discussed in Note 13 to the financial statements, the Company has adopted new accounting guidance in 2018 related to accounting for revenue from contracts with customers. Our opinion is not modified with respect to this matter.

Basis for opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ GRANT THORNTON LLP

We have served as the Company's auditor since 2007.

Newport Beach, California

March 15, 2019

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
Acacia Research Corporation

Opinion on internal control over financial reporting

We have audited the internal control over financial reporting of Acacia Research Corporation and subsidiaries (the “Company”) as of December 31, 2018, based on criteria established in the 2013 Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in the 2013 Internal Control-Integrated Framework issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”), the consolidated financial statements of the Company as of and for the year ended December 31, 2018, and our report dated March 15, 2019 expressed an unqualified opinion on those financial statements.

Basis for opinion

The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report on Internal Control Over Financial Reporting (“Management’s Report”). Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and limitations of internal control over financial reporting

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ GRANT THORNTON LLP

Newport Beach, California
March 15, 2019

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ACACIA RESEARCH CORPORATION
CONSOLIDATED BALANCE SHEETS

As of December 31, 2018 and 2017

(In thousands, except share and per share information)

	2018	2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$128,809	\$136,604
Trading securities - debt	33,642	—
Trading securities - equity	3,012	—
Accounts receivable	32,884	153
Prepaid expenses and other current assets	3,125	2,938
Total current assets	201,472	139,695
Investment at fair value ⁽¹⁾	7,459	104,754
Other investments ⁽¹⁾	8,195	2,195
Patents, net of accumulated amortization	6,587	61,917
Other non-current assets	236	207
	\$223,949	\$308,768
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$8,347	\$7,956
Royalties and contingent legal fees payable	22,688	1,601
Total current liabilities	31,035	9,557
Other liabilities	1,674	3,552
Total liabilities	32,709	13,109
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Preferred stock, par value \$0.001 per share; 10,000,000 shares authorized; no shares issued or outstanding	—	—
Common stock, par value \$0.001 per share; 100,000,000 shares authorized; 49,639,319 shares issued and outstanding as of December 31, 2018 and 50,639,926 shares issued and outstanding as of December 31, 2017	50	51
Treasury stock, at cost, 2,919,828 and 1,729,408 shares as of December 31, 2018 and 2017	(39,272)	(34,640)
Additional paid-in capital	651,156	648,996
Accumulated comprehensive loss	—	(88)
Accumulated deficit	(422,541)	(320,018)
Total Acacia Research Corporation stockholders' equity	189,393	294,301
Noncontrolling interests in operating subsidiaries	1,847	1,358
Total stockholders' equity	191,240	295,659
	\$223,949	\$308,768

⁽¹⁾ Refer to Note 6 for additional information.

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

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ACACIA RESEARCH CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
For the Years Ended December 31, 2018 and 2017
(In thousands, except share and per share information)

	2018	2017
Revenues	\$ 131,506	\$ 65,402
Portfolio operations:		
Inventor royalties	35,168	4,952
Contingent legal fees	31,501	16,682
Patent acquisition expenses	4,000	—
Litigation and licensing expenses - patents	8,866	18,219
Amortization of patents	27,120	22,154
Impairment of patent-related intangible assets	28,210	2,248
Other portfolio expenses	2,602	1,200
Total portfolio operations	137,467	65,455
Net loss	(5,961)	(53)
General and administrative expenses (including non-cash stock compensation expense (credit) of (\$317) in 2018 and \$8,885 in 2017)	18,850	27,219
Operating loss	(24,811)	(27,272)
Other income (expense):		
Change in fair value of investment, net ⁽¹⁾	(59,103)	42,239
Loss on sale of investment ⁽¹⁾	(19,095)	—
Gain on conversion of loans and accrued interest ⁽¹⁾	—	2,671
Gain on exercise of Primary Warrant ⁽¹⁾	—	4,616
Equity in losses of investee ⁽¹⁾	—	(220)
Other income (expense)	(1,629)	1,000
Interest income and other	969	1,605
Total other income (expense)	(78,858)	51,911
Income (loss) from operations before provision for income taxes	(103,669)	24,639
Provision for income taxes	(1,179)	(2,955)
Net income (loss) including noncontrolling interests in subsidiaries	(104,848)	21,684
Net (income) loss attributable to noncontrolling interests in subsidiaries	(181)	496
Net income (loss) attributable to Acacia Research Corporation	\$(105,029)	\$ 22,180
Net income (loss) attributable to common stockholders - basic and diluted	\$(105,029)	\$ 22,147
Basic and diluted income (loss) per common share	\$(2.10)	\$ 0.44
Weighted-average number of shares outstanding, basic	49,969,062	50,495,119
Weighted-average number of shares outstanding, diluted	49,969,062	50,692,012

⁽¹⁾ Refer to Note 6 for additional information.

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

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ACACIA RESEARCH CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
For the Years Ended December 31, 2018 and 2017
(In thousands)

	2018	2017
Net income (loss) including noncontrolling interests in subsidiaries	\$(104,848)	\$21,684
Other comprehensive income (loss):		
Unrealized gain (loss) on short-term investments, net of tax of \$0	—	(40)
Unrealized gain (loss) on foreign currency translation, net of tax of \$0	88	58
Add: reclassification adjustment for (gains) losses included in net income (loss)	—	(30)
Total other comprehensive income (loss)	(104,760)	21,672
Comprehensive income (loss) attributable to noncontrolling interests	(181)	496
Comprehensive income (loss) attributable to Acacia Research Corporation	\$(104,941)	\$22,168

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

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ACACIA RESEARCH CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

For the Years Ended December 31, 2018 and 2017

(In thousands, except share information)

	Common Shares	Common Stock	Treasury Stock	Additional Paid-in Capital	Accumulated Comprehensive Income (Loss)	Accumulated Deficit	Noncontrolling Interests in Operating Subsidiaries	Total
Balance at December 31, 2016	50,476,042	\$ 50	\$(34,640)	\$ 642,453	\$ (76)	\$(342,198)	\$ 1,854	\$ 267,443
Net income attributable to Acacia Research Corporation	—	—	—	—	—	22,180	—	22,180
Stock options exercised	207,863	1	—	744	—	—	—	745
Compensation expense for share-based awards, net of forfeitures	(35,310)	—	—	5,844	—	—	—	5,844
Repurchase of restricted common stock	(8,669)	—	—	(45)	—	—	—	(45)
Net loss attributable to noncontrolling interests in subsidiaries	—	—	—	—	—	—	(496)	(496)
Unrealized gain on foreign currency translation	—	—	—	—	28	—	—	28
Unrealized loss on short-term investments	—	—	—	—	(40)	—	—	(40)
Balance at December 31, 2017	50,639,926	51	(34,640)	648,996	(88)	(320,018)	1,358	295,659
Net loss attributable to Acacia Research Corporation	—	—	—	—	—	(105,029)	—	(105,029)
Cumulative effect of new accounting principle	—	—	—	—	—	2,506	308	2,814
Repurchase of common stock	(1,190,420)	(2)	(4,632)	—	—	—	—	(4,634)
Stock options exercised	82,615	—	—	257	—	—	—	257
Compensation expense for share-based awards, net of forfeitures	166,998	1	—	2,132	—	—	—	2,133
Repurchase of restricted common stock	(59,800)	—	—	(229)	—	—	—	(229)
Net income attributable to noncontrolling interests in subsidiaries	—	—	—	—	—	—	181	181
Unrealized gain on foreign currency translation	—	—	—	—	88	—	—	88
Balance at December 31, 2018	49,639,319	\$ 50	\$(39,272)	\$ 651,156	\$ —	\$(422,541)	\$ 1,847	\$ 191,240

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

ACACIA RESEARCH CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2018 and 2017
(In thousands)

	2018	2017
Cash flows from operating activities:		
Net income (loss) including noncontrolling interests in subsidiaries	\$(104,848)	\$21,684
Adjustments to reconcile net income (loss) including noncontrolling interests in subsidiaries to net cash provided by operating activities:		
Gain on conversion of loans and accrued interest	—	(2,671)
Gain on exercise of Primary Warrant	—	(4,616)
Change in fair value of investment, net	59,103	(42,239)
Loss on sale of investment	19,095	—
Depreciation and amortization	27,145	22,243
Non-cash stock compensation	(317)	8,885
Impairment of patent-related intangible assets	28,210	2,248
Other	564	(374)
Changes in assets and liabilities:		
Accounts receivable	(28,189)	26,597
Prepaid expenses and other assets	(208)	(135)
Accounts payable and accrued expenses	963	(6,349)
Royalties and contingent legal fees payable	19,359	(12,307)
Net cash provided by operating activities	20,877	12,966
Cash flows from investing activities:		
Investment in Investees	(7,000)	(31,514)
Sale of investment	19,097	—
Advances to Investee (Note 6)	—	(4,000)
Purchases of property and equipment	(34)	(2)
Purchases of short-term investments	(102,769)	(448,388)
Sales and maturities of short-term investments	66,640	467,790
Net cash used in investing activities	(24,066)	(16,114)
Cash flows from financing activities:		
Repurchase of common stock	(4,634)	—
Proceeds from the exercise of stock options	257	745
Repurchases of restricted common stock	(229)	(45)
Net cash provided by (used in) financing activities	(4,606)	700
Decrease in cash and cash equivalents	(7,795)	(2,448)
Cash and cash equivalents and restricted cash, beginning	136,604	139,052
Cash and cash equivalents and restricted cash, ending	\$128,809	\$136,604

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

ACACIA RESEARCH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

Description of Business. As used herein, “Acacia” and the “Company” refer to Acacia Research Corporation and/or its wholly and majority-owned and controlled operating subsidiaries, and/or where applicable, its management.

Acacia’s operating subsidiaries invest in, license and enforce patented technologies. Acacia’s operating subsidiaries partner with inventors and patent owners, applying their legal and technology expertise to patent assets to unlock the financial value in their patented inventions. In recent years, Acacia has also invested in technology companies. Acacia leverages its experience, expertise, data and relationships developed as a leader in the IP industry to pursue these opportunities. In some cases, these opportunities will complement, and/or supplement Acacia’s primary licensing and enforcement business.

Acacia’s operating subsidiaries generate revenues and related cash flows from the granting of IP rights for the use of patented technologies that its operating subsidiaries control or own. Acacia’s operating subsidiaries assist patent owners with the prosecution and development of their patent portfolios, the protection of their patented inventions from unauthorized use, the generation of licensing revenue from users of their patented technologies and, where necessary, with the enforcement against unauthorized users of their patented technologies through the filing of patent infringement litigation.

