

INSIGNIA SYSTEMS INC/MN  
Form 10-K  
March 07, 2012  
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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM 10-K**

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

For the year ended December 31, 2011

Commission File Number 1-13471

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**INSIGNIA SYSTEMS, INC.**

(Exact name of registrant as specified in its charter)

**Minnesota**

(State or other jurisdiction of incorporation or organization)

**41-1656308**

(IRS Employer Identification No.)

**8799 Brooklyn Blvd.,  
Minneapolis, MN 55445**

(Address of principal executive offices)

**(763) 392-6200**

(Registrant's telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

|  |  |
|--|--|
| Title of each class:   | Name of each exchange on which registered: |
| Common Stock, \$.01 par value                                    | The NASDAQ Stock Market                    |
| Securities Registered Pursuant to Section 12(g) of the Act: None |  |

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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the securities Act. Yes o 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 o 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 report(s), and (2) has been subject to such filing requirements for the past 90 days. Yes  No o

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 o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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.

## Edgar Filing: INSIGNIA SYSTEMS INC/MN - 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of the last business day of the second quarter (June 30, 2011) was approximately \$52,840,000 based upon the last sale price of the registrant's Common Stock on such date.

Number of shares outstanding of Common Stock, \$.01 par value, as of February 29, 2012, was 13,602,280.

### **DOCUMENTS INCORPORATED BY REFERENCE:**

Insignia Systems, Inc. Proxy Statement to be filed for the Annual Meeting of Shareholders held on May 23, 2012 (Part II Item 5 and Part III Items 10, 11, 12, 13 and 14)

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**Forward-Looking Statements**

Statements made in this Annual Report on Form 10-K, in the Company's other SEC filings, in press releases and in oral statements to shareholders and securities analysts, which are not statements of historical or current facts, are forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results or performance of the Company to be materially different from the results or performance expressed or implied by such forward-looking statements. The words believes, expects, anticipates, seeks and similar expressions identify forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statement was made. These statements are subject to the risks and uncertainties that could cause actual results to differ materially and adversely from the forward-looking statements. These risks and uncertainties include, but are not limited to, the risks described in Part I, Item 1A.

***PART I.***

Item 1. Business

**General**

Insignia Systems, Inc., (the Company) markets in-store advertising products, programs and services to consumer packaged goods manufacturers (customers) and retailers. The Company has been in business since 1990. Since 1998, the Company has been focusing on providing in-store advertising services through the Insignia Point-Of-Purchase Services (POPS) in-store advertising program. Insignia POPS® includes the Insignia POPSign® program.

Insignia's POPSign is a national, account-specific, in-store, shelf-edge advertising program that has been shown to deliver significant sales increases. Funded by consumer packaged goods manufacturers, the program allows manufacturers to deliver vital product information to consumers at the point-of-purchase. The brand information is combined with each retailer's store-specific prices and is displayed on the retailer's unique sign format. The combining of manufacturer and retailer information produces a complete call to action that gets consumers the information they want and need to make purchasing decisions, while building store and brand equity.

For retailers, Insignia's POPSign program is a source of incremental revenue and is the first in-store advertising program that delivers a complete call to action on a product-specific and store-specific basis. For consumer packaged goods manufacturers, Insignia's POPSign program provides access to the optimum retail advertising site for their products—the retail shelf-edge. In addition, manufacturers benefit from significant sales increases, short lead times, micro-marketing capabilities, such as store-specific and multiple language options, and a wide variety of program features and enhancements that provide unique advertising advantages.

The Company's Internet address is [www.insigniasystems.com](http://www.insigniasystems.com). The Company has made all of the reports it files with the SEC available free of charge on its Web site. The Company's Web site is not incorporated by reference into this Report on Form 10-K. Copies of reports can also be obtained free of charge by requesting them from Insignia Systems, Inc., 8799 Brooklyn Boulevard, Minneapolis, Minnesota 55445; Attention: CFO; telephone 763-392-6200.

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### **Industry and Market Background**

According to Point-Of-Purchase Advertising International (POPAI), an industry non-profit trade association, more than 70% of brand purchase decisions are being made in-store. As a result, product manufacturers are constantly seeking in-store vehicles to motivate consumers to buy their branded products. The Company's market studies indicate that the shelf-edge sign represents the final and best opportunity for manufacturers to convince the consumer to buy.

Many consumers seek product information beyond price in order to make educated buying decisions. The Company's marketing studies indicate the most effective sign contains information supplied by the product manufacturer in combination with the retailer's price and design look.

### **Company Products**

#### *Insignia's POPSign Program*

Insignia's POPSign program is an in-store, shelf-edge, point-of-purchase advertising program that enables manufacturers to deliver product-specific messages quickly and accurately in designs and formats that have been pre-approved and supported by participating retailers. Insignia POPSign delivers vital product selling information from manufacturers, such as product uses and features, nutritional information, advertising tag lines and product images. The brand information is combined with the retailer's store-specific prices and is displayed on the retailer's unique sign format that includes its logo and store colors. Each sign is displayed directly in front of the manufacturer's product in the participating retailer's stores. The Company's POPSign program offers special features and enhancements, such as Advantage and Custom Advantage headers that allow manufacturers to add visibility and highlight their brand message at-shelf. The Company offers Color POPSigns with customizable, image-building full-color graphics. Insignia UltraColor® POPSigns offer 75% more area for the full-color creative than Color POPSigns.

The Company sells its POPSign programs directly to consumer packaged goods manufacturers and to Valassis Sales and Marketing Services, Inc. (Valassis) for resale to consumer packaged goods manufacturers. POPSign programs are delivered to retailers participating in the Company's POPSign retail network and to retailers under contract with Valassis and News America Marketing In-Store, LLC (News America).

Utilizing proprietary technology, the Company collects and organizes the data from manufacturers and retailers, then formats, prints and delivers the signs to its POPSign retailers and/or Valassis and News America's contracted retailers for distribution and display. Store personnel place the signs at the shelf for display cycles in participating stores in Insignia's contracted network of retailers. Personnel from a contracted third-party merchandising company place the signs at the shelf for display cycles in participating retail stores in Valassis and News America's contracted network of retailers. The Company charges manufacturers for the signs placed in stores for each cycle. Retailers are paid a fee to display the signs and for product movement data provided to Insignia. The Company pays a fee to Valassis and News America for each program provided to retailers under contract with Valassis and News America.

#### *The Impulse Retail System and SIGNright Sign System*

Prior to 1996, the Company's primary product offering was the Impulse Retail System, a system developed by an independent product design and development firm. In 1996, the Company replaced the Impulse Retail System with the SIGNright Sign System. In 1998, the Company ceased the active domestic sales of the SIGNright Sign System, and in 2011, ceased selling SIGNright cardstock.

Cardstock for the Impulse Sign System is sold by the Company in a variety of sizes and colors that can be customized to include pre-printed custom artwork, such as a retailer's logo. Approximately 3% of 2011 revenues came from the sale of cardstock. The Company expects this percentage to be comparable in future periods.

