

# INTERDIGITAL INC.

## FORM 10-Q (Quarterly Report)

Filed 05/15/02 for the Period Ending 03/31/02

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Industry	Communications Equipment
Sector	Technology
Fiscal Year	12/31

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

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**FORM 10-Q**

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

For the quarterly period ended March 31, 2002

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

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*Commission File Number 1-11152*

**INTERDIGITAL COMMUNICATIONS  
CORPORATION**

(Exact name of registrant as specified in its charter)

PENNSYLVANIA

-----  
(State or other jurisdiction of  
incorporation or organization)

23-1882087

-----  
(I.R.S. Employer  
Identification No.)

781 Third Avenue, King of Prussia, PA 19406-1409  
(Address of principal executive offices and zip code)

Registrant's telephone number, including area code (610) 878-7800

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the latest practicable date.

Common Stock, par value \$.01 per share

54,367,886

-----  
Class

-----  
Outstanding at April 30, 2002

**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES**

**INDEX**

	PAGES
	-----
Part I - Financial Information:	
Item 1. Condensed Consolidated Financial Statements (unaudited):	3
Condensed Consolidated Balance Sheets - March 31, 2002 and December 31, 2001	3
Condensed Consolidated Statements of Operations - Three Months Ended March 31, 2002 and 2001	4
Condensed Consolidated Statements of Cash Flows - Three Months Ended March 31, 2002 and 2001	5
Notes to Condensed Consolidated Financial Statements	6
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	8
Item 3. Quantitative and Qualitative Disclosure About Market Risk	11
Part II - Other Information:	
Item 1. Legal Proceedings	12
Item 6. Exhibits and Reports on Form 8-K	12

**PART I - FINANCIAL INFORMATION**

**Item I. FINANCIAL STATEMENTS**

**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except per share data)

	(Unaudited) MARCH 31, 2002	DECEMBER 31, 2001
ASSETS	-----	-----
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 24,190	\$ 17,892
Short-term investments	54,387	72,471
Accounts receivable, net of allowances of \$-0-	57,598	14,479
Other current assets	5,967	6,385
	-----	-----
Total current assets	142,142	111,227
	-----	-----
PROPERTY AND EQUIPMENT, NET	14,927	14,402
PATENTS, NET	11,515	11,334
OTHER NON-CURRENT ASSETS	15,183	11,418
	-----	-----
	41,625	37,154
	-----	-----
	\$ 183,767	\$ 148,381
	=====	=====
 <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Current portion of long-term debt	\$ 320	\$ 184
Accounts payable	2,157	4,412
Accrued compensation and related expenses	3,984	5,985
Deferred revenue	17,087	10,490
Foreign and domestic taxes payable	5,368	907
Other accrued expenses	2,209	1,553
	-----	-----
Total current liabilities	31,125	23,531
LONG-TERM DEBT	2,112	2,158
LONG-TERM DEFERRED REVENUE	88,954	62,418
	-----	-----
<b>TOTAL LIABILITIES</b>	<b>122,191</b>	<b>88,107</b>
	-----	-----
 <b>COMMITMENTS AND CONTINGENCIES (NOTES 8 AND 9)</b>		
<b>SHAREHOLDERS' EQUITY:</b>		
Preferred Stock, \$.10 par value, 14,399 shares authorized- \$2.50 Convertible Preferred, 55 shares issued and outstanding, liquidation value of \$1,375	5	5
Common Stock, \$.01 par value, 100,000 shares authorized, 54,537 shares and 54,391 shares issued and outstanding	545	544
Additional paid-in capital	272,900	271,682
Accumulated deficit	(201,304)	(201,320)
Unearned compensation	(2,497)	(2,564)
	-----	-----
Treasury stock, 1,500 shares of common held at cost	69,649	68,347
	8,073	8,073
	-----	-----
Total shareholders' equity	61,576	60,274
	-----	-----
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>\$ 183,767</b>	<b>\$ 148,381</b>
	=====	=====

The accompanying notes are an integral part of these statements.

**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(in thousands, except per share data)

(unaudited)

**FOR THE THREE MONTHS**  
**ENDED MARCH 31,**

	2002	2001
	-----	-----
REVENUES	\$ 20,949	\$ 14,687
	-----	-----
OPERATING EXPENSES:		
Sales and marketing	1,090	1,191
General and administrative	3,694	3,601
Patents administration and licensing	2,855	1,724
Development	11,815	10,876
	-----	-----
	19,454	17,392
	-----	-----
Income (loss) from operations	1,495	(2,705)
INTEREST INCOME (EXPENSE):		
Interest income	585	1,549
Interest and financing expenses	(85)	(56)
	-----	-----
Income (loss) before income taxes	1,995	(1,212)
INCOME TAX PROVISION	(1,945)	(909)
	-----	-----
Net income (loss)	50	(2,121)
PREFERRED STOCK DIVIDENDS	(34)	(34)
	-----	-----
NET INCOME (LOSS) APPLICABLE TO COMMON SHAREHOLDERS	\$ 16	\$ (2,155)
	=====	=====
NET INCOME (LOSS) PER COMMON SHARE - BASIC	\$ 0.00	\$ (0.04)
	=====	=====
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING - BASIC	53,966	53,127
	=====	=====
NET INCOME (LOSS) PER COMMON SHARE - DILUTED	\$ 0.00	\$ (0.04)
	=====	=====
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING - DILUTED	56,847	53,127
	=====	=====

The accompanying notes are an integral part of these statements.

**INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands, except per share data)

(unaudited)

	FOR THREE MONTHS ENDED MARCH 31,	
	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss) before preferred stock dividends	\$ 50	\$ (2,121)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities-		
Depreciation and amortization	1,982	1,370
Deferred revenue recognized	(12,867)	(2,669)
Increase in deferred revenue	46,000	19,500
Amortization of unearned compensation	702	770
Increase in deferred charges	(3,978)	(3,738)
Other	--	31
Decrease (increase) in assets-		
Receivables	(43,119)	(12,351)
Other current assets	630	1,466
Increase (decrease) in liabilities-		
Accounts payable	(2,255)	(897)
Accrued compensation	(2,001)	(837)
Other accrued expenses	5,117	1,010
	-----	-----
Net cash provided (used) by operating activities	(9,739)	1,534
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Sale of short-term investments, net	17,970	9,907
Purchases of property and equipment	(2,029)	(3,038)
Patent costs	(659)	(567)
	-----	-----
Net cash provided by investing activities	15,282	6,302
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from exercise of stock options and warrants and employee stock purchase plan	698	408
Lease obligations incurred	195	--
Payments on long-term debt, including capital lease obligations	(104)	(102)
Cash dividends on preferred stock	(34)	(34)
	-----	-----
Net cash provided by financing activities	755	272
	-----	-----
NET INCREASE IN CASH AND CASH EQUIVALENTS	6,298	8,108
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	17,892	12,343
	-----	-----
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 24,190	\$ 20,451
	=====	=====
SUPPLEMENTAL CASH FLOW INFORMATION:		
Interest paid	\$ 47	\$ 54
	=====	=====
Income taxes paid, including foreign withholding taxes	\$ 791	\$ 1,259
	=====	=====

The accompanying notes are an integral part of these statements.

# INTERDIGITAL COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2002

(UNAUDITED)

### 1. BASIS OF PRESENTATION:

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments, consisting only of normal recurring adjustments necessary for a fair statement of the financial position of InterDigital Communications Corporation (collectively with its subsidiaries referred to as InterDigital, the Company, we, us and our) as of March 31, 2002, and the results of operations for the three month periods ended March 31, 2002 and 2001, and cash flows for the three months ended March 31, 2002 and 2001. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q and accordingly do not include all of the detailed schedules, information and notes necessary to present fairly the financial condition, results of operations and cash flows in conformity with generally accepted accounting principles. Therefore, these financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company's latest Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC). The results of operations for interim periods are not necessarily indicative of the results to be expected for the entire year.

Certain reclassifications were made to the statements of cash flows for prior periods to conform to the current presentation.