Acacia’s operating subsidiaries are principals in the licensing and enforcement effort, obtaining control of the rights in the patent portfolio, or control of the patent portfolio outright. Acacia’s operating subsidiaries own or control the rights to multiple patent portfolios, which include U.S. patents and certain foreign counterparts, covering technologies used in a wide variety of industries.

Neither Acacia nor its operating subsidiaries invent new technologies or products; rather, Acacia depends upon the identification and investment in new patents, inventions and companies that own IP through its relationships with inventors, universities, research institutions, technology companies and others. If Acacia’s operating subsidiaries are unable to maintain those relationships and identify and grow new relationships, then they may not be able to identify new technology-based opportunities for sustainable revenue and/or revenue growth.

During fiscal year 2018, Acacia did not obtain control of any new patent portfolios. During fiscal year 2017 Acacia obtained control of one new patent portfolio. In fiscal year 2016, Acacia obtained control of two new patent portfolios.

Acacia was incorporated on January 25, 1993 under the laws of the State of California. In December 1999, Acacia changed its state of incorporation from California to Delaware.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounting Principles. The consolidated financial statements and accompanying notes are prepared on the accrual basis of accounting in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”).

Principles of Consolidation. The accompanying consolidated financial statements include the accounts of Acacia and its wholly and majority-owned and controlled subsidiaries. Material intercompany transactions and balances have been eliminated in consolidation.

Noncontrolling interests in Acacia's majority-owned and controlled operating subsidiaries ("noncontrolling interests") are separately presented as a component of stockholders' equity. Consolidated net income or (loss) is adjusted to include the net (income) or loss attributed to noncontrolling interests in the consolidated statements of operations. Refer to the accompanying consolidated statements of stockholders' equity for total noncontrolling interests.

A wholly owned subsidiary of Acacia is the general partner of the Acacia Intellectual Property Fund, L.P. (the "Acacia IP Fund"), which was formed in August 2010. The Acacia IP Fund is included in the Company's consolidated financial statements since 2010, as Acacia's wholly owned subsidiary, as the general partner, has the ability to control the operations and activities of the Acacia IP Fund. The Acacia IP Fund was terminated as of December 31, 2017 and is in the process of being liquidated.

Revenue Recognition. Revenue is recognized upon transfer of control of promised bundled IP rights (hereinafter "IP Rights") and other contractual performance obligations to licensees in an amount that reflects the consideration we expect to

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ACACIA RESEARCH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

receive in exchange for those IP Rights. Revenue contracts that provide promises to grant the right to use IP Rights as they exist at the point in time at which the IP Rights are granted, are accounted for as performance obligations satisfied at a point in time and revenue is recognized at the point in time that the applicable performance obligations are satisfied and all other revenue recognition criteria have been met.

For the periods presented, revenue contracts executed by the Company primarily provided for the payment of contractually determined, one-time, paid-up license fees in consideration for the grant of certain IP Rights for patented technologies owned or controlled by Acacia ("Paid-up Revenue Agreements"). Revenues also included license fees from sales-based revenue contracts, the majority of which were originally executed in prior periods, that provide for the payment of quarterly license fees based on quarterly sales of applicable product units by licensees ("Recurring Revenue Agreements"). Revenues may also include court ordered settlements or awards related to our patent portfolio ("Other Settlements") or sales of our patent portfolio ("Sales"). IP Rights granted included the following, as applicable: (i) the grant of a non-exclusive, retroactive and future license to manufacture and/or sell products covered by patented technologies, (ii) a covenant-not-to-sue, (iii) the release of the licensee from certain claims, and (iv) the dismissal of any pending litigation. The IP Rights granted were perpetual in nature, extending until the legal expiration date of the related patents. The individual IP Rights are not accounted for as separate performance obligations, as (i) the nature of the promise, within the context of the contract, is to transfer combined items to which the promised IP Rights are inputs and (ii) the Company's promise to transfer each individual IP right described above to the customer is not separately identifiable from other promises to transfer IP Rights in the contract.

Since the promised IP Rights are not individually distinct, the Company combined each individual IP right in the contract into a bundle of IP rights that is distinct, and accounted for all of the IP Rights promised in the contract as a single performance obligation. The IP Rights granted were "functional IP rights" that have significant standalone functionality. Acacia's subsequent activities do not substantively change that functionality and do not significantly affect the utility of the IP to which the licensee has rights. Acacia's operating subsidiaries have no further obligation with respect to the grant of IP Rights, including no express or implied obligation to maintain or upgrade the technology, or provide future support or services. The contracts provide for the grant (i.e., transfer of control) of the licenses, covenants-not-to-sue, releases, and other significant deliverables upon execution of the contract. Licensees legally obtain control of the IP Rights upon execution of the contract. As such, the earnings process is complete and revenue is recognized upon the execution of the contract, when collectability is probable and all other revenue recognition criteria have been met. Revenue contracts generally provide for payment of contractual amounts with 30-90 days of execution of the contract, or the end of the quarter in which the sale or usage occurs for Recurring Revenue Agreements. Contractual payments made by licensees are generally non-refundable.

For sales-based royalties, the Company includes in the transaction price some or all of an amount of estimated variable consideration to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. Notwithstanding, revenue is recognized for a sales-based royalty promised in exchange for a license of IP Rights when the later of (i) the subsequent sale or usage occurs, or (ii) the performance obligation to which some or all of the sales-based royalty has been allocated has been satisfied. Estimates are generally based on historical levels of activity, if available.

Revenues from contracts with significant financing components (either explicit or implicit) are recognized at an amount that reflects the price that a licensee would have paid if the licensee had paid cash for the IP Rights when they transfer to the licensee. In determining the transaction price, the Company adjusts the promised amount of consideration for the effects of the time value of money. As a practical expedient, the Company does not adjust the promised amount of consideration for the effects of a significant financing component if the Company expects, at

contract inception, that the period between when the entity transfers promised IP Rights to a customer and when the customer pays for the IP Rights will be one year or less.

In general, the Company is required to make certain judgments and estimates in connection with the accounting for revenue contracts with customers. Such areas may include identifying performance obligations in the contract, estimating the timing of satisfaction of performance obligations, determining whether a promise to grant a license is distinct from other promised goods or services, evaluating whether a license transfers to a customer at a point in time or over time, allocating the transaction price to separate performance obligations, determining whether contracts contain a significant financing component, and estimating revenues recognized at a point in time for sales-based royalties.

ACACIA RESEARCH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Revenues were comprised of the following for the periods presented (in thousands):

	2018	2017
Paid-up Revenue Agreements	\$ 100,496	\$ 59,020
Recurring Revenue Agreements	13,040	6,382
Other Settlements	3,470	—
Sales	14,500	—
	\$ 131,506	\$ 65,402

Refer to “Inventor Royalties and Contingent Legal Expenses” below for information on related direct costs of revenues.

Portfolio Operations. Cost of revenues include the costs and expenses incurred in connection with Acacia’s patent licensing and enforcement activities, including inventor royalties paid to original patent owners, contingent legal fees paid to external patent counsel, other patent-related legal expenses paid to external patent counsel, licensing and enforcement related research, consulting and other expenses paid to third-parties and the amortization of patent-related investment costs. These costs are included under the caption “Portfolio operations” in the accompanying consolidated statements of operations.

Inventor Royalties and Contingent Legal Expenses. Inventor royalties are expensed in the consolidated statements of operations in the period that the related revenues are recognized. In certain instances, pursuant to the terms of the underlying inventor agreements, upfront advances paid to patent owners by Acacia’s operating subsidiaries are recoverable from future net revenues. Patent costs that are recoverable from future net revenues are amortized over the estimated economic useful life of the related patents, or as the prepaid royalties are earned by the inventor, as appropriate, and the related expense is included in amortization expense in the consolidated statements of operations. Any unamortized upfront advances recovered from net revenues are expensed in the period recovered, and included in amortization expense in the consolidated statements of operations. Cost of revenues for fiscal year 2018 included \$4.0 million of costs to acquire certain patent rights related to revenues recognized in the period.

Contingent legal fees are expensed in the consolidated statements of operations in the period that the related revenues are recognized. In instances where there are no recoveries from potential infringers, no contingent legal fees are paid; however, Acacia’s operating subsidiaries may be liable for certain out of pocket legal costs incurred pursuant to the underlying legal services agreement.

Fair Value Measurements. U.S. GAAP defines fair value as the price that would be received for an asset or the exit price that would be paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants on the measurement date, and also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs, where available. The three-level hierarchy of valuation techniques established to measure fair value is defined as follows:

- (i) Level 1 - *Observable Inputs:* Quoted prices in active markets for identical investments;
- (ii) Level 2 - *Pricing Models with Significant Observable Inputs:* Other significant observable inputs, including quoted prices for similar investments, interest rates, credit risk, etc.; and
- (iii) Level 3 - *Unobservable Inputs:* Significant unobservable inputs, including the entity’s own assumptions in determining the fair value of investments.

Whenever possible, the Company is required to use observable market inputs (Level 1 - quoted market prices) when measuring fair value. In such cases, the level at which the fair value measurement falls is determined based on the

lowest level input that is significant to the fair value measurement. The assessment of the significance of a particular input requires judgment and considers factors specific to the asset or liability being measured. In certain cases, inputs used to measure fair value fall into different levels of the fair value hierarchy. Financial assets and liabilities measured at fair value on a recurring basis were as follows (in thousands):

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	Level 1	Level 2	Level 3
Assets as of December 31, 2018:			
Trading securities - debt	\$—	\$33,642	\$—
Trading securities - equity	3,012	—	—
Investment at fair value - warrants (Note 6)	—	2,064	—
Investment at fair value - common stock (Note 6)	5,395	—	—
Total recurring fair value measurements as of December 31, 2018	\$8,407	\$35,706	\$—
Assets as of December 31, 2017:			
Investments at fair value (Note 6)	\$—	\$—	\$104,754
Liabilities as of December 31, 2018:			
Profits interest units	\$—	\$591	\$—
Liabilities as of December 31, 2017:			
Profits interest units	\$—	\$—	\$3,041

A reconciliation of the activity for fair value measurements categorized within Level 3 for the year ended December 31, 2018 is as follows (in thousands):

	Investment at Fair Value			Other Liabilities
	Common Stock	Warrants	Total	Profits Interest Units
Opening balance as of January 1, 2018	\$90,795	\$13,959	\$104,754	\$3,041
Total gains and losses included in earnings for the period ⁽¹⁾	—	—	—	(2,450)
Non-cash stock compensation expense - Profits Interests	—	—	—	(2,450)
Change in fair value of investment, net	(47,208)	(11,895)	(59,103)	—
Realized loss on sale	(19,095)	—	(19,095)	—
Purchases, issues, sales and settlements	(19,097)	—	(19,097)	—
Transfers to Level 1 and Level 2	(5,395)	(2,064)	(7,459)	(591)
Total recurring fair value measurements ⁽¹⁾	\$—	\$—	\$—	\$—

⁽¹⁾ All gains and losses included in earnings for the period presented relate to assets and liabilities held as of December 31, 2018 and December 31, 2017.

