



MicroVision

2016 Annual Report
and
Proxy Statement for 2017 Annual Meeting of Shareholders

Certain statements contained in this annual report, including those relating to timing of future product introductions, manufacturing capacity, revenue, growth, royalties, product deliveries, benefits of contractual relationships, business strategy, future commercial agreements, supply chain capabilities and relationships, operating results, products, business and technology development, product and technology benefits, industry and consumer demand and those using words such as “goals,” “prepare,” “looking forward,” “foresee,” “expect,” “plan,” “opportunity,” “believe,” “potential,” and “will” are forward-looking statements that involve a number of risks and uncertainties. Factors that could cause actual results to differ materially from those projected in forward-looking statements include the following: our ability to raise additional capital when needed; products incorporating our PicoP® display engine may not achieve market acceptance; commercial partners may not enter into or perform under agreements as anticipated; our or our customers failure to perform under open purchase orders; our financial and technical resources relative to those of our competitors; our ability to keep up with rapid technological change; government regulation of our technologies; our ability to enforce our intellectual property rights and protect our proprietary technologies; the ability to obtain additional contract awards; the timing of commercial product launches and delays in product development; the ability to achieve key technical milestones in key products; dependence on third parties to develop, manufacture, sell and market our products; potential product liability claims; and other risk factors identified from time to time in our SEC reports, including our most recent Annual Report on Form 10-K filed with the SEC. Except as expressly required by federal securities laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changes in circumstances or any other reason.

Dear Fellow Shareholder:

We have made great strides over the past several years positioning MicroVision for continued growth in 2017 and 2018. At the end of 2016 there were multiple products in the market with our technology; we hit the upper end of our 2016 revenue guidance with a year-over-year revenue increase of over 60 percent, marking the second year in a row of significant revenue growth; and operational improvements we made throughout the year resulted in decreased cost and increased gross margin for our components. In November 2016 we announced a co-marketing agreement for laser beam scanning (LBS) solutions with global semiconductor leader STMicroelectronics, and we also announced that two global technology leaders engaged MicroVision for proof-of-concept demonstrators for advanced applications, one for augmented and virtual reality and one for an advanced driver assistance system (ADAS).

Perhaps most significantly we also announced our plans in November 2016 to introduce three different scanning engine products for a variety of applications that can be enhanced by the display and sensing features of our proprietary LBS technology platform. Our ability to launch these engine products in 2017 and 2018 is a result of completing several critical technology programs in 2016 and capitalizing on having a single technology platform with common components that can be applied across different engines for display, interactive projection, and 3D LiDAR sensing.

We expect the new engine line of business to contribute to another year of significant revenue growth in 2017. We expect revenue from our engine sales to be in the range of \$30 million to \$60 million in the 12 to 18 months following the shipment of the first production units, which is expected later this year. Samples of our small form factor display engine became available to potential customers in December 2016, and in March 2017 we received a \$6.7 million order for this display engine. In addition to commercializing our technology through these engine products, we plan to continue to provide our components and/or licenses to OEMs and ODMs that prefer to vertically integrate our technology in their products.

The work we are undertaking with two global technology leaders to deliver prototypes is another source of revenue for 2017. Beyond the revenue for prototypes, the real opportunity lies in the potential to be designed into future products in two high growth markets. We believe that our technology has inherent advantages for augmented/virtual reality and ADAS, and we are pleased to be engaged in programs to demonstrate those advantages to these technology leaders.

We believe that the actions we are taking and the programs we are executing today will create significant value for shareholders. We appreciate the support of all of our shareholders, from those who have believed in us and invested in MicroVision from the start to those who are new to the company, attracted by the opportunities ahead. We are working for all of you to deliver on the promise of our multi-faceted technology and its ability to offer consumers better ways to see, experience and navigate their increasingly complex, connected worlds.

Alexander Y. Tokman
President and Chief Executive Officer

Notice of Annual Meeting
of Shareholders
and
Proxy Statement

MICROVISION, INC.

NOTICE OF 2017 ANNUAL MEETING June 7, 2017

Dear MicroVision Shareholder:

The Annual Meeting of Shareholders of MicroVision, Inc. (the “Company”), will be held at Courtyard Marriott Bellevue/Redmond, 14615 NE 29th Place, Bellevue, WA 98007 on June 7, 2017 at 9:00 a.m. for the following purposes:

1. To elect seven directors to serve until the next annual meeting;
2. To approve an amendment to the 2013 MicroVision, Inc. Incentive Plan;
3. To ratify the selection of Moss Adams LLP as the Company’s independent registered public accounting firm for the current fiscal year;
4. To hold a non-binding advisory vote on the compensation of the Company’s named executive officers;
5. To hold a non-binding advisory vote on the frequency of future executive compensation votes; and
6. To conduct any other business that may properly come before the meeting and any adjournment or postponement of the meeting.

Details of the business to be conducted at the meeting are more fully described in the accompanying Proxy Statement. Please read it carefully before casting your vote.

If you were a shareholder of record on April 13, 2017 (the “Record Date”), you will be entitled to vote on the above matters. A list of shareholders as of the Record Date will be available for shareholder inspection at the headquarters of the Company, 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052, during ordinary business hours, from May 23, 2017 to the date of the Annual Meeting. The list also will be available for inspection at the Annual Meeting.

Important!

Whether or not you plan to attend the Annual Meeting, your vote is very important.

After reading the Proxy Statement, you are encouraged to vote by (1) toll-free telephone call, (2) the Internet or (3) completing, signing and dating the printable proxy card and returning it as soon as possible. If you are voting by telephone or the Internet, please follow the instructions on the proxy card. You may revoke your proxy at any time before it is voted by following the instructions provided below.

Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting of Shareholders to be Held on June 7, 2017. The proxy materials and the annual report to shareholders for the fiscal year ended December 31, 2016 are available at <http://www.microvision.com/investors/proxy.html>.

If you need assistance voting your shares, please call Investor Relations at (425) 882-6629.

The Board of Directors recommends a vote **FOR** the election of the seven nominees for directors, a vote **FOR** approval of the proposed amendment to the 2013 MicroVision, Inc. Incentive Plan, a vote **FOR** ratification of the selection of Moss Adams LLP as the Company’s independent registered public accounting firm, a vote **FOR** the approval, on an advisory basis, of the compensation of the Company’s named executive officers, as such information is disclosed in this Proxy Statement under the heading Executive Compensation (commonly referred to as “say-on-pay”) and a vote to hold a say-on-pay vote once every **THREE YEARS**.

At the Annual Meeting, you will have an opportunity to ask questions about the Company and its operations. You may attend the Annual Meeting and vote your shares in person, even if you previously voted by telephone or the Internet or returned your proxy card. Your proxy (including a proxy granted by telephone or the Internet) may be revoked by sending in another signed proxy card with a later date, sending a letter revoking your proxy to the Company’s Secretary in Redmond, Washington, voting again by telephone or Internet, or attending the Annual Meeting and voting in person.

We look forward to seeing you. Thank you for your ongoing support of and interest in MicroVision, Inc.

Sincerely,



David J. Westgor
Secretary

April 24, 2017
Redmond, Washington

MICROVISION, INC.

6244 185th Avenue NE, Suite 100
Redmond, Washington 98052

PROXY STATEMENT FOR ANNUAL MEETING OF SHAREHOLDERS June 7, 2017

TABLE OF CONTENTS

INFORMATION ABOUT THE ANNUAL MEETING AND VOTING	1
DISCUSSION OF PROPOSALS RECOMMENDED BY THE BOARD	4
Proposal One—Election Of Directors	4
Board Meetings and Committees	6
Shareholder Communication with the Board of Directors	10
Compensation Committee Interlocks and Insider Participation	10
Section 16(a) Beneficial Ownership Reporting Compliance	10
Code of Ethics	10
Proposal Two—Amendment of the 2013 MicroVision, Inc. Incentive Plan	11
Proposal Three—Ratification of the Selection of Independent Registered Public Accounting Firm	15
Proposal Four—Advisory Vote on Executive Compensation	16
Proposal Five—Advisory Vote on Frequency of Executive Compensation Advisory Votes	17
OTHER BUSINESS	17
EXECUTIVE COMPENSATION	18
Compensation Discussion and Analysis	18
Compensation Committee Report	20
Summary Compensation Table for 2016	21
Grants of Plan-Based Awards During 2016	22
Outstanding Equity Awards at Year End 2016	22
Option Exercises and Stock Vested During 2016	23
Potential Payments upon Termination or Change in Control	23
Severance and Employment Agreements	24
Director Compensation for 2016	26
INFORMATION ABOUT MICROVISION COMMON STOCK OWNERSHIP	28
CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE	29
AUDIT COMMITTEE REPORT	29
INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM	30
INFORMATION ABOUT SHAREHOLDER PROPOSALS	31
ADDITIONAL INFORMATION	32
Annual Report	32
Incorporation by Reference	32
Householding	32
Voting by Telephone or the Internet	32

INFORMATION ABOUT THE ANNUAL MEETING AND VOTING

Q: Why did you send me this Notice of Internet Availability of Proxy Materials?

A: We sent you the Notice of Internet Availability of Proxy Materials because the Board of Directors of the Company (the “Board of Directors” or the “Board”) is soliciting your proxy to vote at the 2017 Annual Meeting of Shareholders (the “Annual Meeting”). The Annual Meeting will be held at the Courtyard Marriott Bellevue/Redmond, 14615 NE 29th Place, Bellevue, WA 98007 on June 7, 2017, at 9:00 a.m.

This Proxy Statement summarizes the information regarding the matters to be voted upon at the Annual Meeting. You do not need to attend the Annual Meeting, however, to vote your shares. You may simply vote your shares by telephone or over the Internet in accordance with the instructions contained on the proxy card. You may also print, complete, sign, and return the proxy card to the address in the instructions.

On April 13, 2017 (the “Record Date”) there were 68,122,274 shares of common stock of the Company outstanding. If you owned shares of our common stock at the close of business on the Record Date, you are entitled to one vote for each share of common stock you owned as of that date. We made this Proxy Statement available on or about April 24, 2017 to all shareholders entitled to vote their shares at the Annual Meeting.

Q: How many votes do I have?

A: You have one vote for each share of common stock that you owned on the Record Date. The proxy card will indicate the number of shares.

Q: How do I vote by proxy?

A: If you properly cast your vote by either voting your proxy by telephone or via the Internet or executing and returning the proxy card, and your vote is not subsequently revoked by you, your vote will be voted in accordance with your instructions. If you sign the proxy card but do not make specific choices, your proxy will vote your shares as recommended by the Board as follows:

- “**FOR**” the election of each of the nominees for director;
- “**FOR**” approval of the proposed amendment to the 2013 MicroVision, Inc. Incentive Plan;
- “**FOR**” ratification of the selection of Moss Adams LLP as the Company’s independent registered public accounting firm;
- “**FOR**” the approval, on an advisory basis, of the compensation of the Company’s named executive officers, as such information is disclosed in this Proxy Statement under the heading Executive Compensation (commonly referred to as “say-on-pay”); and
- To hold a say-on-pay vote once every **THREE YEARS**.

If any other matter is presented, your proxy will vote in accordance with his best judgment. At the time we printed this Proxy Statement, we knew of no matters that needed to be acted on at the Annual Meeting other than those discussed in this Proxy Statement.

Q: May my broker vote for me?

A: Under the rules of the Financial Industry Regulatory Authority, if your broker holds your shares in its “street” name, the broker may vote your shares on routine matters even if it does not receive instructions from you. At the Annual Meeting your broker may, without instructions from you, vote on Proposal 3, but not on any of the other proposals.

Q: What are abstentions and broker non-votes?

A: An abstention represents the action by a shareholder to refrain from voting “for” or “against” a proposal. “Broker non-votes” represent votes that could have been cast on a particular matter by a broker, as a shareholder of record, but that were not cast because the broker (i) lacked discretionary voting authority on the matter and did not receive voting instructions from the beneficial owner of the shares or (ii) had discretionary voting authority but nevertheless refrained from voting on the matter.

Q: May I revoke my proxy?

A: Yes. You may change your mind after you send in your proxy card or vote your shares by telephone or via the Internet by following these procedures. To revoke your proxy:

- Vote again by telephone or Internet;
- Send in another signed proxy card with a later date;
- Send a letter revoking your proxy to MicroVision’s Secretary at the Company’s offices in Redmond, Washington; or
- Attend the Annual Meeting and vote in person.

Q: How do I vote in person?

A: If you plan to attend the Annual Meeting and vote in person, we will give you a ballot when you arrive. If your shares are held in a brokerage account or by another nominee, the Notice of Internet Availability of Proxy Materials is being forwarded to you. Follow the instructions on the Notice of Internet Availability of Proxy Materials in order to vote your shares by proxy or in person. Alternatively, you may contact the person in whose name your shares are registered or brokerage if shares are held in street name and obtain a proxy from that person or brokerage and bring it to the Annual Meeting.

Q: What is the quorum requirement for the meeting?

A: The quorum requirement for holding the meeting and transacting business is one-third of the outstanding shares entitled to be voted. The shares may be present in person or represented by proxy at the meeting. Both abstentions and broker non-votes are counted as present for the purpose of determining the presence of a quorum.

Q: What vote is required to approve the election of directors (Proposal 1)?

A: The seven nominees for director who receive the most votes at the 2017 Annual Meeting will be elected. So, if you do not vote for a nominee, or you “withhold authority to vote” for a nominee, your vote will not count either “for” or “against” the nominee. Abstentions and broker non-votes will have no effect on the outcome of voting for directors.

Q: What vote is required to approve the proposed amendment to the 2013 MicroVision, Inc. Incentive Plan (Proposal 2)?

A: The affirmative vote of a majority of the votes properly cast on the proposal at the 2017 Annual Meeting is required to approve the amendment to the 2013 MicroVision, Inc. Incentive Plan. Abstentions and broker non-votes will not be counted “for” or “against” the proposal and will have no effect on the outcome of the vote.

Q: What vote is required to ratify the selection of Moss Adams LLP as the Company’s independent registered public accounting firm (Proposal 3)?

A: The affirmative vote of a majority of the votes properly cast on the proposal at the 2017 Annual Meeting is required to ratify the appointment of Moss Adams LLP as the Company’s independent registered public accounting firm. Abstentions and broker non-votes will have no effect on the outcome of the vote.

Q: What vote is required to approve the vote on the compensation of the Company’s named executive officers (Proposal 4) and the vote on the frequency of future executive compensation votes (Proposal 5)?

A: For Proposal 4, you may vote “**FOR**”, “**AGAINST**”, or “**ABSTAIN**”. For Proposal 5, you may vote to hold a say-on-pay vote once every “**ONE**”, “**TWO**”, or “**THREE**” years, or you may “**ABSTAIN**”.

Because Proposal 4 is an advisory vote, there is technically no minimum vote requirement for that Proposal. Similarly, because Proposal 5 seeks the input of shareholders and provides shareholders with multiple voting options, there is no minimum vote requirement for Proposal 5. Abstentions and broker non-votes will have no effect on the outcome of Proposal 4 or Proposal 5.

Q: Is voting confidential?

A: We keep all the proxies and ballots private as a matter of practice.

Q: Who pays the costs of soliciting these proxies?

A: The Company will pay all the costs of soliciting these proxies. In addition to the solicitation of proxies by mail, our officers and employees also may solicit proxies by telephone, fax or other electronic means of communication, or in person. We will reimburse banks, brokers, nominees, and other fiduciaries for the expenses they incur in forwarding the proxy materials to you.

Q: Who should I call if I have any questions?

A: If you have any questions about the Annual Meeting, voting or your ownership of MicroVision common stock, please call us at (425) 882-6629 or send an e-mail to ir@microvision.com.

DISCUSSION OF PROPOSALS RECOMMENDED BY THE BOARD

Proposal One—Election of Directors

The Board oversees the Company's business affairs and monitors the performance of management. In accordance with corporate governance principles, the Board does not directly involve itself in day-to-day operations of the Company. The directors keep themselves informed through discussions with the Chief Executive Officer, other key executives, and the Company's principal advisers by reading the reports and other materials that the Company sends them regularly and by participating in Board and committee meetings. The Company's directors hold office until their successors have been elected and duly qualified unless the director resigns or by reason of death or other cause is unable to serve. Until any vacancy is filled, the Board will consist of the members who are elected at the Annual Meeting. Proxies cannot be voted for a greater number of persons than the number of nominees named.

If any nominee is unable to stand for election, the shares represented by all valid proxies will be voted for the election of such substitute nominee as the Board may recommend. All of the nominees are currently directors of the Company. The Company is not aware that any nominee is or will be unable to stand for election.

Proxies received from shareholders, unless directed otherwise, will be voted FOR the election of the nominees listed below.

THE BOARD RECOMMENDS A VOTE "FOR" ALL OF THE NOMINEES NAMED BELOW AS DIRECTORS OF THE COMPANY.

We seek individuals to serve as directors with established strong professional reputations, sophistication and experience in strategic planning, leadership, business management, innovation and in substantive areas that affect our business such as: technology development; sourcing, manufacturing and operations; financing; finance and accounting; business operations; government contracts; intellectual property strategy and licensing; legal and regulatory; and sales and marketing. We believe that each of our current directors possesses the professional and personal qualifications necessary for Board service and have highlighted particularly noteworthy attributes for each director in the individual biographies below.

Set forth below are the name, position held and age of each of the nominees for director of the Company. The principal occupation and recent employment history of each nominee is described below, and the number of shares of common stock beneficially owned by each nominee as of April 13, 2017 is set forth on page 28 of this Proxy Statement.

<u>Name</u>	<u>Age</u>	<u>Position</u>
Robert P. Carlile (2)*	61	Director
Yalon Farhi	55	Director
Slade Gorton (1) (3)*	89	Director
Perry Mulligan (1) (2) (3) *	59	Director
Alexander Y. Tokman	55	Director, President and Chief Executive Officer
Brian Turner (1) (2)*	57	Chairman of the Board and Lead Independent Director
Thomas M. Walker *	52	Director

* Independent Director

(1) Member of the Compensation Committee

(2) Member of the Audit Committee

(3) Member of the Nominating Committee

Alexander Y. Tokman has served as President, Chief Executive Officer and a director of the Company since January 2006. Mr. Tokman served as the Company's President and Chief Operating Officer from July 2005 to

January 2006. Mr. Tokman joined the Company after a 10-year tenure at GE Healthcare, a subsidiary of General Electric, where he led several global businesses, most recently as General Manager of its Global Molecular Imaging and Radiopharmacy multi-technology business unit from 2003 to 2005. Prior to that, between 1995 and 2003, Mr. Tokman served in various cross-functional and cross-business leadership roles at GE where he led the definition and commercialization of several medical modalities product segments including PET/CT, which added over \$500 million of revenue growth to the company within the first three years of its commercial introduction. Mr. Tokman is a certified Six Sigma and Design for Six Sigma (DFSS) Black Belt and Master Black Belt and as one of GE's Six Sigma pioneers, he drove the quality culture change across GE Healthcare in the late 1990s. From November 1989 to March 1995 Mr. Tokman served as new technologies programs lead and a head of the I&RD office at Tracor Applied Sciences a subsidiary of then Tracor, Inc. Mr. Tokman has both an M.S. and B.S. in Electrical Engineering from the University of Massachusetts, Dartmouth. As President and Chief Executive Officer of the Company, Mr. Tokman has a deep understanding of the Company and broad executive experience.

Robert P. Carlile, a retired partner at KPMG LLP, joined the Company's board in February 2017. In his 39-year career in public accounting at KPMG and Arthur Andersen, Mr. Carlile served as the lead audit partner on numerous public company engagements operating across different industries including technology, retail, transportation, bio-science, and manufacturing. He worked directly with boards of directors and audit committees of these companies on audits of financial statements and internal controls, registration statements and assistance with mergers, acquisitions and dispositions. In addition to his experience as a lead audit partner Mr. Carlile held a variety of operating leadership positions at KPMG and Arthur Andersen in the Pacific Northwest. In these roles he was responsible for establishing market strategy, fostering community relationships and accomplishing operating results. Mr. Carlile brings expertise to the board in the areas of auditing, accounting and financial reporting, internal controls and corporate governance.

Yalon Farhi joined the Company's board in September 2016. Since 1998, Mr. Farhi, a Colonel in the Israeli Defense Forces (reserves), has served as a motivational lecturer and educator at Bnei-David Institutions, a pre-army and post-army educational program in Israel. From 1998 to January 2016, Mr. Farhi worked as an administrative manager for El-Ami, a non-governmental organization in Israel. Mr. Farhi also serves on the board of directors of DarioHealth Corp., a provider of digital health services. In addition, for the past thirty years, Mr. Farhi has been the owner of a private gardening and land development services company based in Israel. Mr. Farhi received a degree in Education Studies and holds a Teaching Certificate from the Moreshet Yaacov College in Jerusalem. Mr. Farhi brings expertise to the board in international business.

Slade Gorton has served as a director of the Company since September 2003. Mr. Gorton is Of Counsel at the law firm of K&L Gates, LLP. Prior to joining the firm, he represented Washington State in the United States Senate for 18 years. Mr. Gorton began his political career in 1958 as a Washington State Representative and went on to serve as State House Majority Leader. Mr. Gorton served as Attorney General of Washington from 1969-1981, and during that time, he argued 14 cases before the United States Supreme Court. After leaving the Senate, Mr. Gorton served as a Commissioner on the National Commission on Terrorist Attacks Upon the United States ("9-11 Commission"); as a member of the National War Powers Commission and is Co-Chairman of the National Transportation Policy Project. Mr. Gorton also served in the U.S. Army, U.S. Air Force, and the U.S. Air Force Reserves. Mr. Gorton is a former Director of Clearwire, Inc. From his positions as an attorney, in business and government, and prior history as a director of the Company, Mr. Gorton brings expertise in legal matters, corporate governance, general leadership and the Company's business and technology evolution.

Perry Mulligan has served as a director of the Company since January 2010. Mr. Mulligan has over 30 years of experience in operations and supply chain management. Mr. Mulligan was formerly Senior Vice President of Operations for Emulex Corporation where he oversaw Emulex operations, including IT, facilities, supplier management, test engineering and logistics from July 2013 to June 2015. Mr. Mulligan served as Senior Vice President, Operations for QLogic from October 2007 to June 2013, where he was responsible for all aspects of the manufacturing and delivery of products to the customer in addition to overall supply chain design and

manufacturing strategy. Prior to QLogic, Mr. Mulligan was at Solectron from May 2004 to September 2007, where he held the position of Senior Vice President Supply Chain Management and Chief Procurement Officer and was responsible for establishing the overall materials and supply chain strategy. Mr. Mulligan brings extensive experience and knowledge in developing and setting up worldwide manufacturing and sourcing operations and overall supply chain strategy.

Brian Turner has served as a director of the Company since July 2006 and currently serves as Chairman of the Board and Lead Independent Director. Mr. Turner was the Chief Financial Officer of Coinstar Inc. from 2003 until June 2009. Prior to Coinstar, from 2001 to 2003, he served as Senior Vice President of Operations, Chief Financial Officer and Treasurer of Real Networks, Inc., a digital media and technology company. Prior to Real Networks, from 1999 to 2001, Mr. Turner was employed by BSquare Corp., a software company, where he initially served as Senior Vice President of Operations, Chief Financial Officer and Secretary, before being promoted to President and Chief Operating Officer. From 1995 to 1999, Mr. Turner was Chief Financial Officer and Vice President of Administration of Radisys Corp., an embedded software company. Mr. Turner's experience also includes 13 years at PricewaterhouseCoopers LLP where he held several positions including Director, Corporate Finance. Mr. Turner sits on various private company boards as well as on the board of Cray, Inc., a public company. Mr. Turner brings financing expertise and knowledge of operational finance and accounting to the Board.

Thomas M. Walker has served as a director of the Company since November 2013. Mr. Walker served as Executive Vice President of the Company from December 2012 through November 2013. Mr. Walker served as Vice President, General Counsel and Secretary of the Company from May 2002 to December 2012. Prior to joining MicroVision, Mr. Walker served as Senior Vice President, General Counsel and Secretary of Advanced Radio Telecom Corp., a publicly held telecommunications company where he managed domestic and international legal affairs from April 1996 to April 2002. Prior to that, Mr. Walker advised publicly and privately held businesses while practicing in the Los Angeles offices of the law firms of Pillsbury Winthrop and Buchalter Nemer Fields and Younger. Mr. Walker holds a B.A. from Claremont McKenna College and a J.D. from the University of Oregon. Mr. Walker has an in depth knowledge of the Company's business from his time spent as an executive of the Company and also brings an understanding of corporate governance and relevant legal topics to the Board.

Board Meetings and Committees

Our Board of Directors met ten times during 2016. All directors attended at least 75% of the meetings of the Board and meetings of the Board committees on which they served, with the exception of Mr. Farhi, who attended one of the four meetings of the Board that occurred after he joined the Board in September 2016. We have adopted a policy that each of our directors be requested to attend our Annual Meeting each year. All directors attended our annual meeting in 2016.

Independence Determination

No director will be deemed to be independent unless the Board affirmatively determines that the director has no material relationship with the Company, directly or as an officer, share owner, or partner of an organization that has a relationship with the Company. The Board observes all criteria for independence set forth in the NASDAQ listing standards and other governing laws and regulations.

In its annual review of director independence, the Board considers all commercial, banking, consulting, legal, accounting, charitable, or other business relationships any director may have with us. As a result of its annual review, the Board has determined that all of the directors, with the exception of Mr. Tokman and Mr. Farhi, are independent (the "Independent Directors"). The Independent Directors are identified by an asterisk in the table above.

The NASDAQ listing standards have both objective tests and a subjective test for determining who is an “independent director.” The objective tests state, for example, that a director is not considered independent if he or she is our employee or is a partner in or executive officer of an entity to which we made, or from which we received, payments in the current or any of the past three fiscal years that exceed 5% of the recipient’s consolidated gross revenue for that year. The subjective test states that an independent director must be a person who lacks a relationship that, in the opinion of the Board, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. None of the non-employee directors were disqualified from “independent” status under the objective tests. In assessing independence under the subjective test, the Board took into account the standards in the objective tests, and reviewed and discussed additional information provided by the directors and us with regard to each director’s business and personal activities as they may relate to us and our management. Based on all of the foregoing, as required by NASDAQ rules, the Board made a subjective determination as to each Independent Director that no relationship exists which, in the opinion of the Board, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. The Board has not established categorical standards or guidelines to make these subjective determinations, but considers all relevant facts and circumstances.

In addition to the Board-level standards for director independence, the directors who serve on the Audit Committee each satisfy standards established by the Securities and Exchange Commission (the “SEC”) providing that to qualify as “independent” for purposes of membership on that Committee, members of audit committees may not accept, directly or indirectly any consulting, advisory, or other compensatory fee from us other than their director compensation.

Board’s Role in Risk Oversight

It is management’s responsibility to manage risk and bring to the Board’s attention risks that are material to the Company. The Board has oversight responsibility of the processes established to report and monitor systems for the most significant risks applicable to the Company. The Board administers its risk oversight role directly and through its committee structure and the committees’ regular reports to the Board at Board meetings. The Board reviews strategic, financial and execution risks and exposures associated with the annual plan and multi-year plans, major litigation and other matters that may present material risk to our operations, plans, prospects or reputation; acquisitions and divestitures and senior management succession planning.

Board Expertise and Diversity

The Nominating Committee seeks to have a Board that represents diversity as to experience, gender, race and ethnicity, but does not have a formal policy with respect to diversity. We seek a Board that reflects a range of talents, ages, skills, viewpoints, professional experience, educational background and expertise to provide sound and prudent guidance with respect to our operations and interests. All of our directors are financially literate, and three members of our Audit Committee are audit committee financial experts.

Board Leadership Structure

Our Board annually elects a Chairman of the Board. The Board has chosen to separate the roles of Chairman and Chief Executive Officer. Mr. Turner currently serves as Chairman and Lead Independent Director. In this role, among other duties, Mr. Turner meets with our Chief Executive Officer and with senior officers as necessary, schedules and presides at meetings of the Board, including meetings of the Independent Directors, serves as a liaison between the Board and our management, approves meeting schedules and agendas, and undertakes other responsibilities designated by the Board. The Board believes that the separate roles of Mr. Tokman as Chief Executive Officer and Mr. Turner as Chairman and Lead Independent Director currently well serve the interests of us and our shareholders. Mr. Tokman can devote his attention to leading the Company and focus on our business strategy. The Board believes that Mr. Turner provides an appropriate level of independence in the Company’s leadership through his review and approval of meeting agendas and his leadership of the Board.