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

### 2. LEGAL PROCEEDINGS:

InterDigital and InterDigital Technology Corporation (ITC), a wholly-owned subsidiary, remain parties to a certain patent-related litigation with Ericsson Inc. (Ericsson) in which ITC is asserting patent infringement. ITC generally is seeking injunctive relief and monetary damages. Ericsson generally seeks declarations that ITC's patents are invalid and/or that Ericsson's products do not infringe ITC's patents as well as monetary damages. We have not recorded any gain or loss related to this matter other than legal fees, net of insurance reimbursements.

The Company is in arbitration with Samsung Electronics Co., LTD. (Samsung). The arbitration proceeding filed by ITC against licensee Samsung with the International Chamber of Commerce, International Court of Arbitration in February 2002 is continuing. This dispute involves a patent license agreement with Samsung and Samsung's alleged underreporting of, failure to report and failure to pay royalties on its more recent covered sales. Among the issues being addressed in arbitration is whether Samsung can make use of the most favored licensee provision contained in the license agreement and, if so, how such rights would affect Samsung's royalty obligations. The ultimate resolution of the dispute will determine whether or not Samsung must make additional royalty payments to ITC, but will not impact amounts previously paid by Samsung. At March 31, 2002, our balance sheet contained \$7.2 million of deferred revenue associated with the Samsung license agreement, the future recognition and timing of which could be impacted by the ultimate resolution of this matter. No revenue was recognized in the first quarter 2002 in connection with the Samsung license agreement pending the outcome of the dispute resolution. Further, we have not recorded any gain or loss related to this matter other than legal fees.

The Company is party to other legal proceedings which management currently believes will not have a material effect on the Company's results of operations or financial condition.

### 3. INCOME PER SHARE:

The following table sets forth a reconciliation of the shares used in the basic and diluted net income (loss) per share computations:

(In thousands, except per share data)

	Three Months Ended March 31, 2002			Three Months Ended March 31, 2001		
	Income (loss) (Numerator)	Shares (Denominator)	Per-Share Amount	Income (loss) (Numerator)	Shares (Denominator)	Per-Share Amount
Income per Share-Basic:						
Income (loss) available to common stockholders	\$16	53,966	\$0.00	\$(2,155)	53,127	\$(0.04)
Effect of dilutive options and warrants	---	2,881	---	---	---	---
Income per Share-Diluted:						
Income (loss) available to common stockholders + dilutive effects of options and warrants	\$16	56,847	\$0.00	\$(2,155)	53,127	\$(0.04)

For the three months ended March 31, 2002, options outstanding of 4.2 million were excluded from the computation of diluted earnings per share because they were antidilutive. For the three months ended March 31, 2001, all options and warrants were excluded from the computation of diluted earnings per share as a result of a net loss reported in the period.

#### 4. CUSTOMER AGREEMENT:

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

The 3G Agreement provides that NEC is to pay us a royalty on each licensed product sold by NEC. NEC also agreed to pay us a non-refundable advance royalty of \$19.5 million, which was received in April 2002. Once that advance is exhausted, NEC will be obligated to pay us additional royalties as it sells licensed products. We recognized revenue of approximately \$9 million in the first quarter 2002 related to the \$19.5 million advance royalty and will recognize additional revenue as licensed products are sold.

In settlement of the 2G Dispute, NEC has agreed to pay us \$53 million in four equal non-refundable installments, payable in the second and fourth quarters of 2002 and 2003, respectively. The first of these payments was received in April 2002. In exchange for these payments, NEC's royalty obligation for all PHS (Personal Handyphone System) and PDC (Pan Asian Digital Cellular) products sold under the 1995 Agreement will be considered paid up. Otherwise, the 1995 Agreement remains unaltered by the settlement. Currently, NEC has no further royalty payment obligations under that agreement based on existing prepaid units and certain other unique provisions included in the 1995 Agreement. In connection with the \$53 million settlement, we are recognizing revenue on a straight-line basis, from the January 2002 agreement date until February 2006, which is the expected period of use by NEC. In the first quarter 2002, we recognized approximately \$2.6 million of revenue related to this settlement.

We have recognized in accounts receivable amounts due under this agreement within the next 12 months, as well as the associated deferred revenue.



**OVERVIEW**

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto contained elsewhere in this document, in addition to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 filed with the SEC.

**SIGNIFICANT TRANSACTION**

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

The 3G Agreement provides that NEC is to pay us a royalty on each licensed product sold by NEC. NEC also agreed to pay us a non-refundable advance royalty of \$19.5 million, which was received in April 2002. Once that advance is exhausted, NEC will be obligated to pay us additional royalties as it sells licensed products. We recognized revenue of approximately \$9 million in the first quarter 2002 related to the \$19.5 million non-refundable advance royalty and will recognize additional revenue as licensed products are sold.

In settlement of the 2G Dispute, NEC has agreed to pay us \$53 million in four equal non-refundable installments, payable in the second and fourth quarters of 2002 and 2003, respectively. The first of these payments was received in April 2002. In exchange for these payments, NEC's royalty obligation for all PHS (Personal Handyphone System) and PDC (Pan Asian Digital Cellular) products sold under the 1995 Agreement will be considered paid up. Otherwise, the 1995 Agreement remains unaltered by the settlement. Currently, NEC has no further royalty payment obligations under that agreement based on existing prepaid units and certain other unique provisions included in the 1995 Agreement. In connection with the \$53 million settlement, we are recognizing revenue on a straight-line basis, from the January 2002 agreement date until February 2006, which is the expected period of use by NEC. In the first quarter 2002, we recognized approximately \$2.6 million of revenue related to this settlement.

We have recognized in accounts receivable amounts due under this agreement within the next 12 months, as well as the associated deferred revenue.

## FINANCIAL POSITION, LIQUIDITY AND CAPITAL REQUIREMENTS

First quarter 2002 cash flow used for operating activities was \$9.7 million compared to \$1.5 million provided by operating activities in the first quarter of 2001. The decrease in operating cash flow in 2002 resulted from lower cash earnings (net income adjusted for non-cash impacts of depreciation, amortization and deferred revenue recognized) in the period.

Net cash provided from investing activities in the first quarter 2002 was \$15.3 million compared to \$6.3 million in the same period of 2001. In the first three months of 2002, we converted \$18.0 million of short-term, marketable securities into cash compared to \$9.9 million in last year's first quarter. Also, during the first quarter 2002, investments in hardware, software, patents and other equipment decreased to \$2.7 million from \$3.6 million in the first quarter 2001.

Net cash provided by financing activities in the first quarter 2002 was \$0.8 million compared to \$0.3 million in last year's first quarter. The increase in 2002 primarily resulted from higher net proceeds related to option and warrant exercises (\$0.7 million in 2002 versus \$0.4 million in first quarter 2001).

As of March 31, 2002, we had \$78.6 million of cash, cash equivalents and short-term investments, compared to \$90.4 million as of December 31, 2001. Our working capital (excluding cash, cash equivalents, short-term investments, current maturities of debt and current deferred revenue) increased to \$49.8 million at March 31, 2002 from \$8.0 million at December 31, 2001. The increase in first quarter 2002 was due to the recognition of \$46 million of receivables associated with the 2G and 3G obligations from NEC. As noted above, we received \$32.75 million (before non-U.S. source withholding taxes) from NEC in April 2002 and expect to receive an additional payment of \$13.25 million from NEC in the fourth quarter 2002.

We are capable of supporting our operating requirements for the near future through cash and short-term investments on hand, as well as other internally generated funds, primarily from 2G patent licensing royalties. At present, we do not anticipate the need to seek any additional financing through either bank facilities or the sale of debt or equity securities.

As of March 31, 2002, we had net operating loss (NOL) carryforwards of approximately \$149 million for which no deferred tax asset has been recorded. We expect that we will continue to pay source withholding taxes to non-U.S. countries related to royalties, local and state income taxes, and alternative minimum taxes when applicable, but as a result of these NOLs, we do not expect to pay federal income taxes in the near future.

Property and equipment are currently being utilized in our on-going business activities, and we believe that no write-downs are required at this time due to lack of use or technological obsolescence. With respect to patent assets, we believe that the fair value of our patents is at least equal to the carrying value included in the March 31, 2002 balance sheet.