⁽²⁾ Refer to Note 6 for information regarding purchases, issues, sales and settlements activity for the years ended December 31, 2018 and 2017.

Cash and Cash Equivalents. Acacia considers all highly liquid, short-term investments with original maturities of three months or less when purchased to be cash equivalents. For the periods presented, Acacia's cash equivalents are comprised of investments in AAA rated money market funds that invest in first-tier only securities, which primarily includes: domestic commercial paper, securities issued or guaranteed by the U.S. government or its agencies, U.S. bank obligations, and fully collateralized repurchase agreements. Acacia's cash equivalents are measured at fair value using quoted prices that represent Level 1 inputs.

Trading Securities- Debt. Investments in debt securities are reported at fair value on a recurring basis, with related realized and unrealized gains and losses recorded in the statements of operations in other income (expense). Realized and unrealized gains and losses are recorded based on the specific identification method. Interest is included in other

income (expense).

Trading Securities - Equity. Investments in equity securities are reported at fair value on a recurring basis, with related realized and unrealized gains and losses in the value of such securities recorded in the statements of operations in other income (expense). Dividend income is included in other income (expense).

Impairment of Short-term Investments. Acacia evaluates its investments in marketable securities for potential impairment, employing a methodology on a quarterly basis that considers available quantitative and qualitative evidence. If the cost or carrying value of an investment exceeds its estimated fair value, the Company evaluates, among other factors, general market conditions, credit quality of instrument issuers, the duration and extent to which the fair value is less than cost, and the Company's intent and ability to hold, or plans or ability to sell. Fair value is estimated based on publicly available market

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information or other estimates determined by management. Investments are considered to be impaired when a decline in fair value is estimated to be other-than-temporary. Acacia reviews impairments associated with its investments in marketable securities and determines the classification of any impairment as temporary or other-than-temporary. An impairment is deemed other-than-temporary unless (a) Acacia has the ability and intent to hold an investment for a period of time sufficient for recovery of its carrying amount and (b) positive evidence indicating that the investment's carrying amount is recoverable within a reasonable period of time outweighs any evidence to the contrary. All available evidence, both positive and negative, is considered to determine whether, based on the weight of such evidence, the carrying amount of the investment is recoverable within a reasonable period of time. For investments classified as available-for-sale, unrealized losses that are other-than-temporary are recognized in the consolidated statements of operations.

Concentration of Credit Risks. Financial instruments that potentially subject Acacia to concentrations of credit risk are cash equivalents, short-term investments and accounts receivable. Acacia places its cash equivalents and short-term investments primarily in highly rated money market funds and investment grade marketable securities. Cash and cash equivalents are also invested in deposits with certain financial institutions and may, at times, exceed federally insured limits. Acacia has not experienced any significant losses on its deposits of cash and cash equivalents.

Three licensees individually accounted for 45%, 17% and 17%, respectively, of revenues recognized during the year ended December 31, 2018. Three licensees individually accounted for 54%, 21% and 10%, respectively, of revenues recognized during the year ended December 31, 2017. Four licensees individually represented approximately 38%, 36%, 12% and 11%, respectively, of accounts receivable at December 31, 2018. One licensee individually represented 100% of accounts receivable at December 31, 2017.

For 2018 and 2017, 26% and 39%, respectively, of revenues were attributable to licensees domiciled in foreign jurisdictions, based on the jurisdiction of the entity obligated to satisfy payment obligations pursuant to the applicable revenue arrangement. The Company does not have any material foreign operations.

Acacia performs credit evaluations of its licensees with significant receivable balances, if any, and has not experienced any significant credit losses. Accounts receivable are recorded at the executed contract amount and generally do not bear interest. Collateral is not required. An allowance for doubtful accounts may be established to reflect the Company's best estimate of probable losses inherent in the accounts receivable balance, and is reflected as a contra-asset account on the balance sheet and a charge to operating expenses in the statements of operations for the applicable period. The allowance is determined based on known troubled accounts, historical experience, and other currently available evidence. There was no allowance for doubtful accounts established for the periods presented.

Fair Value of Financial Instruments. The carrying value of cash and cash equivalents, accounts receivables, and current liabilities approximates their fair values due to their short-term maturities.

Property and Equipment. Property and equipment are recorded at cost. Major additions and improvements that materially extend useful lives of property and equipment are capitalized. Maintenance and repairs are charged against the results of operations as incurred. When these assets are sold or otherwise disposed of, the asset and related depreciation are relieved, and any gain or loss is included in the consolidated statements of operations for the period of sale or disposal. Depreciation and amortization is computed on a straight-line basis over the following estimated useful lives of the assets:

Furniture and fixtures	3 to 5 years
Computer hardware and software	3 to 5 years
Leasehold improvements	2 to 5 years (Lesser of lease term or useful life of improvement)

Rental payments on operating leases are charged to expense in the consolidated statements of operations on a straight-line basis over the lease term.

Patents. Patents include the cost of patents or patent rights (hereinafter, collectively “patents”) acquired from third-parties or obtained in connection with business combinations. Patent costs are amortized utilizing the straight-line method over their remaining economic useful lives, ranging from one to five years.

Investments at Fair Value. On an individual investment basis, Acacia may elect to account for investments in companies where the Company has the ability to exercise significant influence over operating and financial policies of the investee, at fair value. If the fair value option is applied to an investment that would otherwise be accounted for under the

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equity method of accounting, it is applied to all of the financial interests in the same entity that are eligible items (i.e. common stock and warrants).

Other Investments. Equity investments in common stock and in-substance common stock without readily determinable fair values in companies over which the Company has the ability to exercise significant influence, are accounted for using the equity method of accounting. Acacia includes its proportionate share of earnings and/or losses of its equity method investees in equity in earnings (losses) of investee in the condensed consolidated statements of operations.

Investments in preferred stock with substantive liquidation preferences are accounted for at cost, (subject to impairment considerations, as described below, if any), as adjusted for the impact of changes resulting from observable price changes in orderly transactions for identical or similar investments of the same issuer. In-substance common stock is an investment in an entity that has risk and reward characteristics that are substantially similar to that entity's common stock. An investment in preferred stock with substantive liquidation preferences over common stock, is not substantially similar to common stock, and therefore is not considered in-substance common stock. A liquidation preference is substantive if the investment has a stated liquidation preference that is significant, from a fair value perspective, in relation to the purchase price of the investment. A liquidation preference in an investee that has sufficient subordinated equity from a fair value perspective is substantive because, in the event of liquidation, the investment will not participate in substantially all of the investee's losses, if any.

The initial determination of whether an investment is substantially similar to common stock is made on the initial date of investment if the Company has the ability to exercise significant influence over the operating and financial policies of the investee. That determination is reconsidered if (i) contractual terms of the investment are changed, (ii) there is a significant change in the capital structure of the investee, including the investee's receipt of additional subordinated financing, or (iii) the Company obtains an additional interest in an investment, resulting in the method of accounting for the cumulative interest being based on the characteristics of the investment at the date at which the Company obtains the additional interest. Refer to Note 5 for additional information.

Impairment of Investments. Acacia reviews its investments quarterly for indicators of other-than-temporary impairment. This determination requires significant judgment. In making this judgment, Acacia considers available quantitative and qualitative evidence in evaluating potential impairment of its investments. If the cost of an investment exceeds its fair value, Acacia evaluates, among other factors, general market conditions and the duration and extent to which the fair value is less than cost. Acacia also considers specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, and operational and financing cash flow factors. Once a decline in fair value is determined to be other-than-temporary, an impairment charge is recorded in the consolidated statements of operations and a new cost basis in the investment is established.

Impairment of Long-lived Assets. Acacia reviews long-lived assets and intangible assets for potential impairment annually (quarterly for patents) and when events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. In the event the expected undiscounted future cash flows resulting from the use of the asset is less than the carrying amount of the asset, an impairment loss is recorded equal to the excess of the asset's carrying value over its fair value. If an asset is determined to be impaired, the loss is measured based on quoted market prices in active markets, if available. If quoted market prices are not available, the estimate of fair value is based on various valuation techniques, including a discounted value of estimated future cash flows. In the event that management decides to no longer allocate resources to a patent portfolio, an impairment loss equal to the remaining carrying value of the asset is recorded. Refer to Note 5 for additional information.

Fair value is generally estimated using the “Income Approach,” focusing on the estimated future net income-producing capability of the patent portfolios over the estimated remaining economic useful life. Estimates of future after-tax cash flows are converted to present value through “discounting,” including an estimated rate of return that accounts for both the time value of money and investment risk factors. Estimated cash inflows are typically based on estimates of reasonable royalty rates for the applicable technology, applied to estimated market data. Estimated cash outflows are based on existing contractual obligations, such as contingent legal fee and inventor royalty obligations, applied to estimated license fee revenues, in addition to other estimates of out-of-pocket expenses associated with a specific patent portfolio’s licensing and enforcement program. The analysis also contemplates consideration of current information about the patent portfolio including, status and stage of litigation, periodic results of the litigation process, strength of the patent portfolio, technology coverage and other pertinent information that could impact future net cash flows.

Contingent Liabilities. The Company, from time to time, is involved in certain legal proceedings. Based upon consultation with outside counsel handling its defense in these matters and the Company’s analysis of potential outcomes, if the

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Company determines that a loss arising from such matters is probable and can be reasonably estimated, an estimate of the contingent liability is recorded in its consolidated financial statements. If only a range of estimated loss can be determined, an amount within the range that, based on estimates, assumptions and judgments, reflects the most likely outcome, is recorded as a contingent liability in the consolidated financial statements. In situations where none of the estimates within the estimated range is a better estimate of probable loss than any other amount, the Company records the low end of the range. Any such accrual would be charged to expense in the appropriate period. Litigation expenses for these types of contingencies are recognized in the period in which the litigation services were provided.