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### *Stylus Software*

In late 1993, the Company introduced Stylus; a PC-based software application used by retailers to produce signs, labels, and posters. The Stylus software allows retailers to create signs, labels and posters by manually entering the information or by importing information from a database. Approximately 2% of 2011 revenues came from the sale of Stylus products and maintenance. The Company expects this percentage to be comparable in future periods.

### *Laser Printer and Vinyl Label Supplies*

The Company provides a comprehensive offering of laser printable cardstock and vinyl labels to retailers for their in-store signage and shelf-edge product information needs. Products include adhesive and non-adhesive supplies in a variety of colors, sizes and weights. Approximately 7% of 2011 revenues came from the sale of laser printer and vinyl label supplies. The Company expects this percentage to be comparable in future periods.

### **Marketing and Sales**

The Company directly markets the Insignia POPSign program to food and drug manufacturers and retailers. By utilizing the Insignia POPSign program, these manufacturers and retailers can easily accomplish what had previously been either impossible or extremely difficult: tailoring national in-store advertising programs to regional and local needs with minimal effort. In addition to the benefits provided to manufacturers and retailers, Insignia's POPSign program provides consumers more information and clearer messages to aid in purchasing decisions. The Company believes its POPSign program is the most complete in-store advertising sign program available, benefiting consumer, retailer, and manufacturer.

The Company and Valassis are parties to an Exclusive Reseller Agreement, as amended, which defines a strategic alliance between the companies and is in effect through December 31, 2017. During 2007, Valassis received a five-year warrant to acquire 800,000 shares of Insignia's common stock. On September 1, 2010, the entire warrant was exercised using the cashless exercise alternative provided for in the warrant and 281,511 shares of common stock were issued to Valassis.

Prior to April 1998, the Company marketed the Impulse Retail System and the SIGNright Sign System through telemarketing by in-house sales personnel and independent sales representatives. In May 1998, the Company discontinued the active marketing of the systems. The Company sells cardstock and supplies related to the Impulse Sign System to U.S. and international customers.

The Company markets its Stylus software in the United States and internationally primarily through resellers that integrate Stylus as an Open Database Connectivity design and publishing component into their retail data and information management software applications.

During 2011, 2010 and 2009, foreign sales accounted for less than 1% of total net sales each year. The Company expects sales to foreign distributors will be less than 1% of total net sales in 2012.

### **Competition**

#### *Insignia's POPSign Program*

The Insignia POPSign program faces intense competition for the marketing expenditures of branded product manufacturers for at-shelf advertising-related signage. We face significant competition from News America and Valassis, which provide at-shelf advertising and promotional signage, plus other smaller competitors. Although settlement of prior litigation with News America gives the Company additional opportunities to compete by offering signs with price in specific parts of News America's retail network, the Company will continue to compete for advertising dollars with News America's other at-shelf advertising and promotional signage offerings.

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We believe the main strengths of the Insignia POPSign program in relation to its competitors are:

- the linking of manufacturers to retailers at a central coordination point
- providing a complete call to action service
- supplying product-specific and store-specific messages at the retail shelf
- delivering vital product information and store-specific prices
- short lead times
- significant sales increases

### **Patents and Trademarks**

The Company has developed and is using a number of trademarks, service marks, slogans, logos and other commercial symbols to advertise and sell its products. The Company owns U.S. registered trademarks for Insignia Systems, Inc.® (and Design), Insignia POPS®, POPS Select®, Insignia POPSign®, Insignia ShelfPOPS®, UltraColor®, Stylus®, Stylus Work Center®, SIGNright®, Impulse®, DuraSign®, I-Care®, and Check This Out® and Color POPSign.®

The Company is in the process of obtaining trademark registrations in the United States for the trademark Insignia E-POPS.

The Company licenses the right to use a patented barcode on the sign cards for the Company's Impulse Sign System. Neither revenues from this product line, nor royalties paid under the license agreement, are considered material.

Key employees are required to enter into nondisclosure and invention assignment agreements, and customers, vendors and other third parties also must agree to nondisclosure restrictions prior to disclosure of our trade secrets or other confidential or proprietary information.

### **Product Development**

Product development for Insignia's POPSign program has been conducted internally and includes the proprietary data management and operations system, as well as the current offering of point-of-purchase and other advertising products. Ongoing internal systems enhancements, as well as the development of point-of-purchase and other advertising or promotional products, will be conducted utilizing both internal and external resources as appropriate.

The Stylus software product line remains a viable application for the Company's retail customers. The Company performs development to keep Stylus current and updated to meet industry requirements.

### **Customers**

Nestle Co. and Valassis accounted for 33% and 12%, respectively, of the Company's total net sales for the year ended December 31, 2011. Valassis, Nestle Co., and General Mills, Inc. accounted for 20%, 19% and 15%, respectively, of the Company's total net sales for the year ended December 31, 2010. Valassis and General Mills, Inc. each accounted for 20% of the Company's total net sales for the year ended December 31, 2009. Valassis is a reseller of the Company's POPSign program to consumer packaged goods manufacturers.

### **Backlog**

Sales backlog on March 5, 2012 was approximately \$6.1 million, the vast majority of which is for programs running during the remainder of 2012. The orders are believed to be firm, but there is no assurance that all of the backlog will actually result in revenues. Sales backlog on March 4, 2011 was approximately \$6.0 million.

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### **Seasonality**

The Company's results of operations have fluctuated from quarter to quarter due to variations in net sales and operating expenses. There is no seasonal pattern to these fluctuations.

The results of operations fluctuate from quarter to quarter as a result of the following:

The timing of promotional events for customers;

Variations in the specific products which customers choose to advertise;

Fluctuations in advertising budgets of customers and the amounts they commit to in-store advertising;

Variations in the number of retailers in the Company's network;

Sales incentives to sales staff and strategic partners;

Minimum program level commitments to retailers; and

Professional fees related to litigation and other matters.

### **Employees**

As of March 5, 2012, the Company had 83 employees, including all full-time and part-time employees.

### **Segment Reporting**

The Company operates in a single reportable segment.

## Item 1A. Risk Factors

Our business faces significant risks, including the risks described below. If any of the events or circumstances described in the following risks occurs, our business, financial condition or results of operations could suffer, and the trading price of our common stock could decline.

### **We Are Dependent On Our Contracts with Retailers And Our Ability To Renew Those Contracts When Their Terms Expire**

On an ongoing basis, we negotiate renewals of various retailer contracts. Some of our retailer contracts require us to guarantee minimum payments. If we are unable to offer guarantees at the required levels in the new contracts, and the contracts are not renewed because of that reason or because of other reasons, it will have a material adverse effect on our operations and financial condition.

Our POPS business and results of operations could be adversely affected if the number of retailer partners decreases significantly or if the retailer partners fail to continue to perform their duties in placing and maintaining POPS signs at the shelf in their stores and providing product movement data to us.