## RESULTS OF OPERATIONS

### First Quarter of 2002 Compared to the First Quarter of 2001

#### Revenues

Revenues in first quarter of 2002 totaled \$20.9 million, compared to \$14.7 million in last year's first quarter. Royalty revenue in this year's first quarter increased to \$19 million from \$8.0 million in the first quarter 2001. The increase was due largely to (i) initial patent licensing royalties of over \$9.0 million related to sales of 3G and narrowband CDMA products, about 80% of which was attributable to pre-2002 build-out of 3G systems, particularly in Japan, and (ii) the recognition of \$2.6 million related to the settlement of the above-noted 2G Dispute. In the first quarter 2002, specialized engineering services revenue associated with the validation and completion stage of Wideband Time Division Duplex (WTDD) technology development work for Nokia was \$1.9 million, compared to peak development related revenues of \$6.7 million in the comparable period last year.

## **Operating Expenses**

Development expenses in the first quarter of 2002 increased 9% to \$11.8 million from \$10.9 million in the first quarter of 2001. This increase over last year's first quarter was due primarily to increased staff and activity levels devoted to 3G Wideband Code Division Multiple Access (WCDMA) technology platform and product development.

Sales and marketing expenses of \$1.1 million in the first quarter of 2002 decreased 9% from \$1.2 million in last year's first quarter. The decrease in the first quarter of 2002 was mainly due to reduced trade show activity costs.

General and administrative expenses for the first quarter of 2002 increased slightly to \$3.7 million from \$3.6 million in the first quarter of 2001.

Patents administration and licensing expenses increased 66% to \$2.9 million in the first quarter of 2002 from \$1.7 million in the comparable period of 2001. The increase was due to expansion of patent licensing personnel and related activities, higher costs associated with patent related enforcement activities and commissions related to patent license royalties.

## **Other Income and Expense**

Interest income of \$0.6 million decreased 62% from \$1.5 million in last year's first quarter primarily due to lower yields available in 2002 as compared to 2001.

## **Income Taxes**

The income tax provision in both the first quarter of 2002 and 2001 consisted primarily of withholding taxes associated with patent licensing royalties, principally from Japan.

## **Expected Trends**

Notwithstanding our first quarter financial results, for the near term, our royalty revenue will continue to be affected by sales trends in the mobile wireless market, particularly the sales performance of leading Japanese equipment producers who represent a significant portion of our licensees, whether we are able to expand our licensee base and whether we are successful in other patent enforcement activities. As noted above, we benefited in the first quarter from initial reporting of royalties associated with the pre-2002 build-out that should not be considered in baselining future quarterly royalties.

We still foresee our 2002 operating expenses growing modestly over 2001 levels as we maintain our commitment to investing in technology and product development for 3G WCDMA technology platforms. Based on expected royalties from current licensees and planned expenses, we are optimistic that we will achieve both year-to-year revenue growth in 2002 at the upper end of our previously stated target of 10% to 20% and near breakeven cash flow for the year. We also continue to be aggressive in seeking new 2G and 3G licensing arrangements that, if successful, would produce additional revenue and cash flow beyond our original targets.

(See "Statement Pursuant to the Securities Litigation Reform Act of 1995" below.)

## STATEMENT PURSUANT TO THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

The foregoing Management's Discussion and Analysis contains forward-looking statements reflecting, among other things, the Company's beliefs and expectations as to (i) our ability to expand our licensee base, (ii) revenues, operating expenses, and cash flow, and (iii) our success in patent enforcement and the materiality of the orders and rulings in the Ericsson lawsuit. Words such as "objective", "intend", "believes", "whether", "foresee", "expected", "optimistic", "if successful", and "would" are intended to identify such forward-looking statements.

Such forward-looking statements are subject to risks and uncertainties. We caution the reader that important factors in some cases have affected and, in the future, could materially affect actual results and cause actual results to differ materially from the results expressed in any such forward looking statement due to a variety of factors including, but not limited to the following factors: (i) the market relevance of our technologies; limited or no deployment of WTDD technology; changes in technology preferences of strategic partners or consumers; the availability or development of substitute technologies or competition from competitive technologies; our ability to leverage our existing and enter into additional strategic relationships, (ii) failure of the 3G market to materialize in the manner or time frame anticipated, (iii) the effects of global economic conditions, trade barriers, political instability, governmental licensing decisions, and delays in spectrum licensing, and (iv) changes or lack of changes in the business plans of certain licensees, our ability to enter into additional licenses, the performance of our licensees in selling their products, developments in patent litigation matters, future orders, rulings and opinions of the Judge in the Ericsson case and their resulting impact on licensing. InterDigital undertakes no duty to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise.

### **Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

There have been no material changes in quantitative and qualitative market risk from the disclosure included in our Annual Report on Form 10-K filed on March 29, 2002 for the year ended December 31, 2001 (Form 10-K).

## PART II - OTHER INFORMATION

### Item 1. LEGAL PROCEEDINGS

#### Ericsson

As reported in our Form 10-K, the Company and InterDigital Technology Corporation ("ITC"), the Company's wholly-owned subsidiary, are parties to a lawsuit involving Ericsson Inc. ("Ericsson"). As is typical in such litigation, each party has filed pre-trial motions with the Court under seal seeking to limit issues at trial and to dismiss the other party's case in whole or in part. To date, the Judge has ruled on certain of the pre-trial motions, which have not disposed of the case, and placed those orders under seal. In April 2000, a "Markman" hearing was held for purposes of patent claim construction and the Judge subsequently issued his claim construction rulings. Since the Judge was free to modify the published Special Master's Markman recommendations, no assumption should be made regarding the content of the Judge's claim construction rulings. The Company believes that these orders and rulings have not materially affected the relief ITC is seeking. Court ordered mediation between the parties is continuing. A trial date has not been set.

#### Samsung

As reported in our Form 10-K, the Company is in arbitration with Samsung Electronics Co., Ltd. ("Samsung") regarding a patent license agreement with Samsung and Samsung's alleged underreporting of, failure to report and failure to pay royalties on its more recent covered sales. Based on recent information that has become available to the Company, ITC has revised upwards its estimates of past due royalties owed by Samsung through the end of 2001, and further alleges that royalties continue to be payable with sales of covered products after that date. In Samsung's Answer to ITC's Complaint, Samsung has advanced various arguments that would cause Samsung's ultimate royalty obligation to ITC to be excused or substantially reduced below the amount alleged by ITC if any of such arguments is adopted by the arbitrators. While ITC has advanced what it believes to be strong and persuasive arguments regarding its positions, ITC can give no assurance that the arbitration will be decided in its favor. Moreover, any consensual settlement would likely be at substantially lower levels than the amount alleged in the Complaint. There can be no assurance that any consensual settlement of the arbitrated dispute will be reached.

### Item 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following is a list of exhibits filed as part of this Quarterly Report on Form 10-Q:

**Exhibit 10.50 2002 Stock Award and Incentive Plan.**

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

We filed a Current Report on Form 8-K dated January 16, 2002 under Item 5 - Other Events relating to the Company's announcement that ITC entered into a royalty-bearing license agreement with NEC for sales of wireless products compliant with all 3G and narrowband CDMA standards, as well as the Company's amicable settlement of a 2G patent licensing dispute with NEC in connection with a 1995 license agreement. No financial statements were filed with this report.

**SIGNATURES**

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

**INTERDIGITAL COMMUNICATIONS CORPORATION**

*Date: May 15, 2002*

*/s/ Howard E. Goldberg*

-----  
*Howard E. Goldberg*  
*President and Chief Executive Officer*

*Date: May 15, 2002*

*/s/ R. J. Fagan*

-----  
*Richard J. Fagan*  
*Executive Vice President and Chief*  
*Financial Officer*

**INTERDIGITAL COMMUNICATIONS CORPORATION**

**2002 Stock Award and Incentive Plan**

1. Purpose. The purpose of this 2002 Stock Award and Incentive Plan (the "Plan") is to aid InterDigital Communications Corporation, a Pennsylvania corporation (the "Company"), in attracting, retaining, motivating and rewarding employees and other persons who provide services to the Company or its subsidiaries or affiliates, to provide for equitable and competitive compensation opportunities, to encourage long-term service, to recognize individual contributions and reward achievement of Company goals, and to promote the creation of long-term value for shareholders by closely aligning the interests of Participants with those of shareholders. The Plan authorizes stock-based and cash-based incentives for Participants.