Certain of Acacia's operating subsidiaries are often required to engage in litigation to enforce their patents and patent rights. In connection with any of Acacia's operating subsidiaries' patent enforcement actions, it is possible that a defendant may request and/or a court may rule that an operating subsidiary has violated statutory authority, regulatory authority, federal rules, local court rules, or governing standards relating to the substantive or procedural aspects of such enforcement actions. In such event, a court may issue monetary sanctions against Acacia or its operating subsidiaries or award attorney's fees and/or expenses to a defendant(s), which could be material, and if required to be paid by Acacia or its operating subsidiaries, could materially harm the Company's operating results and financial position.

Stock-Based Compensation. The compensation cost for all stock-based awards is measured at the grant date, based on the fair value of the award, and is recognized as an expense on a straight-line basis over the employee's requisite service period (generally the vesting period of the equity award) which is generally two to four years. The fair value of restricted stock and restricted stock unit awards is determined by the product of the number of shares or units granted and the grant date market price of the underlying common stock. The fair value of each option award is estimated on the date of grant using a Black-Scholes option-pricing model. Stock-based compensation expense for awards with service and/or performance conditions that affect vesting is recorded only for those awards expected to vest using an estimated forfeiture rate.

The Financial Accounting Standards Board ("FASB") issued a new standard, effective January 1, 2017, that allows entities to make a policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. Effective January 1, 2017, the Company elected to account for forfeitures of awards as they occur. The prior standard required the Company to estimate the number of awards for which the requisite service period is expected to be rendered and base the accruals of compensation cost on the estimated number of awards that will vest.

The fair values of stock options granted during the periods presented were estimated using the Black-Scholes option-pricing model, based on the following weighted-average assumptions:

For the Years Ended
December 31, 2018 December 31, 2017

Risk-free interest rate	2.26%	1.77%
Term	4.37	4.37
Volatility	51%	51%
Dividend yield	—%	—%

Due to a lack of sufficient historical stock option exercise experience, the Company utilized the simplified method for estimating the expected term for stock options granted during the periods presented. Expected volatility is based on the historical volatility of the Company's stock for the length of time corresponding to the expected term of the option. The risk-free interest rate is based on the U.S. treasury yield curve on the grant date for the expected term of the option.

Restricted stock awards and stock option awards with performance-based vesting conditions generally vest based upon the Company achieving specified cash flow performance targets over a one and two-year period from the date of grant.

Performance-based stock options awards with market-based vesting conditions vest based upon the Company achieving specified stock price targets over a four-year period. The effect of a market condition is reflected in the estimate of the grant-date fair value of the options utilizing a Monte Carlo valuation technique. Compensation cost is recognized for an option with a market-based vesting condition provided that the requisite service is rendered, regardless of when, if ever, the market condition is satisfied. The service period for options with a market-based vesting condition is inferred from the application of the Monte Carlo valuation technique. The derived service period represents the duration of the median of the distribution of share price paths on which the market condition is satisfied. The duration is the period of time from the service inception date to the expected date of satisfaction, as determined from the valuation technique. Assumptions utilized in connection with the Monte Carlo valuation technique included: estimated risk-free interest rate; expected volatility; and expected dividend yield. The risk-free interest rate was determined based on the yields available on U.S. Treasury zero-coupon

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issues. The expected stock price volatility was determined using historical volatility. The expected dividend yield was based on expectations regarding dividend payments.

Profits Interest Units (“Units”) are accounted for in accordance with Accounting Standards Codification (“ASC”) 718-10, “Compensation - Stock Compensation.” The Units vest as described at Note 9, and therefore, the vesting conditions do not meet the definition of service, market or performance conditions, as defined in ASC 718. As such, the Units are classified as liability awards. Liability classified awards are measured at fair value on the grant date and re-measured each reporting period at fair value until the award is settled. Compensation expense is adjusted each reporting period for changes in fair value prorated for the portion of the requisite service period rendered. Initially, compensation expense was recognized on a straight-line basis over the employee’s requisite service period (generally the vesting period of the equity award) which was five years. Upon full vesting of the award, which occurred during the three months ended September 30, 2017, previously unrecognized compensation expense was immediately recognized in the period, and will continue to be fully recognized for any changes in fair value, until the Units are settled. The Company has a purchase option to purchase the vested Units that are not otherwise forfeited after termination of continuous service. The exercise price of the purchase option is the fair market value of the Units on the date of termination of continuous service. At each reporting date, the value of the Units that are subject to the purchase option will be the measured at the fair value on the termination date. Non-cash stock compensation expense related to the Units is reflected in general and administrative expense in the accompanying consolidated statements of operations.

Income Taxes. Income taxes are accounted for using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in Acacia’s consolidated financial statements or consolidated income tax returns. A valuation allowance is established to reduce deferred tax assets if all, or some portion, of such assets will more than likely not be realized, or if it is determined that there is uncertainty regarding future realization of such assets.

Under U.S. generally accepted accounting principles, a tax position is a position in a previously filed tax return or a position expected to be taken in a future tax filing that is reflected in measuring current or deferred income tax assets and liabilities. Tax positions are recognized only when it is more likely than not (likelihood of greater than 50%), based on technical merits, that the position will be sustained upon examination. Tax positions that meet the more likely than not threshold are measured using a probability weighted approach as the largest amount of tax benefit that is greater than 50% likely of being realized upon settlement.

Segment Reporting. Acacia uses the management approach, which designates the internal organization that is used by management for making operating decisions and assessing performance as the basis of Acacia’s reportable segments. Acacia’s patent licensing and enforcement business constitutes its single reportable segment.

Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Acacia believes that, of the significant accounting policies described herein, the accounting policies associated with revenue recognition, the valuation of the loan and equity instruments discussed at Note 6, stock-based compensation expense including the valuation of profits interests, impairment of patent-related intangible assets, the determination of the economic useful life of amortizable intangible assets, income taxes and valuation allowances against net deferred tax assets, require its most difficult, subjective or complex judgments.

Income (Loss) Per Share. The Company computes net income (loss) attributable to common stockholders using the two-class method required for capital structures that include participating securities. Under the two-class method,

securities that participate in non-forfeitable dividends, such as the Company's outstanding unvested restricted stock, are considered "participating securities."

In applying the two-class method, (i) basic net income (loss) per share is computed by dividing net income (loss) (less any dividends paid on participating securities) by the weighted average number of shares of common stock and participating securities outstanding for the period and (ii) diluted earnings per share may include the additional effect of other securities, if dilutive, in which case the dilutive effect of such securities is calculated by applying the two-class method and the treasury stock method to the assumed exercise or vesting of potentially dilutive common shares. The method yielding the more dilutive result is ultimately reported for the applicable period. Potentially dilutive common stock equivalents primarily consist of employee stock options, and restricted stock units for calculations utilizing the two-class method, and also include unvested restricted stock, when utilizing the treasury method.

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The following table presents the weighted-average number of common shares outstanding used in the calculation of basic and diluted income per share:

	2018	2017
Numerator (in thousands):		
Basic and Diluted		
Net income (loss) attributable to Acacia Research Corporation	\$(105,029)	\$ 22,180
Undistributed earnings allocated to participating securities	—	(33)
Net income (loss) attributable to common stockholders – basic and diluted	\$(105,029)	\$ 22,147
Denominator:		
Weighted-average shares used in computing net loss per share attributable to common stockholders – basic	49,969,062	50,495,119
Effect of potentially dilutive securities:		
Common stock options and restricted stock units	—	196,893
Weighted-average shares used in computing net income (loss) per share attributable to common stockholders – diluted	49,969,062	50,692,012
Basic and diluted net loss per common share	\$(2.10)	\$ 0.44
Anti-dilutive equity-based incentive awards excluded from the computation of diluted loss per share	3,129,719	4,425,187

Treasury Stock. Repurchases of the Company's outstanding common stock are accounted for using the cost method. The applicable par value is deducted from the appropriate capital stock account on the formal or constructive retirement of treasury stock. Any excess of the cost of treasury stock over its par value is charged to additional paid-in capital, and reflected as Treasury Stock on the consolidated balance sheets.

3. SHORT-TERM INVESTMENTS

Short-term investments for the periods presented were comprised of the following (in thousands):

	December 31, 2018			
<u>Security Type</u>	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Trading securities - debt	\$33,643	\$ 18	\$ (19)	\$33,642
Trading securities - equity	3,389	27	(404)	3,012
	\$37,032	\$ 45	\$ (423)	\$36,654

Short-term investments as of December 31, 2018 were comprised of investments in corporate bonds (debt securities) and investments in equity securities of publicly held companies (equity). For the years ended December 31, 2018 and 2017, proceeds from the sale of debt securities were \$65,144,000 and \$467,790,000, respectively. For the year ended December 31, 2018, proceeds from the sale of equity securities was \$1,496,000. There were no short-term investments as of December 31, 2017.

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4. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consist of the following at December 31, 2018 and 2017 (in thousands):

	2018	2017
Payroll and other employee benefits	\$205	\$465
Accrued vacation	144	294
Accrued legal expenses - patent	5,974	5,479
Foreign taxes payable	374	15
Accrued consulting and other professional fees	1,241	1,364
Other accrued liabilities	409	339
	\$8,347	\$7,956

5. PATENTS

Acacia's only identifiable intangible assets are patents and patent rights, with estimated remaining economic useful lives ranging from one to five years. For all periods presented, all of Acacia's identifiable intangible assets were subject to amortization. The gross carrying amounts and accumulated amortization related to investments in intangible assets as of December 31, 2018 and 2017 are as follows (in thousands):

	2018	2017
Gross carrying amount - patents	\$326,167	\$444,137
Accumulated amortization - patents ⁽¹⁾	(319,580)	(382,220)
Patents, net	\$6,587	\$61,917

⁽¹⁾ Includes patent impairment charges for the applicable periods.

The weighted-average remaining estimated economic useful life of Acacia's patents and patent rights is 4 years. Scheduled annual aggregate amortization expense is estimated to be \$2,559,000 in fiscal year 2019, \$1,671,000 in 2020, \$811,000 in 2021, \$811,000 in 2022 and \$735,000 in 2023.