### **Our Results Are Dependent On Our Manufacturing Partners Continued Use Of Our POPS Program**

We are largely dependent on our POPS program. Revenues from this program represented approximately 87%, 91% and 93% of total net sales for fiscal 2011, 2010 and 2009, respectively, which are purchased by branded product manufacturers. We expect the POPS program to represent a higher percentage in fiscal 2012 and future periods. Should brand manufacturers no longer perceive value in the POPS program, or if our POPS program does not continue to result in product sales increases, our business and results of operations would be adversely affected due to our heavy dependence on this program. Additionally, changes in economic conditions could result in reductions in advertising and promotional expenditures by branded product manufacturers, which, in turn, may result in decreased spending for the in-store advertising services we offer.



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**We Face Significant Competition**

We face significant competition from News America and Valassis, which provide at-shelf advertising and promotional signage. Although the settlement with News America gives us additional opportunities to compete by offering signs with price in News America's network, we will continue to compete for advertising dollars with News America's other at-shelf advertising and promotional signage offerings. News America and Valassis have significantly greater financial resources that can be used to market their products. Should our competitors succeed in obtaining more of the at-shelf advertising business from our current customers, our revenues and related operations would be adversely affected.

**Our Customers And Retailers May Be Susceptible To Changes In Economic Conditions**

Our revenues are affected by our customers' marketing and advertising spending and our revenues and results of operations may be subject to fluctuations based upon general economic conditions. Another economic downturn may reduce demand for our products and services or depress pricing of those products and services and have an adverse effect on our results of operations. Retailers may be impacted by changes in consumer spending as well, which may adversely impact our ability to renew contracts with our existing retailers as well as contract with new retailers on terms which are acceptable. In addition, if we are unable to successfully anticipate changing economic conditions, we may be unable to effectively plan for and respond to those changes, and our business could be negatively affected.

**We Have Been Involved In Major Litigation**

For the past several years, we had been involved in major litigation with News America. During 2011, the Company and News America entered into a settlement agreement to resolve the antitrust and false advertising lawsuit that had been outstanding for several years. Although the Company obtained a significant settlement in 2011, if future disputes with News America, or other companies, arise, it could have a material adverse effect on our Company. Additionally, although we are hopeful that litigation will not be a major risk to our Company going forward, mitigation of this risk factor depends, in part, on the ability of News America and us to work together under our exclusive agreement to sell signs with price into News America's network of retailers.

**Our Results Are Dependent On The Success Of Our Relationship With Valassis And Our Selling Arrangement With News America**

Our strategic alliance with Valassis offers an expanded network of retailers for placement of in-store advertising and has thus far has resulted in increased revenues for the Company. If our partnership with Valassis does not continue to be successful, our revenue levels and our participating retailer network could be adversely affected.

Additionally, our results will depend, in part, on the success of our sales and marketing efforts as News America's exclusive agent for signs with price into the News America network of retailers and upon our ability to successfully integrate the operational aspects of the programs. Additionally, if disputes with News America arise in the future regarding the operational aspects of our agreement, it could have an adverse effect on the Company.

**Our Results Of Operations May Be Subject To Significant Fluctuations**

Our quarterly and annual operating results have fluctuated in the past and may vary in the future due to a wide variety of factors including:

the addition or loss of contracts with retailers;

the timing of seasonal events for customers or the loss of customers;

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the timing of new retail stores being added;

the timing of additional selling, marketing and general and administrative expenses; and

competitive conditions in our industry.

Due to these factors, our quarterly and annual net sales, expenses and results of operations could vary significantly in the future and this could adversely affect the market price of our common stock.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

The Company currently leases approximately 41,000 square feet of office and warehouse space in suburban Minneapolis, Minnesota, through February 29, 2016. The Company believes that the 41,000 square feet of space will meet the Company's foreseeable needs.

Item 3. Legal Proceedings

On February 9, 2011, the Company and News America entered into a settlement agreement to resolve the antitrust and false advertising lawsuit that had been outstanding for several years. Pursuant to the settlement agreement, News America paid the Company \$125,000,000, and the Company paid News America \$4,000,000 in exchange for a 10-year arrangement to sell signs with price into News America's network of retailers as News America's exclusive agent.

During the year ended December 31, 2011, the Company incurred legal fees of \$1,588,000, excluding the contingent fees paid in connection with the Company's 2011 settlement with News America. The amount of legal fees and expenses incurred in connection with the lawsuit against News America were significant throughout the first half of 2011 due to trial preparation, start of the trial and settlement activities. Legal fees and expenses are expensed as incurred and are included in general and administrative expenses in the statements of operations.

The Company is subject to various other legal proceedings in the normal course of business. Management believes the outcome of these proceedings will not have a material adverse effect on the Company's financial position or results of operations.

Item 4. Mine Safety Disclosures

None

Table of Contents**PART II.**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securitiesa) **Market Information**

The Company's common stock trades on the NASDAQ Capital Market® under the symbol ISIG. The following table summarizes the high and low sale prices per share of our common stock for the periods indicated as reported on the Nasdaq System.

| 2011           | High    | Low     | 2010           | High    | Low     |
|----------------|---------|---------|----------------|---------|---------|
| First Quarter  | \$ 7.75 | \$ 6.25 | First Quarter  | \$ 6.61 | \$ 3.81 |
| Second Quarter | 7.58    | 3.68    | Second Quarter | 7.54    | 5.11    |
| Third Quarter  | 4.05    | 2.21    | Third Quarter  | 6.93    | 5.15    |
| Fourth Quarter | 2.50    | 1.77    | Fourth Quarter | 7.42    | 5.85    |

b) **Approximate Number of Holders of Common Stock**

As of March 5, 2012, the Company had one class of Common Stock beneficially held by approximately 2,100 owners.

c) **Dividends**

As of December 31, 2010, the Company had never paid a cash dividend on its common stock. On February 22, 2011, the Board declared a one-time special dividend of \$2.00 per share to shareholders of record as of April 1, 2011, paid May 2, 2011. Since this special dividend exceeded 25% of the Company's stock price, in accordance with applicable NASDAQ rules, the ex-dividend date was May 3, 2011, one day following the payment date. Outside of this special dividend, the Board of Directors presently intends to retain all earnings for use in the Company's business and does not anticipate paying cash dividends in the foreseeable future.

d) **Issuer Repurchases of Equity Securities****Stock Repurchase Plan**

On February 22, 2011, the Board of Directors authorized the repurchase of up to \$15,000,000 of the Company's common stock on or before January 31, 2012. On May 25, 2011 the Board amended the plan to increase the maximum share purchase amount from \$15,000,000 to \$20,000,000. The plan does not obligate the Company to repurchase any particular number of shares, and may be suspended at any time at the Company's discretion. The Board of Directors did not extend this plan.