Committees

The Board of Directors has an Audit Committee, a Compensation Committee, and a Nominating Committee. The Board of Directors has adopted a written charter for each of the Audit Committee, Compensation Committee and Nominating Committee. The full text of each charter is available on our website located at www.microvision.com.

The Audit Committee

The Board has an Audit Committee which assists the Board by monitoring and overseeing: (1) our accounting and financial reporting processes and the audits of our financial statements, (2) the integrity of our financial statements, (3) our compliance with legal and regulatory requirements, and (4) the performance of our internal finance and accounting personnel and our independent auditors. The Audit Committee conducts discussions related to our earnings announcements and periodic filings, as well as numerous other informal meetings and communications among the Chair, various Audit Committee members, the independent auditors and/or members of our management. Richard Cowell, Robert Carlile, Perry Mulligan and Brian Turner currently serve on the Audit Committee, with Mr. Cowell serving as Chairman. The Audit Committee met four times during 2016.

Among other matters, the Audit Committee monitors the activities and performance of our external auditors, including the audit scope, external audit fees, auditor independence matters and the extent to which the independent auditor may be retained to perform non-audit services. The Audit Committee and the Board of Directors have ultimate authority and responsibility to select, evaluate and, when appropriate, replace our independent auditor. The Audit Committee also reviews the results of the external audit work with regard to the adequacy and appropriateness of our financial accounting and internal controls. Management and independent auditor presentations to and discussions with the Audit Committee also cover various topics and events that may have significant financial impact or are the subject of discussions between management and the independent auditor. In addition, the Audit Committee generally oversees our internal financial controls and financial disclosure procedures.

The “audit committee financial experts” designated by the Board are Col. Richard A. Cowell (Ret), Robert P. Carlile and Brian Turner, each an independent director. Col. Cowell holds a degree in accounting and has served for over fifteen years as Chair of our Audit Committee. During his twenty five years of service in the United States Army, Col. Cowell oversaw and actively supervised various complex governmental projects that involved government accounting with a breadth and level of complexity comparable to accounting issues raised by our financial statements, including issues relating to estimates, accruals, and reserves. Since retiring from the Army, Col. Cowell served as a Principal at Booz Allen Hamilton, Inc. where he provided consulting services relating to significant and complex accounting issues. Mr. Carlile has thirty-nine years of experience in various roles in Public Accounting at KPMG and Arthur Andersen. Mr. Turner has eight years of experience as a chief financial officer of three public companies and has thirteen years of experience in various roles at PricewaterhouseCoopers LLP, including Director, Corporate Finance. Mr. Turner has been actively involved in and has supervised the preparation of financial statements that present a breadth and complexity of issues comparable to accounting issues raised by our financial statements.

The Compensation Committee

The Compensation Committee makes decisions on behalf of, and recommendations to, the Board regarding salaries, incentives and other forms of compensation for directors, officers, and other key employees, and administers policies relating to compensation and benefits. The Compensation Committee also serves as the Plan Administrator for our stock option plans pursuant to authority delegated by the Board. Slade Gorton, Perry Mulligan and Brian Turner currently serve as members of the Compensation Committee, with Mr. Mulligan serving as chairperson. The Compensation Committee met two times during 2016.

The Nominating Committee

The Nominating Committee counsels the Board of Directors with respect to Board and committee structure and membership. In fulfilling its duties, the Nominating Committee, among other things, will:

- establish criteria for nomination to the Board and its committees, taking into account the composition of the Board as a whole;
- identify, review, and recommend director candidates for the Board;
- recommend directors for election at the annual meeting of shareholders and to fill new or vacant positions;
- establish policies with respect to the process by which our shareholders may recommend candidates to the Nominating Committee for consideration for nomination as a director;
- assess and monitor, with Board involvement, the performance of the Board; and
- recommend directors for membership on Board Committees.

Richard Cowell, Slade Gorton and Perry Mulligan currently serve as members of the Nominating Committee, with Mr. Mulligan serving as Chairman. The Nominating Committee met once during 2016.

The Nominating Committee will consider recommendations for directorships submitted by shareholders, or groups of shareholders, that have beneficially owned at least 5% of our outstanding shares of common stock for at least one year prior to the date the nominating shareholder submits a candidate for nomination as a director. A nominating shareholder or group of nominating shareholders may submit only one candidate for consideration. Shareholders who wish the Nominating Committee to consider their recommendations for nominees for the position of director should submit their request in writing no later than the 120th calendar day before the anniversary of the date of the prior year's annual meeting proxy statement was released to shareholders. Such written requests should be submitted to the Nominating Committee care of the Corporate Secretary, MicroVision, Inc., 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052, and must contain the following information:

- The name, address, and number of shares of common stock beneficially owned by the nominating shareholder and each participant in a nominating shareholder group (including the name and address of all beneficial owners of more than 5% of the equity interests of a nominating shareholder or participant in a nominating shareholder group);
- A representation that the nominating shareholder, or nominating shareholder group, has been the beneficial owner of more than 5% of our outstanding shares of common stock for at least one year and will continue to beneficially own at least 5% of our outstanding shares of common stock through the date of the annual meeting;
- A description of all relationships, arrangements, or understandings between or among the nominating shareholder (or any participant in a nominating shareholder group) and the candidate or any other person or entity regarding the candidate, including the name of such person or entity;
- All information regarding the candidate that we would be required to disclose in a proxy statement filed pursuant to the rules and regulations of the SEC with respect to a meeting at which the candidate would stand for election;
- Confirmation that the candidate is independent, with respect to the Company, under the independence requirements established by us, the SEC, and NASDAQ listing requirements, or, if the candidate is not independent with respect to the Company under all such criteria, a description of the reasons why the candidate is not independent;
- The consent of the candidate to be named as a nominee and to serve as a member of the Board if nominated and elected;

- A representation signed by the candidate that if elected he or she will: (1) represent all shareholders of the Company in accordance with applicable laws, and our certificate of incorporation, by-laws, and other policies; (2) comply with all rules, policies, or requirements generally applicable to non-employee directors; and (3) upon request, complete and sign customary Directors and Officers Questionnaires.

In its assessment of each potential candidate, the Nominating Committee will review the nominee's judgment, experience, independence, understanding of our or other related industries and such other factors the Nominating Committee determines are pertinent in light of the current needs of the Board. The Nominating Committee will also take into account the ability of a director to devote the time and effort necessary to fulfill his or her responsibilities.

Nominees may be suggested by directors, members of management, and, as described above, by shareholders. In identifying and considering candidates for nomination to the Board, the Nominating Committee considers, in addition to the requirements set out in the Nominating Committee charter, quality of experience, our needs and the range of talent and experience represented on the Board.

Shareholder Communication with the Board of Directors

We have adopted written procedures establishing a process by which our shareholders can communicate with the Board of Directors regarding various topics related to the Company. A shareholder desiring to communicate with the Board, or any individual director, should send his or her written message to the Board of Directors (or the applicable director or directors) care of the Corporate Secretary, MicroVision, Inc., 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052. Each submission will be forwarded, without editing or alteration, by the Secretary of the Company to the Board, or the applicable director or directors, on or prior to the next scheduled meeting of the Board. The Board will determine the method by which such submission will be reviewed and considered. The Board may also request the submitting shareholder to furnish additional information it may reasonably require or deem necessary to sufficiently review and consider the submission of such shareholder.

Compensation Committee Interlocks and Insider Participation

All members of the Compensation Committee during 2016 were independent directors, and none of them were our employees or former employees. During 2016, none of our executive officers served on the compensation committee (or equivalent), or the board of directors, of any other entity whose executive officer(s) served on the Compensation Committee or Board of Directors.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires that our directors, executive officers, and greater-than 10% shareholders file reports with the SEC relating to their initial beneficial ownership of our securities and any subsequent changes. They must also provide us with copies of the reports.

Based solely on a review of the copies of such forms in our possession, and on written representations from reporting persons, we believe that all of these reporting persons complied with their filing requirements during 2016.

Code of Ethics

We have adopted a code of ethics applicable to all of our executive officers, known as the Code of Ethics for MicroVision Executives. We have also adopted a code of conduct applicable to our directors, officers, and employees, known as the Code of Conduct. The Code of Ethics for MicroVision Executives and the Code of Conduct are available on our website. In the event that we amend or waive any of the provisions of the Code of Ethics for MicroVision Executives we intend to disclose the same on our website at www.microvision.com.

Proposal Two—Amendment of the 2013 MicroVision, Inc. Incentive Plan

The Board of Directors has authorized an amendment to the 2013 MicroVision, Inc. Incentive Plan (as amended, the “Incentive Plan”), subject to shareholder approval. The amendment will increase the number of shares of common stock reserved for issuance upon exercise of options granted under the Incentive Plan by 1,500,000 to a total of 9,300,000 shares.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE “FOR” THE FOREGOING AMENDMENT OF THE 2013 MICROVISION, INC. INCENTIVE PLAN.

Summary of the Incentive Plan

The Incentive Plan amended, restated and renamed our 2006 Incentive Plan. The Incentive Plan was originally adopted by the Board in 2013 and approved by the shareholders in June of 2013. The Incentive Plan will terminate on the tenth anniversary of the date of approval by the shareholders, unless earlier terminated by the Board. If the proposed amendment to the Incentive Plan is approved, a maximum of 9,300,000 shares of common stock may be delivered in satisfaction of awards made under the Incentive Plan. The maximum number of shares of common stock for which stock options may be granted to any person in any calendar year and the maximum number of shares of common stock subject to stock appreciation rights, or “SARs,” granted to any person in any calendar year will each be 250,000. The maximum benefit that will be paid to any person under other awards in any calendar year will be, to the extent paid in shares, 250,000 shares, and, to the extent paid in cash, \$3,000,000. In the event of a stock dividend, stock split or other change in our capital structure, the Administrator will make appropriate adjustments to the limits described above and will also make appropriate adjustments to the number and kind of shares of stock or securities subject to awards, any exercise prices relating to awards and any other provisions of awards affected by the change. The Administrator may also make similar adjustments to take into account other distributions to stockholders or any other event, if the Administrator determines that adjustments are appropriate to avoid distortion in the operation of the Incentive Plan and to preserve the value of awards.

Administration. The Board of Directors administers the Incentive Plan. The term “Administrator” is used in this Proxy Statement to refer to the person (the Board and its delegates) charged with administering the Incentive Plan. The Administrator has full authority to determine who will receive awards and to determine the types of awards to be granted as well as the amounts, terms, and conditions of any awards. Awards may be in the form of options, SARs, restricted or unrestricted stock, deferred stock, other stock-based awards, or cash awards, and any such award may be a performance-based award. The Administrator has the right to determine any questions that may arise regarding the interpretation and application of the provisions of the Incentive Plan and to make, administer, and interpret such rules and regulations as it deems necessary or advisable. Determinations of the Administrator made under the Incentive Plan are conclusive and bind all parties.

Eligibility. Participation is limited to employees, non-employee directors, as well as consultants and advisors who are selected by the Administrator to receive an award. The group of persons from which the Administrator will select participants consisted of approximately 90 individuals as of April 13, 2017.

Stock Options. The Administrator may, from time to time, award options to any participant subject to the limitations described above. Stock options give the holder the right to purchase shares of common stock of the Company within a specified period of time at a specified price. Two types of stock options may be granted under the Incentive Plan: incentive stock options, or “ISOs”, which are subject to special tax treatment as described below, and nonstatutory options, or “NSOs.” Eligibility for ISOs is limited to employees of the Company and its subsidiaries.

The exercise price of an ISO cannot be less than the fair market value of the common stock at the time of grant. In addition, the expiration date of an ISO cannot be more than ten years after the date of the original grant.

In the case of NSOs, the exercise price and the expiration date are determined in the discretion of the Administrator. The Administrator also determines all other terms and conditions related to the exercise of an option, including the consideration to be paid, if any, for the grant of the option, the time at which options may be exercised and conditions related to the exercise of options.

Stock Appreciation Rights. The Administrator may grant SARs under the Incentive Plan. An SAR entitles the holder upon exercise to receive an amount in cash or common stock or a combination thereof (as determined by the Administrator) computed by reference to appreciation in the value of a share of common stock above a base amount which may not be less than fair market value on the date of grant.

Stock Awards; Deferred Stock. The Incentive Plan provides for awards of nontransferable shares of restricted common stock, as well as unrestricted shares of common stock. Awards of restricted stock and unrestricted stock may be made in exchange for past services or other lawful consideration. Generally, awards of restricted stock are subject to the requirement that the shares be forfeited or resold to the Company unless specified conditions are met. Subject to these restrictions, conditions and forfeiture provisions, any recipient of an award of restricted stock will have all the rights of a stockholder of the Company, including the right to vote the shares and to receive dividends. Other awards under the Incentive Plan may also be settled with restricted stock. The Incentive Plan also provides for deferred grants (“deferred stock”) entitling the recipient to receive shares of common stock in the future on such conditions as the Administrator may specify. Any stock award or award of deferred stock resulting in a deferral of compensation subject to Section 409A of the Code will be construed to the maximum extent possible consistent with the requirements of Section 409A of the Code.

Performance Awards. The Administrator may also make awards subject to the satisfaction of specified performance criteria. Performance awards may consist of common stock or cash or a combination of the two. The performance criteria used in connection with a particular performance award will be determined by the Administrator. In the case of performance awards intended to qualify for exemption under Section 162(m) of the Internal Revenue Code, the Administrator will use objectively determinable measures of performance in accordance with Section 162(m) that are based on any or any combination of the following (determined either on a consolidated basis or, as the context permits, on a divisional, subsidiary, line of business, project or geographical basis or in combinations thereof): sales; revenues; assets; expenses; earnings before or after deduction for all or any portion of interest, taxes, depreciation, or amortization, whether or not on a continuing operations or an aggregate or per share basis; return on equity, investment, capital or assets; one or more operating ratios; borrowing levels, leverage ratios or credit rating; market share; capital expenditures; cash flow; stock price; stockholder return; sales of particular products or services; customer acquisition or retention; acquisitions and divestitures (in whole or in part); joint ventures and strategic alliances; spin-offs, split-ups and the like; reorganizations; or recapitalizations, restructurings, financings (issuances of debt or equity) or refinancings. The Administrator will determine whether the performance targets or goals that have been chosen for a particular performance award have been met.

General Provisions Applicable to All Awards. Neither ISOs nor, except as the Administrator otherwise expressly provides, other awards may be transferred other than by will or by the laws of descent and distribution. During a recipient’s lifetime, an ISO and, except as the Administrator may provide, other non-transferable awards requiring exercise may be exercised only by the recipient. Shares delivered under the Incentive Plan may consist of either authorized but unissued or treasury shares. The number of shares delivered upon exercise of a stock option is determined net of any shares transferred by the optionee to the Company (including through the holding back of shares that would otherwise have been deliverable upon exercise) in payment of the exercise price or tax withholding.

Mergers and Similar Transactions. In the event of a consolidation or merger in which the Company is not the surviving corporation or which results in the acquisition of substantially all of the Company's stock by a person or entity or by a group of persons or entities acting together, or in the event of a sale of substantially all of the Company's assets or a dissolution or liquidation of the Company, the following rules will apply except as otherwise provided in an Award:

- If the transaction is one in which there is an acquiring or surviving entity, the Administrator may provide for the assumption of some or all outstanding awards or for the grant of new awards in substitution therefor by the acquiror or survivor.
- If the transaction is one in which holders of common stock will receive a payment (whether cash, non-cash or a combination), the Administrator may provide for a "cash-out", with respect to some or all awards, equal in the case of each affected award to the excess, if any, of (A) the fair market value of one share of common stock times the number of shares of common stock subject to the award, over (B) the aggregate exercise or purchase price, if any, under the award (in the case of an SAR, the aggregate base price above which appreciation is measured), in each case on such payment terms and other terms, and subject to such conditions, as the Administrator determines.
- If there is no assumption or substitution of any award requiring exercise, each such outstanding award will become fully exercisable prior to the completion of the transaction on a basis that gives the holder of the award a reasonable opportunity to exercise the award and participate in the transaction as a stockholder.
- Each award, other than outstanding shares of restricted stock, unless assumed will terminate upon consummation of the transaction.
- Any share of common stock delivered pursuant to the "cash-out" or acceleration of an award, as described above, may, in the discretion of the Administrator, contain such restrictions, if any, as the Administrator deems appropriate to reflect any performance or other vesting conditions to which the award was subject. In the case of restricted stock, the Administrator may require that any amounts delivered, exchanged or otherwise paid in respect of such stock in connection with the transaction be placed in escrow or otherwise made subject to such restrictions as the Administrator deems appropriate to carry out the intent of the Incentive Plan.

Amendment. The Administrator may at any time or times amend the Incentive Plan or any outstanding Award for any purpose which may at the time be permitted by law, and may at any time terminate the Incentive Plan as to any future grants of awards. The Administrator may not, however, alter the terms of an Award so as to affect adversely the Participant's rights under the Award without the Participant's consent, unless the Administrator expressly reserved the right to do so at the time of the Award.

Federal Income Tax Consequences

The following discussion summarizes certain federal income tax consequences of the grant and exercise of stock options under the Incentive Plan under the law as in effect on the date of this Proxy Statement. The summary does not purport to cover federal employment tax or other federal tax consequences that may be associated with stock options or federal tax consequences associated with other awards under the Incentive Plan, nor does it cover state, local or non-U.S. taxes.

ISOs. In general, an optionee realizes no taxable income for regular income tax purposes upon the grant or exercise of an ISO. However, the exercise of an ISO may result in an alternative minimum tax liability to the optionee. With certain exceptions, a disposition of shares purchased under an ISO within two years from the date of grant or within one year after exercise (a "disqualifying disposition") produces ordinary income to the optionee equal to the value of the shares at the time of exercise less the exercise price. A corresponding deduction is available to the Company. Any additional gain recognized in the disqualifying disposition is treated as a capital gain for which the Company is not entitled to a deduction. In general, if the disqualifying disposition

is an arm's length sale at less than the fair market value of the shares at time of exercise, the optionee's ordinary income, and the Company's corresponding deduction, are limited to the excess, if any, of the amount realized on the sale over the amount paid by the optionee for the stock. If the optionee does not dispose of the shares until after the expiration of these one- and two-year holding periods, any gain or loss recognized upon a subsequent sale is treated as a long-term capital gain or loss for which the Company is not entitled to a deduction.

NSOs. In general, in the case of a NSO, the optionee has no taxable income at the time of grant but realizes income in connection with exercise of the option in an amount equal to the excess (at the time of exercise) of the fair market value of the shares acquired upon exercise over the exercise price; a corresponding deduction is available to the Company; and upon a subsequent sale or exchange of the shares, any recognized gain or loss after the date of exercise is treated as a capital gain or loss for which the Company is not entitled to a deduction.

In general, an ISO that is exercised by the optionee more than three months after termination of employment is treated as an NSO. ISOs are also treated as NSOs to the extent they first become exercisable by an individual in any calendar year for shares having a fair market value (determined as of the date of grant) in excess of \$100,000.

The Administrator may award stock options that are exercisable for restricted stock. Under Section 83 of the Code, an optionee who exercises an NSO for restricted stock will generally have income only when the stock vests. The income will equal the fair market value of the stock at that time less the exercise price. However, the optionee may make a so-called "83(b) election" in connection with the exercise to recognize taxable income at that time. Assuming no other applicable limitations, the amount and timing of the deduction available to the Company will correspond to the income recognized by the optionee. If an ISO is exercised for restricted stock, a timely 83(b) election will have the effect, in general, of fixing the amount taken into account for alternative minimum tax purposes at the excess of the fair market value of the shares at time of exercise over the exercise price. However, for regular income tax purposes the ordinary income and corresponding Company deduction associated with a disqualifying disposition of stock acquired upon exercise of an ISO, where the stock was restricted at time of exercise but vested prior to the disposition, would be determined by reference to the fair market value of the shares on the date of vesting whether or not the optionee made an 83(b) election.

Under the so-called "golden parachute" provisions of the Code, the accelerated vesting of awards in connection with a change in control of the Company may be required to be valued and taken into account in determining whether a participant has received compensatory payments, contingent on the change in control, in excess of certain limits. If these limits are exceeded, a substantial portion of amounts payable to the participant, including the payment consisting of accelerated vesting of awards, may be subject to an additional 20% federal tax and may be nondeductible to the Company.

Under Section 162(m) of the Code, certain remuneration in excess of \$1 million may be nondeductible if paid to any "covered employee" of a publicly held corporation (generally the corporation's chief executive officer and its next three most highly compensated executive officers, excluding the chief financial officer, in the year that the compensation is paid). Stock options issued under the Incentive Plan are intended to qualify for exemption from the Section 162(m) deduction limit.

Stock options awarded under the Incentive Plan are intended to be exempt from the rules of Section 409A of the Code and guidance issued thereunder and will be administered accordingly. However, neither the Company nor the Administrator, nor any person affiliated with or acting on behalf of the Company or the Administrator, will be liable to any participant or to the estate or beneficiary of any participant by reason of any acceleration of income, or any additional tax or interest penalties, resulting from the failure of an award to satisfy the requirements of Section 409A of the Code.

Proposal Three—Ratification of the Selection of Independent Registered Public Accounting Firm

The Audit Committee of the Board has selected Moss Adams LLP as the Company’s independent registered public accounting firm for the current fiscal year, subject to ratification by the Company’s stockholders at the Annual Meeting. The Company has been advised by Moss Adams LLP that it is a registered public accounting firm with the Public Company Accounting Oversight Board (the “PCAOB”) and complies with the auditing, quality control, and independence standards and rules of the PCAOB and the SEC. A representative of Moss Adams LLP is expected to be present at the Annual Meeting to respond to appropriate questions and to make a statement if he or she so desires.

Although stockholder ratification of the selection of Moss Adams LLP as the Company’s independent registered public accounting firm is not required, the Board is nevertheless submitting the selection of Moss Adams LLP to the stockholders for ratification. Unless contrary instructions are given, shares represented by proxies solicited by the Board will be voted for the ratification of the selection of Moss Adams LLP as the independent registered public accounting firm of the Company for the year ending December 31, 2017. Should the selection of Moss Adams LLP not be ratified by the stockholders, the Audit Committee will reconsider the matter. Even in the event the selection of Moss Adams LLP is ratified, the Audit Committee, in its discretion, may direct the appointment of a different independent registered public accounting firm at any time during the year if it determines that such a change is in the best interests of the Company and its stockholders.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE “FOR” THE RATIFICATION OF THE SELECTION OF MOSS ADAMS LLP AS THE COMPANY’S INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM.

Proposal Four—Advisory Vote on Executive Compensation

The Executive Compensation section beginning on page 18 of this Proxy Statement shows 2016 compensation information for our named executive officers.

The Board is asking shareholders to cast a non-binding, advisory vote **FOR** the approval of the compensation paid to the Company's named executive officers, as disclosed in the Executive Compensation section.

Our executive compensation program embodies a pay-for-performance philosophy that is intended to support the Company's business strategy and align the interests of our executives with our shareholders.

For these reasons, the Board is asking shareholders to support this proposal. Although the vote we are asking you to cast is non-binding, the Compensation Committee and the Board value the views of our shareholders and will consider the outcome of the vote when determining future compensation arrangements for our named executive officers.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" THE APPROVAL, ON AN ADVISORY BASIS, OF THE COMPENSATION OF THE COMPANY'S NAMED EXECUTIVE OFFICERS.

Proposal Five—Advisory Vote on Frequency of Executive Compensation Advisory Votes

In Proposal Four, we are asking shareholders to cast an advisory vote for the compensation disclosed in this proxy statement that we paid in 2016 to our named executive officers. This advisory vote is referred to as a “say-on-pay” vote. In this Proposal Five, the Board is asking shareholders to cast a non-binding, advisory vote on how frequently we should have say-on-pay votes in the future. Shareholders will be able to mark the enclosed proxy card or voting instruction form on whether to hold say-on-pay votes every one, two or three years. Alternatively, you may indicate that you are abstaining from voting.

This vote, like the say-on-pay vote itself, is not binding on the Board. The Board believes that every three years is the appropriate frequency. Our executive compensation programs are intended to have a focus that is longer than the current year for which compensation is paid given the stage of the Company and focus on operational and financial milestones necessary to provide longer term success. As a result, the Board believes that our executive compensation programs should be evaluated over a period longer than one year because our programs are designed to reward performance over time, and three years is a more appropriate period over which to evaluate the effectiveness of those programs than one year or two years. While we recognize that there are many views on the appropriateness of any interval of frequency, we believe that conducting an annual advisory vote on executive compensation may unnecessarily focus on short-term performance. However, if a plurality of votes is cast in favor of an interval other than three years, the Board intends to evaluate the frequency with which an advisory vote on executive compensation will be submitted to shareholders in the future.

THE BOARD OF DIRECTORS RECOMMENDS THAT SHAREHOLDERS VOTE FOR THE THREE-YEAR OPTION AS THE FREQUENCY FOR THE ADVISORY VOTE ON EXECUTIVE COMPENSATION.

OTHER BUSINESS

The Company knows of no other matters to be voted on at the Annual Meeting or any adjournment or postponement of the meeting. If, however, other matters are presented for a vote at the meeting, the proxy holders (the individuals designated on the proxy card) will vote your shares according to their judgment on those matters.

EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

Executive Compensation Objectives

The Company's executive compensation program is designed to attract, retain, motivate and recognize high performance executive officers. The Compensation Committee is responsible for and oversees the Company's compensation program. The Company's philosophy is to provide compensation programs that incentivize and reward both the short and long-term performance of the executive officers relative to the Company's performance. Thus, the Compensation Committee utilizes compensation components that measure overall Company performance, including performance against the Company's annual strategic operating plan. In addition, the Compensation Committee seeks to align the interests of the Company's executive officers with its shareholders.

Executive Compensation Components

Overview. The principal elements of the Company's compensation are base salary, incentive bonus awards, and equity awards. The Company's executive compensation policy recognizes that stock price is only one measure of performance, and given industry business conditions and the long-term strategic direction and goals of the Company, it may not necessarily be the best current measure of executive performance. Thus, the Compensation Committee considers the median level of compensation of its peer group and the achievement of the Company's business objectives when determining executive compensation.

Base Salary. Base salaries for the named executive officers are primarily based on the position, taking into account competitive market compensation paid by other companies in the Company's peer group for similar positions. Recommendations from management regarding each named executive officer's base salary based on management's evaluation of the executive officer's performance are also taken into account.

As with total executive compensation, the Compensation Committee believes that executive base salaries should generally target the median base salary of the Company's peer group. Each named executive officer's base salary is also determined by reviewing the other components of the executive officer's compensation to ensure that the total compensation is in line with the Compensation Committee's overall compensation philosophy.

Salaries for 2016 were based on the compensation objectives mentioned above and in the case of Mr. Tokman, his employment agreement. Base salary rates in 2016 for Messrs. Tokman, Holt, Zimmerman and Westgor were \$364,443, \$221,459, \$220,798 and \$217,745, respectively.

Incentive Bonus. The Compensation Committee believes that a portion of an executive officer's total compensation, an incentive bonus, should be based on the Company's performance. The Compensation Committee believes that structuring a significant portion of each executive officer's annual cash compensation as an incentive bonus, and the contingent nature of that compensation, induces an executive officer to execute on both the short and long-term goals of the Company. It has structured the executive compensation program to reflect this philosophy by creating an incentive bonus framework that translates Company financial and operational performance into incentive bonuses.

Each of the named executive officers is eligible for an annual incentive bonus. The amount of the bonus depends generally on the level of Company performance, with a target set as a percentage of base salary. The Compensation Committee approves the target bonus percentages and the actual bonus awards for all executive officers. Target bonus percentages are set to be approximately at the median of the Company's peer group.

In 2016, the Compensation Committee approved 65% as a target bonus award (as a percentage of base salary) for the Chief Executive Officer, and 40% as a target bonus for each of the other named executive officers.

The amount of the bonus actually awarded to executives is determined solely in the discretion of the Compensation Committee for all executive officers. Based on its review of management's evaluation of the Company's performance in 2015, the Compensation Committee, using its discretionary authority, determined that each named executive officer should receive 65% of his target incentive bonus. Bonuses awarded in 2016 to Messrs. Tokman, Holt, Zimmerman and Westgor were \$177,666, \$65,295, \$65,700 and \$64,200, respectively.