Acacia recorded impairment of patent-related intangible asset charges totaling \$28,210,000 and \$2,248,000 for the years ended December 31, 2018 and 2017, respectively. The impairment charges related to impairments of patent portfolios due to a reduction in expected estimated future net cash flows and certain patent portfolios that management determined it would no longer allocate future resources to in connection with the licensing and enforcement of such portfolios, due primarily to adverse litigation outcomes, potential prior art related complexities and/or the overall determination that future resources would be allocated to other licensing and enforcement programs with higher potential return profiles. The impairment charges for the periods presented consisted of the excess of the asset's carrying value over its estimated fair value.

For the year ended December 31, 2018, pursuant to the terms of the respective inventor agreements, certain Acacia operating subsidiaries elected to terminate or sell their rights to patent portfolios, resulting in the acceleration of amortization expense for the patent-related assets totaling \$8,307,000. For the year ended December 31, 2017, there were no terminations or sales of patent portfolios.

For the years ended December 31, 2018 and 2017, capitalized patent costs, accumulated amortization and impairment

charges, and sales proceeds related to patent-related sales and disposals are as follows (in thousands):

	2018	2017
Capitalized patent costs	\$117,970	\$ —
Accumulated amortization / impairment charges	109,663	—
Sales proceeds	14,500	—

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6. INVESTMENTS

Investment at Fair Value

Veritone Investment Agreement. On August 15, 2016, Acacia entered into an Investment Agreement with Veritone, Inc. (“Veritone”) pursuant to which Acacia funded in aggregate \$20 million of loans to Veritone which were converted into 1,523,746 shares of Veritone’s common stock upon the public offering of Veritone common stock on May 17, 2017 (“IPO”), based on a conversion price of \$13.61 per share. Veritone also issued Acacia a total of 154,312 warrants to purchase shares of Veritone’s common stock at an exercise price of \$13.61 per share expiring in 2020.

In addition, in August 2016, Veritone issued Acacia a five-year warrant to purchase up to \$50 million worth of shares of Veritone’s common stock at an exercise price of \$13.61 per share subject to certain adjustments. Upon the consummation of Veritone’s IPO, Acacia exercised its option to purchase an additional 2,150,335 shares of Veritone common stock, at an aggregate purchase price of \$29.3 million. Acacia then received an additional warrant that provides for the issuance of an additional 809,400 shares of Veritone common stock at an exercise price of \$13.61 per share expiring in 2022.

Veritone Bridge Loan. On March 14, 2017, Acacia entered into an additional secured convertible promissory note with Veritone pursuant to which Acacia funded \$4.0 million which was converted into 445,440 shares of Veritone’s common stock at a conversion price of \$13.61 per share in the IPO. Acacia also received a 10-year warrant to purchase up to 156,720 shares of Veritone common stock at an exercise price of \$13.61 per share expiring in 2027. As a result of the foregoing transactions, Acacia received an aggregate total of 4,119,521 of Veritone shares and 1,120,432 of warrants in Veritone. On October 5, 2018, a registration statement on Form S-3 registering all of Acacia’s shares of Veritone common stock was declared effective by the SEC. During the year ended December 31, 2018, Acacia sold 2,700,000 shares Veritone common stock at prices ranging from \$4.95 to \$10.44 and recorded a realized loss of \$19.1 million.

At December 31, 2018, the fair value of the 1,419,521 shares of Veritone common stock owned by Acacia totaled \$5,395,000. At December 31, 2018, the fair value of the 1,120,432 common stock purchase warrants held by Acacia totaled \$2,064,000. The Veritone common shares were subject to a lock-up agreement that expired on August 15, 2018, subsequent to which the fair value of the common stock (Level 1) and fair value of the common stock purchase warrants (Level 2) excluded a DLOM.

Changes in the fair value of Acacia’s investment in Veritone are recorded as unrealized gains or losses in the consolidated statements of operations. For the period from the IPO on May 17, 2017 to December 31, 2017 and for the year ended December 31, 2018, the accompanying consolidated statements of operations reflected the following (in thousands):

	2018	2017
Gain on conversion of loans and accrued interest ⁽¹⁾	\$—	\$2,671
Gain on exercise of warrant ⁽²⁾	—	4,616
Change in fair value of investment, warrants	(11,895)	8,317
Change in fair value of investment, common stock	(47,208)	33,922
Loss on sale of investment, common stock	(19,095)	—
Net realized and unrealized gain (loss) on investment at fair value	\$(78,198)	\$49,526

⁽¹⁾ Pre-conversion difference between carrying value of Loan and accrued interest and the estimated fair value of common stock discounted for lack of marketability.

⁽²⁾ Pre-conversion difference between carrying value of Primary Warrant and the estimated fair value of common stock and 10% Warrant discounted for lack of marketability.

Miso Robotics Investment

In June 2017, Acacia made an investment in the Series A Preferred financing round for Miso Robotics, Inc. (“Miso Robotics”), an innovative leader in robotics and artificial intelligence solutions, totaling \$2,250,000, acquiring a 22.6%

ownership interest in Series A preferred stock of Miso Robotics, and one board seat. In February 2018, Acacia made an additional equity investment in the Series B Preferred financing round for Miso Robotics totaling \$6,000,000, increasing its ownership interest (Series B preferred stock) in Miso Robotics to approximately 30%, and acquiring an additional board seat.

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As of February 2018, the preferred stock was not deemed to be in-substance common stock due to the substantive liquidation preference associated with the preferred stock. As such, as of February 2018, the cumulative investment in Miso Robotics is recorded at cost and assessed for any impairment at each balance sheet date. Prior to February 2018, the equity method of accounting was applied.

7. STOCKHOLDERS' EQUITY

Repurchases of Common Stock. In February 2018, Acacia's Board of Directors authorized the repurchase of up to \$20,000,000 of the Company's outstanding common stock in open market purchases or private purchases, from time to time, in amounts and at prices to be determined by the Board of Directors at its discretion (the "Stock Repurchase Program"). In determining whether or not to repurchase any shares of Acacia's common stock, Acacia's Board of Directors consider such factors as the impact of the repurchase on Acacia's cash position, as well as Acacia's capital needs and whether there is a better alternative use of Acacia's capital. Acacia has no obligation to repurchase any amount of its common stock under the Stock Repurchase Program. Repurchases to date were made in the open market in compliance with applicable SEC rules. The authorization to repurchase shares presented an opportunity to reduce the outstanding share count and enhance stockholder value. The repurchased shares are expected to be retired. Monthly stock repurchases for the periods presented, all of which were purchased as part of a publicly announced plan or program, were as follows:

	Total Number of Shares Purchased	Average Price paid per Share	Approximate Dollar Value of Shares that May Yet be Purchased under the Program	Plan Expiration
May 1, 2018- May 30, 2018	1,190,420	\$ 3.89	\$ 15,366,000	February 28, 2019
Totals for 2018	1,190,420	\$ 3.89		

Tax Benefits Preservation Plan. On March 15, 2016, Acacia's Board of Directors announced that it unanimously approved the adoption of a Tax Benefits Preservation Plan (the "Plan"). The purpose of the Plan is to protect the Company's ability to utilize potential tax assets, such as net operating loss carryforwards ("NOLs") and tax credits to offset potential future taxable income.

The Plan is designed to reduce the likelihood that the Company will experience an ownership change by discouraging any (i) person or group from acquiring beneficial ownership of 4.9% or more of the Company's outstanding common stock and (ii) any existing shareholders who, as of the time of the first public announcement of the adoption of the Plan, beneficially own more than 4.9% of the Company's then-outstanding shares of the Company's common stock from acquiring additional shares of the Company's common stock (subject to certain exceptions). There is no guarantee, however, that the Plan will prevent the Company from experiencing an ownership change.

In connection with the adoption of the Plan, Acacia's Board of Directors authorized and declared a dividend distribution of one right for each outstanding share of the Company's common stock to shareholders of record at the close of business on March 16, 2016. On or after the distribution date, each right would initially entitle the holder to purchase one one-thousandth of a share of the Company's Series A Junior Participating Preferred Stock, \$0.001 par value for a purchase price of \$15.00.

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ACACIA RESEARCH CORPORATION
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8. INCOME TAXES

Acacia's provision for income taxes for the fiscal periods presented consisted of the following (in thousands):

	2018	2017
Current:		
Federal	\$—	\$—
State	87	90
Foreign	1,092	2,865
Total current	1,179	2,955
Deferred:		
Federal	—	—
State	—	—
Total deferred	—	—
Provision for income taxes	\$1,179	\$2,955

The tax effects of temporary differences and carryforwards that give rise to significant portions of deferred tax assets and liabilities consist of the following at December 31, 2018 and 2017 (in thousands):

	2018	2017
Deferred tax assets:		
Net operating loss and capital loss carryforwards and credits	\$104,862	\$90,871
Unrealized loss on investments held at fair value	2,455	—
Stock compensation	1,365	2,635
Fixed assets and intangibles	3,330	6,197
Basis of investments in affiliates	286	984
Accrued liabilities and other	208	167
State taxes	26	35
Total deferred tax assets	112,532	100,889
Valuation allowance	(112,532)	(90,278)
Total deferred tax assets, net of valuation allowance	—	10,611
Deferred tax liabilities:		
Unrealized gain on investments held at fair value	—	(10,587)
Other	(18)	(24)
Total deferred tax liabilities	(18)	(10,611)
Net deferred tax assets (liabilities)	\$(18)	\$—

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ACACIA RESEARCH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A reconciliation of the federal statutory income tax rate and the effective income tax rate is as follows:

	2018	2017
Statutory federal tax rate - (benefit) expense	21 %	35 %
State income and foreign taxes, net of federal tax effect	(1)%	8 %
Foreign tax credit	— %	— %
Noncontrolling interests in operating subsidiaries	— %	1 %
Nondeductible permanent items	(1)%	3 %
Change in tax rate	— %	102 %
Valuation allowance	(20)%	(137)%
	(1)%	12 %

For the periods presented, the Company recorded full valuation allowances against its net deferred tax assets due to uncertainty regarding future realization pursuant to guidance set forth in ASC 740, “Income Taxes.” In future periods, if the Company determines it will more likely than not be able to realize certain of these amounts, the applicable portion of the benefit from the release of the valuation allowance will generally be recognized in the statements of operations in the period the determination is made.