Our share repurchase program activity for the three months ended December 31, 2011 was:

|                     | Total Number<br>Of Shares<br>Repurchased | Average<br>Price Paid<br>Per Share | Total Number Of<br>Shares Purchased As<br>Part Of Publicly<br>Announced Plans<br>Or Programs | Approximate Dollar<br>Value of Shares That<br>May Yet Be Purchased<br>Under The Plans<br>Or Programs |
|---------------------|--|------------------------------------|--|--|
| October 1-31, 2011  | 166,757                                  | \$ 2.33                            | 2,827,016  | \$ 4,691,000   |
| November 1-30, 2011 | 687,001                                  | 2.20                               | 3,514,017  | 3,179,000  |
| December 1-31, 2011 | 258,893                                  | 2.04                               | 3,772,910  | 2,651,000  |

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e) **Stock Performance Graph**

The following graph compares the cumulative total shareholder return on the Company's Common Stock for the five fiscal years beginning December 31, 2006 and ending December 31, 2011, with the cumulative total return on the NASDAQ Stock Market -- U.S. Index and the Russell 2000 Index over the same period (assuming the investment of \$100 in the Company's Stock, the NASDAQ Stock Market U. S. Index and the Russell 2000 Index on December 31, 2006 and the reinvestment of all dividends).

**5-Year Cumulative Total Return Comparison Among  
Insignia Systems, The NASDAQ Stock Market US Index & The Russell 2000 Index**

**Equity Compensation Plans**

The information required by Item 5 concerning compensation plans under which securities may be issued is incorporated herein by reference to the Company's proxy statement for its 2012 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed.

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The following table sets forth selected financial data for each of the five years ended December 31, 2011. The results of operations for the years ended December 31, 2011, 2010, and 2009, and the balance sheet data as of December 31, 2011 and 2010 are derived from our audited financial statements. The results of operations and balance sheet data as of and for the years ended December 31, 2008 and 2007 are derived from our audited statements that are not contained in this filing. The following information should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and with our financial statements and the related notes thereto included elsewhere in this report.

(In thousands, except per share amounts.)

| <b>For the Years Ended December 31</b>                     | <b>2011</b>           | <b>2010</b>          | <b>2009</b>          | <b>2008</b>            | <b>2007</b> |
|--|-----------------------|----------------------|----------------------|------------------------|-------------|
| Net sales  | \$ 17,233             | \$ 30,007            | \$ 28,770            | \$ 31,406              | \$ 24,431   |
| Operating income (loss)                                    | 81,632 <sup>(1)</sup> | 905                  | 3,745 <sup>(3)</sup> | (299)                  | 81          |
| Net income (loss)  | 51,089 <sup>(1)</sup> | 6,596 <sup>(2)</sup> | 3,716 <sup>(3)</sup> | (2,257) <sup>(4)</sup> | 2,343       |
| Net income (loss) per share:                               |                       |                      |                      |                        |             |
| Basic  | \$ 3.35               | \$ 0.42              | \$ 0.25              | \$ (0.15)              | \$ 0.15     |
| Diluted  | \$ 3.29               | \$ 0.39              | \$ 0.23              | \$ (0.15)              | \$ 0.14     |
| Shares used in calculation of net income (loss) per share: |                       |                      |                      |                        |             |
| Basic  | 15,229                | 15,589               | 15,139               | 15,484                 | 15,411      |
| Diluted  | 15,512                | 16,925               | 15,846               | 15,484                 | 16,186      |
| Working capital  | \$ 22,671             | \$ 12,505            | \$ 10,716            | \$ 6,396               | \$ 7,751    |
| Total assets   | 34,594                | 24,601               | 17,839               | 15,593                 | 13,340      |
| Total shareholders' equity                                 | 27,859                | 19,258               | 11,685               | 7,271                  | 9,677       |

(1) Includes a gain from litigation settlement, net, of \$89,762 related to the settlement of a lawsuit more fully described in Note 4 to the financial statements.

(2) Includes a tax benefit of \$5,674 primarily related to the release of the valuation allowance against certain deferred tax assets more fully described in Note 6 to the financial statements.

(3) Includes one-time cash proceeds of \$1,387 from the settlement of a claim against one of the Company's insurers more fully described in Note 4 to the financial statements.

(4) Includes tax expense of \$2,138 related to the increase of the valuation allowance against deferred tax assets.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the financial statements and the related notes included in this Report. This Report contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those in such forward-looking statements as a result of many factors, including those discussed in Forward-Looking Statements and elsewhere in this Report.

**Impact Of The Current Economic Environment**

The Company may be adversely affected by the economic environment in the future if spending levels of its customers are reduced or it is unable to renew contracts with existing retailers or contract with new retailers on terms which are acceptable.

Table of Contents**Results of Operations**

The following table sets forth, for the periods indicated, certain items in the Company's Statements of Operations as a percentage of total net sales.

| <b>Year Ended December 31</b>      | <b>2011</b> | <b>2010</b> | <b>2009</b> |
|------------------------------------|-------------|-------------|-------------|
| Net sales                          | 100.0%      | 100.0%      | 100.0%      |
| Cost of sales                      | 72.0        | 49.4        | 46.7        |
| Gross profit                       | 28.0        | 50.6        | 53.3        |
| Operating expenses:                |             |             |             |
| Selling                            | 33.4        | 23.6        | 23.0        |
| Marketing                          | 9.9         | 5.5         | 5.4         |
| General and administrative         | 31.9        | 18.5        | 16.7        |
| Insurance settlement proceeds      |             |             | (4.8)       |
| Gain on litigation settlement, net | (520.9)     |             |             |
| Total operating expenses           | (445.7)     | 47.6        | 40.3        |
| Operating income                   | 473.7       | 3.0         | 13.0        |
| Other income                       | 0.4         | 0.1         | 0.3         |
| Income before taxes                | 474.1       | 3.1         | 13.3        |
| Income tax (expense) benefit       | (177.6)     | 18.9        | (0.4)       |
| Net income                         | 296.5%      | 22.0%       | 12.9%       |

**Fiscal 2011 Compared to Fiscal 2010**

**Net Sales.** Net sales for the year ended December 31, 2011 decreased 42.6% to \$17,233,000 compared to \$30,007,000 for the year ended December 31, 2010.

Service revenues from our POPSign programs for the year ended December 31, 2011 decreased 44.8% to \$15,032,000 compared to \$27,231,000 for the year ended December 31, 2010. The decrease was primarily due to a 78% decrease in the number of signs placed as well as a 2% decrease in the average sign price. The expiration of the retailer contract with The Kroger Co. on December 31, 2010, had a significant impact on service revenues for the 2011 year. In 2010 and 2009, revenue recognized by advertising in Kroger stores was approximately \$9,417,000 and \$9,883,000, respectively. The impact of the arrangement to sell signs with price into News America's network of retailers is expected to be more significant in 2012.

Product sales for the year ended December 31, 2011 decreased 20.7% to \$2,201,000 compared to \$2,776,000 for the year ended December 31, 2010. The decrease was primarily due to decreased sales of laser sign card and label supplies, thermal sign card supplies and Stylus software based upon decreased demand for these products from our customers.