Equity Awards. The Compensation Committee believes that equity participation is a key component of the Company's executive compensation program. Equity awards are designed to attract and retain executive officers and to motivate them to enhance shareholder value by aligning the financial interests of executive officers with those of shareholders. Each year the Compensation Committee reviews the size and composition of the equity grants to ensure that they are aligned with the Company's compensation philosophy of compensating executives at the median of the Company's peer group. Similar to base salary, a review of equity award levels is conducted to ensure that a named executive officer's equity compensation comports with the Compensation Committee's overall philosophy and objectives and is competitive with the Company's peer group.

The Compensation Committee's practice is to make annual equity awards as part of its overall philosophy of performance-based compensation. Restricted stock units and stock options are awarded by the Compensation Committee to executive officers based on a philosophy of providing equity incentives at the median of the Company's peer group.

In 2016, Messrs. Tokman, Holt, Zimmerman and Westgor were awarded 200,000, 50,000, 50,000 and 50,000 stock options, respectively.

Tax Deductibility of Compensation

Limitations on the deductibility of compensation may occur under Section 162(m) of the Internal Revenue Code of 1986, which generally limits a public company's tax deduction for compensation paid to its named executive officers to \$1 million in any year. In addition, Section 162(m) specifically exempts certain performance-based compensation from the deduction limit. It is the intent of the Compensation Committee to have the Company's compensation program be deductible without limitation. However, the Compensation Committee will take into consideration various other factors, together with Section 162(m) considerations, in making executive compensation decisions and could, in certain circumstances, approve and authorize compensation that is not fully tax deductible.

Processes and Procedures

Role of the Compensation Committee and the Chief Executive Officer in the Compensation Process. The Chief Executive Officer, with the assistance and support of the human resources department and other members of management, provides recommendations regarding the compensation of the executive officers, including himself. The Compensation Committee considers these recommendations and consults with the Chief Executive Officer and other members of management as to his recommendations for the executive officers. The Compensation Committee considers the Chief Executive Officer's recommendations, together with the Compensation Committee's philosophy, objectives and market data in approving these recommendations.

Role of Compensation Consultants in the Compensation Process. The Compensation Committee's charter provides the Compensation Committee with the authority to retain a compensation consulting firm in its discretion.

Compensation Committee Report

The Compensation Committee has reviewed and discussed this Compensation Discussion and Analysis with management. Based on the review and discussions, the Compensation Committee recommended to the Board that the Compensation Discussion and Analysis be included in this Proxy Statement for filing with the Securities and Exchange Commission.

Compensation Committee

Slade Gorton
Perry Mulligan (Chairperson)
Brian Turner

Summary Compensation Table for 2016

This table shows certain information about the compensation we paid our Chief Executive Officer, our Chief Financial Officer, and our two other executive officers as of December 31, 2016. These officers are referred to as named executive officers.

<u>Name and Principal Position</u>	<u>Fiscal Year</u>	<u>Salary (\$)</u>	<u>Bonus (\$)</u>	<u>Stock Awards (\$)(2)</u>	<u>Option Awards (\$)(2)</u>	<u>All Other Compensation (\$)(3)(4)</u>	<u>Total (\$)</u>
Alexander Y. Tokman(1) President and Chief Executive Officer and Director	2016	364,443	177,666	10,934	232,227	7,622	792,892
	2015	362,360	140,528	—	444,209	3,464	950,561
	2014	359,443	85,000	10,787	243,120	—	698,350
Stephen P. Holt Chief Financial Officer	2016	221,459	65,295	—	58,057	7,399	352,210
	2015	214,942	50,676	—	111,052	2,336	379,006
	2014	208,588	31,000	—	60,780	—	300,368
Dale E. Zimmerman Vice President, Research and Development	2016	220,798	65,700	—	58,057	—	344,555
	2015	216,583	41,840	—	111,052	—	369,475
	2014	211,833	31,000	—	60,780	—	303,613
David J. Westgor Vice President, General Counsel and Secretary	2016	217,745	64,200	—	58,057	5,549	345,551
	2015	210,250	49,200	—	111,052	2,026	372,528
	2014	200,833	31,000	—	60,780	—	292,613

- (1) In 2016 and 2014 Mr. Tokman elected to receive restricted stock awards in lieu of an increase in base salary.
- (2) Reflects the fair value of stock and option awards on the grant date in accordance with FASB ASC Topic 718.
- (3) Perquisites and other personal benefits are valued on an aggregate incremental cost basis. All figures shown below in footnote 5 represent the direct dollar cost incurred in providing these perquisites and other personal benefits to the named executive officers.
- (4) The table below shows all other amounts under All Other Compensation for fiscal 2014, 2015 and 2016:

<u>Name and Principal Position</u>	<u>Fiscal Year</u>	<u>Perquisites and Personal Benefits</u>	<u>Employer contribution to 401(k) account (5)</u>
Alexander Y. Tokman	2016	—	7,622
	2015	—	3,464
	2014	—	—
Stephen P. Holt	2016	—	7,399
	2015	—	2,336
	2014	—	—
Dale E. Zimmerman	2016	—	—
	2015	—	—
	2014	—	—
David J. Westgor	2016	—	5,549
	2015	—	2,026
	2014	—	—

- (5) This column represents the amount of matching contributions made to our qualified 401(k) retirement plan for each of our named executive officers. In June 2015 the Company began making contributions to our qualified 401(k) retirement plan for all employees.

Grants of Plan-Based Awards During 2016

The following table shows grants of plan based awards to our named executive officers in 2016:

Name	Grant Date	Estimated Possible Payments Under Non-Equity Incentive Plan Awards Target (\$)	All Other Stock Awards: Number of Shares of Stock or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards (\$/Sh)(1)	Grant Date Fair Value of Stock and Option Awards (\$)(2)
Alexander Y. Tokman . . .	6/1/2016	243,995	5,785	200,000	1.89	243,161
Stephen P. Holt	6/1/2016	88,584	—	50,000	1.89	58,057
Dale E. Zimmerman	6/1/2016	88,319	—	50,000	1.89	58,057
David J. Westgor	6/1/2016	87,098	—	50,000	1.89	58,057

(1) All option awards were granted with an exercise price equal to the closing price of our common stock on the NASDAQ Global Market on the date of grant.

(2) Reflects the fair value of option and stock awards on the date of grant in accordance with FASB ASC Topic 718.

Outstanding Equity Awards at Year-End 2016

The following table shows outstanding equity awards for our named executive officers as of December 31, 2016:

Name		Option Awards				Stock Awards	
		Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date	Number of Shares of Stock That Have Not Vested (#)	Market Value of Shares of Stock That Have Not Vested (\$)
Alexander Y. Tokman	1	26,969	—	35.12	4/19/2017		
	1	18,509	—	17.84	3/25/2018		
	3	8,594	—	17.84	3/25/2018		
	1	16,714	—	14.88	4/23/2019		
	3	8,750	—	14.88	4/23/2019		
	1	13,928	—	27.28	4/26/2020		
	3	5,878	—	27.28	4/26/2020		
	4	80,000	—	1.80	8/3/2022		
	2	2,807	—	2.28	8/8/2023		
	2	225,000	—	2.28	8/8/2023		
	1	100,000	100,000	1.76	6/3/2024		
	1	50,000	150,000	3.26	6/2/2025		
	1	—	200,000	1.89	6/1/2026		
Stephen P. Holt	1	30,000	10,000	2.20	5/7/2023		
	2	40,000	—	2.28	8/8/2023		
	1	25,000	25,000	1.76	6/3/2024		
	1	12,500	37,500	3.26	6/2/2025		
	1	—	50,000	1.89	6/1/2026		
Dale E. Zimmerman	1	3,750	—	7.62	8/04/2021		
	4	40,000	—	1.80	8/03/2022		
	2	65,000	—	2.28	8/08/2023		
	1	25,000	25,000	1.76	6/3/2024		
	1	12,500	37,500	3.26	6/2/2025		
	1	—	50,000	1.89	6/1/2026		

Name	Option Awards				Stock Awards	
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date	Number of Shares of Stock That Have Not Vested (#)	Market Value of Shares of Stock That Have Not Vested (\$)
David J. Westgor	1	3,125	—	45.44	6/7/2017	
	1	1,888	—	17.84	3/25/2018	
	3	625	—	17.84	3/25/2018	
	3	1,750	—	14.88	4/23/2019	
	1	2,805	—	14.88	4/23/2019	
	1	1,876	—	27.28	4/26/2020	
	3	1,032	—	27.28	4/26/2020	
	1	1,467	—	10.40	4/6/2021	
	4	15,000	—	1.80	8/3/2022	
	2	15,000	—	2.28	8/8/2023	
	1	25,000	25,000	1.76	6/3/2024	
	1	12,500	37,500	3.26	6/2/2025	
	1	—	50,000	1.89	6/1/2026	

- (1) The indicated option vests 25% on each anniversary of the grant date.
- (2) The indicated option vests 33% on each anniversary of the grant date.
- (3) The indicated options vested 100% on the date of grant.
- (4) The indicated options vested 34% on 8/15/2012, 33% on 8/15/2013 and 33% on 8/15/2014.

Option Exercises and Stock Vested During 2016

None of our named executive officers exercised stock options, and no shares were acquired upon vesting of stock awards held by our named executive officers, during 2016.

Potential Payments upon Termination or Change in Control

All of our named executive officers, except for Mr. Tokman, are employed at will and do not have employment agreements. Mr. Tokman's employment agreement is summarized below. Under the 2013 Incentive Plan, 100% of each of the named executive officers' options which have not been exercised will become fully vested and immediately exercisable upon a change of control of the Company that does not result in an assumption, substitution or pay off of such award by the acquiring company. In addition, 100% of each named executive officers restricted stock units will become fully vested upon a change of control at the Company.

The following table sets forth aggregate estimated payment obligations to each of our named executive officers assuming a termination without cause, or a change in control, occurred on December 31, 2016:

	Payments Due in Connection with a Termination of Employment without Cause or for Good Reason	Payments Due in Connection with a Change of Control and Termination of Employment without Cause or for Good Reason (1)	Payments Due in Connection with Change in Control (2)
Alexander Y. Tokman	759,210	1,430,687	—
Stephen P. Holt	9,341	393,701	—
Dale E. Zimmerman	15,268	398,505	—
David J. Westgor	28,259	406,305	—

- (1) We included the estimated intrinsic value of accelerating any award of stock options or awards that are accelerated upon a change in control. In the case of a change in control, we assumed that all such awards

would be cashed out at closing using the closing price of our common stock on the NASDAQ Global Market on December 30, 2016, which was \$1.26 per share on an as-adjusted basis. See the section titled ‘Outstanding Equity Awards at Fiscal Year-End 2016’ for information regarding unvested equity awards.

(2) See “Severance and Employment Agreements—Change of Control Severance Plan.”

Severance and Employment Agreements

Mr. Tokman’s Employment Agreement

Payment upon Termination. Under Mr. Tokman’s employment agreement with the Company dated April 7, 2009, as amended, if he dies, becomes disabled, retires, terminates his employment other than for “good reason” or is terminated by us for “cause,” he will be provided his earned but unpaid base salary, earned but unused vacation time, any bonus compensation for the prior year which is unpaid on the date of termination to the extent bonuses are paid to other officers, 18 months of certain group and medical benefits for Mr. Tokman’s family and any business expenses which have not yet been reimbursed by us. If we terminate him “other than for cause,” or if he terminates his employment for “good reason,” he will receive, in addition to the amounts listed in the foregoing sentence, his base salary for 18 months following the date of his termination, plus an amount equal to his target bonus for the year prior to the termination, and we will continue to pay certain group medical and dental expenses in that 18-month period. We do not accelerate the vesting of equity incentives for our executive officers in the event of a termination of employment. In the event of a change in control of the Company, all unvested stock options vest upon the change in control if the change in control does not result in an assumption, substitution or pay off of such award by the acquiring company, and the Compensation Committee has the discretion to remove the vesting restrictions on all unvested restricted shares.

In determining whether a termination occurred with or without “cause,” “cause” is deemed to exist under Mr. Tokman’s employment agreement when there is a repeated willful failure to perform or gross negligence in the performance of his duties; fraud, embezzlement or other dishonesty with respect to us; a material breach of his obligations of confidentiality, non-competition, or non-solicitation against us; or commission of a felony or other crime involving moral turpitude.

In determining whether Mr. Tokman has “good reason” to terminate his employment, “good reason” is deemed to exist when: we have failed to continue him in a certain position; there is a substantial diminution in the nature and scope of his responsibilities; there is a material failure of us to provide him with base salary and benefits, excluding an inadvertent failure which is cured within a certain time period; or his office is relocated more than thirty-five miles from the then-current location of our principal offices without his consent. Mr. Tokman may only terminate his employment for good reason if he (a) gives notice to us within ninety (90) days of the initial occurrence of the event or condition constituting good reason, setting forth in reasonable detail the nature of such good reason; (b) we fail to cure within thirty (30) days following such notice; and (c) Mr. Tokman terminates his employment within thirty (30) days following the end of the thirty (30)-day cure period (if we fail to cure).

Payment upon a Change in Control. In the event of a change of control and the termination of Mr. Tokman’s employment “other than for cause” by us within two years following a change of control or if Mr. Tokman terminates his employment for “good reason” within six months following a change of control, we must pay Mr. Tokman an amount equal to two times the sum of one year of base salary plus a payment equal to his target bonus. The foregoing amount will be paid in a single lump sum. We must also pay the full cost of Mr. Tokman’s continued participation in our group health and dental plans for two years or, if less, for so long as he remains entitled to continue such participation under applicable law. In addition, 100% of his options, restricted stock or other equity awards which have not been exercised and have not expired or been surrendered or cancelled, will become exercisable in accordance with the applicable award agreement.

Our obligation to pay the severance amounts mentioned in this “Payments upon a Termination or Change in Control” section is subject to Mr. Tokman signing an employee release. Also, Mr. Tokman must comply with

certain confidential information and assignment of intellectual property obligations. Further, Mr. Tokman is subject to a non-compete and non-solicit obligation for 12 months following his termination.

Change of Control Severance Plan

In November 2011, the Company adopted a Change of Control Severance Plan (the “Severance Plan”). Under the Severance Plan, a “change of control” is defined as the occurrence of any of the following events: (i) the acquisition by any person or group of more than 50% of the then outstanding securities of the Company entitled to vote generally in the election of directors; (ii) individuals who constitute the board of directors cease for any reason to constitute at least a majority of the board, provided, however, that any individual becoming a director whose election, or nomination for election, by the Company’s shareholders, was approved by a vote of at least a majority of the incumbent directors are considered as though such individual were a member of the incumbent board; (iii) certain reorganizations, recapitalizations, mergers or consolidations; (iv) the sale, transfer or other disposition of all or substantially all of the assets of the Company; or (v) approval by the shareholders of the Company of a complete liquidation or dissolution of the Company.

In the event that a “designated participant,” including Stephen Holt, David J. Westgor and Dale Zimmerman is terminated on, or during the two-year period following, a change of control, for any reason other than by the Company for cause (or, in the case of a participant other than a designated participant, any termination of the participant’s employment, on or during the eighteen-month period following a change of control, by the Company other than for cause or by the participant for good reason), the Company will pay the participant an amount equal to one year of base salary at the rate in effect at the date of termination or, if higher, on the date of the change of control, plus a payment equal to the target bonus for which the participant is eligible, which amount shall be payable within ten business days following the later of the effective date of the release of claims described below or the date it is received by the Company. If, however, the timing associated with the execution, revocation and effectiveness of the release of claims would otherwise allow the payment described above to be made in either of two taxable years, such payment will not be made prior to the first day of the second taxable year. The Company will also pay the full cost of the participant’s continued participation in the Company’s group health and dental plans for one year or, if less, for so long as the participant remains entitled to continue such participation under applicable law. In addition, all options held by the participant which are not exercisable, and which have not been exercised and have not expired or been surrendered or cancelled, will become initially exercisable upon termination and will otherwise be and remain exercisable in accordance with their terms, and all other equity-based compensation awards granted to the participant, including, restricted stock and restricted stock units, will become vested and become free of restrictions.

Payment under the Plan is contingent upon the participant executing and delivering to the Company a release from all claims in any way resulting from, arising out of or connected with such participant’s employment with the Company.

Director Compensation for 2016

The following table provides information concerning our non-employee directors during the year ended December 31, 2016. Mr. Tokman was not paid additional compensation for his service as director and his compensation is fully reflected in the other tables contained in this Proxy Statement. Ms. Horan resigned from the Board in February 2017. Because Mr. Carlile did not join the Board until February 2017, he did not receive any compensation for service as a director in 2016.

<u>Name</u>	<u>Fees Earned or Paid in Cash (\$)</u>	<u>Stock Awards (\$)(1)(3)</u>	<u>Option Awards (\$)(2)(3)</u>	<u>Total (\$)</u>
Richard A. Cowell	52,000	18,900	—	70,900
Yalon Farhi	22,000	—	23,152	45,152
Slade Gorton	42,000	18,900	—	60,900
Jeanette Horan	41,000	18,900	—	59,900
Perry Mulligan	49,000	18,900	—	67,900
Brian Turner	53,000	18,900	—	71,900
Thomas M. Walker	40,000	18,900	—	58,900

- (1) Reflects the fair value of stock awards granted in 2016 in accordance with FASB ASC Topic 718.
- (2) Reflects the fair value of option awards on the grant date in accordance with FASB ASC Topic 718.
- (3) The following table shows the number of outstanding shares underlying option and stock awards for each of our non-employee directors as of December 31, 2016:

<u>Name</u>	<u>Option Awards (#)</u>	<u>Stock Awards (#)(4)</u>
Richard A. Cowell	24,375	41,974
Yalon Farhi	30,000	—
Slade Gorton	24,375	41,974
Jeanette Horan	24,375	41,974
Perry Mulligan	20,625	41,087
Brian Turner	24,375	41,974
Thomas M. Walker	191,312	51,839

- (4) 10,000 shares vest the earlier of one year from the June 1, 2016 grant date, or the day before the next scheduled annual meeting of shareholders.

Each non-employee director is granted a non-statutory option to purchase 15,000 shares of common stock on the date on which he or she is first elected or appointed to the Board of Directors. These options are fully vested and immediately exercisable upon the date of grant. Under the terms of a director compensation plan approved by the Board of Directors, each of our non-employee directors also receives, upon his or her initial appointment or election and upon each subsequent reelection to the Board of Directors, an option to purchase 15,000 shares that vests in full on the earlier of (i) the day prior to the date of our annual meeting of shareholders next following the date of grant, or (ii) one year from the date of grant, provided the non-employee director continues to serve as a director on the vesting date. If a non-employee director ceases to be a director for any reason other than death or disability before his or her term expires, then any outstanding unvested options issued to such Independent Director will be forfeited. Options vested as of the date of termination for any reason other than death or disability are exercisable through the date of expiration. The exercise price for each option is equal to the closing price of our common stock as reported on the NASDAQ Global Market on the date of grant. The options generally expire on the tenth anniversary of the date of grant.

Notwithstanding the terms of the aforementioned director compensation plan, in each of our last four fiscal years, the Board of Directors has approved the issuance of 10,000 shares of the Company's restricted stock to each of our non-employee directors upon his or her reelection to the Board of Directors, in lieu of the option award described in the foregoing paragraph.

In addition, each non-employee director generally receives the following cash compensation for his or her service as a director:

- A fee of \$20,000 that accrues as of the date of appointment or election to the Board of Directors, and as of the date of each subsequent reelection;
- A fee of \$3,000 for the Board chair or \$2,000 per director for each Board meeting attended by the director; and
- A fee of \$3,000 for the committee chair or \$2,000 per committee member for each committee meeting attended by the director that is held on a day other than a day on which a Board meeting is held.

All directors are reimbursed for reasonable travel and other out-of-pocket expenses incurred in attending meetings of the Board of Directors.

INFORMATION ABOUT MICROVISION COMMON STOCK OWNERSHIP

Security Ownership of Certain Beneficial Owners and Management

The following table shows as of April 13, 2017, the number of shares of our common stock beneficially owned by our directors and nominees, the named executive officers, and all directors and executive officers as a group and each person known by us to own beneficially more than 5% of our outstanding common stock.

<u>Name of Beneficial Owner</u>	<u>Number of Shares (1)</u>	<u>Percent of Common Stock (2)</u>
Alexander Y. Tokman(3)	887,870	1.3%
Stephen P. Holt(4)	164,346	*
David J. Westgor(5)	136,555	*
Dale E. Zimmerman(6)	199,048	*
Robert Carlile(7)	30,000	*
Richard A. Cowell(8)	68,811	*
Yalon Farhi(7)	30,000	*
Slade Gorton(8)	163,182	*
Perry Mulligan(9)	102,307	*
Brian Turner(8)	90,963	*
Thomas M. Walker(10)	244,151	*
AWM Investment Company, Inc.(11)	6,124,766	9.0%
All executive officers and directors as a group (11 persons)(12)	2,117,233	3.0%

* Less than 1% of the outstanding shares of common stock.

- (1) Beneficial ownership is determined in accordance with the rules of the SEC and generally includes voting or investment power with respect to securities. Shares of common stock subject to options or warrants that are currently exercisable or convertible or may be exercised or converted within sixty days are deemed to be outstanding and to be beneficially owned by the person holding these options or warrants for the purpose of computing the number of shares beneficially owned and the percentage of ownership of the person holding these securities, but are not outstanding for the purpose of computing the percentage ownership of any other person or entity. Subject to community property laws where applicable, and except as otherwise noted, we believe that each shareholder named in this table has sole voting and investment power with respect to the shares indicated as beneficially owned thereby.
- (2) Percentage of common stock is based on 68,122,274 shares of common stock outstanding as of April 13, 2017.
- (3) Includes 707,149 shares issuable upon exercise of options.
- (4) Includes 155,000 shares issuable upon exercise of options.
- (5) Includes 119,568 shares issuable upon exercise of options.
- (6) Includes 183,750 shares issuable upon exercise of options.
- (7) Includes 30,000 shares issuable upon exercise of options.
- (8) Includes 24,375 shares issuable upon exercise of options.
- (9) Includes 20,625 shares issuable upon exercise of options.
- (10) Includes 191,312 shares issuable upon exercise of options.
- (11) Based solely on information set forth in a Schedule 13G filed with the SEC on February 10, 2017.
- (12) Includes 1,510,529 shares issuable upon exercise of options.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Under the Code of Conduct adopted by us, officers, directors and employees must avoid even the appearance of a conflict of interest. Under the Code of Ethics for MicroVision Executives we have adopted, all of our executive officers must report any material transaction or relationship that reasonably could be expected to give rise to a conflict of interest. We also review questionnaires completed by all directors and executive officers for potential “related-person transactions” between us and related persons. The Board’s Audit Committee is responsible for review, approval, or ratification of related-person transactions. The Audit Committee determines whether the related person has a material interest in a transaction and may approve, ratify, rescind, or take other action with respect to the transaction in its discretion.

AUDIT COMMITTEE REPORT

Review of the Company’s Audited Financial Statements

The Audit Committee serves as the representative of the Board for general oversight of Company’s financial accounting and reporting, systems of internal control, audit process, and monitoring compliance with laws and regulations and standards of business conduct. Management has responsibility for preparing Company’s financial statements, as well as for Company’s financial reporting process. Moss Adams LLP, acting as an independent registered public accounting firm, is responsible for expressing an opinion on the conformity of Company’s audited financial statements with generally accepted accounting principles.

The Audit Committee has reviewed and discussed the audited consolidated financial statements of the Company for the fiscal year ended December 31, 2016 with the Company’s management, and management represented to the Audit Committee that the Company’s consolidated financial statements were prepared in conformity with generally accepted accounting principles. The Audit Committee has discussed with Moss Adams LLP, the Company’s independent auditors for the fiscal year ended December 31, 2016, the matters required to be discussed by the Public Company Accounting Oversight Board (PCAOB) AS 1301, Communications with Audit Committees.

The Audit Committee received from Moss Adams LLP the written disclosures required by Rule 3526 of the PCAOB (Communication with Audit Committee Concerning Independence) and discussed with the firm its independence. Based on the review and discussions noted above, and subject to the limitations on the role and responsibilities of the Audit Committee referred to in the Charter of the Audit Committee, the Audit Committee recommended to the Board that the Company’s audited consolidated financial statements be included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2016 for filing with the SEC.

This report of the Audit Committee shall not be deemed to be incorporated by reference by any general statement incorporating by reference this Proxy Statement into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that the Company specifically incorporates this information by reference.

Audit Committee

Richard A. Cowell, Chairman
Robert P. Carlile
Perry Mulligan
Brian Turner

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Accountant Fees and Services

Our independent auditors, Moss Adams LLP, billed the following fees to us for audit and other services for fiscal year 2016 and fiscal year 2015, respectively:

Audit Fees

The aggregate fees billed for professional services rendered by Moss Adams LLP for the audit of our annual financial statements and the review of the financial statements included in our Quarterly Reports on Form 10-Q were \$352,450 for 2016 and \$275,718 for 2015.

Audit Related Fees

Audit related fees include the aggregate fees billed for professional services rendered by Moss Adams LLP in connection with the audit of the Company's 401(k) plan. Fees for audit related services totaled \$14,572 in 2016 and \$13,500 in 2015.

Tax Fees

Tax fees include the aggregate fees billed for professional services rendered by Moss Adams LLP in connection with federal, state and foreign tax compliance and tax advice. Fees for tax services totaled \$23,061 in 2016 and \$30,778 in 2015.

All Other Fees

Fees for all other services not described above include fees for subscriptions to online accounting research tools. Fees for these services totaled \$2,728 and \$2,598 billed by Moss Adams LLP for 2016 and 2015, respectively.

The Audit Committee has considered whether the provision of services under the heading "All Other Fees" is compatible with maintaining the accountants' independence and has determined that it is consistent with such independence.

Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Auditor

The Audit Committee pre-approves all audit services and all permitted non-audit services by the independent auditors. The Audit Committee has delegated the authority to take such action between meetings to the Audit Committee chairman, who reports the decisions made to the full Audit Committee at its next scheduled meeting.

The Audit Committee evaluates whether our use of the independent auditors for permitted non-audit services is compatible with maintaining the independence of the independent auditors. The Audit Committee's policies prohibit us from engaging the independent auditors to provide any services relating to bookkeeping or other services related to accounting records or financial statements, financial information systems design and implementation, appraisal or valuation services, fairness opinions or contribution-in-kind reports, actuarial services, or internal audit outsourcing services unless it is reasonable to conclude that the results of these services will not be subject to audit procedures. The Audit Committee's policies completely prohibit us from engaging the independent auditors to provide any services relating to any management function, expert services not related to the audit, legal services, broker-dealer, investment adviser, or investment banking services or human resource consulting.

INFORMATION ABOUT SHAREHOLDER PROPOSALS

In order for a shareholder proposal to be considered for inclusion in the Company's Proxy Statement for the 2017 Annual Meeting, the written proposal must be received by the Company no later than the 120th calendar day before the anniversary of the date of the prior year's annual meeting proxy statement was released to shareholders. Shareholder proposals must comply with SEC regulations regarding the inclusion of shareholder proposals in company sponsored proxy materials and must contain the information required in the Company's bylaws for shareholder proposals. If you wish to obtain a free copy of the Company's bylaws, please contact Investor Relations, MicroVision, Inc., 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052.

If a shareholder proposal is not included in the Company's Proxy Statement for the 2016 Annual Meeting, it may be raised from the floor during the meeting if written notice of the proposal is received by the Company not less than 60 nor more than 90 days prior to the meeting or, if less than 60 days' notice of the date of the meeting is given, by the close of business on the 10th business day following the first public announcement of the meeting.

You also may propose candidates for consideration by the Nominating Committee for nomination as directors by writing to us. In order to nominate a director for election at next year's annual meeting of shareholders, you must comply with the director recommendation procedures described on pages 9 and 10 of this Proxy Statement.

ADDITIONAL INFORMATION

Annual Report

The Company's Annual Report for the fiscal year ended December 31, 2016 was first made available to the shareholders of the Company with this Proxy Statement on or about April 24, 2017. The Annual Report is not to be treated as part of the proxy solicitation material or as having been incorporated by reference herein.

Incorporation by Reference

To the extent that this Proxy Statement is incorporated by reference into any other filing by the Company under the Securities Act of 1933, as amended or the Securities Exchange Act of 1934, as amended, the sections of this Proxy Statement entitled "Compensation Committee Report" and "Audit Committee Report" will not be deemed incorporated, unless otherwise specifically provided in such filing.

A copy of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016, as filed with the SEC, may be obtained by shareholders without charge by written or oral request to Investor Relations, MicroVision, Inc., 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052, telephone (425) 882-6629, or may be accessed on the Internet at www.sec.gov.