At December 31, 2018, Acacia had U.S. federal and state income tax net operating loss carryforwards (“NOLs”) totaling approximately \$222,861,000 and \$19,471,000, expiring between 2026 and 2038, and 2028 and 2038, respectively. Capital loss carryovers totaled \$19,952,000 at December 31, 2018, expiring between 2019 and 2023.

As of December 31, 2018, Acacia had approximately \$51,508,000 of foreign tax credits, expiring between 2020 and 2026. In general, foreign taxes withheld may be claimed as a deduction on future U.S. corporate income tax returns, or as a credit against future U.S. income tax liabilities, subject to certain limitations.

Tax expense for the periods presented primarily reflects foreign taxes withheld on revenue agreements executed with licensees in foreign jurisdictions and other state taxes. Excluding the impact of the change in valuation allowance and the impact of the federal tax rate change under the change in tax law described below, annual effective tax rates were 19% and 47% for fiscal years 2018 and 2017, respectively. Results for fiscal year 2018 included an unrealized loss on Acacia’s investment in Veritone which created a deferred tax asset totaling approximately \$2,455,000. Results for fiscal year 2017 included an unrealized gain on Acacia’s investment in Veritone which created a deferred tax liability totaling approximately \$10,587,000. The 2017 deferred tax liability was reversed in fiscal year 2018 as a result of the 2018 unrealized loss on Acacia’s investment in Veritone and the realized loss on the sale of Veritone common stock. The effective tax rate reflects both the recognition of the deferred tax liability and the reversal of the valuation allowance.

Effective January 1, 2017, the Company adopted a new standard that requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. The adoption of this standard resulted in the Company recognizing gross federal and state deferred tax assets of \$21,350,000 and \$1,559,000, respectively, for the year ended December 31, 2017 related to the impact of share-based payments to employees in prior periods. These deferred tax assets are fully offset by a valuation allowance and were impacted by the change in tax rate described below.

Acacia is subject to taxation in the U.S. and in various state jurisdictions and incurs foreign tax withholdings on revenue agreements with licensees in certain foreign jurisdictions. With no material exceptions, Acacia is no longer

subject to U.S. federal or state examinations by tax authorities for years before 2011. The California Franchise Tax Board is auditing the 2011 through 2016 California combined income tax returns. The California Franchise Tax Board has proposed adjustments for 2011 and 2012 that, if expensed, would not be material to the consolidated statements of operations for the periods presented. We have protested these adjustments.

At December 31, 2018 and 2017, the Company had total unrecognized tax benefits of approximately \$808,000. No interest and penalties have been recorded for the unrecognized tax benefits for the periods presented. At December 31, 2017, if recognized, approximately \$808,000 of tax benefits, net of valuation allowance, would impact the Company's effective tax rate. The Company does not expect that the liability for unrecognized tax benefits will change significantly within the next 12 months.

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ACACIA RESEARCH CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Acacia recognizes interest and penalties with respect to unrecognized tax benefits in income tax expense. Acacia has identified no uncertain tax position for which it is reasonably possible that the total amount of unrecognized tax benefits will significantly increase or decrease within 12 months.

On December 22, 2017, new U.S. tax legislation was enacted that has significantly changed the U.S. federal income taxation of U.S. corporations, including by reducing the U.S. corporate income tax rate to 21%, revising the rules governing net operating losses and foreign tax credits, and introducing new anti-base erosion provisions. For the year ended December 31, 2017, we reflected a write-down of our deferred income tax assets (including the value of our net operating loss carryforwards and our tax credit carryforwards) due the reduction of the U.S. corporate income tax rate and recorded a reduction of approximately \$25,261,000 related to the revaluation of our deferred tax assets. This amount was not adjusted during the year ended December 31, 2018. Given the full valuation allowance provided for net deferred tax assets as of December 31, 2018 and 2017, the change in tax law did not have a material impact on our consolidated financial statements.

9. EQUITY-BASED INCENTIVE PLANS

Stock-Based Incentive Plans

The 2013 Acacia Research Corporation Stock Incentive Plan (“2013 Plan”) and the 2016 Acacia Research Corporation Stock Incentive Plan (“2016 Plan”) (collectively, the “Plans”) were approved by the stockholders of Acacia in May 2013 and June 2016, respectively. All Plans allow grants of stock options, stock awards and performance shares with respect to Acacia common stock to eligible individuals, which generally includes directors, officers, employees and consultants. Except as noted below, the terms and provisions of the Plans are identical in all material respects.

Acacia’s compensation committee administers the discretionary option grant and stock issuance programs. The compensation committee determines which eligible individuals are to receive option grants or stock issuances under those programs, the time or times when the grants or issuances are to be made, the number of shares subject to each grant or issuance, the status of any granted option as either an incentive stock option or a non-statutory stock option under the federal tax laws, the vesting schedule to be in effect for the option grant or stock issuance and the maximum term for which any granted option is to remain outstanding. The exercise price of options is generally equal to the fair market value of Acacia’s common stock on the date of grant. Options generally begin to be exercisable six months to one year after grant and generally expire seven to ten years after grant. Stock options with time-based vesting generally vest over two to three years and restricted shares with time based vesting generally vest in full after two to three years (generally representing the requisite service period). The Plans terminate no later than the tenth anniversary of the approval of the incentive plans by Acacia’s stockholders.

The Plans provide for the following separate programs:

Discretionary Option Grant Program. Under the discretionary option grant program, Acacia’s compensation committee may grant (1) non-statutory options to purchase shares of common stock to eligible individuals in the employ or service of Acacia or its subsidiaries (including employees, non-employee board members and consultants) at an exercise price not less than 85% of the fair market value of those shares on the grant date, and (2) incentive stock options to purchase shares of common stock to eligible employees at an exercise price not less than 100% of the fair market value of those shares on the grant date (not less than 110% of fair market value if such employee actually or constructively owns more than 10% of Acacia’s voting stock or the voting stock of any of its subsidiaries).

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Stock Issuance Program. Under the stock issuance program, eligible individuals may be issued shares of common stock directly, upon the attainment of performance milestones or the completion of a specified period of service or as a bonus for past services. Under this program, the purchase price for the shares shall not be less than 100% of the fair market value of the shares on the date of issuance, and payment may be in the form of cash or past services rendered. The eligible individuals shall have full stockholder rights with respect to any shares of Common Stock issued to them under the Stock Issuance Program, whether or not their interest in those shares is vested. Accordingly, the eligible individuals shall have the right to vote such shares and to receive any regular cash dividends paid on such shares.

Automatic Option Grant Program. Through fiscal year 2016, each non-employee director received restricted stock units or stock options for the number of shares determined by dividing the annual retainer by the grant date fair value of Acacia's common stock on the grant date. In addition, each new non-employee director received restricted

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stock units or stock options for the number of shares determined by dividing the annual board of directors retainer by the grant date fair value of Acacia's common stock on the commencement date. These restricted stock units and stock options vested in a series of twelve quarterly installments over the three year period following the grant date, subject to immediate acceleration upon a change in control. Acacia will deliver the unrestricted shares corresponding to the vested restricted stock units within thirty (30) days after the first to occur of the following events: (i) the fifth (5th) anniversary of the grant date; or (ii) termination of the non-employee director's service as a member of the Company's Board of Directors. The non-employee directors do not have any rights, benefits or entitlements with respect to any shares unless and until the shares have been delivered.

The number of shares of Common Stock initially reserved for issuance under the 2013 Plan was 4,750,000 shares. No new additional shares will be added to the 2013 Plan without security holder approval (except for shares subject to outstanding awards that are forfeited or otherwise returned to the 2013 Plan). The stock issuable under the 2013 Plan shall be shares of authorized but unissued or reacquired Common Stock, including shares repurchased by the Company on the open market. In June 2016, 625,390 shares of common stock available for issuance under the 2013 Plan were transferred into the 2016 Plan. At December 31, 2018, there were 709,000 shares available for grant under the 2013 Plan.

The number of shares of Common Stock initially reserved for issuance under the 2016 Plan was 4,500,000 shares plus 625,390 shares of common stock available for issuance under the 2013 Plan, as of the effective date of the Plan. At December 31, 2018, there were 3,689,000 shares available for grant under the 2016 Plan.

Upon the exercise of stock options, the granting of restricted stock, or the delivery of shares pursuant to vested restricted stock units, it is Acacia's policy to issue new shares of common stock. Acacia's board of directors may amend or modify the Plans at any time, subject to any required stockholder approval. As of December 31, 2018, there are 7,938,000 shares of common stock reserved for issuance under the Plans.

Stock-based award grant activity for the periods presented was as follows:

	2018		2017	
	Shares	Aggregate fair value (in thousands)	Shares	Aggregate fair value (in thousands)
Restricted stock awards with time-based service conditions	102,000	\$ 386	—	\$ —
Stock options with time-based service vesting conditions	930,000	1,588	1,368,000	2,930
Total incentive awards granted	1,032,000	\$ 1,974	1,368,000	\$ 2,930

The following table summarizes stock option activity for the Plans for the year ended December 31, 2018:

	Options	Weighted-Average Exercise Price	Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2017	5,830,000	\$5.13		
Granted	930,000	\$3.91		
Exercised	(83,000)	\$3.12		
Expired/forfeited	(3,168,000)	\$5.00		
Outstanding at December 31, 2018	3,509,000	\$4.96	4.1 years	\$ —
Vested	2,339,000	\$4.82	3.2 years	\$ —

Exercisable at December 31, 2018 2,339,000 \$4.82 3.2 years \$ —

The aggregate intrinsic value of options exercised during the years ended December 31, 2018 and 2017 was \$51,000 and \$296,000, respectively. The aggregate intrinsic value of options vested during the year ended December 31, 2018 was \$0. The aggregate fair value of options granted during the year ended December 31, 2018 was \$1,588,000. The aggregate fair value of options vested during the years ended December 31, 2018 and 2017 was \$1,918,000 and \$2,009,000, respectively. As of December 31, 2018, the total unrecognized compensation expense related to nonvested stock option awards was \$844,000, which is expected to be recognized over a weighted-average term of approximately 1 year.

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The following table summarizes nonvested restricted share activity for the year ended December 31, 2018:

	Nonvested Restricted Shares	Weighted Average Grant Date Fair Value
Nonvested restricted stock at December 31, 2017	123,000	\$ 4.77
Granted	102,000	\$ 3.79
Vested	(225,000)	\$ 4.32
Canceled	—	\$ —
Nonvested restricted stock at December 31, 2018	—	\$ —

The weighted-average grant date fair value of nonvested restricted stock granted during the years ended December 31, 2018 and 2016 was \$3.79 and \$3.12, respectively. There were no grants of restricted stock during the year ended December 31, 2017. The aggregate fair value of restricted stock that vested during the years ended December 31, 2018 and 2017 was \$972,000 and \$1,560,000, respectively. As of December 31, 2018, there was no unrecognized compensation expense related to nonvested restricted stock awards.