2. Definitions. In addition to the terms defined in Section 1 above and elsewhere in the Plan, the following capitalized terms used in the Plan have the respective meanings set forth in this Section:

(a) "Award" means any Non-qualified Stock Option, SAR, Restricted Stock, Deferred Stock, Stock granted as a bonus or in lieu of another award, Dividend Equivalent, Other Stock-Based Award, or Performance Award, together with any related right or interest, granted to a Participant under the Plan.

(b) "Beneficiary" means the legal representatives of the Participant's estate entitled by will or the laws of descent and distribution to receive the benefits under a Participant's Award upon a Participant's death, provided that, if and to the extent authorized by the Committee, a Participant may be permitted to designate a Beneficiary, in which case the "Beneficiary" instead shall be the person(s) (if any are then surviving), trust(s) or entity(ies) which have been designated by the Participant in his or her most recent written beneficiary designation filed with the Committee to receive the benefits specified under the Participant's Award upon such Participant's death.

(c) "Board" means the Company's Board of Directors.

(d) "Change in Control" and related terms have the meanings specified in Section 8.

(e) "Code" means the Internal Revenue Code of 1986, as amended.

(f) "Committee" means a committee of two or more directors designated by the Board to administer the Plan. The full Board may perform any function of the Committee hereunder, in which case the term "Committee" shall refer to the Board. Initially, the Compensation and Stock Option Committee of the Board of Directors will be designated as the "Committee" under the Plan.

- (g) "Deferred Stock" means a right, granted to a Participant under Section 6(e), to receive Stock or other Awards or a combination thereof at the end of a specified deferral period.
- (h) "Dividend Equivalent" means a right, granted to a Participant under Section 6(g), to receive cash, Stock, other Awards or other property equal in value to all or a specified portion of the dividends paid with respect to a specified number of shares of Stock.
- (i) "Effective Date" means the effective date specified in Section 10(r).
- (j) "Eligible Person" has the meaning specified in Section 5.
- (k) "Exchange Act" means the Securities Exchange Act of 1934, as amended.
- (l) "Fair Market Value" means the fair market value of Stock, Awards or other property as determined by the Committee or under procedures established by the Committee. Unless otherwise determined by the Committee, the Fair Market Value of Stock shall be the closing sale price reported on the composite tape of the principal stock exchange on which the Stock is listed on the day as of which such value is being determined or, if there is no sale on that day, then on the last previous day on which a sale was reported.
- (m) "Non-qualified Stock Option" means an option to purchase Stock or other Awards pursuant to Section 6(b), which option is designated as a non-qualified stock option and is not intended to qualify as an incentive stock option within the meaning of Code Section 422.
- (n) "Other Stock-Based Awards" means Awards granted to a Participant under Section 6(h).
- (o) "Participant" means a person who has been granted an Award under the Plan which remains outstanding, including a person who is no longer an Eligible Person.
- (p) "Performance Award" means a conditional right, granted to a Participant under Section 6(i), to receive cash, Stock or other Awards or payments, as determined by the Committee, based upon performance criteria specified by the Committee.
- (q) "Restricted Stock" means Stock granted to a Participant under Section 6(d) which is subject to certain restrictions and to a risk of forfeiture.
- (r) "Stock" means the Company's Common Stock, and any other equity securities of the Company that may be substituted or resubstituted for Stock pursuant to Section 10(c).



(s) "Stock Appreciation Rights" or "SAR" means a right granted to a Participant under Section 6(c).

### 3. Administration.

(a) Authority of the Committee. The Plan shall be administered by the Committee, which shall have full and final authority, in each case subject to and consistent with the provisions of the Plan, to select Eligible Persons to become Participants; to grant Awards; to determine the type and number of Awards, the dates on which Awards may be exercised and on which the risk of forfeiture or deferral period relating to Awards shall lapse or terminate, the acceleration of any such dates, the expiration date of any Award, whether, to what extent, and under what circumstances an Award may be settled, or the exercise price of an Award may be paid, in cash, Stock, other Awards, or other property, and other terms and conditions of, and all other matters relating to, Awards; to prescribe documents evidencing or setting terms of Awards (such Award documents need not be identical for each Participant), amendments thereto, rules and regulations for the administration of the Plan and amendments thereto, and standardized terms and conditions of awards and amendments thereto (which, if so specified by the Committee, shall be deemed to be incorporated into and a part of this Plan); to construe and interpret the Plan and Award documents and correct defects, supply omissions or reconcile inconsistencies therein; and to make all other decisions and determinations as the Committee may deem necessary or advisable for the administration of the Plan. Decisions of the Committee with respect to the administration and interpretation of the Plan shall be final, conclusive, and binding upon all persons interested in the Plan, including Participants, Beneficiaries, transferees under Section 10(b) and other persons claiming rights from or through a Participant, and shareholders.

(b) Manner of Exercise of Committee Authority. The express grant of any specific power to the Committee, and the taking of any action by the Committee, shall not be construed as limiting any power or authority of the Committee. The Committee may delegate to officers or managers of the Company or any subsidiary or affiliate, or committees thereof, the authority, subject to such terms as the Committee shall determine, to perform such functions, including administrative functions.

(c) Limitation of Liability. The Committee and each member thereof, and any person acting pursuant to authority delegated by the Committee, shall be entitled, in good faith, to rely or act upon any report or other information furnished by any executive officer, other officer or employee of the Company or a subsidiary or affiliate, the Company's independent auditors, consultants or any other agents assisting in the administration of the Plan. Members of the Committee, any person acting pursuant to authority delegated by the Committee, and any officer or employee of the Company or a subsidiary or affiliate acting at the direction or on behalf of the Committee or a delegate shall not be personally liable for any action or determination taken or made in good faith with respect to the Plan, and shall, to the extent permitted by law, be fully indemnified and protected by the Company with respect to any such action or determination.

#### 4. Stock Subject to Plan.

(a) Overall Number of Shares Available for Delivery. Subject to adjustment as provided in Section 10(c), the total number of shares of Stock reserved and available for delivery in connection with Awards under the Plan shall be one million five hundred thousand. Any shares of Stock delivered under the Plan shall consist of authorized and unissued shares or treasury shares.

(b) Share Counting Rules. The Committee may adopt reasonable counting procedures to ensure appropriate counting, avoid double counting (as, for example, in the case of tandem or substitute awards) and make adjustments if the number of shares of Stock actually delivered differs from the number of shares previously counted in connection with an Award. Shares subject to an Award that is canceled, expired, forfeited, settled in cash or otherwise terminated without a delivery of shares to the Participant will again be available for Awards, and shares withheld in payment of the exercise price or taxes relating to an Award and shares equal to the number surrendered in payment of any exercise price or taxes relating to an Award shall be deemed to constitute shares not delivered to the Participant and shall be deemed again to be available for Awards under the Plan. In addition, in the case of any Award granted in substitution for an award of a company or business acquired by the Company or a subsidiary or affiliate, shares issued or issuable in connection with such substitute Award shall not be counted against the number of shares reserved under the Plan, but shall be available under the Plan by virtue of the Company's assumption of the plan or arrangement of the acquired company or business.