Householding

Only one copy of the Notice of Internet Availability of Proxy Materials is being delivered to shareholders residing at the same address, unless such shareholders have notified the Company of their desire to receive multiple copies. The Company will promptly deliver, upon oral or written request, a separate copy of the Notice of Internet Availability of Proxy Materials to any shareholder residing at an address to which only one copy was mailed. Requests for additional copies should be directed to Investor Relations. Shareholders residing at the same address and currently receiving only one copy of the Notice of Internet Availability of Proxy Materials may contact Investor Relations to request multiple copies of this Proxy Statement in the future. Shareholders residing at the same address and currently receiving multiple copies of the Notice of Internet Availability of Proxy Materials may contact Investor Relations to request that only a single copy of the Notice of Internet Availability of Proxy Materials be mailed in the future. Contact Investor Relations by phone at (425) 882-6629, by fax at (425) 936-4403, by mail to Investor Relations, MicroVision, Inc., 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052, or by e-mail to ir@microvision.com.

Voting by Telephone or the Internet

Provision has been made for you to vote your shares of common stock by telephone or via the Internet. You may also vote your shares by mail. Please see the proxy card or voting instruction form accompanying this Proxy Statement for specific instructions on how to cast your vote by any of these methods.

Votes submitted by telephone or via the Internet must be received by 5:00 p.m., Seattle, Washington time, on June 6, 2017. Submitting your vote by telephone or via the Internet will not affect your right to vote in person should you decide to attend the Annual Meeting.

The telephone and Internet voting procedures are designed to authenticate shareholders' identities, to allow shareholders to give their voting instructions and to confirm that shareholders' instructions have been recorded properly. The Company has been advised that the Internet voting procedures that have been made available to you are consistent with the requirements of applicable law. Shareholders voting via the Internet should understand that there may be costs associated with electronic access, such as usage charges from Internet access providers and telephone companies, which must be borne by the shareholder.

Annual Report

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

FORM 10-K

(Mark one)

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

For the fiscal year ended December 31, 2016

OR

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

For the transition period from _____ to _____

Commission File Number: 001-34170



MicroVision, Inc.

(Exact name of Registrant as specified in its charter)

Delaware

(State or Other Jurisdiction of Incorporation or Organization)

91-1600822

(I.R.S. Employer Identification Number)

6244 185th Avenue NE, Suite 100

Redmond, Washington 98052

(Address of Principal Executive Offices, including Zip Code)

(425) 936-6847

(Registrant's Telephone Number, including Area Code)

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

Title of class

Common Stock, \$0.001 par value per share

Name of exchange on which registered

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input type="checkbox"/>

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 common stock held by non-affiliates of the registrant as of June 30, 2016 was approximately \$87.0 million (based upon the closing price of \$1.68 per share for the registrant's common stock as reported by the NASDAQ Global Market on that date).

The number of shares of the registrant's common stock outstanding as of February 27, 2017 was 68,122,000.

Documents Incorporated by Reference

Portions of the registrant's definitive Proxy Statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the registrant's 2017 Annual Meeting of Shareholders (the "2017 Proxy Statement") are incorporated herein by reference in Part III of this Annual Report on Form 10-K to the extent stated herein.

MICROVISION, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE YEAR ENDED DECEMBER 31, 2016

TABLE OF CONTENTS

	Page
Part I.	
Item 1. Business	4
Item 1A. Risk Factors	10
Item 1B. Unresolved Staff Comments	16
Item 2. Properties	16
Item 3. Legal Proceedings	17
Item 4. Mine Safety Disclosures	17
Item 4A. Executive Officers of the Registrant	17
Part II.	
Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	18
Item 6. Selected Financial Data	18
Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations	19
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	29
Item 8. Financial Statements and Supplementary Data	29
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	49
Item 9A. Controls and Procedures	49
Item 9B. Other Information	51
Part III.	
Item 10. Directors, Executive Officers and Corporate Governance	51
Item 11. Executive Compensation	51
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	51
Item 13. Certain Relationships and Related Transactions and Director Independence	51
Item 14. Principal Accounting Fees and Services	51
Part IV.	
Item 15. Exhibits, Financial Statement Schedules	51
Signatures	54

PART I.

Preliminary Note Regarding Forward-Looking Statements

This Annual Report contains forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and is subject to the safe harbor created by those sections. Such statements may include, but are not limited to, projections of revenues, income or loss, capital expenditures, plans for product development and cooperative arrangements, technology development by third parties, future operations, financing needs or plans of MicroVision, Inc. ("we" or "us"), as well as assumptions relating to the foregoing. The words "anticipate," "could," "would," "believe," "estimate," "expect," "goal," "may," "plan," "project," "will," and similar expressions identify forward-looking statements. Factors that could cause actual results to differ materially from those projected in our forward-looking statements include risk factors identified below in Item 1A.

ITEM 1. BUSINESS

Overview

MicroVision, Inc. is a pioneer in laser beam scanning (LBS) technology that we market under our brand name PicoP®. We have developed our proprietary PicoP® scanning technology that can be adopted by our customers to create high-resolution miniature projection and three-dimensional sensing and image capture solutions. PicoP® scanning technology is based on our patented expertise in micro-electrical mechanical systems (MEMS), laser diodes, opto-mechanics, and electronics and how those elements are packaged into a small form factor, low power scanning engine that can display, interact and sense, depending on the needs of the application. For display, the engine can project a high-quality image on any surface (pico projection), a windshield (head-up display or HUD), or a retina (augmented reality or AR). For sensing, we use infrared (IR) lasers to capture three-dimensional data in the form of a point cloud. Interactivity uses the 3D sensing function and the display function to project an image that the user can then interact with as one would a touch screen.

We have licensed our patented PicoP® scanning technology to other companies for incorporation into their scanning engines for projection. We sell our licensees key components needed to produce their laser scanning engines and/or license our technology in exchange for a royalty fee for each scanning engine they sell. Companies to whom we license our PicoP® scanning technology are typically original design manufacturers (ODMs) or original equipment manufacturers (OEMs) who are in the business of making components or products ready for sale to end users. To date, we have primarily focused on the consumer electronics market, however, we believe that our LBS technology creates a platform that can support multiple applications and markets including enterprise, medical, industrial and automotive.

In November 2016, we announced a growth strategy for 2017 and beyond that includes selling LBS engines to ODMs and OEMs in addition to our strategy of licensing LBS technology to licensees to offer their own solutions. We plan to offer three scanning engines to support a wide array of applications: a small form factor display engine for consumer products, an interactive display engine for smart Internet of Things (IoT) products, and a mid-range light detection and ranging (LiDAR) engine for autonomous vehicles, industrial products and robotics.

While we are optimistic about our technology and the potential for future revenues, we have incurred substantial losses since inception and we expect to incur a significant loss during the fiscal year ending December 31, 2017.

MicroVision, Inc. was founded in 1993 as a Washington corporation and reincorporated in 2003 under the laws of the State of Delaware. Our headquarters is located at 6244 185th Avenue NE, Suite 100, Redmond, Washington 98052, and our telephone number is (425) 936-6847.

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports are available free-of-charge from the investor page of our website, accessible at www.microvision.com, as soon as reasonably practicable after such material is electronically filed with the Securities and Exchange Commission (SEC). Copies of these filings may also be obtained by visiting the Public Reference Room of the SEC at 100 F Street NE, Washington, D.C. 20549, or by calling the SEC directly at 1-800-SEC-0330 (1-800-732-0330). In addition, the SEC maintains a website, www.sec.gov, which contains current, quarterly and annual reports, proxy and information statements and other information regarding issuers that file electronically.

Technology

Our patented PicoP® scanning technology combines a MEMS scanning mirror, laser diode light sources, electronics, and optics that are controlled using our proprietary system control algorithms. The bi-directional MEMS scanning mirror is a key component of our technology platform and is one of our core competencies. We also have patents for two mirror MEMS solutions. Our most recent MEMS design is a silicon device with a one millimeter mirror at the center. This mirror is connected to small flexures that allow it to oscillate vertically and horizontally to capture (sensing) or reproduce (display) an image pixel-by-pixel. Scanning engines with our technology can operate in three modes: display only, display and sensing combined, and sensing only. For applications that include a projected display, our PicoP® scanning technology creates a brilliant, full color, high-contrast, uniform image over the entire field-of-view from a small and thin engine with low power consumption. For 3D scanning applications, our engine is also small, high resolution, and low power with the low lag and low persistence features that are important for such applications. We believe that our proprietary technology offers significant advantages over traditional display and 3D sensing systems. Depending on the specific product application, these advantages may include:

- Ability to perform projection and three-dimensional sensing and image capture from a single device;
- Leveraging our custom MEMS and application-specific integrated circuits (ASICs) components across multiple engine types for economies of scale;
- Focus-free operation;
- HD resolution;
- Low power requirements to enable battery operated devices and applications;
- Large screen size up to 200 inches from short distances;
- Small and thin engine size;
- 80,000:1 contrast ratio with true black;
- High-brightness, high-dynamic range, and brightness uniformity;
- Rich, saturated color reproduction;
- Short throw projection with multi-mode operation for table top and wall mode;
- 3D sensing as a touch interface or point cloud;
- Real-time interactive capture of moving targets;
- Dynamic, programmable resolution and frame rate 3D scanning; and
- Expandable 90, 180, 270 and 360 degree coverage for LiDAR applications.

In addition to these advantages, an overarching benefit of our PicoP® scanning technology is its ability to offer a key combination of lumens per-watt per-cubic centimeter: in essence, more lumens at lower power in a smaller form factor. Competing technologies may offer more lumens in total but not in as small and power efficient design as our PicoP® scanning technology. This combination is of particular importance for small, portable devices operated by battery. Equally important for consumer ease-of-use and for mobile projection applications is the focus-free attribute of our PicoP® scanning technology.

Business Strategy

Our business strategy is to commercialize our PicoP® scanning technology by enabling ODMs and OEMs to produce end-user products via three go-to-market paths:

- Design and sell LBS engines directly to ODMs and OEMs to incorporate inside their products;
- License our LBS technology and sell key components to ODMs and OEMs to create their own scanning engines; and
- License LBS technology to ODMs and OEMs who developed their own key components.

By providing these options, we permit ODMs and OEMs to integrate and embed our technology across a broad range of display and 3D sensing product applications in the way that best matches their technical capabilities and timelines for bringing their products to market. We create product concept reference designs to enable ODMs and OEMs to develop and rapidly build products that capitalize on the benefits of our PicoP® scanning technology for many of the applications we promote for our technology. We are also developing value-added features intended to help our customers differentiate their potential products. We pursue cooperative marketing and development relationships with suppliers and other companies interested in growing the LBS market to extend the reach of our team and strengthen our

position in the market. In 2016, we announced a co-marketing relationship with ST Microelectronics that includes joint sales and marketing activities for LBS solutions.

The key elements of our business strategy include the following:

- Continue to improve the performance of our PicoP® scanning technology platform by advancing the key application attributes such as higher brightness for displays, lower power, smaller size, and greater accuracy and longer distances for 3D sensing;
- Develop value-added features and applications that complement our core technology;
- Partner with ODMs and OEMs to help them develop scanning engines based on our technology or to select an engine to purchase from our offerings, and to help them integrate the engines into their products;
- Support ODMs and supply partners to ensure availability of high quality scanning engines in quantities to support the consumer electronics market;
- Supply scanning engines for ODMs and OEMs who opt to buy rather than build engines as licensees for their products;
- Supply key scanning engine components for products being developed by ODMs and OEMs who license our PicoP® scanning technology and/or license rights to ODMs and OEMs to produce such components;
- Partner with other companies that are interested in growing the LBS market to cooperatively promote our solutions and develop solutions for future products and capabilities where appropriate; and
- Maintain a position of LBS leadership with our intellectual property around our PicoP® scanning technology.

Markets for Our Technology

Our PicoP® scanning technology platform strategy is focused on addressing four primary market segments:

- Pico projection/interactive pico projection;
- 3D sensing for automotive and industrial applications;
- Augmented/Virtual Reality (AR/VR); and
- Head up displays (HUD) for automobiles.

We see pico projection, interactive pico projection and short range 3D sensing as the most promising applications for our technology in the near to mid-term. We expect AR/VR and HUD to be mid to long-term opportunities. We have concentrated on pico projection over the past several years and, in 2016, we announced plans for other engine solutions for interactive pico projection and 3D sensing. We also began a development program in late 2016 with a leading technology company for an advanced driver assistance system (ADAS) proof-of-concept demonstrator. We believe AR and VR eyewear displays can also benefit from our technology, and we are actively exploring these opportunities. In 2016, we were engaged by another leading technology company to develop a proof-of-concept demonstrator for an AR application. In the automotive HUD market, we have supported customer evaluations for an LBS HUD.

In pico projection, our goal is to enable a large screen viewing experience produced by a small projector for mobile devices such as smartphones, tablets and other consumer electronics products. The scanning engine can either be embedded in the mobile device directly or in a small standalone companion product that is paired with the mobile device wirelessly or via a protocol such as HDMI. These potential products would allow users to watch digital videos, play games, and display images and other data onto a variety of surfaces, freeing users from the limitations of a small screen. Products that incorporate our PicoP® scanning technology have been announced and brought to market by our licensees and their customers in 2016.

We believe combining interactivity with projection can enable a whole new category of smart IoT products. Our engine, which combines interactivity and projection in a single, integrated module supports time-of-flight (ToF) 3D sensing, can act as a touch interface with the projected image, mimicking the experience users are accustomed to with a smartphone or tablet touchscreen.

For the automotive market, an engine using our PicoP® scanning technology could be combined with other components and systems to form a HUD system to be embedded into a vehicle or integrated into a portable, standalone aftermarket HUD. We have produced prototypes that demonstrate the ability of PicoP® scanning technology to project high-resolution virtual images in the driver's field-of-view, providing the driver with a variety of information related to the vehicle's operation. The small form factor display engine we plan to offer in 2017 is well suited to aftermarket HUD products. We have also begun to investigate opportunities to apply our technology to emerging applications for

in-car connectivity and infotainment systems and our mid-range LiDAR engine can be integrated into autonomous vehicles and vehicle ADAS applications for 3D special measurement and navigation assistance.

Another possible application area for our PicoP® scanning technology that we have refocused on in the past year is eyewear displays, also known as AR and VR. We have a long history with this application, and the eyewear ecosystem has progressed to a point where we see future growth opportunities. We are in the exploratory phases with prospective customers in identifying which AR and VR applications offer the most promise for our technology inside their future products.

In addition to display and projection applications, our PicoP® scanning technology has the ability to capture and sense three-dimensional information. We believe there are market opportunities to use our technology to capture images and sense objects. There are multiple methods of performing 3D image capture and sensing using our LBS technology. The first we plan to commercialize is time of flight (ToF), which we are incorporating into our interactive display engine as well as our mid-range LiDAR engine. In addition to the automotive applications discussed above, the mid-range LiDAR engine could enable machine vision for robots, drones, industrial vehicles, and applications.

Products and Services

In 2015 and 2016, our revenue was primarily derived from the sale of our proprietary components and license and royalty fees for PicoP® scanning technology. The key components we offer for inclusion in an LBS engine are our MEMS and ASICs. Our licensees can purchase none, some, or all of the key components we offer depending on their capability and desire to manufacture them and the terms of the licensing agreement.

Our planned 2017 engine product offerings are targeted to a wide variety of ODMs and OEMs for multiple applications, and they consist of:

- A small form factor, high definition display engine for applications where form factor and flexibility of product design are required;
- An interactive display engine that integrates display and 3D sensing to allow the user to interact with projected images; and
- A mid-range LiDAR engine for autonomous, industrial products and robotics.

We began delivering samples of the display engine to customers in December 2016 and expect to be ready for mass production with that engine in the second quarter of 2017. For the interactive display engine, we expect to begin delivering engine samples in the second quarter of 2017 with mass production readiness in the third quarter. We anticipate having samples of the mid-range LiDAR engine in the second half of 2017 and be mass production ready in the first half of 2018.

In addition to product sales and license and royalty fees, we generate revenue from engineering services for custom development and support services for our customers. Historically, our engineering services from collaborative research and development and contract agreements have been a significant portion of our total revenue. In 2015, we transitioned our business to focus more to product sales and royalty revenue, and engineering services has become a smaller part of our business. We expect product sales and royalty revenue to be a significant portion of our total revenue in the future.

Research and Development

We believe our research and development efforts have earned us a leadership position in the field of LBS technology and applications as applied to consumer electronics, automotive and other markets. Our ability to attract customers and grow revenue will depend on our ability to maintain our LBS technology leadership, to continually improve performance, reduce costs, reduce the size of component parts and scanning engines, and to increase the number of applications and products enabled by our PicoP® scanning technology.

Our research and development team is located in Redmond, Washington and as of December 31, 2016, was comprised of 49 engineering and technical staff in optics, computer vision, software engineering, electrical engineering, and MEMS design.

Sales and Marketing

Our sales and marketing approach is account based, business-to-business targeting of ODMs and OEMs. We license our PicoP® scanning technology and sell components used in the production of scanning engines to our licensees and sell scanning engines to our customers. Our customers are typically companies that want to buy or build LBS engines for incorporation into their products. We also engage end product manufacturers and retailers in our target markets to educate them about product opportunities based on our PicoP® scanning technology.

We currently have sales and business development representatives based in the United States and several parts of Asia, focused on business development in the Americas, Europe and Asia. Our sales and business development representatives are supported by a technical sales engineering team that assists customers during the “design win” and “design in” cycles. The technical sales engineering team operates from Redmond, Washington, Taiwan and Japan. Our marketing team is located in Redmond, Washington. We engage potential customers directly, participate in trade shows, use social media, and maintain a website and cooperate on co-marketing activities with key partners.

Manufacturing

We currently use contract manufacturers to produce the products we sell. Our products include scanning engines as well as components that are integral to a scanning engine incorporating our PicoP® scanning technology and include MEMS and ASICs that incorporate our designs and are produced to order by semiconductor foundries.

In addition to our business of licensing technology and selling components, beginning in 2017, we expect our product offerings to include scanning engine products manufactured by a contract manufacturer based on our proprietary design.

Our manufacturing is not currently subject to seasonal variations as our shipments have been relatively small and are in the early stages of product introduction. In the future, depending on our customers’ product mix, we may be affected by seasonal fluctuations which could affect working capital demands.

We provide forecasts that allow our contract manufacturers to stock component parts and other materials and plan capacity. Our contract manufacturers procure raw materials in volumes consistent with our forecasts, manufacture and/or assemble the products and perform tests according to our specifications. Products are either shipped to our customers or shipped to our Redmond, Washington headquarters to be inventoried as finished goods. We procure some specific components and either sell them or consign them to our contract manufacturers. We hold some inventories of these components. Our contract manufacturers procure additional raw materials we do not own when the finished goods are completed by our contract manufacturer. Title to the products transfers from our contract manufacturers to us and then to our customers upon shipment from the manufacturer. If raw materials are unused, or the products are not sold within specified periods of time, we may incur carrying charges or obsolete material charges for component parts that our contract manufacturers purchased to build products to meet our forecasts or customer orders.

Many of the raw materials used in our components are standard to the consumer electronics industry. Our MEMS, MEMS die, and ASICs are currently manufactured to our specifications by separate single-source suppliers.

Human Factors, Ergonomics and Safety

We work with third party independent experts in the field of laser safety to assist in meeting safety specifications. In addition, we monitor developments in the area of permissible laser exposure limits as established by International Electrotechnical Commission (IEC) and others. Independent experts have concluded that laser exposure to the eye resulting from use of LBS devices under normal operating conditions would be below the calculated maximum permissible exposure level set by the IEC.

Competitive Conditions

The information display and 3D sensing industries are highly competitive. Potential products incorporating our PicoP® scanning technology, including any LBS engines we develop, will compete with manufacturers of established technologies, such as flat panel display devices, as well as companies developing new display and 3D sensing technologies. Our competitors include companies such as Texas Instruments, Intel, Syndiant, Velodyne, Quanergy,

Innoluce, Opus, Mirrorcle, Maradin, Himax, Pioneer, Sony (LCOS) and others, some of which have much greater financial, technical and other resources than us. Many of our competitors are currently developing alternative miniature display and 3D sensing technologies. Our competitors may succeed in developing innovative technologies and products that could render our technology or our proposed products commercially infeasible or technologically obsolete.

Pico projectors are a class of miniaturized projectors that are generally handheld, battery operated, mobile projectors. Most of the competing projectors currently on the market are either liquid crystal on silicon (LCOS) panel solutions or Texas Instruments' DLP™ display technology primarily using light-emitting diode (LED) light sources. Each of these projection solutions can create images of varying resolution, brightness, image quality, battery life, and ease-of-use.

The information display and 3D sensing industries have been characterized by rapid and significant technological advances. Our PicoP® scanning technology platform and potential products may not remain competitive with such advances, and we may not have sufficient funds to invest in new technologies, products or processes. Although we believe our technology platform and proposed products could deliver images of a substantially higher quality and resolution from a smaller form factor device than those of commercially available LCOS and DLP based display products, manufacturers of competing technologies may develop further improvements to screen display technology that could reduce or eliminate the anticipated advantages of our proposed products.

3D sensing is a new market for us and we believe we are developing products that will have cost and performance benefits over what competitors may offer. However, manufacturers of competing technologies may develop further improvements to size of their modules, performance for mid-range LiDAR and lower costs that could reduce or eliminate the anticipated advantages of our proposed products.

Intellectual Property and Proprietary Rights

We create intellectual property from three sources: internal research and development activities, technology acquisitions, and performance on development contracts. The inventions covered by our patent applications generally relate to systems controls in our PicoP® scanning technology, component miniaturization, power reduction, feature enhancements, specific implementation of various system components, and design elements to facilitate mass production. Protecting these key-enabling technologies and components is a fundamental aspect of our strategy to penetrate diverse markets with unique products. As such, we intend to continue to develop our portfolio of proprietary and patented LBS technologies at the system, component, and process levels.

We believe our extensive patent portfolio is the largest, broadest, and earliest filed LBS technology portfolio and includes applications such as automotive HUD, augmented reality, range finding, portable media devices, image capture, and projection applications. We have over 500 issued patents, pending patents and licensed patents worldwide.

Since our inception in 1993, we have acquired under license agreements exclusive rights to various LBS technologies, including, among others, rights related to the ability to superimpose images on the user's field-of-view with a retinal display, and rights related to the design and fabrication of micro-miniature devices using semiconductor fabrication techniques. In some cases, the licensors have retained limited, non-commercial rights with respect to the technology, including the right to use the technology for non-commercial research and for instructional purposes.

Our ability to compete effectively in the information display and 3D sensing markets may depend, in part, on our ability and the ability of our licensors to maintain the proprietary nature of these technologies.

We also rely on unpatented proprietary technology. To protect our rights in these areas, we require all employees, and where appropriate, contractors, consultants, advisors and collaborators, to enter into confidentiality and non-compete agreements. There can be no assurance, however, that these agreements will provide meaningful protection for our trade secrets, know-how or other proprietary information in the event of any unauthorized use, misappropriation or disclosure of such trade secrets, know-how or other proprietary information.

We have registered the name “PicoP®” and “MicroVision®” with the United States Patent and Trademark Office.

Employees

As of February 27, 2017, we had 81 full-time employees. None of our employees are represented by a labor union.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below together with the other information set forth in this report, which could materially affect our business, financial condition and future results. The risks described below are not the only risks facing our company. Risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and operating results.

Risk Factors Related to Our Business and Industry

We have a history of operating losses and expect to incur significant losses in the future.

We have had substantial losses since our inception. We cannot assure you that we will ever become or remain profitable.

- As of December 31, 2016, we had an accumulated deficit of \$499.8 million.
- We incurred consolidated net losses of \$450.7 million from inception through 2013, \$18.1 million in 2014, \$14.5 million in 2015, and \$16.5 million in 2016.

The likelihood of our success must be considered in light of the expenses, difficulties and delays frequently encountered by companies formed to develop and commercialize new technologies. In particular, our operations to date have focused primarily on research and development of our PicoP® scanning technology platform and development of demonstration units. We are unable to accurately estimate future revenues and operating expenses based upon historical performance.

We cannot be certain that we will succeed in obtaining additional development revenue or commercializing our technology or products. In light of these factors, we expect to continue to incur significant losses and negative cash flow at least through 2017 and likely thereafter. We cannot be certain that we will achieve positive cash flow at any time in the future.

We will require additional capital to fund our operations and to implement our business plan. If we do not obtain additional capital, we may be required to curtail our operations substantially. Raising additional capital may dilute the value of current shareholders' shares.

Based on our current operating plan, and without additional proceeds from the sale of shares under our existing Common Stock Purchase Agreement or At-the-Market (ATM) facility discussed in Note 8 to our financial statements, we anticipate that we have sufficient cash and cash equivalents to fund our operations into the third quarter of 2017. We will require additional capital to fund our operating plan past that time. We plan to obtain additional capital through the issuance of equity or debt securities, product sales and/or licensing activities.

Our ability to raise proceeds from the sale of shares under our Common Stock Purchase Agreement is subject to limitations and conditions, including a \$1.00 minimum stock price. In addition, pursuant to the Common Stock Purchase Agreement, we agreed that we will not enter into any "variable rate" transactions with any third party from the date of the Purchase Agreement until the expiration of the twenty-four month period following the date of the Purchase Agreement, subject to certain exceptions, which could limit our ability to raise capital through certain sales of equity. In connection with our December 2016 underwritten public offering, we also agreed in the underwriting agreement not to issue shares pursuant to the Common Stock Purchase Agreement, or any other arrangement with Lincoln Park Capital Fund, LLC (Lincoln Park), for a period of six months from the date thereof without the consent of the underwriter.

We are introducing new technology into an emerging market which creates significant uncertainty about our ability to accurately project revenue, costs and cash flows. Our capital requirements will depend on many factors, including, but not limited to, the rate at which ODMs and OEMs introduce products incorporating our PicoP® scanning technology and the market acceptance and competitive position of such products. If revenues are less than we anticipate, if the mix of revenues and the associated margins varies from anticipated amounts or if expenses exceed the amounts budgeted, we may require additional capital earlier than expected to fund our operations. In addition, our operating plan provides

for the development of strategic relationships with suppliers of components, products and systems, and equipment manufacturers that may require additional investments by us.

Additional capital may not be available to us or, if available, may not be available on terms acceptable to us or on a timely basis. Raising additional capital may involve issuing securities with rights and preferences that are senior to our common stock and may dilute the value of our current shareholders' shares. If adequate capital resources are not available on a timely basis, we may consider limiting our operations substantially. This limitation of operations could include reducing investments in our production capabilities or research and development projects, staff, operating costs, and capital expenditures. Reducing operations may jeopardize our ability to achieve our business goals or satisfy our customer requirements.

Qualifying a new or alternative contract manufacturer or foundry for our products could cause us to experience delays that result in lost revenues and damaged customer relationships.

We rely on single or limited-source suppliers to manufacture our products, including our MEMS die in wafer form. The lead time to establish a relationship with a new or alternative contract manufacturer(s) or foundry is a time-consuming process, as our unique technology may require significant manufacturing process adaptation to achieve full manufacturing capacity. Accordingly, we may be unable to establish a relationship with new or alternative contract manufacturers in the short-term, or at all, at prices or on other terms that are acceptable to us.

Changes in our supply chain may result in increased cost and delay and may subject us to risks and uncertainties regarding, but not limited to, product warranty, product liability and quality control standards. The loss of any single or limited-source supplier, the failure of any of these suppliers to perform as expected or the disruption in the supply chain of components from these suppliers could cause significant delays in product deliveries, which may result in lost revenues and damaged customer relationships. To the extent that we are not able to establish a relationship with a new or alternative contract manufacturer(s) or foundry in a timely manner, we may be unable to meet contract or production milestones, which could have a material adverse effect on our financial condition, results of operations and cash flows.

Our success will depend, in part, on our ability to secure significant third party manufacturing resources.

Our success will depend, in part, on our ability to provide our components and future products in commercial quantities at competitive prices and on schedule. Accordingly, we will be required to obtain access, through business partners or contract manufacturers, to manufacturing capacity and processes for the commercial production of our expected future products.

Our foreign contract manufacturers could experience severe financial difficulties or other disruptions in their business, and such continued supply could be significantly reduced or terminated. In addition, we cannot be certain that we will successfully obtain access to needed manufacturing resources concurrent with a significant increase in our planned production levels. Future manufacturing limitations of our suppliers could constrain the number of products that we are able to develop and produce.

We are dependent on third parties in order to develop, manufacture, sell and market products incorporating our PicoP® scanning technology, scanning engines, and the scanning engine components.