The following table summarizes restricted stock unit activity for the year ended December 31, 2018:

	Restricted Stock Units	Weighted Average Grant Date Fair Value
Nonvested restricted stock units outstanding at December 31, 2017	2,000	\$ 16.72
Vested	(2,000)	\$ 16.72
Nonvested restricted stock units outstanding at December 31, 2018	—	\$ —
Vested restricted stock units outstanding at December 31, 2018	31,000	\$ 15.43

There were no restricted units granted during the years ended December 31, 2018 and 2017. The aggregate fair value of restricted stock units that vested during the years ended December 31, 2018 and 2017 was \$40,000 and \$200,000, respectively. As of December 31, 2018, there was no unrecognized compensation expense related to restricted stock unit awards.

Profits Interest Plan

On February 16, 2017, AIP Operation LLC, a Delaware limited liability company (“AIP”), and an indirect subsidiary of Acacia, adopted a Profits Interest Plan (the “Plan”) that provides for the grant of membership interests in AIP to certain members of management and the Board of Directors of Acacia as compensation for services rendered for or on behalf of AIP. Each profits interest unit granted pursuant to the Plan is intended to qualify as a “profits interest” for U.S. federal income tax purposes and will only have value to the extent the fair value of AIP increases beyond the fair value at the issuance date of the membership interests. The membership interests are represented by units (the “Units”) reserved for the issuance of awards under the Plan. The Units entitle the holders to share in or be allocated certain AIP profits and losses and to receive or share in AIP distributions pursuant to the AIP Limited Liability Company Operating Agreement entered into as of February 16, 2017 (the “LLC Agreement”). In connection with the adoption of the Plan, a form of Profits Interest Agreement was approved pursuant to which Units may be granted from time to

time. Units vest upon AIP's achievement of certain performance milestones (one-third upon 150% appreciation, and the remaining two-thirds upon 300% appreciation in value of Acacia's aggregate investment in Veritone), subject to the continued service of the recipient, and are subject to the terms and conditions of the Plan, the Profits Interest Agreement and the LLC Agreement. The Units were fully vested in September 2017.

Acacia owns 60% of the membership interests in AIP and at all times will control AIP. Acacia from time to time may contribute to AIP certain assets or securities related to portfolio companies in which Acacia holds an interest. Units may be awarded as one-time, discretionary grants to recipients. As of December 31, 2018, AIP holds the Veritone 10% Warrant described at Note 6.

Profits interests totaling 400 Units, or 40% of the membership interests in AIP, were granted in February 2017, with an aggregate grant date fair value of \$722,000. The fair value of the Units totaled \$591,000 as of December 31, 2018. Upon full vesting of the units in September 2017, all previously unrecognized compensation expense was immediately recognized.

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Compensation expense for the periods presented was comprised of the following:

	2018	2017
Restricted stock awards with time-based service conditions	\$460	\$1,025
Restricted stock unit awards with time-based service conditions	1	161
Restricted stock awards with performance-based vesting conditions	—	121
Stock options with time-based service vesting conditions	1,672	2,165
Stock options with market-based vesting conditions	—	2,372
Profits interests units	(2,450)	3,041
Total compensation expense	\$(317)	\$8,885

10. COMMITMENTS AND CONTINGENCIES

Operating Leases

Acacia leases certain office space under various operating lease agreements expiring at various dates from 2019 through 2020. Minimum annual rental commitments, net of guaranteed sublease income, for operating leases having initial or remaining noncancellable lease terms in excess of one year are as follows (in thousands):

Years ending December 31,

2019	\$599
2020	89
Total minimum lease payments	\$688

Rent expense for the years ended December 31, 2018 and 2017 approximated \$1,106,000 and \$1,392,000, respectively. Rental payments are expensed in the statements of operations in the period to which they relate. Scheduled rent increases are amortized on a straight-line basis over the lease term. During the year ended December 31, 2018, we recorded a one-time charge of \$629,000 for the excess of lease payments over anticipated sublease income through expiration of the lease.

Inventor Royalties and Contingent Legal Expenses

In connection with the investment in certain patents and patent rights, certain of Acacia's operating subsidiaries executed related agreements which grant to the former owners of the respective patents or patent rights, the right to receive inventor royalties based on future net revenues (as defined in the respective agreements) generated as a result of licensing and otherwise enforcing the respective patents or patent portfolios.

Acacia's operating subsidiaries may retain the services of law firms that specialize in patent licensing and enforcement and patent law in connection with their licensing and enforcement activities. These law firms may be retained on a contingent fee basis whereby such law firms are paid on a scaled percentage of any negotiated fees, settlements or judgments awarded based on how and when the fees, settlements or judgments are obtained.

Patent Enforcement

Certain of Acacia's operating subsidiaries are often required to engage in litigation to enforce their patents and patent rights. In connection with any of Acacia's operating subsidiaries' patent enforcement actions, it is possible that a defendant may request and/or a court may rule that an operating subsidiary has violated statutory authority, regulatory authority, federal rules, local court rules, or governing standards relating to the substantive or procedural aspects of such enforcement actions. In such event, a court may issue monetary sanctions against Acacia or its operating subsidiaries or award attorney's fees and/or expenses to a defendant(s), which could be material.

Other

On June 17, 2015, Celltrace Communications Ltd. ("Celltrace") filed a lawsuit against Acacia in U.S. District Court for the Southern District of New York, Case No. 1:15-cv-04746, alleging, among other things, significant damages for alleged breach of contract, unjust enrichment and fraud. Acacia disputes the allegations and does not believe that Celltrace is entitled to any damages. Acacia successfully moved to compel arbitration of the dispute, and the District Court stayed the litigation

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pending arbitration before the International Court of Arbitration for the International Chamber of Commerce (the “ICC”). Celltrace appealed the decision to the U.S. Court of Appeals for the Second Circuit, which denied the appeal. Celltrace filed its request for arbitration of the claims with the ICC on November 28, 2016. Acacia filed an answer denying all allegations of wrongdoing and asserting affirmative defenses. A tribunal was appointed to preside over the arbitration and conducted its first case management conference on June 26, 2017. The parties conducted discovery and submitted their cases in chief to the tribunal in a series of written submissions per the tribunal’s orders between January 2018 and December 2018. The tribunal held an evidentiary hearing with live witness testimony in New York City between February 4, 2019 and February 13, 2019. At the end of the hearing, the tribunal set a schedule for post-hearing briefing by the parties, which is currently scheduled to conclude in April 2019, after which the tribunal will render a decision. Acacia continues to vigorously contest all allegations of wrongdoing.

On December 6, 2017, the Federal Court of Canada allowed a counterclaim for invalidity of a patent asserted by Rapid Completions LLC and awarded costs payable by Rapid Completions LLC in an amount to be determined.

Acacia is subject to claims, counterclaims and legal actions that arise in the ordinary course of business. Management believes that the ultimate liability with respect to these claims and legal actions, if any, will not have a material effect on Acacia’s consolidated financial position, results of operations or cash flows. Fiscal year 2018 operating expenses included expenses for settlement and contingency accruals totaling \$2,602,000, net of prior accruals.

Guarantees and Indemnifications

Certain of Acacia’s operating subsidiaries have made guarantees and indemnities under which they may be required to make payments to a guaranteed or indemnified party, in relation to certain transactions, including revenue transactions in the ordinary course of business. In connection with certain facility leases, Acacia and certain of its operating subsidiaries have indemnified lessors for certain claims arising from the facilities or the leases. Acacia indemnifies its directors and officers to the maximum extent permitted under the laws of the State of Delaware. However, Acacia has a directors and officers insurance policy that may reduce its exposure in certain circumstances and may enable it to recover a portion of future amounts that may be payable, if any. The duration of the guarantees and indemnities varies and, in many cases is indefinite but subject to statute of limitations. The majority of guarantees and indemnities do not provide any limitations of the maximum potential future payments that Acacia could be obligated to make. To date, Acacia has made no payments related to these guarantees and indemnities. Acacia estimates the fair value of its indemnification obligations to be insignificant based on this history and therefore, have not recorded any liability for these guarantees and indemnities in the accompanying consolidated balance sheets. Additionally, no events or transactions have occurred that would result in a material liability at December 31, 2018.

Other

In August 2010, a wholly owned subsidiary of Acacia became the general partner of the Acacia IP Fund, which was formed in August 2010. The Acacia IP Fund invests in, licenses and enforces IP consisting primarily of patents, patent rights, and patented technologies. The Acacia IP Fund was terminated as of December 31, 2017. The final distribution to the partners of the Acacia IP Fund will be made in 2019.

11. RETIREMENT SAVINGS PLAN AND EXECUTIVE SEVERANCE POLICY

Retirement Savings Plan. Acacia has an employee savings and retirement plan under section 401(k) of the Code (the “Plan”). The Plan is a defined contribution plan in which eligible employees may elect to have a percentage of their compensation contributed to the Plan, subject to certain guidelines issued by the Internal Revenue Service. Acacia

may contribute to the Plan at the discretion of the board of directors. There were no contributions made by Acacia during the periods presented.

Executive Severance Policy. Under Acacia's Amended Executive Severance Policy, full-time employees as of July 2017 and prior with the title of Senior Vice President and higher ("SVP and higher") are entitled to receive certain benefits upon termination of employment. If employment of an SVP and higher employee is terminated for other than cause or other than on account of death or disability, Acacia will (i) promptly pay to the SVP and higher employee a lump sum amount equal to the aggregate of (a) accrued obligations (i.e., annual base salary through the date of termination to the extent not theretofore paid and any compensation previously deferred (together with any accrued interest or earnings thereon) and any accrued vacation pay, and reimbursable expenses, in each case to the extent not theretofore paid) and (b) three (3) months of base salary

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

for each full year that the SVP and higher employee was employed by the Company (the “Severance Period”), up to a maximum of twelve (12) months (eighteen (18) months for executive officers of Acacia Research Corporation) of base salary, and (ii) provide to the SVP and higher employee, Acacia paid COBRA coverage for the medical and dental benefits selected in the year in which the termination occurs, for the duration of the Severance Period. Results for the year ended December 31, 2018 and 2017 include \$2,458,000 and \$1,421,000 in benefits paid under the executive severance policy.

12. SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for state income taxes totaled \$140,000 and \$181,000 for the years ended December 31, 2018 and 2017, respectively. Foreign taxes withheld totaled \$1,093,000 and \$2,865,000 for the years ended December 31, 2018 and 2017, respectively. Refer to Note 4 for accrued foreign taxes payable.

Refer to Note 6 for information regarding noncash investing activity related to the investment in Veritone for the periods presented.

13. RECENT ACCOUNTING PRONOUNCEMENTS

Recent Accounting Pronouncements - Recently Adopted.

In May 2014, the FASB issued a new accounting standards update addressing revenue from contracts with customers, which clarifies existing accounting literature relating to how and when a company recognizes revenue. Under the standard, a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods and services. In doing so, the Company is required to use more judgment and make more estimates in connection with the accounting for revenue contracts with customers than under previous guidance, as described in Note 2. Under the standard, (i) an entity should account for a promise to provide a customer with a right to access the entity’s IP as a performance obligation satisfied over time because the customer will simultaneously receive and consume the benefit from the entity’s performance of providing access to its IP as the performance occurs, and (ii) an entity’s promise to provide a customer with the right to use its IP is satisfied at a point in time. In addition, revenues from contracts with significant financing components should be recognized at an amount that reflects the price that a customer would have paid if the customer had paid cash for the goods or services when they transfer to the customer (i.e. adjustment for the time value of money). For sales and usage based royalties, the new standard requires that the Company include in the transaction price some or all of an amount of estimated variable consideration to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved.

The Company used the modified retrospective method of adoption and recognized the cumulative effect of initially applying the new revenue standard as an adjustment to the opening balance of retained earnings on January 1, 2018. Comparative prior year periods were not adjusted. The new accounting standard was applied to all contracts at the date of initial application. The cumulative effect of applying the new revenue standard, primarily relating to financing components of contracts executed in prior periods and estimates of variable consideration for sales and usage based royalty agreements executed in prior periods, was as follows (in thousands):

Balance at December 31, 2017	Adjustments Due to ASC 606	Balance at January
------------------------------------	----------------------------------	--------------------------

1, 2018**Balance Sheets:**

Accounts receivable	\$ 153	\$ 4,542	\$ 4,695
Royalties and contingent legal fees payable	1,601	1,728	3,329
Accumulated deficit	(320,018)	2,506	(317,512)
Noncontrolling interests	1,358	308	1,666

The impact of the adoption of the new accounting standard on the condensed consolidated balance sheet and statement of operations was as follows (in thousands):

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December 31, 2018

	Balance as Reported	Balance under Legacy GAAP	Effect of Change
Balance Sheets:			
Accounts receivable	\$32,884	\$28,500	\$4,384
Royalties and contingent legal fees payable	22,688	20,404	2,284

**Year Ended December 31,
2018**

	Balance as Reported	Balance under Legacy GAAP	Effect of Change
Statements of Operations:			
Revenues	\$131,506	\$131,723	\$217
Inventor royalties	\$35,168	\$34,295	\$(873)
Contingent legal fees	\$31,501	\$32,020	\$519

In May 2017, the FASB issued amended guidance to clarify when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value, the vesting conditions or the classification of the award changes as a result of the change in terms or conditions. This amendment is effective prospectively for annual periods beginning on or after December 15, 2017. The adoption of this standard did not have a material impact on the Company's condensed consolidated financial statements.

Recent Accounting Pronouncements - Not Yet Adopted.

In February 2016, the FASB issued an accounting standard update which requires lessees to recognize most leases on the balance sheet. This is expected to increase both reported assets and liabilities. The new lease standard does not substantially change lessor accounting. For public companies, the standard will be effective for the first interim reporting period within annual periods beginning after December 15, 2018, although early adoption is permitted. Lessees and lessors will be required to apply the new standard at the beginning of the earliest period presented in the financial statements in which they first apply the new guidance, using a modified retrospective transition method. The requirements of this standard include a significant increase in required disclosures. The Company has two leases with terms that extend beyond 12 months at December 31, 2018. Both leases have guaranteed sublease income through the termination of the lease. Management does not believe that the impact that adopting this new accounting guidance will have a material effect on its financial statements and footnote disclosures and expects to adopt the new standard effective January 1, 2019.

14. FAIR VALUE DISCLOSURES

Acacia holds the following types of financial instruments at December 31, 2018 and 2017.

Trading securities - debt. Debt securities includes corporate bonds with fair value that is determined by third party quotations from outside pricing services and/or computerized pricing models, which may be based on transactions, bids or estimates. Acacia classifies the fair value of corporate bonds within Level 2 of the valuation hierarchy.

Trading securities - equity. Equity securities includes investments in public companies common stock and are recorded at fair value based on the quoted market price of each share on the valuation date. The fair value of these securities are within Level 1 of the valuation hierarchy.

Investments at fair value - common stock. Acacia's equity investment in Veritone common stock is recorded at fair value based on the quoted market price of Veritone's common stock on the applicable valuation date. The fair value at December 31, 2017 was adjusted for an estimated discount for lack of marketability ("DLOM") associated with the restricted nature of the common shares under a lock-up agreement at December 31, 2017 (Level 3 input). At December 31, 2018, there were no restrictions on the common shares and the investment in common shares was transferred from Level 3 to Level 1.

Investments at fair value - warrants. Warrants are recorded at fair value, as based on the Black-Scholes option-pricing model (Level 2). Warrants on securities under a lock-up agreement are adjusted for an estimated discount for lack of marketability ("DLOM") associated with the restricted nature of the common shares (Level 3).

Profits interests. For the year ended December 31, 2018, the fair value of the Units was estimated at 40% of the fair value of the 10% Warrant, based on the Black-Scholes option-pricing model (Level 2). For the year ended December 31, 2017, the fair value of the Units was estimated based on probable vesting dates and values for the applicable instruments (i.e. common stock and warrants related to Acacia's Veritone investment described at Note 6) underlying or associated with the Units (Level 3).

15. RELATED PARTY TRANSACTIONS

During the year ended December 31, 2018, the Company paid \$976,000 in expenses related to the reimbursement of costs incurred by Sidus Investment Management, LLC ("Sidus") on behalf of the participants (together with Sidus, the "Participants") named in the proxy statement filed on June 7, 2018 by the Participants, in connection with a contested proxy election. These expenses are included in general and administrative expenses on the consolidated statements of operations. Alfred V. Tobia, Jr. and Clifford Press are related parties as each of them are Participants and members of the Company's Board of Directors. In addition, Sidus is a related party as Mr. Tobia is a Co-Founder and Managing Member at Sidus.

ACACIA RESEARCH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
16. QUARTERLY FINANCIAL DATA (unaudited)

The following table sets forth unaudited consolidated statements of operations data for the eight quarters in the period ended December 31, 2018. This information has been derived from Acacia's unaudited condensed consolidated financial statements that have been prepared on the same basis as the audited consolidated financial statements and, in the opinion of management, include all adjustments, consisting of normal recurring adjustments, necessary for a fair statement of the information when read in conjunction with the audited consolidated financial statements and related notes thereto. Acacia's quarterly results have been, and may in the future be, subject to significant fluctuations. As a result, Acacia believes that results of operations for interim periods should not be relied upon as any indication of the results to be expected in any future periods.

	Quarter Ended							
	Mar. 31, 2018	Jun. 30, 2018	Sept. 30, 2018	Dec. 31, 2018	Mar. 31, 2017	Jun. 30, 2017	Sept. 30, 2017	Dec. 31, 2017
	(Unaudited, in thousands, except share and per share information)							
Revenues	\$62,093	\$6,485	\$13,725	\$49,203	\$8,854	\$16,457	\$36,633	\$3,458
Portfolio operations:								
Inventor royalties	21,744	1,241	1,181	11,002	666	4,273	—	13
Contingent legal fees	15,759	1,037	2,949	11,756	627	3,236	12,173	646
Patent acquisition expenses	4,000	—	—	—	—	—	—	—
Litigation and licensing expenses - patents	2,989	2,639	1,549	1,689	6,386	4,134	4,073	3,626
Amortization of patents	5,330	5,278	4,952	11,560	5,515	5,571	5,625	5,443
Impairment of patent-related intangible assets	—	28,210	—	—	—	—	2,248	—
Other portfolio expenses	—	—	2,202	400	—	—	—	1,200
Total portfolio operations	49,822	38,405	12,833	36,407	13,194	17,214	24,119	10,928
Net revenue (loss)	12,271	(31,920)	892	12,796	(4,340)	(757)	12,514	(7,470)
General and administrative expenses (including non-cash stock compensation expense)	3,301	6,916	5,855	2,778	7,236	7,167	12,956	(140)
Operating income (loss)	8,970	(38,836)	(4,963)	10,018	(11,576)	(7,924)	(442)	(7,330)
Total other income (expense)	(40,890)	10,615	(27,595)	(20,988)	696	(4,862)	159,027	(102,950)
Income (loss) before provision for income taxes	(31,920)	(28,221)	(32,558)	(10,970)	(10,880)	(12,786)	158,585	(110,280)
Provision for income taxes	(191)	(285)	(306)	(397)	(1,241)	(1,478)	(216)	(20)
Net income (loss) including noncontrolling interests	(32,111)	(28,506)	(32,864)	(11,367)	(12,121)	(14,264)	158,369	(110,300)
Net (income) loss attributable to noncontrolling interests in subsidiaries	73	79	(331)	(2)	291	12	96	97
Net income (loss) attributable to Acacia Research Corporation	\$(32,038)	\$(28,427)	\$(33,195)	\$(11,369)	\$(11,830)	\$(14,252)	\$158,465	\$(110,203)
Net income (loss) per common share attributable to Acacia Research Corporation:								
Basic and diluted income (loss) per share	\$(0.63)	\$(0.57)	\$(0.67)	\$(0.23)	\$(0.24)	\$(0.28)	\$3.13	\$(2.18)
Weighted-average number of shares outstanding, basic	50,632,958	50,061,812	49,557,748	49,639,172	50,333,056	50,499,948	50,554,234	50,590,460
Weighted-average number of shares outstanding, diluted	50,632,958	50,061,812	49,557,748	49,639,172	50,333,056	50,499,948	50,599,974	50,590,460