**Gross Profit.** Gross profit for the year ended December 31, 2011 decreased 68.2% to \$4,818,000 compared to \$15,171,000 for the year ended December 31, 2010. Gross profit as a percentage of total net sales decreased to 28.0% for 2011 compared to 50.6% for 2010.

Gross profit from our POPSign program revenues for the year ended December 31, 2011 decreased 71.0% to \$4,129,000 compared to \$14,248,000 for the year ended December 31, 2010. The decrease in gross profit from our POPSign program was primarily due to an increase in retailer expenses coupled with higher fixed costs relative to net sales. Gross profit as a percentage of POPSign program revenues decreased to 27.5% for 2011 compared to 52.3% for 2010, due primarily to the factors described above.

Gross profit from our product sales for the year ended December 31, 2011 decreased 25.4% to \$689,000 compared to \$923,000 for the year ended December 31, 2010. Gross profit as a percentage of product sales decreased to 31.3% for 2011 compared to 33.3% for 2010. The decreases were primarily due to decreased sales and the effect of fixed costs.

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### *Operating Expenses*

**Selling.** Selling expenses for the year ended December 31, 2011 decreased 18.8% to \$5,753,000 compared to \$7,082,000 for the year ended December 31, 2010, primarily due to lower commissions from lower sales volumes. Selling expenses as a percentage of total net sales increased to 33.4% in 2011 compared to 23.6% in 2010, primarily due to lower net sales in 2011.

**Marketing.** Marketing expenses for the year ended December 31, 2011 increased 4.0% to \$1,700,000 compared to \$1,635,000 for the year ended December 31, 2010, primarily due to increased staffing-related expenses. Marketing expenses as a percentage of total net sales increased to 10.0% in 2011 compared to 5.5% in 2010, primarily due to the factors described above coupled with lower net sales in 2011.

**General and Administrative.** General and administrative expenses for the year ended December 31, 2011 decreased 1.0% to \$5,495,000 compared to \$5,549,000 for the year ended December 31, 2010, primarily due to reduced legal fees of \$493,000, partially offset by increased staffing-related expenses of \$439,000. General and administrative expenses as a percentage of total net sales increased to 31.9% in 2011 compared to 18.5% in 2010, primarily due to lower net sales in 2011.

Legal fees were \$1,588,000 for the year ended December 31, 2011 compared to \$2,081,000 for the year ended December 31, 2010. The legal fees in each year were incurred primarily in connection with the News America litigation described elsewhere herein. The amount of legal fees and expenses that were incurred in connection with the lawsuit against News America were significant throughout the first half of 2011 in connection with trial preparation, commencement of the trial and settlement activities.

**Gain From Litigation Settlement, Net.** During the year ended December 31, 2011, we settled a lawsuit with News America, for which we received \$125,000,000. The \$125,000,000 settlement was reduced by contingent legal fees of \$31,250,000 that were paid by us to our lead trial counsel, as well as bonuses of \$3,988,000 that were paid to employees, which produced the net amount recorded as Gain From Litigation Settlement, Net of \$89,762,000.

**Other Income.** Other income (net) for the year ended December 31, 2011 was \$63,000 compared to other income of \$17,000 for the year ended December 31, 2010. The increase in other income (net) in 2011 was primarily the result of increased interest income on higher cash equivalent balances throughout 2011.

**Income Taxes.** During the year ended December 31, 2011, the Company recorded \$30,606,000 of tax expense. The expense was mainly the result of the gain on the settlement of litigation with News America. During the year ended December 31, 2010, the Company recorded a \$6,883,000 net release of the valuation allowance due to the taxable income as a result of the News America lawsuit settlement on February 9, 2011. In light of the settlement the Company believed it was more likely than not that these deferred tax assets would be realized in 2011.

**Net Income.** The net income for the year ended December 31, 2011 was \$51,089,000 compared to \$6,596,000 for the year ended December 31, 2010.

### **Fiscal 2010 Compared to Fiscal 2009**

**Net Sales.** Net sales for the year ended December 31, 2010 increased 4.3% to \$30,007,000 compared to \$28,770,000 for the year ended December 31, 2009.

Service revenues from our POPSign programs for the year ended December 31, 2010 increased 2.1% to \$27,231,000 compared to \$26,666,000 for the year ended December 31, 2009. The increase was primarily due to an increase of 7.1% in the average sign price, which was partially offset by a 5.2% decrease in the number of signs placed. The expiration of the retailer contract with The Kroger Co. on December 31, 2010, could have a material adverse impact on service revenues for the 2011 year. In 2010 and 2009, revenue recognized by advertising in Kroger stores was \$9,417,000 and \$9,883,000, respectively. The positive impact of the arrangement to sell signs with price into News America's network of retailers cannot be determined at this time.

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Product sales for the year ended December 31, 2010 increased 31.9% to \$2,776,000 compared to \$2,104,000 for the year ended December 31, 2009. The increase was primarily due to increased sales of laser sign card and label supplies based on increased demand for these products from one of our customers, offset by lower sales of thermal sign card supplies and Stylus software based upon decreased demand for these products from our customers.

**Gross Profit.** Gross profit for the year ended December 31, 2010 decreased 1.1% to \$15,171,000 compared to \$15,341,000 for the year ended December 31, 2009. Gross profit as a percentage of total net sales decreased to 50.6% for 2010 compared to 53.3% for 2009.

Gross profit from our POPSign program revenues for the year ended December 31, 2010 decreased 2.8% to \$14,248,000 compared to \$14,652,000 for the year ended December 31, 2009. The decrease in gross profit of \$404,000 was primarily due to an increase in retailer expenses, which more than offset the effect of increased services revenues. Gross profit as a percentage of POPSign program revenues decreased to 52.3% for 2010 compared to 55.0% for 2009, due primarily to the increase in retailer expenses.

Gross profit from our product sales for the year ended December 31, 2010 increased 34.0% to \$923,000 compared to \$689,000 for the year ended December 31, 2009. Gross profit as a percentage of product sales increased to 33.3% for 2010 compared to 32.8% for 2009. The increases were primarily due to increased sales and the effect of fixed costs.

### **Operating Expenses**

**Selling.** Selling expenses for the year ended December 31, 2010 increased 6.8 % to \$7,082,000 compared to \$6,632,000 for the year ended December 31, 2009, primarily due to increased POPs staffing levels and increased travel related expenses. Selling expenses as a percentage of total net sales increased to 23.6% in 2010 compared to 23.0% in 2009, primarily due to the factors described above.

**Marketing.** Marketing expenses for the year ended December 31, 2010 increased 6.2% to \$1,635,000 compared to \$1,540,000 for the year ended December 31, 2009, primarily due to increased staffing related expenses. Marketing expenses as a percentage of total net sales increased to 5.5% in 2010 compared to 5.4% in 2009, primarily due to the factors described above.

**General and Administrative.** General and administrative expenses for the year ended December 31, 2010 increased 15.3% to \$5,549,000 compared to \$4,811,000 for the year ended December 31, 2009, primarily due to increased staffing levels, travel related expenses, and increased legal costs related to the News America litigation. General and administrative expenses as a percentage of total net sales increased to 18.5% in 2010 compared to 16.7% in 2009, primarily due to the factors described above.