5. Eligibility. Awards may be granted under the Plan only to Eligible Persons. For purposes of the Plan, an "Eligible Person" means an employee of the Company or any subsidiary or affiliate, or a consultant or other person who provides substantial services to the Company or subsidiary or affiliate, but excluding any person who (i) is the Company's president, principal financial officer, principal accounting officer (or, if there is no such accounting officer, the controller), any vice-president of the Company in charge of a principal business unit, division or function (such as sales, administration or finance), any other person who performs a policy-making function for the Company, (ii) is an officer of one or more of the Company's subsidiaries to the extent that he or she performs such policy-making functions identified in clause (i) for the Company, or (iii) is a member of the Board. The term "Eligible Person" shall also include any person who has been offered employment by the Company or a subsidiary or affiliate, provided that such prospective employee may not receive any payment or exercise any right relating to an Award until such person has commenced employment with the Company or a subsidiary or affiliate of the Company. An employee on leave of absence may be considered as still in the employ of the Company or a subsidiary or affiliate for purposes of eligibility for participation in the Plan, if so determined by the Committee. A joint venture in which the Company or a subsidiary has a substantial direct or indirect equity investment may be deemed an affiliate, if so determined by the Committee, but such determination shall be solely for purposes of this Plan.

#### 6. Specific Terms of Awards.

(a) General. Awards may be granted on the terms and conditions set forth in this Section 6; provided that no Award may be granted after the close of business on the date of the Company's annual meeting of shareholders held in 2003. In addition, the Committee may impose on any Award or the exercise thereof, at the date of grant or thereafter (subject to Section 10(e)), such additional terms and conditions, not inconsistent with the provisions of the Plan, as the Committee shall determine, including terms requiring forfeiture of Awards in the event of termination of employment or service by the Participant and terms permitting a Participant to make elections relating to his or her Award. The Committee shall retain full power and discretion with respect to any term or condition of an Award that is not mandatory under the Plan. The Committee may require payment of consideration for an Award, except as otherwise limited by the Plan.

(b) Non-qualified Stock Options. The Committee is authorized to grant Non-qualified Stock Options to Participants on the following terms and conditions:

(i) Exercise Price. The exercise price per share of Stock purchasable under a Non-qualified Stock Option shall be determined by the Committee, but such exercise price shall be not less than the Fair Market Value of a share of Stock on the date of grant of such Non-qualified Stock Option, subject to Sections 6(f) and 8(a), unless the Committee finds there to exist extraordinary circumstances such that the grant of a Non-Qualified Stock Option with an exercise price less than such Fair Market Value is appropriate.

(ii) Option Term; Time and Method of Exercise. The Committee shall determine the term of each Non-qualified Stock Option. The Committee shall determine the time or times at which or the circumstances under which a Non-qualified Stock Option may be exercised in whole or in part (including based on achievement of performance goals and/or future service requirements), the methods by which such exercise price may be paid or deemed to be paid and the form of such payment (subject to Section 10(k)), including, without limitation, cash, Stock, other Awards or awards granted under other plans of the Company or any subsidiary or affiliate, or other property (including notes and other contractual obligations of Participants to make payment on a deferred basis, such as through "cashless exercise" arrangements, to the extent permitted by applicable law), and the methods by or forms in which Stock will be delivered or deemed to be delivered in satisfaction of Non-qualified Stock Options to Participants (including deferred delivery of shares representing the Non-qualified Stock Option "profit," at the election of the Participant or as mandated by the Committee, with such deferred shares subject to any vesting, forfeiture or other terms as the Committee may specify).

(c) Stock Appreciation Rights. The Committee is authorized to grant SARs to Participants on the following terms and conditions:

(i) Right to Payment. An SAR shall confer on the Participant to whom it is granted a right to receive, upon exercise thereof, the excess of (A) the Fair Market Value of one share of Stock on the date of exercise (or, in the case of a "Limited SAR," the Fair Market Value determined by reference to the Change in Control Price, as defined under Section 8(d) hereof) over (B) the grant price of the SAR as determined by the Committee.

(ii) Other Terms. The Committee shall determine at the date of grant or thereafter, the time or times at which and the circumstances under which a SAR may be exercised in whole or in part (including based on achievement of performance goals and/or future service requirements), the method of exercise, method of settlement, form of consideration payable in settlement, method by or forms in which Stock will be delivered or deemed to be delivered to Participants, and whether or not a SAR shall be free-standing or in tandem or combination with any other Award. Limited SARs that may only be exercised in connection with a Change in Control or other event as specified by the Committee may be granted on such terms, not inconsistent with this Section 6(c), as the Committee may determine.

(d) Restricted Stock. The Committee is authorized to grant Restricted Stock to Participants on the following terms and conditions:

(i) Grant and Restrictions. Restricted Stock shall be subject to such restrictions on transferability, risk of forfeiture and other restrictions, if any, as the Committee may impose, which restrictions may lapse separately or in combination at such times, under such circumstances (including based on achievement of performance goals and/or future service requirements), in such installments or otherwise and under such other circumstances as the Committee may determine at the date of grant or thereafter. Except to the extent restricted under the terms of the Plan and any Award document relating to the Restricted Stock, a Participant granted Restricted Stock shall have all of the rights of a shareholder, including the right to vote the Restricted Stock and the right to receive dividends thereon (subject to any mandatory reinvestment or other requirement imposed by the Committee).

(ii) Forfeiture. Except as otherwise determined by the Committee, upon termination of employment or service during the applicable restriction period, Restricted Stock that is at that time subject to restrictions shall be forfeited and reacquired by the Company; provided that the Committee may provide, by rule or regulation or in any Award document, or may determine in any individual case, that restrictions or forfeiture conditions relating to Restricted Stock will lapse in whole or in part, including in the event of terminations resulting from specified causes.

(iii) Certificates for Stock. Restricted Stock granted under the Plan may be evidenced in such manner as the Committee shall determine. If certificates representing Restricted Stock are registered in the name of the Participant, the Committee may require that such certificates bear an appropriate legend referring to the terms, conditions and restrictions applicable to such Restricted Stock, that the Company retain physical possession of the certificates, and that the Participant deliver a stock power to the Company, endorsed in blank, relating to the Restricted Stock.

(iv) Dividends and Splits. As a condition to the grant of an Award of Restricted Stock, the Committee may require that any dividends paid on a share of Restricted Stock shall be either (A) paid with respect to such Restricted Stock at the dividend payment date in cash, in kind, or in a number of shares of unrestricted Stock having a Fair Market Value equal to the amount of such dividends, or (B) automatically reinvested in additional Restricted Stock or held in kind, which shall be subject to the same terms as applied to the original Restricted Stock to which it relates, or (C) deferred as to payment, either as a cash deferral or with the amount or value thereof automatically deemed reinvested in shares of Deferred Stock, other Awards or other investment vehicles, subject to such terms as the Committee shall determine or permit a Participant to elect. Unless otherwise determined by the Committee, Stock distributed in connection with a Stock split or Stock dividend, and other property distributed as a dividend, shall be subject to restrictions and a risk of forfeiture to the same extent as the Restricted Stock with respect to which such Stock or other property has been distributed.

(e) **Deferred Stock.** The Committee is authorized to grant Deferred Stock to Participants, which are rights to receive Stock, other Awards, or a combination thereof at the end of a specified deferral period, subject to the following terms and conditions:

(i) **Award and Restrictions.** Issuance of Stock will occur upon expiration of the deferral period specified for an Award of Deferred Stock by the Committee (or, if permitted by the Committee, as elected by the Participant). In addition, Deferred Stock shall be subject to such restrictions on transferability, risk of forfeiture and other restrictions, if any, as the Committee may impose, which restrictions may lapse at the expiration of the deferral period or at earlier specified times (including based on achievement of performance goals and/or future service requirements), separately or in combination, in installments or otherwise, and under such other circumstances as the Committee may determine at the date of grant or thereafter. Deferred Stock may be satisfied by delivery of Stock, other Awards, or a combination thereof (subject to Section 10(k)), as determined by the Committee at the date of grant or thereafter.

(ii) **Forfeiture.** Except as otherwise determined by the Committee, upon termination of employment or service during the applicable deferral period or portion thereof to which forfeiture conditions apply (as provided in the Award document evidencing the Deferred Stock), all Deferred Stock that is at that time subject to such forfeiture conditions shall be forfeited; provided that the Committee may provide, by rule or regulation or in any Award document, or may determine in any individual case, that restrictions or forfeiture conditions relating to Deferred Stock will lapse in whole or in part, including in the event of terminations resulting from specified causes.