Our business strategy for commercializing our technology in products incorporating PicoP® scanning technology includes entering into development, manufacturing, sales and marketing arrangements with ODMs, OEMs and other third parties. These arrangements reduce our level of control over production and distribution and may subject us to risks and uncertainties regarding, but not limited to, product warranty, product liability and quality control standards. We cannot be certain that we will be able to negotiate arrangements on acceptable terms, if at all, or that these arrangements will be successful in yielding commercially viable products. If we cannot establish these arrangements, we would require additional capital to undertake such activities on our own and would require extensive manufacturing, sales and marketing expertise that we do not currently possess and that may be difficult to obtain.

In addition, we could encounter significant delays in introducing our PicoP® scanning technology or find that the development, manufacture or sale of products incorporating our technology would not be feasible. To the extent that we enter into development, manufacturing, sales and marketing or other arrangements, our revenues will depend upon the performance of third parties. We cannot be certain that any such arrangements will be successful.

We cannot be certain that our technology platform or products incorporating our PicoP® scanning technology will achieve market acceptance. If our technology platform or products incorporating our technology do not achieve market acceptance, our revenues may not grow.

Our success will depend in part on customer acceptance of our PicoP® scanning technology. Our technology may not be accepted by manufacturers who use display and 3D sensing technologies in their products, by systems integrators, ODMs, and OEMs who incorporate the scanning engine components into their products or by end users of these products. To be accepted, our PicoP® scanning technology must meet the expectations of our current and potential customers in the consumer electronics, automotive, and other markets. If our technology platform or products incorporating our PicoP® scanning technology do not achieve market acceptance, we may not be able to continue to develop our technology.

Future products incorporating our PicoP® scanning technology and scanning engines are dependent on advances in technology by other companies.

Our PicoP® scanning technology will continue to rely on technologies, such as laser diode light sources and other components that are developed and produced by other companies. The commercial success of certain future products incorporating our PicoP® scanning technology will depend, in part, on advances in these and other technologies by other companies. We may, from time to time, contract with and support companies developing key technologies in order to accelerate the development of them for our or our customers' specific uses. There are no guarantees that such activities will result in useful technologies or products that will be profitable.

We are dependent on a small number of customers for our revenue. Our quarterly performance may vary substantially and this variance, as well as general market conditions, may cause our stock price to fluctuate greatly and potentially expose us to litigation.

In 2016, one commercial customer accounted for \$13.5 million in revenue, representing 91% of our total revenue. In 2015, the same commercial customer accounted for \$9.0 million in revenue, representing 98% of our total revenue. In 2014, the same single commercial customer accounted for \$2.0 million in revenue, representing 58% of our total revenue. A second commercial customer in 2014 accounted for \$577,000 in revenue, representing 17% of our total revenue. Our customers take time to obtain, and the loss of a significant customer could negatively affect our revenue. Our quarterly operating results may vary significantly based upon:

- Market acceptance of products incorporating our PicoP® scanning technology;
- Changes in evaluations and recommendations by any securities analysts following our stock or our industry generally;
- Announcements by other companies in our industry;
- Changes in business or regulatory conditions;
- Announcements or implementation by our competitors of technological innovations or new products;
- The status of particular development programs and the timing of performance under specific development agreements;
- Economic and stock market conditions; or
- Other factors unrelated to our company or industry.

In one or more future quarters, our results of operations may fall below the expectations of securities analysts and investors and the trading price of our common stock may decline as a consequence. In addition, following periods of volatility in the market price of a company's securities, shareholders often have instituted securities class action litigation against that company. If we become involved in a class action suit, it could divert the attention of management and, if adversely determined, could require us to pay substantial damages.

We or our customers may fail to perform under open orders or agreements, which could adversely affect our operating results and cash flows.

Our backlog of open orders totaled \$942,000 as of December 31, 2016. We or our customers may be unable to meet the performance requirements and obligations under open orders or agreements, including performance specifications or delivery dates, required by such purchase orders or agreements. Furthermore, our customers may be unable or unwilling to perform their obligations thereunder on a timely basis, or at all if, among other reasons, our products and technologies do not achieve market acceptance, our customers' products and technologies do not achieve market

acceptance or our customers otherwise fail to achieve their operating goals. To the extent we are unable to perform under such purchase orders or agreements or to the extent customers are unable or unwilling to perform, our operating results and cash flows could be adversely affected.

It may become more difficult to sell our stock in the public market or maintain our listing on the NASDAQ Global Market.

Our common stock is listed on The NASDAQ Global Market. To maintain our listing on this market, we must meet NASDAQ's listing maintenance standards. If we are unable to continue to meet NASDAQ's listing maintenance standards for any reason, our common stock could be delisted from The NASDAQ Global Market. If our common stock were delisted, we likely would seek to list our common stock on The NASDAQ Capital Market, the American Stock Exchange or on a regional stock exchange. Listing on such other market or exchange could reduce the liquidity of our common stock. If our common stock were not listed on The NASDAQ Capital Market or an exchange, trading of our common stock would be conducted in the Over-the-Counter (OTC) market on an electronic bulletin board established for unlisted securities or directly through market makers in our common stock. If our common stock were to trade in the OTC market, an investor would find it more difficult to dispose of, or to obtain accurate quotations for the price of, the common stock.

A delisting from The NASDAQ Global Market and failure to obtain listing on another market or exchange would subject our common stock to so-called penny stock rules that impose additional sales practice and market-making requirements on broker-dealers who sell or make a market in such securities. Consequently, removal from The NASDAQ Global Market and failure to obtain listing on another market or exchange could affect the ability or willingness of broker-dealers to sell or make a market in our common stock and the ability of purchasers of our common stock to sell their securities in the secondary market.

On February 27, 2017, the closing price of our common stock was \$1.71 per share.

Our lack of financial and technical resources relative to our competitors may limit our revenues, potential profits, overall market share or value.

Our products and potential products incorporating our PicoP® scanning technology will compete with established manufacturers of existing products and companies developing new technologies. Many of our competitors have substantially greater financial, technical and other resources than we have. Because of their greater resources, our competitors may develop products or technologies that may be superior to our own. The introduction of superior competing products or technologies could result in reduced revenues, lower margins or loss of market share, any of which could reduce the value of our business.

We may not be able to keep up with rapid technological change and our financial results may suffer.

The information display and 3D sensing industries have been characterized by rapidly changing technology, accelerated product obsolescence and continuously evolving industry standards. Our success will depend upon our ability to further develop our PicoP® scanning technology platform and to cost effectively introduce new products and features in a timely manner to meet evolving customer requirements and compete with competitors' product advances. We may not succeed in these efforts due to:

- Delays in product development;
- Lack of market acceptance for our technology or products incorporating our PicoP® scanning technology; or
- Lack of funds to invest in product research, development and marketing.

The occurrence of any of the above factors could result in decreased revenues, market share and value of our business.

We could face lawsuits related to our use of PicoP® scanning technology or other technologies. Defending these suits would be costly and time-consuming. An adverse outcome, in any such matter, could limit our ability to commercialize our technology or products incorporating our PicoP® scanning technology, reduce our revenues and increase our operating expenses.

We are aware of several patents held by third parties that relate to certain aspects of light scanning displays and 3D sensing products. These patents could be used as a basis to challenge the validity, limit the scope or limit our ability to obtain additional or broader patent rights of our patents or patents we have licensed. A successful challenge to the validity of our patents or patents we have licensed could limit our ability to commercialize our technology or products incorporating our PicoP® scanning technology and, consequently, materially reduce our revenues. Moreover, we cannot be certain that patent holders or other third parties will not claim infringement by us with respect to current and future technology. Because U.S. patent applications are held and examined in secrecy, it is also possible that presently pending U.S. applications will eventually be issued with claims that will be infringed by our products or our technology.

The defense and prosecution of a patent suit would be costly and time-consuming, even if the outcome were ultimately favorable to us. An adverse outcome in the defense of a patent suit could subject us to significant costs, require others and us to cease selling products incorporating our technology, require us to cease licensing our technology or require disputed rights to be licensed from third parties. Such licenses, if available, would increase our operating expenses. Moreover, if claims of infringement are asserted against our future co-development partners or customers, those partners or customers may seek indemnification from us for any damages or expenses they incur.

If we fail to manage expansion effectively, our revenue and expenses could be adversely affected.

Our ability to successfully offer products incorporating PicoP® scanning technology and implement our business plan in a rapidly evolving market requires an effective planning and management process. The growth in business and relationships with customers and other third parties has placed, and will continue to place, a significant strain on our management systems and resources. We will need to continue to improve our financial and managerial controls, reporting systems and procedures, and will need to continue to train and manage our work force.

If we fail to adequately reduce and control our manufacturing, supply chain and operating costs, our business, financial condition, and operating results could be adversely affected.

We incur significant costs related to procuring components and increasing our production capabilities to manufacture our products. We may experience delays, cost overruns or other unexpected costs associated with an increase in production. If we are unsuccessful in our efforts to reduce and control our manufacturing, supply chain and operating costs and keep costs aligned with the levels of revenues we generate, our business and financial condition could suffer.

Our technology and products incorporating our PicoP® scanning technology may be subject to future environmental, health and safety regulations that could increase our development and production costs.

Our technology and products incorporating our PicoP® scanning technology could become subject to future environmental, health and safety regulations or amendments that could negatively impact our ability to commercialize our technology and products incorporating our PicoP® scanning technology. Compliance with any such new regulations would likely increase the cost to develop and produce products incorporating our PicoP® scanning technology, and violations may result in fines, penalties or suspension of production. If we become subject to any environmental, health, or safety laws or regulations that require us to cease or significantly change our operations to comply, our business, financial condition and operating results could be adversely affected.

Our operating results may be adversely impacted by worldwide political and economic uncertainties and specific conditions in the markets we address.

In the recent past, general worldwide economic conditions have experienced a downturn due to slower economic activity, concerns about inflation, increased energy costs, decreased consumer confidence, reduced corporate profits and capital spending, and adverse business conditions. Any continuation or worsening of the current global economic and financial conditions could materially adversely affect: (i) our ability to raise, or the cost of, needed capital, (ii) demand for our current and future products, and (iii) our ability to commercialize products. We cannot predict the timing, strength, or duration of any economic slowdown or subsequent economic recovery, worldwide, regionally or in the display industry.

Because we plan to continue using foreign contract manufacturers, our operating results could be harmed by economic, political, regulatory and other factors in foreign countries.

We currently use foreign contract manufacturers and plan to continue to use foreign contract manufacturers to manufacture current and future products, where appropriate. These international operations are subject to inherent risks, which may adversely affect us, including, but not limited to:

- Political and economic instability;
- High levels of inflation, historically the case in a number of countries in Asia;
- Burdens and costs of compliance with a variety of foreign laws, regulations and sanctions;
- Foreign taxes and duties;
- Changes in tariff rates or other trade, tax or monetary policies; and
- Changes or volatility in currency exchange rates and interest rates.

Our contract manufacturers' facilities could be damaged or disrupted by a natural disaster or labor strike, either of which would materially affect our financial position, results of operations and cash flows.

A major catastrophe, such as an earthquake, monsoon, flood or other natural disaster, labor strike, or work stoppage at our contract manufacturers' facilities, our suppliers, or our customers, could result in a prolonged interruption of our business. A disruption resulting from any one of these events could cause significant delays in product shipments and the loss of sales and customers, which could have a material adverse effect on our financial condition, results of operations, and cash flows.

If our licensors and we are unable to obtain effective intellectual property protection for our products, processes and technology, we may be unable to compete with other companies.

Intellectual property protection for our products, processes and technology is important and uncertain. If we do not obtain effective intellectual property protection for our products, processes and technology, we may be subject to increased competition. Our commercial success will depend, in part, on our ability and the ability of our licensors, to maintain the proprietary nature of our PicoP® scanning technology and other key technologies by securing valid and enforceable patents and effectively maintaining unpatented technology as trade secrets.

We protect our proprietary PicoP® scanning technology by seeking to obtain United States and foreign patents in our name, or licenses to third party patents, related to proprietary technology, inventions, and improvements that may be important to the development of our business. However, our patent position and the patent position of our licensors involve complex legal and factual questions. The standards that the United States Patent and Trademark Office and its foreign counterparts use to grant patents are not always applied predictably or uniformly and can change.

Additionally, the scope of patents are subject to interpretation by courts and their validity can be subject to challenges and defenses, including challenges and defenses based on the existence of prior art. Consequently, we cannot be certain as to the extent to which we will be able to obtain patents for our new products and technology or the extent to which the patents that we already own or license from others, protect our products and technology. Reduction in scope of protection or invalidation of our licensed or owned patents, or our inability to obtain new patents, may enable other companies to develop products that compete directly with ours on the basis of the same or similar technology.

We also rely on the law of trade secrets to protect unpatented know-how and technology to maintain our competitive position. We try to protect this know-how and technology by limiting access to the trade secrets to those of our employees, contractors and partners, with a need-to-know such information and by entering into confidentiality agreements with parties that have access to it, such as our employees, consultants and business partners. Any of these parties could breach the agreements and disclose our trade secrets or confidential information, or our competitors might learn of the information in some other way. If any trade secret not protected by a patent were to be disclosed to or independently developed by a competitor, our competitive position could be negatively affected.

We could be subject to significant product liability claims that could be time-consuming and costly, divert management attention and adversely affect our ability to obtain and maintain insurance coverage.

We could be subject to product liability claims if any of the product applications are alleged to be defective or cause harmful effects. For example, because some of the scanning engines incorporating our PicoP® scanning technology could scan a low power beam of colored light into the user's eye, the testing, manufacture, marketing and sale of these products involve an inherent risk that product liability claims will be asserted against us.

Additionally, any misuse of our technology or products incorporating our PicoP® scanning technology by end users or third parties that obtain access to our technology, could result in negative publicity and could harm our brand and reputation. Product liability claims or other claims related to our products or our technology, regardless of their outcome, could require us to spend significant time and money in litigation, divert management time and attention, require us to pay significant damages, harm our reputation or hinder acceptance of our products. Any successful product liability claim may prevent us from obtaining adequate product liability insurance in the future on commercially desirable or reasonable terms. An inability to obtain sufficient insurance coverage at an acceptable cost or otherwise to protect against potential product liability claims could prevent or inhibit the commercialization of our products and our PicoP® scanning technology.

Our contracts and collaborative research and development agreements have long sales cycles, which makes it difficult to plan our expenses and forecast our revenues.

Our contracts and collaborative research and development agreements have long sales cycles that involve numerous steps including determining the product application, exploring the technical feasibility of a proposed product, evaluating the costs of manufacturing a product or qualifying a new or alternative contract manufacturer for production. Our long sales cycle, which can last several years, makes it difficult to predict the quarter in which revenue recognition will occur. Delays in entering into contracts and collaborative research and development agreements could cause significant variability in our revenues and operating results for any particular period.

Our contracts and collaborative research and development agreements may not lead to any product or any products that will be profitable.

Our contracts and collaborative research and development agreements, including without limitation, those discussed in this document, are exploratory in nature and are intended to develop new types of products for new applications. Our efforts may prove unsuccessful and these relationships may not result in the development of any product or any products that will be profitable.

Our operations could be adversely impacted by information technology system failures, network disruptions, or cyber security breaches.

We rely on information technology systems to process, transmit, store, and protect electronic data between our employees, our customers and our suppliers. Our systems are vulnerable to damage or interruptions due to events beyond our control, including, but are not limited to, natural disasters, power loss, telecommunications failures, computer viruses, hacking, or other cyber security issues. Our system redundancy may be inadequate and our disaster recovery planning may be ineffective or insufficient to account for all eventualities. Additionally, we maintain insurance coverage to address certain aspects of cyber risks. Such insurance coverage may be insufficient to cover all losses or all claims that may arise, should such an event occur.

Loss of any of our key personnel could have a negative effect on the operation of our business.

Our success depends on our executive officers and other key personnel and on the ability to attract and retain qualified new personnel. Achievement of our business objectives will require substantial additional expertise in the areas of sales and marketing, research and product development and manufacturing. Competition for qualified personnel in these fields is intense, and the inability to attract and retain additional highly skilled personnel, or the loss of key personnel, could hinder our ability to compete effectively in the information display and 3D sensing markets and adversely affect our business strategy execution and results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We currently lease approximately 23,900 square feet of combined use office, laboratory and manufacturing space at our corporate headquarters in Redmond, Washington. The 65 month lease expires in January 2019.

ITEM 3. LEGAL PROCEEDINGS

On March 31, 2014, Asia Optical Co., Inc., a supplier pursuant to an agreement entered into in 2008, filed a complaint for arbitration with the American Arbitration Association claiming that we ordered products from them and failed to take delivery of and pay for such products. The relief sought in the complaint is \$3.6 million plus attorneys' fees, interest and arbitration costs. We contest the claim and are defending against it. An adverse outcome of these proceedings could materially and adversely affect our financial condition. At this stage, we cannot predict the likelihood of an unfavorable outcome or the range of potential loss.

We are also subject to various claims and pending or threatened lawsuits in the normal course of business. We are not currently party to any other legal proceedings that we believe are reasonably possible to have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 4A. EXECUTIVE OFFICERS OF THE REGISTRANT

Executive officers are appointed by our Board of Directors and hold office until their successors are elected and duly qualified. The following persons serve as executive officers of MicroVision, Inc.:

Alexander Y. Tokman, age 55, has served as President, Chief Executive Officer and Director of MicroVision since January 2006. Mr. Tokman served as MicroVision's President and Chief Operating Officer from July 2005 to January 2006. Mr. Tokman joined MicroVision after a ten-year tenure at GE Healthcare, a subsidiary of General Electric, where he led several global businesses, most recently as General Manager of its Global Molecular Imaging and Radiopharmacy multi-technology business unit from 2003 to 2005. Prior to that, between 1995 and 2003, Mr. Tokman served in various cross-functional and cross-business leadership roles at GE where he led the definition and commercialization of several medical modalities product segments including PET/CT, which added over \$500 million of revenue growth to the company within the first three years of its commercial introduction. Mr. Tokman is a certified Six Sigma and Design for Six Sigma (DFSS) Black Belt and Master Black Belt and as one of GE's Six Sigma pioneers, he drove the quality culture change across GE Healthcare in the late 1990s. From November 1989 to March 1995, Mr. Tokman served as new technologies programs lead and the head of the I&RD office at Tracor Applied Sciences, a subsidiary of then Tracor, Inc. Mr. Tokman holds a B.S. and an M.S. in electrical engineering from the University of Massachusetts, Dartmouth.

Stephen P. Holt, age 54, joined MicroVision in April 2013 as Chief Financial Officer. Prior to MicroVision, from May 2007 to May 2012, he served as Chief Financial Officer of PixelOptics, where he played a lead role in bringing the company's first electronic focusing eyewear product to market. At this venture capital-backed start-up, Mr. Holt raised capital and negotiated strategic partner agreements to license technology in addition to implementing policies and procedures to create an infrastructure capable of supporting rapid growth while maintaining a strong internal control environment. From March 2006 to April 2007, he was the Chief Financial Officer of Interstate Distributors, a trucking and transportation services company. From December 2003 to March 2006, he was the Chief Financial Officer of a group of companies consisting of Activelight, Boxlight, Cinelight and Projector Wholesale Supply. These companies were value-added resellers and distributors of audio-visual and projection equipment. Mr. Holt, a Certified Management Accountant, holds a B.S. from California State University, Chico and an M.B.A. from Santa Clara University.

David J. Westgor, age 63, was appointed Vice President, General Counsel and Secretary in November 2013, after serving as General Counsel since December 2012 and Deputy General Counsel since June 2007. In his current role, Mr. Westgor oversees the legal department, advises the Board of Directors and executive team on corporate governance matters, and provides support for the company's business activities. Before joining MicroVision, Mr. Westgor was Senior Counsel at Medtronic Physio-Control, where he had primary responsibility for the legal affairs of its medical and informatics business units. Mr. Westgor graduated from Loyola Law School and practiced in the Los Angeles office of Pillsbury Winthrop. He moved to the Seattle area to become in-house counsel at Advanced Radio Telecom, a broadband telecommunications company. Mr. Westgor holds a B.A. from St. Olaf College and an M.F.A. degree from the Art Institute of Chicago.

Dale E. Zimmerman, age 57, has served as Vice President of Research and Development since June 2012 and as Director of Systems Engineering from June 2011 to May 2012. Prior to MicroVision, from February 2006 to

December 2008, he served as Vice President of Product Strategy of Silicon Image, a company specializing in high speed serial interface solutions for HDTV, PC and storage products. From 1996 to 2006, he served as General Manager of DLP TV for Texas Instruments, where he played an important role in launching the first conference room projectors, home theater projectors, and HDTVs. His teams have received many awards, including three Emmys and CES Innovation Best of Show. He holds both a B.S. and an M.S. degree in electrical and electronics engineering from Massachusetts Institute of Technology (MIT) and a second M.S. in electrical engineering from Stanford University.

PART II.

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

Our common stock began trading publicly on August 27, 1996. Our common stock trades on The NASDAQ Global Market under the ticker symbol "MVIS." We have never declared or paid cash dividends on our common stock. We currently anticipate that we will retain all future earnings to fund the operations of our business and do not anticipate paying dividends on the common stock in the foreseeable future.

As of February 27, 2017, there were approximately 112 holders of record of 68,122,000 shares of common stock outstanding. As many of our shares of common stock are held by brokerages and institutions on behalf of shareholders, we are unable to estimate the total number of beneficial holders of our common stock represented by these record holders.

Quarter Ended	Common Stock	
	HIGH	LOW
2015		
March 31, 2015	\$ 4.23	\$ 1.72
June 30, 2015	3.88	2.86
September 30, 2015	3.54	2.56
December 31, 2015	3.47	2.20
2016		
March 31, 2016	\$ 3.08	\$ 1.65
June 30, 2016	2.21	1.64
September 30, 2016	2.07	1.30
December 31, 2016	1.85	0.89
January 1, 2017 to February 27, 2017	\$ 1.94	\$ 1.15

ITEM 6. SELECTED FINANCIAL DATA

A summary of selected financial data as of and for the five years ended December 31, 2016 is set forth below. It should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this Annual Report on Form 10-K.

(In thousands, except per share data)

Statement of Operations Data	Year Ended December 31,				
	2016	2015	2014	2013	2012
Revenue	\$ 14,761	\$ 9,188	\$ 3,485	\$ 5,852	\$ 8,365
Net loss available for common shareholders	(16,472)	(14,542)	(18,120)	(13,178)	(22,693)
Basic and diluted net loss per share	(0.32)	(0.31)	(0.44)	(0.47)	(1.05)
Weighted-average shares outstanding basic and diluted	51,958	46,540	41,599	28,025	21,595
Balance Sheet Data					
Cash and cash equivalents	\$ 15,139	\$ 7,888	\$ 8,349	\$ 5,375	\$ 6,850
Working capital (deficit)	10,104	3,371	5,040	(3,878)	1,831
Total assets	20,106	14,042	11,945	8,447	12,938
Long-term liabilities	5,388	6,491	488	481	20
Total shareholders' equity (deficit)	7,474	(153)	6,872	(1,696)	5,054

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

Overview

Our business strategy is to commercialize our PicoP® scanning technology by enabling ODMs and OEMs to produce end-user products via three go-to-market paths:

1. Design and sell LBS engines directly to ODMs and OEMs to incorporate inside their products;
2. License our LBS technology and sell key components to ODMs and OEMs to create their own scanning engines; and
3. License LBS technology to ODMs and OEMs who developed their own key components.

In 2014, our revenue was primarily derived from engineering services from collaborative research and development and contract agreements. In 2015 and 2016, our revenue was primarily generated from product sales and royalty revenue, and engineering services has become a smaller part of our business. We expect product sales to be a significant portion of our total revenue in the future.

In 2016, 87% of our revenue was generated from product sales, less than 1% was generated from performance on contracts for prototype units, 7% was generated from a prorated portion of the \$8.0 million upfront payment, and 5% was generated from ongoing per unit royalties. Sony Corporation (Sony) accounted for 91% of our total revenue in 2016.

In 2015, 70% of our revenue was generated from product sales, 17% was generated from performance on support services contracts, 10% was generated from a prorated portion of the \$8.0 million upfront payment, and 3% was generated from ongoing per unit royalties. Sony accounted for 98% of our total revenue in 2015.

In 2014, 49% of our revenue was generated from performance on collaborative research and development agreements, 40% was generated from performance on contracts to deliver customized prototype units, 10% was generated from product sales, and 1% was generated from ongoing per unit royalties. Sony accounted for 58% of our total revenue and a worldwide logistics company accounted for 17% of our total revenue in 2014.

We have incurred substantial losses since inception and expect to incur a significant loss during the fiscal year ending December 31, 2017. We have funded operations to date primarily through the sale of common stock, convertible preferred stock, warrants, the issuance of convertible debt and, to a lesser extent, from development contract revenues, product sales and licensing activities. There can be no assurance that additional capital will be available or that, if available, it will be available on terms acceptable to us on a timely basis. We cannot be certain that we will succeed in commercializing our technology or products. These factors raise substantial doubt regarding our ability to continue as a going concern. These financial statements were prepared assuming we will continue as a going concern and do not include any adjustments that might be necessary should we be unable to continue as a going concern.

Key accounting policies and estimates

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that materially affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent liabilities. We evaluate our estimates on a continuous basis. We base our estimates on historical data, terms of existing contracts, our evaluation of trends in the information display and 3D sensing industries, information provided by our current and prospective customers and strategic partners, information available from other outside sources and on various other assumptions we believe to be reasonable under the circumstances. The results form the basis for making judgments regarding the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following key accounting policies require significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue recognition

We recognize revenue when: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred and there are no uncertainties regarding customer acceptance, (iii) fees are fixed or determinable, and (iv) collection is reasonably assured.

We generate revenue from many sources and activities. We enter into arrangements that can include various combinations of product sales, services, and licensing activities. For multiple-element arrangements, we use a hierarchy to determine the contract consideration to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third party evidence of selling price (TPE), and (iii) best estimate of selling price. To date, our revenue sources can be classified as: product revenue, royalty revenue, contract revenue, or development revenue.

Product revenue

Our product sales generally include acceptance provisions. We recognize product revenue upon acceptance of the product by the customer or expiration of the contractual acceptance period, after which there are no rights of return. No estimates are made for product returns because revenue is recognized upon expiration of the contractual acceptance period.

Royalty revenue

We recognize revenue on upfront license fees over the expected time frame that we provide services or have ongoing obligations under the agreement. Ongoing per unit royalties are recognized when reported by our customer to us on a quarterly basis. Currently, we recognize revenue for ongoing per unit royalties one quarter in arrears when reported by our customer, representing when such amounts are fixed and determinable, and all other revenue recognition criteria are met.

Contract revenue

Our contract revenue in a particular period is dependent upon when we enter into a contract, the value of the contracts we have entered into, and the availability of technical resources to perform work on the contracts.

We recognize contract revenue related to the sale of prototype units and evaluation kits upon acceptance of the deliverables by the customer or expiration of the contractual acceptance period, after which there are no rights of return.

We recognize contract revenue on long-term, cost plus fixed fee, and fixed price contracts using the percentage-of-completion method. Under the percentage-of-completion method, revenue is recognized as work progresses on the contract. The percentage-of-completion method relies on estimates of total expected contract revenue and costs. At the end of each period, we estimate the labor, material and other costs required to complete the contract using data provided by our technical team, project managers, vendors, outside consultants and others and compare these to costs incurred to date.

Recognized revenues are subject to amendments for actual costs incurred. Amendments to revenue and costs to complete estimates are recognized in the period in which the facts become known. In the future, amendments to estimates could significantly impact recognized revenue in any one reporting period. If we are unable to estimate costs on a contract, revenue is recognized using the completed-contract method. Under the completed-contract method, revenue and contract costs are deferred and both are recognized when all deliverables are completed.

Development revenue

We evaluate the performance criteria and terms of our collaborative research and development agreements to determine whether revenue should be recognized under a performance-based method or milestone method. Significant items covered in our evaluation include the following:

- The nature of our obligation under the agreement;
- Whether provisions leading to variable revenues exist;
- Whether any payments are refundable;

- Whether the deliverables should be treated as a single unit of accounting or separated into multiple units;
- Whether substantive milestones exist;
- Whether milestone payments are commensurate with either our level of effort or the increase in value of the customer's rights; and
- Whether a licensing agreement exists.

At the end of each period, we evaluate total estimated costs for each agreement. Amendments to the estimated costs are recognized in the period in which the facts become known. Any related costs for work performed under collaborative research and development agreements are expensed in the periods incurred and included in the Statement of Operations in research and development expense.