Legal fees were \$2,081,000 for the year ended December 31, 2010 compared to \$1,838,000 for the year ended December 31, 2009. The legal fees in each year were incurred primarily in connection with the News America litigation described elsewhere herein. The amount of legal fees and expenses that were incurred in connection with the lawsuit against News America were significant throughout the first half of 2011 in connection with trial preparation, commencement of the trial and settlement activities.

**Insurance Settlement Proceeds.** The Company received a payment of \$1,387,000 in the first quarter of 2009 from an insurer as part of a settlement of the Company's claim that the insurer owed the Company defense costs for claims asserted against the Company and one of its officers in the News America litigation.



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**Other Income (Expense).** Other income (net) for the year ended December 31, 2010 was \$17,000 compared to other income (net) of \$86,000 for the year ended December 31, 2009. Included in other income (net) was interest income of \$39,000 for the year ended December 31, 2010 compared to interest income of \$127,000 for the year ended December 31, 2009. Interest income for the 2010 year was lower due to significantly lower interest rates which more than offset the effect of higher average cash, cash equivalent and short-term investment balances in 2010. Lower interest expense of \$22,000 for the year ended December 31, 2010 versus \$40,000 for the year ended December 31, 2009 was due to scheduled principal payments made in 2009 to reduce amounts owed to a retailer.

**Income Taxes.** During the year ended December 31, 2010 the Company recorded a \$6,883,000 net release of the valuation allowance. The release was due to the taxable income as a result of the News America lawsuit settlement on February 9, 2011. In light of the settlement the Company believed it was more likely than not that these deferred tax assets would be realized in 2011. The Company recorded income tax expense of \$115,000 for the year ended December 31, 2009, related to alternative minimum tax liability.

**Net Income.** The net income for the year ended December 31, 2010 was \$6,596,000 compared to \$3,716,000 for the year ended December 31, 2009.

**Liquidity and Capital Resources**

The Company has financed its operations with proceeds from public and private stock sales and sales of its services and products. At December 31, 2011, working capital was \$22,671,000 compared to \$12,505,000 at December 31, 2010. During the year ended December 31, 2011, cash, cash equivalents, and short-term investments increased by \$9,506,000 from \$13,696,000 at December 31, 2010 to \$23,202,000 at December 31, 2011.

Net cash provided by operating activities during the year ended December 31, 2011 was \$58,910,000. Net income of \$51,089,000, plus non-cash adjustments of \$6,960,000 and changes in operating assets and liabilities of \$861,000 were the items that contributed to the cash provided by operating activities. The non-cash adjustments of \$6,960,000 consisted of depreciation and amortization, deferred income tax expense and stock-based compensation expense. The most significant component of the \$861,000 change in operating assets and liabilities was income tax payable. Income tax payable increased during 2011 due to the taxable income generated from the settlement with News America and the timing of the subsequent tax payments. The Company expects accounts receivable, accounts payable, accrued liabilities and deferred revenue to fluctuate during future periods depending on the level of POPSign revenues and related business activity as well as billing arrangements with customers and payment terms with retailers.

Net cash of \$5,695,000 was used in investing activities during the year ended December 31, 2011, due mainly to the acquisition of a selling arrangement and purchases of property and equipment. The acquisition of the selling arrangement of \$4,000,000 was made to expand the Company's retail network. Proceeds of \$500,000 during the year consisted entirely of redemptions of twenty-six week certificates of deposit. Purchases of property and equipment totaled \$2,195,000 during the year ended December 31, 2011 and consisted primarily of a laser die cutter to be used to expand the Company's product offerings.

Net cash of \$43,209,000 was used in financing activities during the year ended December 31, 2011. Dividends paid of \$31,335,000 and the repurchase of common stock (net) of \$17,369,000 were partially offset by net proceeds of \$3,126,000 resulting from the issuance of common stock under the employee stock purchase plan and the employee stock option plan, and excess tax benefit from stock options of \$2,369,000.

On February 9, 2011, the Company entered into a settlement agreement in its antitrust and false advertising lawsuit against News America. As part of the settlement agreement News America paid the Company \$125,000,000, less \$4,000,000 related to the Company's purchase of a ten-year selling arrangement. Litigation counsel for the Company received a contingent fee payment of \$31,250,000 which resulted in a net cash payment to the Company of \$89,750,000. After performance bonus plan payments of \$3,988,000 and estimated federal and state income taxes of \$27,762,500 (utilizing the Company's net operating loss carry forwards), net settlement proceeds were approximately \$58,000,000.

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The Board of Directors on February 22, 2011 approved a series of actions. First, the Board of Directors authorized a special \$2.00 per common share dividend which resulted in a payment of \$31,335,000. Second, the Board approved a Performance Bonus Plan, providing for the payment of \$3,988,000 to certain employees of the Company. Third, the Board authorized the repurchase of up to \$15,000,000 of the Company's common stock on or before January 31, 2012. The plan did not obligate the Company to repurchase any particular number of shares, and may be suspended at any time at the Company's discretion. On May 25, 2011, the Board amended the plan to increase the maximum share purchase amount from \$15,000,000 to \$20,000,000. The Board of Directors did not extend this plan.

The Company believes that based upon current business conditions, its existing cash balance and future cash from operations will be sufficient for its cash requirements in the foreseeable future. However, there can be no assurances that this will occur or that the Company will be able to secure additional financing from public or private stock sales or from other financing agreements if needed.

### **Critical Accounting Policies**

Our discussion of our financial condition and results of operations is based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. During the preparation of these financial statements, we are required to make estimates and assumptions that affect the reported amounts of assets, liabilities, net revenues, costs and expenses and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions, including those related to revenue recognition, allowance for doubtful accounts, income taxes, and stock-based compensation expense. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. The results of our analysis form the basis for making assumptions about 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, and the impact of such differences may be material to our financial statements.

We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our financial statements:

**Revenue Recognition.** The Company recognizes revenue from Insignia POPSigns ratably over the period of service, which is typically a two-week display cycle. We recognize revenue related to equipment, software and sign card sales at the time the products are shipped to customers. Revenue associated with maintenance agreements is recognized ratably over the life of the contract. Revenue that has been billed and not yet recognized is reflected as deferred revenue on our balance sheet.

**Allowance for Doubtful Accounts.** An allowance is established for estimated uncollectible accounts receivable. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company, the condition of the general economy and the industry as a whole and other relevant facts and circumstances. Unexpected changes in the aforementioned factors could result in materially different amounts.

**Impairment of Long-Lived Assets.** The Company periodically evaluates the carrying value of its long-lived assets for impairment indicators. If indicators of impairment are present, we evaluate the carrying value of the assets in relation to the future cash flows of the underlying operations to assess recoverability of the assets. The estimates of these future cash flows are based on assumptions and projections believed by management to be reasonable and supportable. They require management's subjective judgments and take into account assumptions about revenue and expense growth rates. Impaired assets are then recorded at their estimated fair market value.