(iii) **Dividend Equivalents.** Unless otherwise determined by the Committee, Dividend Equivalents on the specified number of shares of Stock covered by an Award of Deferred Stock shall be either (A) paid with respect to such Deferred Stock at the dividend payment date in cash or in shares of unrestricted Stock having a Fair Market Value equal to the amount of such dividends, or (B) deferred with respect to such Deferred Stock, either as a cash deferral or with the amount or value thereof automatically deemed reinvested in additional Deferred Stock, other Awards or other investment vehicles having a Fair Market Value equal to the amount of such dividends, as the Committee shall determine or permit a Participant to elect.

(f) **Bonus Stock and Awards in Lieu of Obligations.** The Committee is authorized to grant Stock as a bonus, or to grant Stock or other Awards in lieu of obligations of the Company or a subsidiary or affiliate to pay cash or deliver other property under the Plan or under other plans or compensatory arrangements, subject to such terms as shall be determined by the Committee.

(g) Dividend Equivalents. The Committee is authorized to grant Dividend Equivalents to a Participant, entitling the Participant to receive cash, Stock, other Awards, or other property equivalent to all or a portion of the dividends paid with respect to a specified number of shares of Stock. Dividend Equivalents may be awarded on a freestanding basis or in connection with another Award. The Committee may provide that Dividend Equivalents shall be paid or distributed when accrued or shall be deemed to have been reinvested in additional Stock, Awards, or other investment vehicles, and subject to restrictions on transferability, risks of forfeiture and such other terms as the Committee may specify.

(h) Other Stock-Based Awards. The Committee is authorized, subject to limitations under applicable law, to grant to Participants such other Awards that may be denominated or payable in, valued in whole or in part by reference to, or otherwise based on, or related to, Stock or factors that may influence the value of Stock, including, without limitation, convertible or exchangeable debt securities, other rights convertible or exchangeable into Stock, purchase rights for Stock, Awards with value and payment contingent upon performance of the Company or business units thereof or any other factors designated by the Committee, and Awards valued by reference to the book value of Stock or the value of securities of or the performance of specified subsidiaries or affiliates or other business units. The Committee shall determine the terms and conditions of such Awards. Stock delivered pursuant to an Award in the nature of a purchase right granted under this Section 6(h) shall be purchased for such consideration, paid for at such times, by such methods, and in such forms, including, without limitation, cash, Stock, other Awards, notes, or other property, as the Committee shall determine. Cash awards, as an element of or supplement to any other Award under the Plan, may also be granted pursuant to this Section 6(h).

(i) Performance Awards. The Committee is authorized to grant Performance Awards on the terms and conditions specified in this Section 6(i). Performance Awards may be denominated as a cash amount, number of shares of Stock, or specified number of other Awards (or a combination) which may be earned upon achievement or satisfaction of performance conditions specified by the Committee. In addition, the Committee may specify that any other Award shall constitute a Performance Award by conditioning the right of a Participant to exercise the Award or have it settled, and the timing thereof, upon achievement or satisfaction of such performance conditions as may be specified by the Committee. The Committee may use such business criteria and other measures of performance as it may deem appropriate in establishing any performance conditions, and may exercise its discretion to reduce or increase the amounts payable under any Award subject to performance conditions.

#### 7. Certain Provisions Applicable to Awards.

(a) Stand-Alone, Additional, Tandem, and Substitute Awards. Awards granted under the Plan may, in the discretion of the Committee, be granted either alone or in addition to, in tandem with, or in substitution or exchange for, any other Award or any award granted under another plan of the Company, any subsidiary or affiliate, or any business entity to be acquired by the Company or a subsidiary or affiliate, or any other right of a Participant to receive payment from the Company or any subsidiary or affiliate. Awards granted in addition to or in tandem with other Awards or awards may be granted either as of the same time as or a different time from the grant of such other Awards or awards. Subject to Section 10(k), the Committee may determine that, in granting a new Award, the in-the-money value of any surrendered Award or award may be applied to reduce the exercise price of any Non-qualified Stock Option, grant price of any SAR, or purchase price of any other Award.

(b) Term of Awards. The term of each Award shall be for such period as may be determined by the Committee.

(c) Form and Timing of Payment under Awards; Deferrals. Subject to the terms of the Plan (including Section 10(k)) and any applicable Award document, payments to be made by the Company or a subsidiary or affiliate upon the exercise of a Non-qualified Stock Option or other Award or settlement of an Award may be made in such forms as the Committee shall determine, including, without limitation, cash, Stock, other Awards or other property, and may be made in a single payment or transfer, in installments, or on a deferred basis. The settlement of any Award may be accelerated, and cash paid in lieu of Stock in connection with such settlement, in the discretion of the Committee or upon occurrence of one or more specified events (subject to Section 10(k)). Installment or deferred payments may be required by the Committee (subject to

Section 10(e)) or permitted at the election of the Participant on terms and conditions established by the Committee. Payments may include, without limitation, provisions for the payment or crediting of reasonable interest on installment or deferred payments or the grant or crediting of Dividend Equivalents or other amounts in respect of installment or deferred payments denominated in Stock.

(d) Loan Provisions. With the consent of the Committee, and subject at all times to, and only to the extent, if any, permitted under and in accordance with, laws and regulations and other binding obligations or provisions applicable to the Company, the Company may make, guarantee, or arrange for a loan or loans to a Participant with respect to the exercise of any Non-qualified Stock Option or other payment in connection with any Award, including the payment by a Participant of any or all federal, state, or local income or other taxes due in connection with any Award. Subject to such limitations, the Committee shall have full authority to decide whether to make a loan or loans hereunder and to determine the amount, terms, and provisions of any such loan or loans, including the interest rate, if any, to be charged in respect of any such loan or loans, whether the loan or loans are to be with or without recourse against the borrower, the terms on which the loan is to be repaid and conditions, if any, under which the loan or loans may be forgiven.

## 8. Change in Control.

(a) Effect of "Change in Control" on Non-Performance Based Awards. In the event of a "Change in Control," the following provisions shall apply to non-performance based Awards, including Awards as to which performance conditions previously have been satisfied or are deemed satisfied under Section

8(b), unless otherwise provided by the Committee in the Award document:

(i) All deferral of settlement, forfeiture conditions and other restrictions applicable to Awards granted under the Plan shall lapse and such Awards shall be fully payable as of the time of the Change in Control without regard to deferral and vesting conditions, except to the extent of any waiver by the Participant or other express election to defer beyond a Change in Control and subject to applicable restrictions set forth in Section 10(a);

(ii) Any Award carrying a right to exercise that was not previously exercisable and vested shall become fully exercisable and vested as of the time of the Change in Control and shall remain exercisable and vested for the balance of the stated term of such Award without regard to any termination of employment or service by the Participant other than a termination for "cause" (as defined in any employment or severance agreement between the Company or a subsidiary or affiliate and the Participant then in effect or, if none, as defined by the Committee and in effect at the time of the Change in Control), subject only to applicable restrictions set forth in Section 10(a); and

(iii) The Committee may, in its discretion, determine to extend to any Participant who holds a Non-qualified Stock Option the right to elect, during the 60-day period immediately following the Change in Control, in lieu of acquiring the shares of Stock covered by such Non-qualified Stock Option, to receive in cash the excess of the Change in Control Price over the exercise price of such Non-qualified Stock Option, multiplied by the number of shares of Stock covered by such Non-qualified Stock Option, and to extend to any Participant who holds other types of Awards denominated in shares the right to elect, during the 60-day period immediately following the Change in Control, in lieu of receiving the shares of Stock covered by such Award, to receive in cash the Change in Control Price multiplied by the number of shares of Stock covered by such Award.

(b) Effect of "Change in Control" on Performance-Based Awards. In the event of a "Change in Control," with respect to an outstanding Award subject to achievement of performance goals and conditions, such performance goals and conditions shall be deemed to be met or exceeded if and to the extent so provided by the Committee in the Award document governing such Award or other agreement with the Participant.