License agreements

In March 2015, we signed a license agreement as part of a multiple-element arrangement with Sony for our PicoP® scanning technology. The license agreement granted Sony a non-exclusive license to manufacture and sell scanning engines that use our PicoP® scanning technology.

For multiple-element arrangements, we use a hierarchy to determine the contract consideration to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third party evidence of selling price (TPE) and (iii) best estimate of selling price. Because VSOE and TPE do not exist for the March 2015 agreement, we have allocated the contract consideration based on our best estimate.

Under the terms of this multiple-element arrangement, we received an \$8.0 million upfront payment in March 2015 and we will receive a per unit royalty for each display module sold by Sony containing our PicoP® scanning technology. We recognize revenue on the initial \$8.0 million payment on a straight-line basis within royalty revenues on the statement of operations, over a period of eight years which is the expected time frame that we will provide services under the agreement. Ongoing per unit royalties are reported by Sony to us on a quarterly basis. Currently, we recognize revenue for ongoing per unit royalties one quarter in arrears when reported by Sony, representing when such amounts are fixed and determinable, and all other revenue recognition criteria are met. Products delivered under multiple-element arrangements will be recognized upon acceptance of the deliverables by the customer or the expiration of the contractual acceptance period, after which there are no rights of return.

Intangible assets

Our intangible assets consist exclusively of purchased patents. The patents are amortized using the straight-line method over their estimated period of benefit, ranging from one to seventeen years. We evaluate the recoverability of intangible assets periodically by taking into account events or circumstances that may warrant revised estimates of useful lives or that indicate the asset may be impaired. We compare the projected undiscounted net cash flows associated with the related intangible assets or group of assets over their remaining lives against their respective carrying amounts. Measurement of an impairment loss for our intangible assets is based on the difference between the fair value of the asset and its carrying value.

Inventory valuation

Inventory is computed using the first-in, first-out (FIFO) method and is stated at the lower of cost and net realizable value. We make judgments and estimates to value our inventory and make adjustments to its carrying value. We review several factors in determining the market value of our inventory including: evaluating the replacement cost of the raw materials, the net realizable value of the finished goods, and the likelihood of obsolescence. If we do not achieve our targeted sales prices, if market conditions for our components or products were to decline, or if we do not achieve our sales forecast, additional reductions in the carrying value of the inventory would be required.

Warranty

We provide a warranty on scanning engines and components incorporating our PicoP® scanning technology, and we accrue warranty reserves at the time revenue is recognized. Warranty reserves include management's best estimate of the projected costs to repair or to replace any items under warranty based upon the actual units of revenue recognized in the period. We review our reserves each period to ensure that our accruals are adequate in meeting expected future warranty obligations, and we will adjust our estimates as needed. These estimates are inherently uncertain and changes to our historical or projected experience may cause material changes to our warranty reserves in the future.

Share-based compensation

We issue share-based compensation to employees in the form of stock options and restricted stock units (RSUs). We account for the share-based awards by recognizing the fair value of share-based compensation expense on a straight-line basis over the service period of the award, net of estimated forfeitures. The fair value of stock options is estimated on the grant date using the Black-Scholes option pricing model. The fair value of RSUs is determined by the closing price of our common stock on the grant date. Changes in estimated inputs or using other option valuation methods may result in materially different option values and share-based compensation expense.

Income taxes

Significant judgment is required in evaluating our tax position and in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We record a valuation allowance when necessary to reduce deferred tax assets to the amount expected to be realized. Based on our history of losses since inception, the available objective evidence creates sufficient uncertainty regarding the realizability of the deferred tax assets. Our actual tax exposure may differ from our estimates and any such differences may impact income our tax expense in the period in which such determination is made.

The key accounting policies described above are not intended to be a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles, with no need for us to apply judgment or make estimates. There are also areas in which our judgment in selecting any available alternative would not produce a materially different result to our consolidated financial statements. Additional information about our accounting policies, and other disclosures required by generally accepted accounting principles, are set forth in the notes to our consolidated financial statements.

Inflation has not had a material impact on our revenues or income from continuing operations over the three most recent fiscal years.

Results of Operations

YEAR ENDED DECEMBER 31, 2016 COMPARED TO YEAR ENDED DECEMBER 31, 2015.

Product revenue

	<u>2016</u>	<u>% of total revenue</u>	<u>2015</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Product revenue	\$ 12,849	87.0	\$ 6,452	70.2	\$ 6,397	99.1

Product revenue is revenue from sales of our products, which are MEMS and ASICS. Product revenue was higher during the year ended December 31, 2016, compared to the same period in 2015, due to higher product sales to Sony as part of continued shipments of orders we received during 2015 and 2014 totaling \$14.6 million and \$3.8 million, respectively, for key components to be integrated into display modules it manufactures and sells. During 2016, we completed delivery of all outstanding orders from Sony and the backlog of product orders at December 31, 2016 was zero compared to \$11.0 million at December 31, 2015.

Royalty revenue

	<u>2016</u>	<u>% of total revenue</u>	<u>2015</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Royalty revenue	\$ 1,803	12.2	\$ 1,165	12.7	\$ 638	54.8

Royalty revenue is revenue derived from license agreements to our PicoP® scanning technology. Royalty revenue was higher during the year ended December 31, 2016, compared to the same period in 2015, as a result of higher royalty payments we received from Sony for display modules it sold.

During the year ended December 31, 2016, we recognized \$801,000 from ongoing per unit royalties, and \$1.0 million from a prorated portion of the \$8.0 million upfront payment. During the year ended December 31, 2015, we recognized \$316,000 from ongoing per unit royalties, and \$849,000 from a prorated portion of the \$8.0 million upfront

payment. At December 31, 2016, remaining unrecognized upfront license fees are included in current and long-term deferred revenues, amounting to \$999,000 and \$5.1 million, respectively. At December 31, 2015, unrecognized upfront license fees are included in current and long-term deferred revenues, amounting to \$1.0 million and \$6.1 million, respectively.

Contract revenue

	<u>2016</u>	<u>% of total revenue</u>	<u>2015</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Contract revenue	\$ 109	0.8	\$ 1,571	17.1	\$ (1,462)	(93.1)

Contract revenue includes revenue from support service contracts and the sale of prototype units and evaluation kits based on our PicoP® scanning engine. In June 2015, we recognized the full contract value of \$1.5 million in revenue having completed all deliverables and obligations under an agreement to provide support services to Sony for the production readiness, initial production and market launch for display modules incorporating our PicoP® scanning technology.

The contract backlog, including orders for prototype units and evaluation kits, at December 31, 2016 was \$942,000 compared to \$45,000 at December 31, 2015, and is scheduled for completion during the next twelve months.

Cost of product revenue

	<u>2016</u>	<u>% of product revenue</u>	<u>2015</u>	<u>% of product revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Cost of product revenue	\$ 10,320	80.3	\$ 6,384	98.9	\$ 3,936	61.7

Cost of product revenue includes the direct and allocated indirect costs of products sold to customers. Cost of product revenue can fluctuate significantly from period to period, depending on the volume and product mix and the level of manufacturing overhead expense. Cost of product revenue as a percentage of net product revenue decreased during the year ended December 31, 2016, compared to 2015, driven primarily by a significant increase in product deliveries to Sony.

During the year ended December 31, 2016, we expensed approximately \$1.1 million of manufacturing overhead associated with production capacity in excess of production requirements, compared to \$873,000 in 2015. Additionally, during the year ended December 31, 2016, we recorded a provision for scrap of \$187,000 compared to \$287,000 in 2015.

Cost of contract revenue

	<u>2016</u>	<u>% of contract revenue</u>	<u>2015</u>	<u>% of contract revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Cost of contract revenue	\$ 54	49.5	\$ 796	50.7	\$ (742)	(93.2)

Cost of contract revenue includes both the direct and allocated indirect costs of performing on contracts and producing prototype units and evaluation kits based on our PicoP® scanning engines. The decrease in cost of contract revenue for the year ended December 31, 2016, compared to 2015, was primarily attributed to reduced contract activity compared to the prior year.

Research and development expense

	<u>2016</u>	<u>2015</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Research and development expense	\$ 12,134	\$ 8,680	\$ 3,454	39.8

Research and development expense consists of compensation related costs of employees and contractors engaged in internal research and product development activities, direct material to support development programs, laboratory operations, outsourced development and processing work, and other operating expenses. We assign our research and development resources based on the business opportunity of the available projects, the skill mix of the resources available and the contractual commitments we have made to our customers.

The increase in research and development expense during the year ended December 31, 2016, compared to 2015, was attributable to the allocation of resources to internal research and development activities that were previously designated to a commercial contract in prior periods in addition to higher costs related to subcontractors and increased personnel-related compensation and benefits expenses.

We believe that a substantial level of continuing research and development expense will be required to further develop our PicoP® scanning technology.

Sales, marketing, general and administrative expense

	<u>2016</u>	<u>2015</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Sales, marketing, general and administrative expense	\$ 8,743	\$ 7,879	\$ 864	11.0

Sales, marketing, general and administrative expense includes compensation and support costs for marketing, sales, management and administrative staff, and for other general and administrative costs, including legal and accounting services, consultants and other operating expenses.

The increase in sales, marketing, general and administrative expense during the year ended December 31, 2016, compared to 2015, was primarily due to increased personnel-related compensation and benefits expenses, professional fees and business development costs.

Gain on sale of previously reserved inventory

	<u>2016</u>	<u>2015</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Gain on sale of previously reserved inventory	\$ (32)	\$ (1)	\$ (31)	3,100.0

Gain on sale of previously reserved inventory includes the sales of excess component inventory for discontinued products that was fully reserved in prior periods. The activity during the years ended December 31, 2016 and 2015 was primarily the sale of previously reserved excess component inventory.

YEAR ENDED DECEMBER 31, 2015 COMPARED TO YEAR ENDED DECEMBER 31, 2014.

Product revenue

	<u>2015</u>	<u>% of total revenue</u>	<u>2014</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Product revenue	\$ 6,452	70.2	\$ 352	10.1	\$ 6,100	1,733.0

Product revenue was higher during the year ended December 31, 2015, than the same period in 2014, due to higher product sales to Sony as part of continued shipments of orders we received during 2015 and 2014 totaling \$14.6 million and \$3.8 million, respectively, for key components to be integrated into display modules it manufactures and sells. The backlog of product orders at December 31, 2015 was \$11.0 million compared to \$3.6 million at December 31, 2014. All backlog at December 31, 2015 was fulfilled during 2016.

Royalty revenue

	<u>2015</u>	<u>% of total revenue</u>	<u>2014</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Royalty revenue	\$ 1,165	12.7	\$ 40	1.1	\$ 1,125	2,812.5

Royalty revenue was higher during the year ended December 31, 2015, compared to the same period in 2014, as a result of the prorated revenue that was recognized from the \$8.0 million upfront license fee we received from Sony in March 2015 and ongoing per unit royalties on display modules it sells.

During the year ended December 31, 2015, we recognized \$316,000 from ongoing per unit royalties, and \$849,000 from a prorated portion of the \$8.0 million upfront payment. During the year ended December 31, 2014, we recognized \$40,000 from ongoing per unit royalties.

Contract revenue

	<u>2015</u>	<u>% of total revenue</u>	<u>2014</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Contract revenue	\$ 1,571	17.1	\$ 1,402	40.2	\$ 169	12.1

During the year ended December 31, 2015, we recognized the full contract value of \$1.5 million in revenue, having completed all deliverables and obligations under the agreement. During the year ended December 31, 2014, our contract revenue included the delivery of prototype units to customers in the automotive and consumer electronics industries, as well as the delivery of customized scanning engines to a worldwide logistics company during the third quarter of that year.

The contract backlog, including orders for prototype units and evaluation kits, at December 31, 2015 was \$45,000 compared to \$1.5 million at December 31, 2014.

Development revenue

	<u>2015</u>	<u>% of total revenue</u>	<u>2014</u>	<u>% of total revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Development revenue	\$ -	-	\$ 1,691	48.5	\$ (1,691)	(100.0)

In March 2013, we entered into a \$4.6 million collaborative research and development agreement with Sony to incorporate our PicoP® scanning technology into a display module that could enable a variety of new products. As of September 30, 2014, we had completed all deliverables and obligations under the collaborative research and development agreement and had recognized the full contract value of \$4.6 million. Based on the terms of this agreement, we recognized development revenue as work progressed on the agreement and as our customer accepted the deliverables using a proportional method based on the lesser of the cumulative proportion of total estimated costs to be incurred under the agreement versus the cash payments received plus outstanding billings for work accepted by the customer.

Cost of product revenue

	<u>2015</u>	<u>% of product revenue</u>	<u>2014</u>	<u>% of product revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Cost of product revenue	\$ 6,384	98.9	\$ 228	64.8	\$ 6,156	2,700.0

Cost of product revenue was higher during the year ended December 31, 2015, than the same period in 2014, as a result of higher volume of product sales to Sony.

Cost of contract revenue

	<u>2015</u>	<u>% of contract revenue</u>	<u>2014</u>	<u>% of contract revenue</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>						
Cost of contract revenue	\$ 796	50.7	\$ 816	58.2	\$ (20)	(2.5)

The decrease in cost of contract revenue during the year ended December 31, 2015 was primarily attributed to reduced contract activity compared to the prior year.

Research and development expense

	<u>2015</u>	<u>2014</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Research and development expense	\$ 8,680	\$ 9,067	\$ (387)	(4.3)

The decrease in research and development expense during the year ended December 31, 2015, compared to 2014, was primarily attributable to the allocation of resources to a commercial contract during the period, and these costs were recognized as cost of contract revenue upon completion of all deliverables and obligations under the agreement.

Sales, marketing, general and administrative expense

	<u>2015</u>	<u>2014</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Sales, marketing, general and administrative expense	\$ 7,879	\$ 7,005	\$ 874	12.5

The increase in sales, marketing, general and administrative expense during the year ended December 31, 2015, compared to 2014, was primarily attributed to increased business development payroll costs and higher outsourced professional and contract services costs.

Gain on sale of previously reserved inventory

	<u>2015</u>	<u>2014</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Gain on sale of previously reserved inventory	\$ (1)	\$ (463)	\$ 462	(99.8)

The activity during the years ended December 31, 2015 and 2014 was primarily the sale of previously reserved excess component inventory.

Loss on warrant exchange

	<u>2015</u>	<u>2014</u>	<u>\$ change</u>	<u>% change</u>
<i>(In thousands)</i>				
Loss on warrant exchange	\$ -	\$ (4,967)	\$ 4,967	(100.0)

In February 2014, we issued 3.7 million shares of our common stock under the exchange provisions of our then-outstanding warrants. During the year ended December 31, 2014, we recorded a loss of \$5.0 million on the exchange as the fair market value of the common stock issued was greater than the obligation recorded due to an increase in our stock price from December 31, 2013 to the date the warrants were exchanged.

Income taxes

No provision for income taxes has been recorded because we have experienced net losses from inception through December 31, 2016. At December 31, 2016, we had net operating loss carryforwards of approximately \$371.6 million for federal income tax reporting purposes. In addition, we have research and development tax credits of \$7.0 million. The net operating loss carryforwards and research and development credits available to offset future taxable income, if any, will expire in varying amounts from 2018 to 2036, if not previously used.

In addition to the tax benefits above, we have \$310,000 of capital loss carryforwards that are scheduled to expire in 2017. In certain circumstances, as specified in the Internal Revenue Code, a 50% or more ownership change by certain combinations of our shareholders during any three year period would result in a limitation on our ability to use a portion of our net operating loss carryforwards.

We recognize interest accrued and penalties related to unrecognized tax benefits in tax expense. We did not have any unrecognized tax benefits at December 31, 2016 or at December 31, 2015.

Liquidity and Capital Resources

We have incurred significant losses since inception. We have funded operations to date primarily through the sale of common stock, convertible preferred stock, warrants, the issuance of convertible debt and, to a lesser extent, from development contract revenues, product sales, and licensing activities. At December 31, 2016, we had \$15.1 million in cash and cash equivalents.

Based on our current operating plan, and without additional proceeds from the sale of shares under our existing Common Stock Purchase Agreement or ATM facility discussed in Note 8, we anticipate that we have sufficient cash and cash equivalents to fund our operations into the third quarter of 2017. We will require additional capital to fund our operating plan past that time. We plan to obtain additional capital through the issuance of equity or debt securities, product sales and/or licensing activities. There can be no assurance that additional capital will be available or that, if available, it will be available on terms acceptable to us on a timely basis. If adequate capital resources are not available on a timely basis, we intend to consider limiting our operations substantially. This limitation of operations could include reducing our planned investment in development projects, staff, operating costs, capital expenditures and investments in research and development. Our ability to raise proceeds from the sale of shares under our Common Stock Purchase Agreement is subject to limitations and conditions, including a \$1.00 minimum stock price. In

connection with our December 2016 underwritten public offering, we also agreed in the underwriting agreement not to issue shares pursuant to the Common Stock Purchase Agreement, or any other arrangement with Lincoln Park, for a period of six months from the date thereof without the consent of the underwriter.

These factors raise substantial doubt regarding our ability to continue as a going concern. These financial statements were prepared assuming we will continue as a going concern and do not include any adjustments that might be necessary should we be unable to continue as a going concern.

Operating activities

Cash used in operating activities totaled \$14.8 million during 2016, compared to \$5.8 million in 2015, and \$13.0 million in 2014. The change in cash flows from operating activities in 2015 primarily reflects an \$8.0 million upfront payment we received under the terms of the license agreement with Sony for our PicoP® scanning technology. Cash used in operating activities resulted primarily from cash used to fund our net loss, after adjusting for non-cash charges such as realized gains and losses on warrant exchange, share-based compensation, depreciation and amortization charges and changes in operating assets and liabilities.

Investing activities

Cash used in investing activities totaled \$891,000 in 2016, compared to \$1.1 million in 2015, and \$173,000 in 2014. Purchases of property and equipment totaled \$895,000 in 2016, compared to \$1.1 million in 2015, and \$207,000 in 2014. We received proceeds totaling \$4,000 from the sale of property and equipment during 2016. There was no activity in the sale of property and equipment during 2015, compared to sales proceeds of \$34,000 in 2014.

Financing activities

Cash provided by financing activities totaled \$23.0 million in 2016, compared to \$6.5 million in 2015, and \$16.1 million in 2014. Principal payments under capital leases and long-term debt was \$15,000 in 2016, zero in 2015, and \$15,000 in 2014.

The following is a list of our financing activities during 2016, 2015 and 2014.

- In December 2016, we raised approximately \$2.1 million before issuance costs of approximately \$18,000 through a registered direct offering of 2.0 million shares of our common stock.
- In December 2016, we raised approximately \$13.0 million before issuance costs of approximately \$1.2 million through an underwritten public offering of approximately 12.1 million shares of our common stock.
- In September 2016, we entered into a Common Stock Purchase Agreement with Lincoln Park Capital Fund, LLC (Lincoln Park) granting us the right to sell shares of our common stock having an aggregate value of up to \$17.0 million. Under the terms of the agreement, Lincoln Park made an initial purchase of \$2.0 million in shares of common stock at a purchase price of \$1.50 per share. Subject to various limitations and conditions set forth in the agreement, including a \$1.00 minimum stock price, we may sell up to an additional \$15.0 million in shares of common stock, from time to time, at our sole discretion to Lincoln Park over a twenty-four month period beginning September 2016. In consideration for entering into the agreement, we issued 522,556 shares of common stock, having a value of \$721,000 based on the closing stock price on the date of grant, to Lincoln Park as a commitment fee. We incurred an additional \$133,000 in issuance costs. As of December 31, 2016, \$15.0 million in shares of common stock remain available under our Common Stock Purchase Agreement.
- In March 2016, we raised approximately \$6.9 million before issuance costs of approximately \$650,000 through an underwritten public offering of approximately 4.1 million shares of our common stock. The offering included the exercise in full of the underwriter's option to purchase up to an additional 529,411 shares of our common stock.
- In May 2015, we entered into an ATM agreement with Meyers Associates, L.P. Under the terms of the agreement, we may, from time to time, at our discretion, offer and sell shares of our common stock having an aggregate value of up to \$6.0 million. As of December 31, 2016, we have received gross proceeds of approximately \$3.1 million before issuance costs of approximately \$109,000 from the sale of 1.2 million shares of our common stock.
- During the year ended December 31, 2015, we received approximately \$3.3 million from the exercise of warrants to purchase 1.5 million shares of our common stock, which warrants were issued in connection with earlier financing transactions.

- During the three months ended March 31, 2015, we received gross proceeds of \$1.0 million as part of an ATM agreement we entered into with Meyers Associates, L.P. in June 2014. We have completed sales under this agreement, having received total proceeds of approximately \$4.5 million before issuance costs of approximately \$206,000 from the sale of 2.0 million shares of our common stock.
- In March 2014, we raised approximately \$13.9 million before issuance costs of approximately \$1.0 million through an underwritten public offering of 7.2 million shares of our common stock and warrants to purchase 2.1 million shares of our common stock.

Our capital requirements will depend on many factors, including, but not limited to, the rate at which ODMs and OEMs introduce products incorporating our PicoP® scanning technology and the market acceptance and competitive position of such products. Our ability to raise capital will depend on numerous factors, including the following:

- Market acceptance of products incorporating our PicoP® scanning technology;
- Changes in evaluations and recommendations by any securities analysts following our stock or our industry generally;
- Announcements by other companies in our industry;
- Changes in business or regulatory conditions;
- Announcements or implementation by our competitors of technological innovations or new products;
- The status of particular development programs and the timing of performance under specific development agreements;
- Economic and stock market conditions;
- The cost of filing, prosecuting, defending and enforcing any patent claims and other intellectual property rights;
- Our ability to establish cooperative development, joint venture and licensing arrangements; or
- Other factors unrelated to our company or industry.

If we are successful in establishing ODM or OEM co-development and joint venture arrangements, we expect our partners to fund certain non-recurring engineering costs for technology development and/or for product development. Nevertheless, we expect our capital requirements to remain high as we expand our activities and operations with the objective of commercializing our PicoP® scanning technology.

Contractual obligations

The following table lists our contractual obligations as of December 31, 2016 (in thousands):

Contractual Obligations	Payments Due By Period				Total
	< 1 year	1-3 years	3-5 years	> 5 years	
Open purchase obligations *	\$ 6,420	\$ -	\$ -	\$ -	\$ 6,420
Minimum payments under operating leases	439	484	-	-	923
Minimum payments under long-term liabilities	32	53	-	-	85
Minimum payments under research, royalty and licensing agreements	12	24	24	36 †	96
	<u>\$ 6,903</u>	<u>\$ 561</u>	<u>\$ 24</u>	<u>\$ 36</u>	<u>\$ 7,524</u>

* *Open purchase obligations represent commitments to purchase inventory, materials, capital equipment, maintenance agreements and other goods used in the normal operation of our business.*

+ *License and royalty obligations continue through the lives of the underlying patents, which is currently through at least 2024.*

Recent accounting pronouncements

See Note 2, “Summary of significant accounting policies,” in the Notes to the consolidated financial statements found in Part II, Item 8 of this Form 10-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate and Market Liquidity Risks

As of December 31, 2016, all of our cash and cash equivalents have variable interest rates. Therefore, we believe our exposure to market and interest rate risks is not material.

Our investment policy generally directs that the investment managers should select investments to achieve the following goals: principal preservation, adequate liquidity, and return. As of December 31, 2016, our cash and cash equivalents are comprised of short-term highly rated money market savings accounts. The values of cash and cash equivalents as of December 31, 2016, are as follows (in thousands):

	<u>Amount</u>	<u>Percent</u>
Cash and cash equivalents	\$ 15,139	100 %
Less than one year	-	-
	<u>\$ 15,139</u>	<u>100 %</u>

Foreign Exchange Rate Risk

Our major contract and collaborative research and development agreements, product sales, and licensing activity payments are currently made in U.S. dollars. However, in the future we may enter into contracts or collaborative research and development agreements in foreign currencies that may subject us to foreign exchange rate risk. We have entered into purchase orders and supply agreements in foreign currencies in the past and may enter into such arrangements, from time to time, in the future. We believe our exposure to currency fluctuations related to these arrangements is not material. We may enter into foreign currency hedges to offset material exposure to currency fluctuations when we can adequately determine the timing and amounts of the exposure.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

	Page
Report of Independent Registered Public Accounting Firm	30
Consolidated Balance Sheets as of December 31, 2016 and 2015	31
Consolidated Statements of Operations for the years ended December 31, 2016, 2015 and 2014	32
Consolidated Statements of Shareholders' Equity (Deficit) for the years ended December 31, 2016, 2015 and 2014	33
Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014	34
Notes to Consolidated Financial Statements	35

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
MicroVision, Inc.

We have audited the accompanying consolidated balance sheets of MicroVision, Inc. (the “Company”) as of December 31, 2016, and the related consolidated statements of operations, shareholders’ equity (deficit), and cash flows for each of the three years in the period ended December 31, 2016. Our audits also included the financial statement schedule listed in the Index at Item 15(A). These consolidated financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of MicroVision, Inc. as of December 31, 2016 and 2015, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

The accompanying consolidated financial statements have been prepared assuming the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has incurred losses from operations and has an accumulated deficit, which raises substantial doubt about its ability to continue as a going concern. Management’s plans regarding these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), MicroVision, Inc.’s internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 6, 2017 expressed an unqualified opinion thereon.