**Income Taxes.** Deferred income taxes are determined based on the estimated future tax effects of differences between the financial statement and tax basis of assets and liabilities given the provisions of enacted tax laws. Deferred income tax provisions and benefits are based on changes to the assets or liabilities from year to year. In providing for deferred taxes, we consider tax regulations of the jurisdictions in which we operate, estimates of future taxable income, and available tax planning strategies. If tax regulations, operating results or the ability to implement tax-planning strategies vary, adjustments to the carrying value of deferred tax assets and liabilities may be required. Valuation allowances are recorded related to deferred tax assets based on the "more likely than not" criteria.

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We recognize the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

During the year ended December 31, 2011, the Company utilized the full federal net operating loss carryforward and the majority of the state net operating loss carryforward available to it as a result of the taxable income generated from the lawsuit settlement with News America on February 9, 2011.

**Stock-Based Compensation.** We measure and recognize compensation expense for all stock-based payments at fair value. We use the Black-Scholes option pricing model to determine the weighted average fair value of options and employee stock purchase plan rights. The determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as by assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

The expected terms of the options and employee stock purchase plan rights are based on evaluations of historical and expected future employee exercise behavior. The risk-free interest rate is based on the U.S. Treasury rates at the date of grant with maturity dates approximately equal to the expected life at grant date. Volatility is based on historical and expected future volatility of the Company's stock. The Company has not historically issued any dividends, beyond the one-time special dividend declared on February 22, 2011 and paid on May 2, 2011, and does not expect to in the future. Forfeitures are estimated at the time of the grant and revised, if necessary, in subsequent periods if actual forfeitures differ from estimates.

If factors change and we employ different assumptions in the valuation of grants in future periods, the compensation expense that we record may differ significantly from what we have recorded in the current period.

## **New Accounting Pronouncements**

In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2009-13, *Multiple-Deliverable Revenue Arrangements – a consensus of the FASB Emerging Issues Task Force*, that provides amendments to the criteria for separating consideration in multiple-deliverable arrangements. As a result of these amendments, multiple-deliverable revenue arrangements will be separated in more circumstances than under previous U.S. GAAP. The ASU does this by establishing a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence (VSOE) if available, third-party evidence if VSOE is not available, or estimated selling price if neither VSOE nor third-party evidence is available. A vendor will be required to determine its best estimate of selling price in a manner that is consistent with that used to determine the price to sell the deliverable on a standalone basis. This ASU also eliminates the residual method of allocation and will require that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method, which allocates any discount in the overall arrangement proportionally to each deliverable based on its relative selling price. This standard became effective for the Company in January 2011 and did not have a material impact on the Company's results of operations or financial condition.

In October 2009, the FASB issued ASU 2009-14, *Certain Revenue Arrangements That Include Software Elements – a consensus of the FASB Emerging Issues Task Force*. This ASU removes tangible products containing software components and nonsoftware components that function together to deliver the tangible product's essential functionality from the scope of the software revenue guidance in Subtopic 985-605 of the Codification. Additionally, ASU 2009-14 provides guidance on how a vendor should allocate arrangement consideration to deliverables in an arrangement that includes both tangible products and software that is not essential to the product's functionality. This standard became effective for the Company in January 2011 and did not have a material impact on the Company's results of operations or financial condition.

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In December 2009, the FASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures Topic 820 Improving Disclosures about Fair Value Measurements*. This ASU requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement as set forth in Codification Subtopic 820-10. The FASB's objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Some of the new disclosures are effective for reporting periods beginning after December 15, 2009, with the remaining new disclosures effective for reporting periods beginning after December 15, 2010. The adoption of this ASU did not have a material impact on the Company's financial statements.

In July 2010, the FASB issued ASU No. 2010-20, *Receivables Topic 310 Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, to enhance the disclosures required for financing receivables (for example, loans, trade accounts receivable, notes receivable, and receivables relating to a lessor's leveraged, direct financing, and sales-type leases) and allowances for credit losses. The amended disclosures are designed to provide more information to financial statement users regarding the credit quality of a creditor's financing receivables and the adequacy of its allowance for credit losses. The amended guidance is effective for period-end balances beginning with the first interim or annual reporting period ending on or after December 15, 2010. The amended guidance is effective for activity during a reporting period beginning on or after December 15, 2010. The Company adopted the amended guidance and it did not have a significant impact on the Company's financial statements.

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820) Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. This ASU provides a consistent definition of fair value between U.S. GAAP and International Financial Reporting Standards. Additionally, the ASU changes certain fair value measurement principles and expands the disclosures for fair value measurements. ASU 2011-04 is effective for interim and annual periods beginning after December 15, 2011 and is to be applied prospectively. The adoption of this ASU is not expected to have a material impact on the Company's financial statements.

**Contractual Obligations**

The following table summarizes the Company's contractual obligations and commercial commitments as of December 31, 2011:

**Payments due by Period**

|   | <b>Total</b> | <b>Less than<br/>1 Year</b> | <b>2-3 Years</b> | <b>4-5 Years</b> | <b>After<br/>5</b> |
|---|--------------|-----------------------------|------------------|------------------|--------------------|
| <b>Contractual obligations:</b>             |              |                             |                  |                  |                    |
| Operating leases, excluding operating costs | \$ 1,997,000 | \$ 465,000                  | \$ 958,000       | \$ 574,000       | \$                 |
| Payments to retailers*                      | 1,854,000    | 807,000                     | 1,047,000        |                  |                    |
| Purchase commitments                        | 489,000      | 436,000                     | 53,000           |                  |                    |
| Reserve for tax uncertainties               | 424,000      |                             | 424,000          |                  |                    |
| Total contractual obligations               | \$ 4,764,000 | \$ 1,708,000                | \$ 2,482,000     | \$ 574,000       | \$                 |

\*On an ongoing basis, the Company negotiates renewals of various retailer agreements, some of which provide for fixed or store-based payments rather than sign placement-based payments. Upon the completion of renewals, the annual commitment amounts could be in excess of the amounts above.

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**Off-Balance Sheet Transactions**

None.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 8. Financial Statements and Supplementary Data

**Index to Financial Statements**

The following are included on the pages indicated:

|  |       |
|--|-------|
| <u>Reports of Independent Registered Public Accounting Firms</u>                               | 21-24 |
| <u>Balance Sheets as of December 31, 2011 and 2010</u>   | 25    |
| <u>Statements of Operations for the years ended December 31, 2011, 2010 and 2009</u>           | 26    |
| <u>Statements of Shareholders' Equity for the years ended December 31, 2011, 2010 and 2009</u> | 27    |
| <u>Statements of Cash Flows for the years ended December 31, 2011, 2010 and 2009</u>           | 28    |
| <u>Notes to Financial Statements</u>   | 29    |

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**Report of Independent registered Public Accounting firm**

To the Board of Directors and Shareholders  
Insignia Systems, Inc.