(c) Definition of "Change in Control." A "Change in Control" shall be deemed to have occurred if, after the Effective Date, there shall have occurred any of the following:

(i) Any "person," as such term is used in Section 13(d) and 14(d) of the Exchange Act (other than the Company, any trustee or other fiduciary holding securities under an employee benefit plan of the Company, or any company owned, directly or indirectly, by the shareholders of the Company in substantially the same proportions as their ownership of stock of the Company), acquires voting securities of the Company and immediately thereafter is a "50% Beneficial Owner." For purposes of this provision, a "50% Beneficial Owner" shall mean a person who is the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 50% or more of the combined voting power of the Company's then-outstanding voting securities;



(ii) During any period of two consecutive years commencing on or after the Effective Date, individuals who at the beginning of such period constitute the Board, and any new director (other than a director designated by a person (as defined above) who has entered into an agreement with the Company to effect a transaction described in subsections (i),

(iii), (iv) or (v) of this definition) whose election by the Board or nomination for election by the Company's shareholders was approved by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors at the beginning of the period or whose election or nomination for election was previously so approved (the "Continuing Directors") cease for any reason to constitute at least a majority thereof;

(iii) The shareholders of the Company have approved a merger, consolidation, recapitalization, or reorganization of the Company, or a reverse stock split of any class of voting securities of the Company, or the consummation of any such transaction if shareholder approval is not obtained, other than any such transaction which would result in at least 50% of the combined voting power of the voting securities of the Company or the surviving entity outstanding immediately after such transaction being beneficially owned by the persons who were shareholders of the Company immediately prior to the transaction in substantially the same proportion as their ownership of the voting power immediately prior to the transaction; provided that, for purposes of this Section 8(c)(iii), such continuity of ownership (and preservation of relative voting power) shall be deemed to be satisfied if the failure to meet such 50% threshold (or to substantially preserve such relative ownership of the voting securities) is due solely to the acquisition of voting securities by an employee benefit plan of the Company, such surviving entity or a subsidiary thereof; and provided further, that, if consummation of the corporate transaction referred to in this Section 8(c)(iii) is subject, at the time of such approval by shareholders, to the consent of any government or governmental agency or approval of the shareholders of another entity or other material contingency, no Change in Control shall occur until such time as such consent and approval has been obtained and any other material contingency has been satisfied;

(iv) The shareholders of the Company accept shares in a share exchange in which the shareholders of the Company immediately before such share exchange do not or will not own directly or indirectly immediately following such share exchange more than 50% of the combined voting power of the outstanding voting securities of the corporation resulting from or surviving such share exchange in substantially the same proportion as the ownership of the Voting Securities outstanding immediately before such share exchange;

(v) The shareholders of the Company have approved a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets (or any transaction having a similar effect); provided that, if consummation of the transaction referred to in this Section 8(c)(v) is subject, at the time of such approval by shareholders, to the consent of any government or governmental agency or approval of the shareholders of another entity or other material contingency, no Change in Control shall occur until such time as such consent and approval has been obtained and any other material contingency has been satisfied; and

(vi) Any other event which the Board of Directors of the Company determines shall constitute a Change in Control for purposes of this Plan.

(d) Definition of "Change in Control Price." The "Change in Control Price" means an amount in cash equal to the higher of (i) the amount of cash and fair market value of property that is the highest price per share paid (including extraordinary dividends) in any transaction triggering the Change in Control or any liquidation of shares following a sale of substantially all assets of the Company, or (ii) the highest Fair Market Value per share at any time during the 60-day period preceding and 60-day period following the Change in Control.

#### 9. Additional Award Forfeiture Provisions.

(a) Events Triggering Forfeiture. Notwithstanding any other provision of this Plan, the forfeitures specified in this Section 9(a) will be triggered if the Participant's employment or engagement is terminated by the Company and the Board makes a determination that the Participant, at any time during the Participant's employment with or engagement by the Company or a subsidiary or affiliate of the Company or at any time during the one-year period following such employment or engagement (i) has engaged in any type of disloyalty to the Company, including without limitation, insubordination, fraud, embezzlement, theft or dishonesty in the course of his employment or engagement, or (ii) has been convicted of a felony, or (iii) has disclosed any confidential or proprietary information without the consent of the Company or (iv) has breached the terms of any written confidentiality agreement or any non-competition agreement with the Company in any material respect. In the event of a termination and Board determination described in the preceding sentence, all unexercised Non-qualified Stock Options and unexercised or otherwise unsettled Awards held by the Participant shall terminate upon the earlier of the date of termination of employment or engagement or the date of the Board's determination.

(b) Committee Discretion. The Committee may, in its discretion, waive in whole or in part the Company's right to forfeiture under this Section, but no such waiver shall be effective unless evidenced by a writing signed by a duly authorized officer of the Company. In addition, the Committee may impose additional conditions on Awards by inclusion of appropriate provisions in the document evidencing or governing any such Award.

#### 10. General Provisions.

(a) Compliance with Legal and Other Requirements. The Company may, to the extent deemed necessary or advisable by the Committee, postpone the issuance or delivery of Stock or payment of other benefits under any Award until completion of such registration or qualification of such Stock or other required action under any federal or state law, rule or regulation, listing or other required action with respect to any stock exchange or automated quotation system upon which the Stock or other securities of the Company are listed or quoted, or compliance with any other obligation of the Company, as the Committee may consider appropriate, and may require any Participant to make such representations, furnish such information and comply with or be subject to such other conditions as it may consider appropriate in connection with the issuance or delivery of Stock or payment of other benefits in compliance with applicable laws, rules, and regulations, listing requirements, or other obligations. The foregoing notwithstanding, in connection with a Change in Control, the Company shall take or cause to be taken no action, and shall undertake or permit to arise no legal or contractual obligation, that results or would result in any postponement of the issuance or delivery of Stock or payment of benefits under any Award or the imposition of any other conditions on such issuance, delivery or payment, to the extent that such postponement or other condition would represent a greater burden on a Participant than existed on the 90th day preceding the Change in Control.

(b) Limits on Transferability; Beneficiaries. No Award or other right or interest of a Participant under the Plan shall be pledged, hypothecated or otherwise encumbered or subject to any lien, obligation or liability of such Participant to any party (other than the Company or a subsidiary or affiliate thereof), or assigned or transferred by such Participant otherwise than by will or the laws of descent and distribution or to a Beneficiary upon the death of a Participant, and such Awards or rights that may be exercisable shall be exercised during the lifetime of the Participant only by the Participant or his or her guardian or legal representative, except that Awards and other rights may be transferred to one or more transferees during the lifetime of the Participant, and may be exercised by such transferees in accordance with the terms of such Award, but only if and to the extent such transfers are permitted by the Committee, subject to any terms and conditions which the Committee may impose thereon (including limitations the Committee may deem appropriate in order that offers and sales under the Plan will meet applicable requirements of registration forms under the Securities Act of 1933 specified by the Securities and Exchange Commission). A Beneficiary, transferee, or other person claiming any rights under the Plan from or through any Participant shall be subject to all terms and conditions of the Plan and any Award document applicable to such Participant, except as otherwise determined by the Committee, and to any additional terms and conditions deemed necessary or appropriate by the Committee.

(c) Adjustments. In the event that any large, special and non-recurring dividend or other distribution (whether in the form of cash or property other than Stock), recapitalization, forward or reverse split, stock dividend, reorganization, merger, consolidation, spin-off, combination, repurchase, share exchange, liquidation, dissolution or other similar corporate transaction or event affects the Stock such that an adjustment is determined by the Committee to be appropriate under the Plan, then the Committee shall, in such manner as it may deem equitable, adjust any or all of (i) the number and kind of shares of Stock which may be delivered in connection with Awards granted thereafter, (ii) the number and kind of shares of Stock subject to or deliverable in respect of outstanding Awards and (iii) the exercise price, grant price or purchase price relating to any Award or, if deemed appropriate, the Committee may make provision for a payment of cash or property to the holder of an outstanding Non-qualified Stock Option (subject to Section 10(k)). In addition, the Committee is authorized to make adjustments in the terms and conditions of, and the criteria included in, Awards (including Performance Awards and performance goals and any hypothetical funding pool relating thereto) in recognition of unusual or nonrecurring events (including, without limitation, events described in the preceding sentence, as well as acquisitions and dispositions of businesses and assets) affecting the Company, any subsidiary or affiliate or other business unit, or the financial statements of the Company or any subsidiary or affiliate, or in response to changes in applicable laws, regulations, accounting principles, tax rates and regulations or business conditions or in view of the Committee's assessment of the business strategy of the Company, any subsidiary or affiliate or business unit thereof, performance of comparable organizations, economic and business conditions, personal performance of a Participant, and any other circumstances deemed relevant.