/s/ Moss Adams LLP

Seattle, Washington
March 6, 2017

MicroVision, Inc.
Consolidated Balance Sheets
(In thousands)

Assets	December 31,	
	2016	2015
Current assets		
Cash and cash equivalents	\$ 15,139	\$ 7,888
Accounts receivable, net of allowances of \$26 and \$38, respectively	245	1,687
Inventory	1,233	862
Other current assets	731	638
Total current assets	17,348	11,075
Property and equipment, net	1,537	1,669
Restricted cash	435	435
Intangible assets, net	718	845
Other assets	68	18
Total assets	\$ 20,106	\$ 14,042
 Liabilities and shareholders' equity (deficit)		
Current liabilities		
Accounts payable	\$ 2,195	\$ 2,183
Accrued liabilities	3,882	3,399
Deferred revenue	999	2,122
Billings on uncompleted contracts in excess of related costs	168	-
Total current liabilities	7,244	7,704
Deferred revenue, net of current portion	5,150	6,149
Deferred rent, net of current portion	185	342
Other long-term liabilities	53	-
Total liabilities	12,632	14,195
Commitments and contingencies (Note 11)		
Shareholders' equity (deficit)		
Preferred stock, par value \$0.001; 25,000 shares authorized; zero and zero shares issued and outstanding, respectively	-	-
Common stock, par value \$0.001; 100,000 shares authorized; 68,093 and 47,423 shares issued and outstanding at December 31, 2016 and 2015, respectively	68	47
Additional paid-in capital	507,249	483,171
Accumulated deficit	(499,843)	(483,371)
Total shareholders' equity (deficit)	7,474	(153)
Total liabilities and shareholders' equity (deficit)	\$ 20,106	\$ 14,042

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

MicroVision, Inc.
Consolidated Statements of Operations
(In thousands, except per share data)

	Year Ended December 31,		
	2016	2015	2014
Product revenue	\$ 12,849	\$ 6,452	\$ 352
Royalty revenue	1,803	1,165	40
Contract revenue	109	1,571	1,402
Development revenue	-	-	1,691
Total revenue	<u>14,761</u>	<u>9,188</u>	<u>3,485</u>
Cost of product revenue	10,320	6,384	228
Cost of contract revenue	54	796	816
Total cost of revenue	<u>10,374</u>	<u>7,180</u>	<u>1,044</u>
Gross profit	<u>4,387</u>	<u>2,008</u>	<u>2,441</u>
Research and development expense	12,134	8,680	9,067
Sales, marketing, general and administrative expense	8,743	7,879	7,005
Gain on sale of previously reserved inventory	(32)	(1)	(463)
Total operating expenses	<u>20,845</u>	<u>16,558</u>	<u>15,609</u>
Loss from operations	<u>(16,458)</u>	<u>(14,550)</u>	<u>(13,168)</u>
Loss on warrant exchange	-	-	(4,967)
Other income (expense), net	(14)	8	15
Net loss	<u>\$ (16,472)</u>	<u>\$ (14,542)</u>	<u>\$ (18,120)</u>
Net loss per share - basic and diluted	<u>\$ (0.32)</u>	<u>\$ (0.31)</u>	<u>\$ (0.44)</u>
Weighted-average shares outstanding - basic and diluted	<u>51,958</u>	<u>46,540</u>	<u>41,599</u>

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

MicroVision, Inc.
Consolidated Statements of Shareholders' Equity (Deficit)
(In thousands)

	<u>Common Stock</u>		<u>Additional</u>	<u>Accumulated</u>	<u>Total</u>
	<u>Shares</u>	<u>Par value</u>	<u>paid-in capital</u>	<u>deficit</u>	<u>shareholders' equity (deficit)</u>
Balance at January 1, 2014	32,069	\$ 32	\$ 448,981	\$ (450,709)	\$ (1,696)
Share-based compensation expense	105	-	705	-	705
Sales of common stock and warrants	8,871	9	16,105	-	16,114
Exchange of warrants	3,713	4	9,865	-	9,869
Net loss	-	-	-	(18,120)	(18,120)
Balance at December 31, 2014	<u>44,758</u>	<u>\$ 45</u>	<u>\$ 475,656</u>	<u>\$ (468,829)</u>	<u>\$ 6,872</u>
Share-based compensation expense	86	-	1,011	-	1,011
Exercise of warrants and options	1,510	1	3,299	-	3,300
Sales of common stock and warrants	1,069	1	3,205	-	3,206
Net loss	-	-	-	(14,542)	(14,542)
Balance at December 31, 2015	<u>47,423</u>	<u>\$ 47</u>	<u>\$ 483,171</u>	<u>\$ (483,371)</u>	<u>\$ (153)</u>
Share-based compensation expense	87	-	1,223	-	1,223
Exercise of options	4	-	7	-	7
Sales of common stock and warrants	20,579	21	22,848	-	22,869
Net loss	-	-	-	(16,472)	(16,472)
Balance at December 31, 2016	<u>68,093</u>	<u>\$ 68</u>	<u>\$ 507,249</u>	<u>\$ (499,843)</u>	<u>\$ 7,474</u>

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

MicroVision, Inc.
Consolidated Statements of Cash Flows
(In thousands)

	Year Ended December 31,		
	2016	2015	2014
Cash flows from operating activities			
Net loss	\$ (16,472)	\$ (14,542)	\$ (18,120)
Adjustments to reconcile net loss to net cash used in operations:			
Depreciation	1,120	429	414
Amortization of intangible assets	127	128	132
Impairment of intangible assets	-	-	40
Non-cash share-based compensation expense	1,223	1,007	713
Loss on warrant exchange	-	-	4,967
Inventory write-downs	187	287	42
Other non-cash adjustments	27	(62)	(91)
Change in:			
Accounts receivable	1,442	(1,018)	(645)
Inventory	(558)	(1,033)	(109)
Other current and non-current assets	(143)	(147)	(155)
Accounts payable	(174)	493	(25)
Accrued liabilities	301	590	335
Deferred revenue	(2,122)	8,271	-
Billings on uncompleted contracts in excess of related costs	168	(230)	(450)
Other long-term liabilities	53	-	-
Net cash used in operating activities	<u>(14,821)</u>	<u>(5,827)</u>	<u>(12,952)</u>
Cash flows from investing activities			
Proceeds on sale of property and equipment	4	-	34
Purchases of property and equipment	(895)	(1,140)	(207)
Net cash used in investing activities	<u>(891)</u>	<u>(1,140)</u>	<u>(173)</u>
Cash flows from financing activities			
Principal payments under capital leases and long-term debt	(15)	-	(15)
Net proceeds from issuance of common stock and warrants	22,978	6,506	16,114
Net cash provided by financing activities	<u>22,963</u>	<u>6,506</u>	<u>16,099</u>
Net increase (decrease) in cash and cash equivalents	7,251	(461)	2,974
Cash and cash equivalents at beginning of period	7,888	8,349	5,375
Cash and cash equivalents at end of period	<u>\$ 15,139</u>	<u>\$ 7,888</u>	<u>\$ 8,349</u>
Supplemental schedule of non-cash investing and financing activities			
Non-cash additions to property and equipment	<u>\$ 351</u>	<u>\$ 165</u>	<u>\$ 101</u>
Issuance of common stock for exchange of warrants	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 9,869</u>
Issuance of common stock for commitment fee	<u>\$ 721</u>	<u>\$ -</u>	<u>\$ -</u>

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

MicroVision, Inc.
Notes to Consolidated Financial Statements
For the year ended December 31, 2016

1. THE COMPANY AND LIQUIDITY

MicroVision, Inc. is a pioneer in LBS technology that we market under our brand name PicoP®. We have developed our proprietary PicoP® scanning technology that can be adopted by our customers to create high-resolution miniature projection and three-dimensional sensing and image capture solutions. PicoP® scanning technology is based on our patented expertise in MEMS, laser diodes, opto-mechanics, and electronics and how those elements are packaged into a small form factor, lower power scanning engine that can display, interact and sense, depending on the needs of the application. For display, the engine can project a high-quality image on any surface (pico projection), a windshield (HUD), or a retina (AR). For sensing, we use IR lasers to capture three-dimensional data in the form of a point cloud. Interactivity uses the 3D sensing function and the display function to simultaneously project an image that the user can then interact with as one would a touch screen.

We have incurred significant losses since inception and expect to incur a significant loss during the fiscal year ending December 31, 2017. We have funded operations to date primarily through the sale of common stock, convertible preferred stock, warrants, the issuance of convertible debt and, to a lesser extent, from development contract revenues, product sales and licensing activities. At December 31, 2016, we had \$15.1 million in cash and cash equivalents.

Based on our current operating plan, and without additional proceeds from the sale of shares under our existing Common Stock Purchase Agreement or ATM facility discussed in Note 8, we anticipate that we have sufficient cash and cash equivalents to fund our operations into the third quarter of 2017. We will require additional capital to fund our operating plan past that time. We plan to obtain additional capital through the issuance of equity or debt securities, product sales and/or licensing activities. There can be no assurance that additional capital will be available or that, if available, it will be available on terms acceptable to us on a timely basis. If adequate capital resources are not available on a timely basis, we intend to consider limiting our operations substantially. This limitation of operations could include reducing our planned investment in our production capabilities or research and development projects, staff, operating costs, capital expenditures. Our ability to raise proceeds from the sale of shares under our Common Stock Purchase Agreement is subject to limitations and conditions, including a \$1.00 minimum stock price. In connection with our December 2016 underwritten public offering, we also agreed in the underwriting agreement not to issue shares pursuant to the Common Stock Purchase Agreement, or any other arrangement with Lincoln Park, for a period of six months from the date thereof without the consent of the underwriter.

Our capital requirements will depend on many factors, including, but not limited to, the rate at which ODMs or OEMs introduce products incorporating PicoP® scanning technology and the market acceptance and competitive position of such products. If revenues are less than anticipated, if the mix of revenues vary from anticipated amounts, or if expenses exceed the amounts budgeted, we may require additional capital earlier than expected to further the development of our technologies, for expenses associated with product development, and to respond to competitive pressures or to meet unanticipated development difficulties. In addition, our operating plan provides for the development of strategic relationships with systems and equipment manufacturers that may require additional investments by us.

These factors raise substantial doubt regarding our ability to continue as a going concern. These financial statements were prepared assuming we will continue as a going concern and do not include any adjustments that might be necessary should we be unable to continue as a going concern.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles of the United States requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from our estimates. We have identified the following areas where estimates and assumptions have been made in preparing the financial statements: revenue recognition, inventory valuation, valuation of share-based payments, intangibles impairment assessment, depreciable lives assessment and related disclosure of contingent assets and liabilities.

Cash and cash equivalents and fair value of financial instruments

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the authoritative guidance establishes a three level fair value inputs hierarchy, and requires an entity to maximize the use of observable valuation inputs and minimize the use of unobservable inputs. We use market data, assumptions and risks we believe market participants would use in measuring the fair value of the asset or liability, including the risks inherent in the inputs and the valuation techniques.

Our financial instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities. The carrying value of our financial instruments approximates fair value due to their short maturities. Our cash equivalents are comprised of short-term highly rated money market savings accounts.

Intangible assets

Our intangible assets consist exclusively of purchased patents. The patents are amortized using the straight-line method over their estimated period of benefit, ranging from one to seventeen years. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. Recoverability of these assets is measured by comparison of their carrying values to the projected undiscounted net cash flows associated with the related intangible assets or group of assets over their remaining lives. Measurement of an impairment loss for our intangible assets is based on the difference between the fair value of the asset and its carrying value.

Inventory

Inventory consists of raw materials and finished goods assemblies. Inventory is computed using the first-in, first-out (FIFO) method and is stated at the lower of cost and net realizable value. Management periodically assesses the need to account for obsolescence of inventory and adjusts the carrying value of inventory to its net realizable value when required. In addition, we reduce the value of our inventory to its estimated scrap value when management determines that it is not probable that the inventory will be consumed through the normal course of business during the next twelve months.

Property and equipment

Property and equipment is stated at cost and depreciated over the estimated useful lives of the assets (two to five years) using the straight-line method. As our production needs change, we periodically assess the remaining estimated useful life of our production equipment. If necessary, we adjust the depreciation on our production equipment to reflect the remaining estimated useful life. Leasehold improvements are depreciated over the shorter of estimated useful lives or the lease term. Costs for repairs and maintenance are charged to expense as incurred and expenditures for major improvements are capitalized at cost. Gains or losses on the disposition of assets are reflected in the income statements at the time of disposal.

Restricted cash

As of December 31, 2016 and 2015, restricted cash was in money market savings accounts and serve as collateral for \$435,000 in irrevocable letters of credit. The restricted cash balance includes a letter of credit which is outstanding in connection with a lease agreement for our corporate headquarters building in Redmond, Washington. The balance is required over the term of the lease, which expires in January 2019.

Revenue recognition

We recognize revenue when: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred and there are no uncertainties regarding customer acceptance, (iii) fees are fixed or determinable, and (iv) collection is reasonably assured.

We generate revenue from many sources and activities. We enter into arrangements that can include various combinations of product sales, services, and licensing activities. For multiple-element arrangements, we use a hierarchy to determine the contract consideration to be used for allocating revenue to deliverables: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third party evidence of selling price (TPE), and (iii) best estimate of

selling price. To date, our sources can be classified as: product revenue, royalty revenue, contract revenue, or development revenue.

Product revenue

Product revenue is revenue from our sales of our products, which are MEMS and ASICs. Our product sales generally include acceptance provisions. We recognize product revenue upon acceptance of the product by the customer or the expiration of the contractual acceptance period, after which there are no rights of return. Our product revenue, from period to period, may vary substantially due to the timing of product orders from customers, product shipments, production constraints and availability of components and raw materials.

Fulfillment and delivery of the backlog is dependent upon the successful supply chain development and delivery of required components to us. From time to time, raw materials and manufacturing delays and components received that do not meet quality standards have resulted in delivery delays to our customers.

Royalty revenue

Royalty revenue is revenue under license agreements to our PicoP® scanning technology. We recognize revenue on upfront license fees over the expected time frame that we provide services or have ongoing obligations under the agreement. Ongoing per unit royalties are recognized when reported by our customer to us on a quarterly basis. Currently, we recognize revenue for ongoing per unit royalties one quarter in arrears when reported by our customer, representing when such amounts are fixed and determinable, and all other revenue recognition criteria are met.

Contract revenue

Contract revenue includes revenue from support service contracts and the sale of prototype units and evaluation kits based on our PicoP® scanning engine. Our contract revenue in a particular period is dependent upon when we enter into a contract, the value of the contracts we have entered into, and the availability of technical resources to perform work on the contracts. We recognize contract revenue related to the sale of prototype units and evaluation kits upon acceptance of the deliverables by the customer or expiration of the contractual acceptance period, after which there are no rights of return.

We recognize contract revenue on long-term, cost plus fixed fee, and fixed price contracts using the percentage-of-completion method. Under the percentage-of-completion method, revenue is recognized as work progresses on the contract. The percentage-of-completion method relies on estimates of total expected contract revenue and costs. At the end of each period, we estimate the labor, material and other costs required to complete the contract using data provided by our technical team, project managers, vendors, outside consultants, and others and compare these to costs incurred to date.

Recognized revenues are subject to amendments for actual costs incurred. Amendments to revenue and costs to complete estimates are recognized in the period in which the facts become known. In the future, amendments to estimates could significantly impact recognized revenue in any one reporting period. If we are unable to estimate costs on a contract, revenue is recognized using the completed-contract method. Under the completed-contract method, revenue and contract costs are deferred and both are recognized when all deliverables are completed.

Development revenue

Development revenue is revenue from performance on collaborative research and development agreements with commercial customers researching and developing commercial applications for our technology. We evaluate the performance criteria and terms of our collaborative research and development agreements to determine whether revenue should be recognized under a performance-based method or milestone method. Significant items included in our evaluation include the following:

- The nature of our obligation under the agreement;
- Whether provisions leading to variable revenues exist;
- Whether any payments are refundable;
- Whether the deliverables should be treated as one unit of accounting or separated into multiple units;
- Whether substantive milestones exist;

- Whether milestone payments are commensurate with either our level of effort or the increase in value of the customer's rights; and
- Whether a licensing agreement exists.

At the end of each period, we evaluate total estimated costs for each agreement. Amendments to the estimated costs are recognized in the period in which the facts become known. The costs for work performed under collaborative research and development agreements are expensed in the periods incurred and included in the statement of operations in research and development expense.

Cost of product revenue

Cost of product revenue includes the direct and allocated indirect costs of products sold to customers. Direct costs include labor, materials, reserves for estimated warranty expenses, and other costs incurred directly, or charged to us by our contract manufacturers in the manufacture of these products. Indirect costs include labor, manufacturing overhead, and other costs associated with operating our manufacturing capabilities and capacity. Manufacturing overhead includes the costs of procuring, inspecting and storing material, facility and other costs, and is allocated to cost of product revenue based on the proportion of indirect labor which supported production activities. The cost of product revenue can fluctuate significantly from period to period, depending on the product mix and volume, the level of manufacturing overhead expense and the volume of direct material purchased.

Cost of contract revenue

Cost of contract revenue includes both the direct and allocated indirect costs of performing on contracts and producing prototype units and evaluation kits based on our PicoP® scanning engine. Direct costs include labor, materials and other costs incurred directly in producing prototype units and evaluation kits or performing on a contract. Indirect costs include labor and other costs associated with operating our research and development department and building our technical capabilities and capacity. Cost of contract revenue is determined by the level of direct and indirect costs incurred, which can fluctuate substantially from period to period.

Our overhead, which includes the costs of procuring, inspecting and storing material, and facility and depreciation costs, is allocated to inventory, cost of product revenue, cost of contract revenue, and research and development expense based on the level of effort supporting production or research and development activity.

Concentration of credit risk and major customers and suppliers

Concentration of credit risk

Financial instruments that potentially subject us to a concentration of credit risk are primarily cash equivalents and accounts receivable. We typically do not require collateral from our customers. As of December 31, 2016, our cash and cash equivalents are comprised of short-term highly rated money market savings accounts.

Concentration of major customers and suppliers

In 2016, one commercial customer accounted for \$13.5 million in revenue, representing 91% of our total revenue. In 2015, the same commercial customer accounted for \$9.0 million in revenue, representing 98% of our total revenue. In 2014, the same commercial customer accounted for \$2.0 million in revenue, representing 58% of our total revenue, and a second commercial customer accounted for \$577,000 in revenue, representing 17% of our total revenue.

In 2016, one commercial customer accounted for \$182,000, or 74% of our net accounts receivable balance, and a second commercial customer accounted for \$54,000, or 22% of our net accounts receivable balance. In 2015, one commercial customer accounted for \$1.5 million, or 91% of our net accounts receivable balance.

A significant concentration of our components and the products we sell are currently manufactured and obtained from single or limited-source suppliers, which are primarily located in foreign countries. The loss of any single or limited-source supplier, the failure of any of these suppliers to perform as expected, or the disruption in the supply chain of components from these suppliers could subject us to risks and uncertainties regarding, but not limited to, increased cost of sales, possible loss of revenues, or significant delays in product deliveries, any of which could adversely affect our financial condition and operating results.

Income taxes

Deferred tax assets and liabilities are recorded for differences between the financial statement and tax bases of the assets and liabilities that will result in taxable or deductible amounts in the future, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Income tax expense is recorded for the amount of income tax payable for the period increased or decreased by the change in deferred tax assets and liabilities during the period.

Net loss per share

Basic net loss per share is calculated using the weighted-average number of common shares outstanding during the periods. Net loss per share, assuming dilution, is calculated using the weighted-average number of common shares outstanding and the dilutive effect of all potentially dilutive securities, including common stock equivalents and convertible securities. Net loss per share, assuming dilution, is equal to basic net loss per share because the effect of dilutive securities outstanding during the periods, including options and warrants computed using the treasury stock method, is anti-dilutive.

The components of basic and diluted net loss per share were as follows (in thousands, except loss per share data):

	Year Ended December 31,		
	2016	2015	2014
Numerator:			
Net loss available for common shareholders	\$ <u>(16,472)</u>	\$ <u>(14,542)</u>	\$ <u>(18,120)</u>
Denominator:			
Weighted-average common shares outstanding	<u>51,958</u>	<u>46,540</u>	<u>41,599</u>
Net loss per share - basic and diluted	\$ <u>(0.32)</u>	\$ <u>(0.31)</u>	\$ <u>(0.44)</u>

During each of the years ended December 31, 2016, 2015 and 2014, we excluded the following securities from net loss per share as the effect of including them would have been anti-dilutive. The shares shown represent the number of shares of common stock which would be issued upon conversion in the respective years shown below (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Options outstanding and warrants exercisable	<u>7,764</u>	<u>8,185</u>	<u>8,953</u>
Nonvested restricted stock units	<u>60</u>	<u>60</u>	<u>60</u>
	<u>7,824</u>	<u>8,245</u>	<u>9,013</u>

Research and development

Research and development expense consists of compensation related costs of employees and contractors engaged in internal research and product development activities, direct material to support development programs, laboratory operations, outsourced development and processing work, and other operating expenses. We assign our research and development resources based on the business opportunity of the available projects, the skill mix of the resources available and the contractual commitments we have made to our customers. Research and development costs are expensed as incurred. We believe that a substantial level of continuing research and development expense will be required to further develop our technology.

Share-based compensation

We issue share-based compensation to employees in the form of stock options and restricted stock units (RSUs). We account for the share-based awards by recognizing the fair value of share-based compensation expense on a straight-line basis over the service period of the award, net of estimated forfeitures. The fair value of stock options is estimated on the grant date using the Black-Scholes option pricing model. The fair value of RSUs is determined by the closing price of our common stock on the grant date. Changes in estimated inputs or using other option valuation methods may result in materially different option values and share-based compensation expense.

The following table summarizes the amount of share-based compensation expense by line item on the Statement of Operations (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Cost of product revenue	\$ 37	\$ 19	\$ -
Cost of contract revenue	-	-	28
Research and development expense	350	282	34
Sales, marketing, general and administrative expense	836	706	651
	<u>\$ 1,223</u>	<u>\$ 1,007</u>	<u>\$ 713</u>

Reclassifications

Certain reclassifications have been made to prior year financial statements to conform to classifications used in the current year. These reclassifications had no impact on net loss, shareholders' equity or cash flows, as previously reported.

Recent accounting pronouncements

In November 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2016-18 (ASU 2016-18), Restricted Cash. The standard requires restricted cash and cash equivalents to be included with cash and cash equivalents on the statement of cash flows. The new standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted. The new guidance shall be applied using a retrospective approach. As of December 31, 2016 and 2015, we have \$435,000 of restricted cash, and as such we do not expect the implementation of this standard to have a material effect on our financial statements.

In August 2016, the FASB issued Accounting Standards Update 2016-15 (ASU 2016-15), Statement of Cash Flows (Topic 230): Clarification of Certain Cash Receipts and Cash Payments. The objective of ASU 2016-15 is to eliminate the diversity in practice related to the classification of certain receipts and payments in the statement of cash flows, by adding or clarifying guidance on eight specific cash flow issues. For public business entities, ASU 2016-15 is effective for annual and interim reporting periods beginning after December 15, 2017, with early adoption permitted. The amendments in this update should be applied retrospectively to all periods presented, unless deemed impracticable, in which case, prospective application is permitted. We do not expect the implementation of this standard to have a material effect on our financial statements.

In June 2016, the FASB issued Accounting Standards Update 2016-13 (ASU 2016-13), Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 amends the impairment model to utilize an expected loss methodology in place of the currently used incurred loss methodology, which will result in the more timely recognition of losses. ASU 2016-13 is effective for public entities with fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The new guidance shall be applied on a modified-retrospective approach. We do not expect the implementation of this standard to have a material effect on our financial statements.

In March 2016, the FASB issued Accounting Standards Update 2016-09 (ASU 2016-09), Improvements to Employee Share-Based Payment Accounting. ASU 2016-09 simplifies several aspects of the accounting for share-based payment award transactions including a) income tax consequences; b) classification of awards as either equity or liabilities; and c) classification on the statement of cash flows. ASU 2016-09 is effective for public entities in the fiscal years beginning after December 15, 2016, and for interim periods within those fiscal years. Various elements of the amendments will be applied using either a modified retrospective transition method, retrospectively, or prospectively. Early adoption is permitted. We do not expect the implementation of this standard to have a material effect on our financial statements.

In February 2016, the FASB issued Accounting Standards Update 2016-02 (ASU 2016-02), Leases (Topic 842). ASU 2016-02 requires lessees to recognize a right-of-use asset and lease liability in the balance sheet for all leases, including operating leases, with terms of more than twelve months. Recognition, measurement and presentation of expenses and cash flows from a lease by a lessee have not significantly changed from previous guidance. The amendments also

require qualitative disclosures along with specific quantitative disclosures. The new guidance will be effective for fiscal years beginning after December 15, 2018, and interim periods within those years, with early adoption permitted. The amendments must be applied on a modified retrospective basis. We anticipate the adoption of this standard will have a material impact on our financial statements. While we are continuing to assess all the potential impacts of the standard, we currently believe the most significant impact relates to our accounting for our office lease. Under the new guidance, the net present value of the obligation for our office lease will appear on the balance sheet. Currently, it is classified as an operating lease and payments are expensed in the period incurred.

In November 2015, the FASB issued Accounting Standards Update 2015-17 (ASU 2015-17), *Income Taxes: Balance Sheet Classification of Deferred Taxes*. ASU 2015-17 eliminates the current requirement to present deferred tax liabilities and assets as current and non-current on the balance sheet and requires that all deferred tax liabilities and assets, and any related valuation allowance, be classified as non-current on the balance sheet. ASU 2015-17 is effective for public entities in fiscal years beginning after December 15, 2016, and for the interim periods within those fiscal years. The new guidance can be applied retrospectively or prospectively and early adoption is permitted. We do not expect the implementation of this standard to have a material effect on our financial statements as our net deferred tax assets are reduced to \$0 by a full valuation allowance.

In July 2015, the FASB issued Accounting Standards Update 2015-11 (ASU 2015-11), *Inventory (Topic 330): Simplifying the Measurement of Inventory*, which changes the measurement principle for inventory from the lower of cost or market to the lower of cost and net realizable value. ASU 2015-11 defines net realizable value as estimated selling prices in the ordinary course of business, less predictable costs of completion, disposal, and transportation. The new guidance must be applied on a prospective basis and is effective for fiscal years beginning after December 15, 2016, and interim periods within those years, with early adoption permitted. We do not expect the implementation of this standard to have a material effect on our financial statements.

In May 2014, the FASB issued Accounting Standards Update 2014-09 (ASU 2014-09), *Revenue from Contracts with Customers*, an updated standard on revenue recognition. The core principle of the new standard is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively, and improve guidance for multiple-element arrangements. ASU 2014-09 will be effective for us as of January 1, 2018, with early adoption permitted as of January 1, 2017. We have chosen to implement the new standard as of January 1, 2018 using the full retrospective approach, meaning we will restate each prior reporting period presented. We have performed a review of our revenue generated from significant product and service contracts with customers subject to ASU 2014-09, and we expect the implementation of this standard to have a material impact on our financial statements. While we are continuing to assess all potential impacts of this standard, we currently believe the most significant impact relates to our accounting for the \$8.0 million upfront license fee payment under the PicoP® scanning technology license agreement we signed with Sony in March 2015. Under current guidance, we are recognizing the upfront license fee payment of \$8.0 million on a straight-line basis over a period of eight years. Under the new guidance, we expect to recognize the entire \$8.0 million upfront license fee payment in the first quarter of 2015, which will increase 2015 revenues by \$7.2 million, and reduce reported 2016 revenues by \$1.0 million. We currently expect no changes to the timing of our recognition of the ongoing per unit royalties; they will continue to be recognized one quarter in arrears when reported by Sony. We expect revenue related to our components sales to remain substantially unchanged.

3. LONG-TERM CONTRACTS

In March 2015, we signed a license agreement with Sony for our PicoP® scanning technology. The license agreement granted Sony a non-exclusive license to our technology to incorporate into display modules it manufactures and sells for up to eight years. As part of the agreement, we received an \$8.0 million upfront license fee in March 2015, and we will receive ongoing per unit royalties for each display module it sells.

In October 2014, we entered into a \$1.5 million agreement with Sony for display module support services as part of the production readiness and commercialization of display modules incorporating PicoP® scanning technology. We recognized the full contract value of \$1.5 million in revenue in June 2015, having completed all deliverables and obligations under the agreement.

The following table summarizes the costs incurred on our revenue contracts (in thousands):

	December 31,	
	2016	2015
Costs and estimated earnings incurred on uncompleted contracts	\$ 193	\$ -
Billings on uncompleted contracts	(236)	-
	<u>\$ (43)</u>	<u>\$ -</u>

Included in consolidated balance sheets under the following captions:

Other current assets	125	
Billings on uncompleted contracts in excess of related costs	(168)	-
	<u>\$ (43)</u>	<u>\$ -</u>

4. INVENTORY

Inventory consists of the following (in thousands):

	December 31,	
	2016	2015
Raw materials	\$ 999	\$ 232
Finished goods	234	630
	<u>\$ 1,233</u>	<u>\$ 862</u>

We recorded inventory write-downs of \$187,000 in 2016, \$287,000 in 2015, and \$42,000 in 2014. At December 31, 2016 and 2015, we recorded aggregate write-downs of \$6.6 million and \$6.9 million, respectively, offsetting inventory on-hand deemed to be obsolete or scrap inventory. We may enter into arrangements to sell the obsolete or scrap inventory resulting in a gain in the period such transactions are realized.

5. ACCRUED LIABILITIES

Accrued liabilities consists of the following (in thousands):

	December 31,	
	2016	2015
Bonuses	\$ 1,350	\$ 1,150
Adverse purchase commitments	500	500
Payroll and payroll taxes	398	353
Compensated absences	393	357
Warranty	316	239
Relocation	204	85
Deferred rent credit	158	146
Other	563	569
	<u>\$ 3,882</u>	<u>\$ 3,399</u>

6. PROPERTY AND EQUIPMENT

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

	December 31,	
	2016	2015
Production equipment	\$ 4,580	\$ 4,150
Leasehold improvements	494	494
Computer hardware and software/lab equipment	4,968	4,618
Office furniture and equipment	1,096	1,087
	<u>11,138</u>	<u>10,349</u>
Less: Accumulated depreciation	(9,601)	(8,680)
	<u>\$ 1,537</u>	<u>\$ 1,669</u>

Depreciation expense was \$1.1 million in 2016, \$429,000 in 2015, and \$414,000 in 2014. In the fourth quarter of 2016, we recorded additional depreciation expense of \$297,000, as a result of a change in the estimated useful life of

production equipment to be replaced in connection with our current business strategy to sell LBS engines directly to ODMs and OEMs.

Capital leases are collateralized by the related assets financed and by security deposits held by the lessors under the lease agreements. The cost and accumulated depreciation of equipment under capital leases was \$704,000 in each of the years ended December 31, 2016 and 2015.

7. INTANGIBLE ASSETS

Our intangible assets consist exclusively of technology-based purchased patents. The gross value of our intangible assets was \$1.6 million in each of the years ended December 31, 2016 and 2015. Amortization expense was \$127,000 in 2016, \$128,000 in 2015, and \$132,000 in 2014. In 2016 and 2015, there were no impairments recorded and none of our patents were abandoned in prosecution. In 2014, we recorded an impairment amounting to \$40,000 on five patents that were abandoned in prosecution. The following table outlines our estimated future amortization expense related to intangible assets held at December 31, 2016 (in thousands):

Years Ended December 31,	<u>Amount</u>
2017	\$ 116
2018	115
2019	115
2020	98
2021	80
Thereafter	194
	<u><u>\$ 718</u></u>

8. COMMON STOCK

In December 2016, we raised approximately \$2.1 million before issuance costs of approximately \$18,000 through a registered direct offering of 2.0 million shares of our common stock.