(d) Tax Provisions.

(i) Withholding. The Company and any subsidiary or affiliate is authorized to withhold from any Award granted, any payment relating to an Award under the Plan, including from a distribution of Stock, or any payroll or other payment to a Participant, amounts of withholding and other taxes due or potentially payable in connection with any transaction involving an Award, and to take such other action as the Committee may deem advisable to enable the Company and Participants to satisfy obligations for the payment of withholding taxes and other tax obligations relating to any Award. This authority shall include authority to withhold or receive Stock or other property and to make cash payments in respect thereof in satisfaction of a Participant's withholding obligations, either on a mandatory or elective basis in the discretion of the Committee. Other provisions of the Plan notwithstanding, only the minimum amount of Stock deliverable in connection with an Award necessary to satisfy statutory withholding requirements will be withheld.

(ii) Required Consent to and Notification of Code Section 83(b) Election. No election under Section 83(b) of the Code (to include in gross income in the year of transfer the amounts specified in Code Section 83(b)) or under a similar provision of the laws of a jurisdiction outside the United States may be made unless expressly permitted by the terms of the Award document or by action of the Committee in writing prior to the making of such election. In any case in which a Participant is permitted to make such an election in connection with an Award, the Participant shall notify the Company of such election within ten days of filing notice of the election with the Internal Revenue Service or other governmental authority, in addition to any filing and notification required pursuant to regulations issued under Code Section 83(b) or other applicable provision.

(e) Changes to the Plan. The Board may amend, suspend or terminate the Plan or the Committee's authority to grant Awards under the Plan without the consent of shareholders or Participants; provided, however, that any amendment to the Plan shall be submitted to the Company's shareholders for approval not later than the earliest annual meeting for which the record date is after the date of such Board action if such shareholder approval is required by any federal or state law or regulation or the rules of any stock exchange or automated quotation system on which the Stock may then be listed or quoted, and the Board may otherwise, in its discretion, determine to submit other amendments to the Plan to shareholders for approval; and provided further, that, without the consent of an affected Participant, no such Board action may materially and adversely affect the rights of such Participant under any outstanding Award. With regard to other terms of Awards, the Committee shall have no authority to waive or modify any such Award term after the Award has been granted to the extent the waived or modified term would be mandatory under the Plan for any Award newly granted at the date of the waiver or modification.

(f) Right of Setoff. The Company or any subsidiary or affiliate may, to the extent permitted by applicable law, deduct from and set off against any amounts the Company or a subsidiary or affiliate may owe to the Participant from time to time, including amounts payable in connection with any Award, owed as wages, fringe benefits, or other compensation owed to the Participant, such amounts as may be owed by the Participant to the Company, including but not limited to amounts owed under Section 10(a), although the Participant shall remain liable for any part of the Participant's payment obligation not satisfied through such deduction and setoff. By accepting any Award granted hereunder, the Participant agrees to any deduction or setoff under this Section 10(f).

(g) **Unfunded Status of Awards; Creation of Trusts.** The Plan is intended to constitute an "unfunded" plan for incentive and deferred compensation. With respect to any payments not yet made to a Participant or obligation to deliver Stock pursuant to an Award, nothing contained in the Plan or any Award shall give any such Participant any rights that are greater than those of a general creditor of the Company; provided that the Committee may authorize the creation of trusts and deposit therein cash, Stock, other Awards or other property, or make other arrangements to meet the Company's obligations under the Plan. Such trusts or other arrangements shall be consistent with the "unfunded" status of the Plan unless the Committee otherwise determines with the consent of each affected Participant.

(h) **Nonexclusivity of the Plan.** The adoption of the Plan by the Board shall not be construed as creating any limitations on the power of the Board or a committee thereof to adopt such other incentive arrangements, apart from the Plan, as it may deem desirable.

(i) **Payments in the Event of Forfeitures; Fractional Shares.** Unless otherwise determined by the Committee, in the event of a forfeiture of an Award with respect to which a Participant paid cash consideration, the Participant shall be repaid the amount of such cash consideration. No fractional shares of Stock shall be issued or delivered pursuant to the Plan or any Award. The Committee shall determine whether cash, other Awards or other property shall be issued or paid in lieu of such fractional shares or whether such fractional shares or any rights thereto shall be forfeited or otherwise eliminated.

(j) **Certain Limitations Relating to Accounting Treatment of Awards.** Other provisions of the Plan notwithstanding, the Committee's authority under the Plan (including under Sections 7(c), 10(c) and 10(d)) is limited to the extent necessary to ensure that any Non-qualified Stock Option or other Award of a type that the Committee has intended to be subject to fixed accounting with a measurement date at the date of grant or the date performance conditions are satisfied under APB 25 shall not become subject to "variable" accounting solely due to the existence of such authority.

(k) **Governing Law.** The validity, construction, and effect of the Plan, any rules and regulations relating to the Plan and any Award document shall be determined in accordance with the laws of the Commonwealth of Pennsylvania, without giving effect to principles of conflicts of laws, and applicable provisions of federal law.

(l) **Awards to Participants Outside the United States.** The Committee may modify the terms of any Award under the Plan made to or held by a Participant who is then resident or primarily employed outside of the United States in any manner deemed by the Committee to be necessary or appropriate in order that such Award shall conform to laws, regulations, and customs of the country in which the Participant is then resident or primarily employed, or so that the value and other benefits of the Award to the Participant, as affected by foreign tax laws and other restrictions applicable as a result of the Participant's residence or employment abroad shall be comparable to the value of such an Award to a Participant who is resident or primarily employed in the United States.

(m) Limitation on Rights Conferred under Plan. Neither the Plan nor any action taken hereunder shall be construed as (i) giving any Eligible Person or Participant the right to continue to provide services to the Company or a subsidiary or affiliate, (ii) interfering in any way with the right of the Company or a subsidiary or affiliate to terminate the employment or engagement of any Eligible Person at any time, (iii) giving an Eligible Person or Participant any claim to be granted any Award under the Plan or to be treated uniformly with other Participants, employees or service providers, or (iv) conferring on a Participant any of the rights of a shareholder of the Company unless and until the Participant is duly issued or transferred shares of Stock in accordance with the terms of an Award or a Non-qualified Stock Option is duly exercised. Except as expressly provided in the Plan and an Award document, neither the Plan nor any Award document shall confer on any person other than the Company and the Participant any rights or remedies thereunder.

(n) Severability; Entire Agreement. If any of the provisions of this Plan or any Award document is finally held to be invalid, illegal or unenforceable (whether in whole or in part), such provision shall be deemed modified to the extent, but only to the extent, of such invalidity, illegality or unenforceability, and the remaining provisions shall not be affected thereby; provided, that, if any of such provisions is finally held to be invalid, illegal, or unenforceable because it exceeds the maximum scope determined to be acceptable to permit such provision to be enforceable, such provision shall be deemed to be modified to the minimum extent necessary to modify such scope in order to make such provision enforceable hereunder. The Plan and any Award documents contain the entire agreement of the parties with respect to the subject matter thereof and supersede all prior agreements, promises, covenants, arrangements, communications, representations and warranties between them, whether written or oral with respect to the subject matter thereof.

(o) References to Legal and Regulatory Provisions. References in this Plan to any provision of law, including the Code and the Exchange Act, or rule or regulation (including accounting principles and interpretations) shall include subsequently adopted amendments and any successor provisions, rules or regulations.

(p) Plan Effective Date and Termination. The Plan shall become effective upon its adoption by the Board. Unless earlier terminated by action of the Board of Directors and subject to Section 6(a), the Plan will remain in effect until such time as no Stock remains available for delivery under the Plan and the Company has no further rights or obligations under the Plan with respect to outstanding Awards under the Plan.