In December 2016, we raised approximately \$13.0 million before issuance costs of approximately \$1.2 million through an underwritten public offering of approximately 12.1 million shares of our common stock.

In September 2016, we entered into a Common Stock Purchase Agreement with Lincoln Park granting us the right to sell shares of our common stock having an aggregate value of up to \$17.0 million. Under the terms of the agreement, Lincoln Park made an initial purchase of \$2.0 million in shares of common stock at a purchase price of \$1.50 per share. Subject to various limitations and conditions set forth in the agreement, including a \$1.00 minimum stock price, we may sell up to an additional \$15.0 million in shares of common stock, from time to time, at our sole discretion to Lincoln Park over a twenty-four month period beginning September 2016. In consideration for entering into the agreement, we issued 522,556 shares of common stock, having a value of \$721,000 based on the closing stock price on the date of grant, to Lincoln Park as a commitment fee. We incurred an additional \$133,000 in issuance costs. As of December 31, 2016, \$15.0 million in shares of common stock remain available under our Common Stock Purchase Agreement. In connection with our December 2016 underwritten public offering, we also agreed in the underwriting agreement not to issue shares pursuant to the Common Stock Purchase Agreement, or any other arrangement with Lincoln Park, for a period of six months from the date thereof.

In March 2016, we raised approximately \$6.9 million before issuance costs of approximately \$650,000 through an underwritten public offering of approximately 4.1 million shares of our common stock. The offering included the exercise in full of the underwriter's option to purchase up to an additional 529,411 shares of our common stock.

In May 2015, we entered into an ATM agreement with Meyers Associates, L.P. Under the terms of the agreement, we may, from time to time, at our discretion, offer and sell shares of our common stock having an aggregate value of up to \$6.0 million. As of December 31, 2016, we have received gross proceeds of approximately \$3.1 million before issuance costs of approximately \$109,000 from the sale of 1.2 million shares of our common stock.

During the year ended December 31, 2015, we received approximately \$3.3 million from the exercise of warrants to purchase 1.5 million shares of our common stock, which warrants were issued in connection with earlier financing transactions.

During the three months ended March 31, 2015, we received gross proceeds of approximately \$1.0 million as part of an ATM agreement we entered into with Meyers Associates, L.P. in June 2014. We have completed sales under this agreement, having received total proceeds of approximately \$4.5 million before issuance costs of approximately \$206,000 from the sale of 2.0 million shares of our common stock.

In March 2014, we raised approximately \$13.9 million before issuance costs of approximately \$1.0 million through an underwritten offering of 7.2 million shares of our common stock and warrants to purchase 2.1 million shares of our common stock.

In February 2014, we issued 3.7 million shares of our common stock under the exchange provisions of the warrants issued in connection with our May and September 2013 financing activities. We recognized a loss of \$5.0 million on the exchange as the fair market value of the common stock issued was greater than the obligation recorded due to an increase in our stock price since December 31, 2013.

9. WARRANTS

The warrants to purchase 2.1 million shares of our common stock that we sold in our March 2014 offering have an exercise price of \$2.47 per share and expire on the fifth anniversary of the date of issuance.

In combination with our registered direct offerings of common stock in May 2013 and September 2013, we issued warrants to purchase common stock. At each balance sheet date that the warrants were outstanding, we evaluated the fair value of the warrants and any change in value was recorded as a non-operating gain or loss on the statement of operations. Due to the conditional exchange provision of the warrants, the determination of the fair value of the warrant liability varied depending on our common stock price.

In February 2014, we issued 3.7 million shares of our common stock under the exchange provision of our then-outstanding warrants. We did not receive additional cash consideration in the exchange transaction. We recorded a loss of \$5.0 million during the year ended December 31, 2014 on the exchange, as the fair market value of the common stock issued was greater than the obligation recorded due to the increase in stock price from December 31, 2013 to the date the warrants were exchanged.

The following table summarizes activity with respect to our common stock warrants for the periods shown below (in thousands):

	Warrants to purchase common shares	Weighted- average exercise price
Outstanding at January 1, 2014	8,091	\$ 3.07
Granted:		
Exercise price less than intrinsic value	-	-
Exercise price greater than intrinsic value	2,148	2.47
Exercised	(3,713)	2.67
Canceled/expired	-	-
Outstanding at December 31, 2014	<u>6,526</u>	3.08
Granted:		
Exercise price less than intrinsic value	-	-
Exercise price greater than intrinsic value	-	-
Exercised	(1,487)	2.19
Canceled/expired	-	-
Outstanding at December 31, 2015	<u>5,039</u>	3.34
Granted:		
Exercise price less than intrinsic value	-	-
Exercise price greater than intrinsic value	-	-
Exercised	-	-
Canceled/expired	(1,278)	6.24
Outstanding at December 31, 2016	<u><u>3,761</u></u>	\$ 2.23
Exercisable at December 31, 2016	<u><u>3,761</u></u>	\$ 2.23

There were no common stock warrants issued in 2016 or 2015.

The following table summarizes information about our common stock warrants outstanding and exercisable at December 31, 2016 (in thousands):

Range of exercise prices	Warrants outstanding			Warrants exercisable	
	Outstanding at December 31, 2016	Weighted-average remaining contractual term (in years)	Weighted-average exercise price	Exercisable at December 31, 2016	Weighted-average exercise price
\$1.76 - 3.08	3,761	1.38	\$ 2.23	3,761	\$ 2.23
	3,761			3,761	

10. SHARE-BASED COMPENSATION

We use the straight-line attribution method to allocate the fair value of share-based compensation awards over the requisite service period for each award. The valuation of and accounting for share-based awards includes a number of complex and subjective estimates. These estimates include, but are not limited to, the future volatility of our stock price, future stock option exercise behaviors, estimated employee turnover, and award forfeiture rates. We recognized \$1.2 million, \$1.0 million, and \$713,000 in share-based compensation expense for the years ended December 31, 2016, 2015, and 2014, respectively. During the year ended December 31, 2014, we reduced the share-based compensation expense by \$344,000 to adjust estimated forfeitures to actual.

Description of Incentive Plans

We currently have two share-based incentive plans; the 2013 Incentive Plan and the Independent Director Stock Option Plan.

The 2013 Incentive Plan has 7.8 million shares authorized, of which 2.0 million shares were available for awards as of December 31, 2016. The Independent Director Stock Option Plan has 113,000 shares authorized, of which 19,000 shares or awards relating thereto were issued and outstanding as of December 31, 2016. In June 2008, we determined not to issue additional options from the Independent Director Stock Option Plan.

Options Valuation Methodology and Assumptions

We use the Black-Scholes option valuation model to determine the fair value of options granted and use the closing price of our common stock as the fair market value of our stock on that date.

We consider historical stock price volatilities, volatilities of similar companies and other factors in determining estimates of future volatilities.

We use historical lives, including post-termination exercise behavior, as the basis for estimating expected lives.

Risk-free rates are based on the U.S. Treasury Yield Curve, as published by the U.S. Treasury.

The following table summarizes the weighted-average valuation assumptions and weighted-average grant date fair value of options granted during the periods shown below:

Assumptions (weighted-average)	Year Ended December 31,		
	2016	2015	2014
Volatility	84%	98%	100%
Expected term (in years)	4.0	4.0	4.0
Risk-free rate	1.2%	1.3%	1.3%
Expected dividends	0.0%	0.0%	0.0%
Pre-vest forfeiture rate	8.5%	8.5%	8.5%
Grant date fair value of options granted	\$ 1.12	\$ 2.20	\$ 1.22

Options Activity and Positions

The following table summarizes activity and positions with respect to options for the periods shown below (in thousands):

Options	Shares	Weighted-average exercise price	Weighted-average	Aggregate intrinsic value
			remaining contractual term (in years)	
Outstanding as of January 1, 2014	1,905	\$ 8.86	7.4	\$ 1,500
Granted	717	1.78	-	-
Exercised	-	-	-	-
Forfeited or expired	(195)	9.49	-	-
Outstanding as of December 31, 2014	2,427	6.72	7.4	18,700
Granted	849	3.23	-	-
Exercised	(23)	1.88	-	-
Forfeited or expired	(107)	13.98	-	-
Outstanding as of December 31, 2015	3,146	5.56	7.3	1,613
Granted	1,167	1.83	-	-
Exercised	(3)	1.77	-	-
Forfeited or expired	(307)	12.58	-	-
Outstanding as of December 31, 2016	4,003	\$ 3.94	7.3	\$ 4
Vested and expected to vest as of December 31, 2016	3,747	\$ 4.06	7.2	\$ 3
Exercisable as of December 31, 2016	2,032	\$ 5.61	5.8	\$ -

The intrinsic value of options exercised during the year ended December 31, 2016 was \$3,000 compared to \$29,000 in 2015. There were no option exercises during the year ended December 31, 2014.

The total grant date fair value of options vested during the years ended December 31, 2016, 2015 and 2014 was \$998,000, \$591,000 and \$3.3 million, respectively. As of December 31, 2016, our unamortized share-based compensation was \$2.4 million related to options, which we plan to amortize over the next 2.7 years.

As of December 31, 2016, our unamortized share-based compensation related to the RSUs was \$50,000, which we plan to amortize over the next five months.

11. COMMITMENTS AND CONTINGENCIES

Litigation

On March 31, 2014, Asia Optical Co., Inc., a supplier pursuant to an agreement entered into in 2008, filed a complaint for arbitration with the American Arbitration Association, claiming that we ordered products from them and failed to take delivery of and pay for such products. The relief sought in the complaint is \$3.6 million plus attorneys' fees, interest and arbitration costs. We contest the claim and are defending against it. An adverse outcome of these proceedings could materially and adversely affect our financial condition. At this stage, we cannot predict the likelihood of an unfavorable outcome or the range of potential loss.

We are also subject to various claims and pending or threatened lawsuits in the normal course of business. We are not currently party to any legal proceedings that management believes are reasonably possible to have a material adverse effect on our financial position, results of operations or cash flows.

Purchase commitments

At December 31, 2016, we have \$6.4 million in open purchase obligations that represent commitments to purchase inventory, materials, capital equipment, and other goods used in the normal operation of our business.

Lease commitments

We lease our office space and certain equipment under operating leases with initial or remaining terms in excess of one year. Future minimum rental commitments under operating leases for years ending December 31, are as follows (in thousands):

Years Ended December 31,	Operating leases
2017	\$ 439
2018	446
2019	38
2020	-
2021	-
Thereafter	-
Total minimum lease payments	\$ <u>923</u>

Net rent expense was \$483,000 in 2016, \$465,000 in 2015, and \$542,000 in 2014.

Adverse purchase commitments

We have periodically entered into noncancelable purchase contracts in order to ensure the availability of materials to support production of our products. We continuously assess our outstanding commitments and recognize a loss on purchase commitments, when required, if such commitments are in excess of our product needs or the costs are not expected to be recoverable. As of December 31, 2016, we have \$500,000 accrued for commitments to purchase materials for the SHOWWX™ pico projector that were in excess of estimated future proceeds from sales of that product.

12. INCOME TAXES

A provision for income taxes has not been recorded for 2016, 2015 and 2014, due to the valuation allowances placed against the net operating losses and deferred tax assets arising during such periods. A valuation allowance has been recorded for all deferred tax assets. Based on our history of losses since inception, the available objective evidence creates sufficient uncertainty regarding the realizability of the deferred tax assets.

At December 31, 2016, we have net operating loss carryforwards of approximately \$371.6 million for federal income tax reporting purposes. In addition, we have research and development tax credits of \$7.0 million. The net operating loss carryforwards and research and development credits available to offset future taxable income, if any, will expire in varying amounts from 2018 to 2036, if not previously used.

In addition to the tax benefits above, we have \$310,000 of capital loss carryforwards that are scheduled to expire in 2017. In certain circumstances, as specified in the Internal Revenue Code, a 50% or more ownership change by certain combinations of our shareholders during any three year period would result in limitations on our ability to use a portion of our net operating loss carryforwards.

Deferred tax assets are summarized as follows (in thousands):

	December 31,	
	2016	2015
Deferred tax assets, current		
Reserves	\$ 2,351	\$ 2,581
Other	910	749
Total gross deferred tax assets, current	<u>3,261</u>	<u>3,330</u>
Deferred tax assets, non-current		
Net operating loss carryforwards	126,335	122,281
R&D credit carryforwards	6,998	6,747
Depreciation/amortization deferred	20,024	20,848
Deferred revenue	2,091	-
Other	8,135	7,954
Total gross deferred tax assets, non-current	<u>163,583</u>	<u>157,830</u>
Net deferred taxes before valuation allowance	166,844	161,160
Less: Valuation allowance	<u>(166,844)</u>	<u>(161,160)</u>
Deferred tax assets	<u>\$ -</u>	<u>\$ -</u>

The valuation allowance, permanent items, and the research and development credit carryforwards account for substantially all of the difference between our effective income tax rate and the federal statutory tax rate of 34%.

Certain net operating losses arise from the deductibility for tax purposes of compensation under nonqualified stock options equal to the difference between the fair value of the stock on the date of exercise and the exercise price of the options. For financial reporting purposes, the tax effect of this deduction, when recognized, is accounted for as a credit to shareholders' equity.

We did not have any unrecognized tax benefits at December 31, 2016 or 2015.

We recognize interest accrued and penalties related to unrecognized tax benefits in tax expense. During the years ended December 31, 2016, 2015, and 2014, we did not recognize any interest or penalties.

We file income tax returns in the U.S. federal jurisdiction and various states. Due to our operating loss and credit carryforwards, the U.S. federal statute of limitations remains open for 1998 and onward.

13. RETIREMENT SAVINGS PLAN

We have a retirement savings plan that qualifies under Internal Revenue Code Section 401(k). The plan covers all qualified employees. Contributions to the plan are made at the discretion of our Board of Directors. During the years ended December 31, 2016 and 2015, we contributed \$214,000 and \$108,000 to the plan, respectively. There were no contributions to the plan during 2014.

14. QUARTERLY FINANCIAL INFORMATION (Unaudited)

The following table summarizes our unaudited quarterly financial information for the periods shown below (in thousands, except per share data):

	Fiscal Year 2016			
	December 31,	September 30,	June 30,	March 31,
Revenue	\$ 2,905	\$ 4,000	\$ 4,155	\$ 3,701
Gross profit	505	1,207	1,563	1,112
Net loss	(5,370)	(4,070)	(3,476)	(3,553)
Net loss per share, basic and diluted	(0.09)	(0.08)	(0.07)	(0.07)

	Fiscal Year 2015			
	December 31,	September 30,	June 30,	March 31,
Revenue	\$ 1,846	\$ 2,398	\$ 4,043	\$ 901
Gross profit	379	585	1,187	(143)
Net loss	(4,298)	(3,513)	(2,769)	(3,962)
Net loss per share, basic and diluted	(0.09)	(0.07)	(0.06)	(0.09)

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

There have been no changes in or disagreements with accountants on accounting or financial disclosure matters during our fiscal years ended December 31, 2016, 2015 and 2014.

ITEM 9A. CONTROLS AND PROCEDURES

(a) *Evaluation of Disclosure Controls and Procedures.* Our Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) evaluated our disclosure controls and procedures (as defined in Rules 13a-15(e)) under the Securities and Exchange Act of 1934, as amended (the “Exchange Act”), prior to the filing of this Form 10-K. Based upon that evaluation, our CEO and CFO concluded that, as of December 31, 2016, our disclosure controls and procedures were effective.

(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 such term is defined in Exchange Act Rules 13a-15(f). Our management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its evaluation under the framework in *Internal Control — Integrated Framework (2013)*, our management concluded that our internal control over financial reporting was effective as of December 31, 2016.

(c) *Limitations on the Effectiveness of Controls.* Because of 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.

The effectiveness of our internal control over financial reporting as of December 31, 2016 has been audited by Moss Adams LLP, an independent registered public accounting firm, as stated in its report, which is included herein.

(d) *Changes in Internal Control Over Financial Reporting.* There was no change in our internal control over financial reporting during the quarter ended December 31, 2016 which has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
MicroVision, Inc.

We have audited MicroVision, Inc.'s (the "Company") internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. 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. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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.

In our opinion, MicroVision, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of MicroVision, Inc. as of December 31, 2016 and 2015, and the consolidated statements of operations, shareholders' equity (deficit), and cash flows for each of the three years in the period ended December 31, 2016, and our report dated March 6, 2017 expressed an unqualified opinion on those consolidated financial statements and financial statement schedule.

/s/ Moss Adams LLP

Seattle, Washington
March 6, 2017

ITEM 9B. OTHER INFORMATION

None.

PART III.

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information regarding executive officers is included in Part I of this Annual Report on Form 10-K in Item 4A. The information required by this Item 10 of Form 10-K and not provided in Item 4A will be included under the caption “Discussion of Proposals Recommended by the Board” in our 2017 Proxy Statement and is incorporated herein by reference. Our 2017 Proxy Statement will be filed with the SEC prior to our 2017 Annual Meeting of Shareholders.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item 11 of Form 10-K will be included under the captions “Executive Compensation,” “Compensation Committee Interlocks and Insider Participation,” and “Director Compensation for 2016” in our 2017 Proxy Statement and are incorporated herein by reference.

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

Information as of December 31, 2016, regarding equity compensation plans approved and not approved by shareholders is summarized in the following table (in thousands, except per share data):

Plan Category	Equity Compensation Plan Information		
	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for further issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by shareholders	4,003	\$ 3.94	1,988
Equity compensation plans not approved by shareholders	-	-	-
Total	<u>4,003</u>		<u>1,988</u>

The other information required by this Item 12 of Form 10-K will be included under the caption “Information about MicroVision Common Stock Ownership” in our 2017 Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information required by this Item 13 of Form 10-K will be included under the captions “Certain Relationships and Related Transactions” and “Board Meetings and Committees” in our 2017 Proxy Statement and are incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item 14 of Form 10-K will be included under the caption “Independent Registered Public Accounting Firm” in our 2017 Proxy Statement and is incorporated herein by reference.

PART IV.

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(A) Documents filed as part of this Annual Report on Form 10-K:

1. Consolidated Financial Statements

- Report of Independent Registered Public Accounting Firm
- Consolidated Balance Sheets as of December 31, 2016 and 2015
- Consolidated Statements of Operations for the years ended December 31, 2016, 2015 and 2014
- Consolidated Statements of Shareholders' Equity (Deficit) for the years ended December 31, 2016, 2015 and 2014
- Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014
- Notes to Consolidated Financial Statements

2. Financial Statement Schedules

Schedule II

MicroVision, Inc.
Valuation and Qualifying Accounts and Reserves Schedule
(In thousands)

Year Ended December 31,	Balance at beginning of fiscal period	Additions		Deductions	Balance at end of fiscal period
		Charges to costs and expenses	Charges to other accounts		
2014					
Allowance for receivables from related parties	\$ 400	\$ -	\$ -	\$ -	\$ 400
Tax valuation allowance	153,301	-	3,370	-	156,671
2015					
Allowance for receivables from related parties	\$ 400	\$ -	\$ -	\$ (30)	\$ 370
Tax valuation allowance	156,671	-	4,489	-	161,160
2016					
Allowance for receivables from related parties	\$ 370	\$ -	\$ -	\$ (370)	\$ -
Tax valuation allowance	161,160	-	5,684	-	166,844

All other schedules are omitted because they are not applicable, or because the information required is included in the consolidated financial statements and notes thereto.

3. Exhibits

The following exhibits are referenced or included in this Annual Report on Form 10-K.

<u>Exhibit Number</u>	<u>Description</u>
3.1	Amended and Restated Certificate of Incorporation of MicroVision, Inc., as amended. ⁽⁴⁾
3.2	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of MicroVision, Inc. ⁽⁶⁾
3.3	Bylaws of MicroVision, Inc. ⁽⁹⁾
4.1	Form of Specimen Stock Certificate for Common Stock. ⁽¹⁾
4.2	Warrant Agreement dated June 20, 2012 by and between MicroVision, Inc. and American Stock Transfer and Trust Company, LLC. ⁽⁷⁾
4.3	Form of Warrant dated March 18, 2014 issued under the Securities Purchase Agreement dated as of March 13, 2014 by and between MicroVision, Inc. and the investors named therein. ⁽¹⁰⁾

10.1	2013 MicroVision, Inc. Incentive Plan, as amended. ^{(1)*}
10.2	Independent Director Stock Option Plan, as amended. ^{(2)*}
10.3	Employment Agreement between MicroVision, Inc. and Alexander Y. Tokman dated April 7, 2009. ⁽³⁾
10.4	Second Amendment to Lease Agreement between Arden Realty, L.P. and MicroVision, Inc., dated January 15, 2013. ⁽⁸⁾
10.5	Change of Control Severance Plan. ⁽⁵⁾
23.1	Consent of Independent Registered Public Accounting Firm – Moss Adams LLP.
31.1	Principal Executive Officer Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Principal Financial Officer Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Principal Executive Officer Certification pursuant to Rule 13a-14(b) or Rule 15d-14(b) and Section 1350, Chapter 63 of Title 18, United States Code (18 U.S.C. 1350), as adopted pursuant to Section 906 of Sarbanes-Oxley Act of 2002.
32.2	Principal Financial Officer Certification pursuant to Rule 13a-14(b) or Rule 15d-14(b) and Section 1350, Chapter 63 of Title 18, United States Code (18 U.S.C. 1350), as adopted pursuant to Section 906 of Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

- (1) Incorporated by reference to the Company's Post-Effective Amendment to Form S-3 Registration Statement, Registration No. 333-102244.
- (2) Incorporated by reference to the Company's Form 10-Q for the quarterly period ended June 30, 2002.
- (3) Incorporated by reference to the Company's Form 10-Q for the quarterly period ended March 31, 2009.
- (4) Incorporated by reference to the Company's Form 10-Q for the quarterly period ended September 30, 2009.
- (5) Incorporated by reference to the Company's Form 10-K for the year ended December 31, 2011.
- (6) Incorporated by reference to the Company's Current Report on Form 8-K filed on February 17, 2012.
- (7) Incorporated by reference to the Company's Current Report on Form 8-K filed on June 18, 2012.
- (8) Incorporated by reference to the Company's Form 10-Q for the quarterly period ended March 31, 2013.
- (9) Incorporated by reference to the Company's Current Report on Form 8-K filed on November 27, 2013.
- (10) Incorporated by reference to the Company's Current Report on Form 8-K filed on March 13, 2014.
- (11) Incorporated by reference to the Company's Form 10-Q for the quarterly period ended September 30, 2016.

† *Subject to confidential treatment.*

* *Management contracts and compensatory plans and arrangements required to be filed as exhibits pursuant to Item 15(b) of this Annual Report on Form 10-K.*

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.

MicroVision, Inc.

Date: March 6, 2017

By /s/ Alexander Y. Tokman
Alexander Y. Tokman
Chief Executive Officer and Director

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 in the following capacities on March 6, 2017.

Signature	Title
<u>/s/ Alexander Y. Tokman</u> Alexander Y. Tokman	Chief Executive Officer and Director (Principal Executive Officer)
<u>/s/ Stephen P. Holt</u> Stephen P. Holt	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
<u>/s/ Robert P. Carlile</u> Robert P. Carlile	Director
<u>/s/ Richard A. Cowell</u> Richard A. Cowell	Director
<u>/s/ Yalon Farhi</u> Yalon Farhi	Director
<u>/s/ Slade Gorton</u> Slade Gorton	Director
<u>/s/ Perry Mulligan</u> Perry Mulligan	Director
<u>/s/ Brian V. Turner</u> Brian V. Turner	Director
<u>/s/ Thomas M. Walker</u> Thomas M. Walker	Director

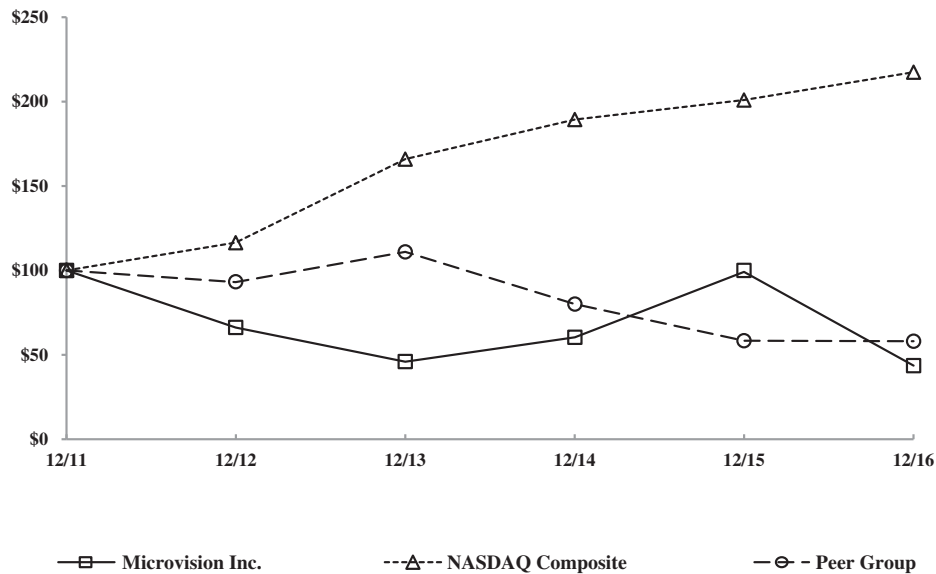
Stock Performance Graph

Comparison of 5-Year cumulative total return among MicroVision, Inc., NASDAQ Market Index, and Peer Group Index

The following graph compares the cumulative total shareholder return on an initial \$100 investment in the Company's common stock for the five fiscal years ended December 31, 2016, to two indices: The NASDAQ[®] Market Index and an index of peer companies selected by the Company ("Peer Group"). The companies in the Peer Group are eMagin Corporation, Kopin Corporation, and Neonode Inc. The graph and table assume that \$100 was invested on December 31, 2011, in the Company's common stock, the NASDAQ Market Index, and the Peer Group and that all dividends were reinvested. The past performance of the Company's common stock is not an indication of future performance. We cannot assure you that the price of the Company's common stock will appreciate at any particular rate or at all in future years.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*

Among Microvision Inc., the NASDAQ Composite Index,
and a Peer Group



*\$100 invested on 12/31/11 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

	<u>12/11</u>	<u>12/12</u>	<u>12/13</u>	<u>12/14</u>	<u>12/15</u>	<u>12/16</u>
Microvision Inc.	100.00	66.30	45.82	60.40	99.28	43.74
NASDAQ Composite	100.00	116.66	166.01	189.42	201.25	217.50
Peer Group	100.00	93.04	110.96	80.08	58.51	57.96

Corporate Information

Board of Directors	Robert P. Carlile	Retired Partner at KPMG LLP
	Yalon Farhi	Business Owner and Security Consultant
	Slade Gorton	Of Counsel, K&L Gates, LLP; Former U.S. Senator
	Perry Mulligan	Former Senior Vice President, Operations, Emulex Corporation
	Alexander Y. Tokman	President and Chief Executive Officer, MicroVision, Inc.
	Brian Turner	Former Chief Financial Officer, Coinstar, Inc.
	Thomas M. Walker	Former Executive Vice President, MicroVision, Inc.
Executive Officers	Alexander Y. Tokman	President and Chief Executive Officer
	Stephen P. Holt	Chief Financial Officer
	David J. Westgor	Vice President, General Counsel & Secretary
	Dale Zimmerman	Vice President, Research and Development
Transfer Agent	American Stock Transfer and Trust Company 59 Maiden Lane, New York, NY 10038 Shareholder Services P: 800-937-5449	
Stock Listing	MicroVision, Inc. common stock is traded on the NASDAQ Stock Market under the Symbol MVIS	
Investor Inquiries	MicroVision, Inc. Attn: Investor Relations, 6244 185th Ave NE, Suite 100, Redmond, WA 98052 P: 425-936-6847 ir@microvision.com	
Corporate Counsel	Ropes & Gray LLP Prudential Tower, 800 Boylston St., Boston, MA 02199-3600	
Independent Accountants	Moss Adams LLP 999 Third Avenue, Seattle, WA 98104-4019	



MicroVision

www.microvision.com

MicroVision, Inc. 6244 185th Ave NE, Suite 100 Redmond, WA 98052 USA Tel 425.936.MVIS (6847) Fax 425-936-6997