We have audited the accompanying balance sheets of Insignia Systems, Inc. (a Minnesota corporation) (the Company) as of December 31, 2011 and 2010, and the related statements of operations, shareholders' equity and cash flows for each of the two years in the period ended December 31, 2011. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Insignia Systems, Inc. as of December 31, 2011 and 2010, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2011, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Insignia Systems, Inc.'s internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 7, 2012, expressed an unqualified opinion.

Minneapolis, Minnesota  
March 7, 2012

/s/ Baker Tilly Virchow Krause, LLP

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**Report of Independent registered Public Accounting firm**

Board of Directors and Shareholders  
Insignia Systems, Inc.

We have audited Insignia Systems, Inc. (a Minnesota corporation) (the Company) internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). 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 Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the effectiveness of 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, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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, Insignia Systems, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control Integrated Framework* issued by COSO.

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We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of Insignia Systems, Inc. as of December 31, 2011 and 2010, and the related statements of operations, shareholders' equity and cash flows for each of the two years in the period ended December 31, 2011, and our report dated March 7, 2012, expressed an unqualified opinion on those financial statements.

Minneapolis, Minnesota  
March 7, 2012

/s/ Baker Tilly Virchow Krause, LLP



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**Report of Independent registered Public Accounting firm**

To the Board of Directors and Shareholders  
Insignia Systems, Inc.

We have audited the Insignia Systems, Inc. (a Minnesota corporation) statements of operations, shareholders' equity and cash flows for the year ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements 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 the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of Insignia Systems, Inc. for the year ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

/s/ Grant Thornton LLP

Minneapolis, Minnesota  
March 31, 2010

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**Insignia Systems, Inc.**  
**BALANCE SHEETS**

| As of December 31   | 2011                 | 2010                 |
|---|----------------------|----------------------|
| <b>ASSETS</b>   |                      |                      |
| <b>Current Assets:</b>  |                      |                      |
| Cash and cash equivalents   | \$ 23,202,000        | \$ 13,196,000        |
| Short-term investments  |                      | 500,000              |
| Accounts receivable, net  | 2,663,000            | 3,227,000            |
| Inventories   | 321,000              | 414,000              |
| Deferred tax assets, net  | 483,000              | 151,000              |
| Prepaid expenses and other  | 1,187,000            | 360,000              |
| <b>Total Current Assets</b>   | <b>27,856,000</b>    | <b>17,848,000</b>    |
| <b>Other Assets:</b>  |                      |                      |
| Property and equipment, net   | 2,759,000            | 975,000              |
| Non-current deferred tax assets, net                                      |                      | 5,551,000            |
| Other assets, net   | 3,979,000            | 227,000              |
| <b>Total Assets</b>   | <b>\$ 34,594,000</b> | <b>\$ 24,601,000</b> |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                                |                      |                      |
| <b>Current Liabilities:</b>   |                      |                      |
| Accounts payable  | \$ 2,444,000         | \$ 2,335,000         |
| Income tax payable  | 748,000              |                      |
| <b>Accrued liabilities:</b>   |                      |                      |
| Retailer payments   | 90,000               | 1,119,000            |
| Compensation  | 1,353,000            | 809,000              |
| Legal   | 30,000               | 376,000              |
| Employee stock purchase plan  | 139,000              | 170,000              |
| Other   | 290,000              | 400,000              |
| Deferred revenue  | 91,000               | 134,000              |
| <b>Total Current Liabilities</b>  | <b>5,185,000</b>     | <b>5,343,000</b>     |
| <b>Long-Term Liabilities:</b>   |                      |                      |
| Accrued compensation  | 800,000              |                      |
| Deferred tax liabilities, net   | 326,000              |                      |
| Accrued income taxes  | 424,000              |                      |
| <b>Total Long-Term Liabilities</b>  | <b>1,550,000</b>     |                      |
| <b>Commitments and Contingencies</b>                                      |                      |                      |
| <b>Shareholders Equity:</b>   |                      |                      |
| Common stock, par value \$.01:  |                      |                      |
| Authorized shares - 40,000,000  |                      |                      |
| Issued and outstanding shares - 13,630,000 in 2011 and 15,847,000 in 2010 | 136,000              | 159,000              |
| Additional paid-in capital  | 22,418,000           | 33,548,000           |
| Retained earnings (accumulated deficit)                                   | 5,305,000            | (14,449,000)         |
| <b>Total Shareholders Equity</b>  | <b>27,859,000</b>    | <b>19,258,000</b>    |
| <b>Total Liabilities and Shareholders Equity</b>                          | <b>\$ 34,594,000</b> | <b>\$ 24,601,000</b> |

*See accompanying notes to financial statements.*

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**Insignia Systems, Inc.**  
STATEMENTS OF OPERATIONS

| Year Ended December 31                              | 2011          | 2010          | 2009          |
|---|---------------|---------------|---------------|
| Services revenues                                   | \$ 15,032,000 | \$ 27,231,000 | \$ 26,666,000 |
| Products revenues                                   | 2,201,000     | 2,776,000     | 2,104,000     |
| Total Net Sales                                     | 17,233,000    | 30,007,000    | 28,770,000    |
| Cost of services                                    | 10,903,000    | 12,983,000    | 12,014,000    |
| Cost of goods sold                                  | 1,512,000     | 1,853,000     | 1,415,000     |
| Total Cost of Sales                                 | 12,415,000    | 14,836,000    | 13,429,000    |
| Gross Profit  | 4,818,000     | 15,171,000    | 15,341,000    |
| <b>Operating Expenses:</b>                          |               |               |               |
| Selling   | 5,753,000     | 7,082,000     | 6,632,000     |
| Marketing   | 1,700,000     | 1,635,000     | 1,540,000     |
| General and administrative                          | 5,495,000     | 5,549,000     | 4,811,000     |
| Insurance settlement proceeds                       |               |               | (1,387,000)   |
| Gain from litigation settlement, net                | (89,762,000)  |               |               |
| Total Operating Expenses                            | (76,814,000)  | 14,266,000    | 11,596,000    |
| Operating Income                                    | 81,632,000    | 905,000       | 3,745,000     |
| <b>Other Income (Expense):</b>                      |               |               |               |
| Interest income                                     | 63,000        | 39,000        | 127,000       |
| Interest expense                                    |               | (22,000)      | (40,000)      |
| Other expense, net                                  |               |               | (1,000)       |
| Total Other Income                                  | 63,000        | 17,000        | 86,000        |
| Income Before Income Taxes                          | 81,695,000    | 922,000       | 3,831,000     |
| Income tax benefit (expense)                        | (30,606,000)  | 5,674,000     | (115,000)     |
| Net Income  | \$ 51,089,000 | \$ 6,596,000  | \$ 3,716,000  |
| Net income per share:                               |               |               |               |
| Basic   | \$ 3.35       | \$ 0.42       | \$ 0.25       |
| Diluted   | \$ 3.29       | \$ 0.39       | \$ 0.23       |
| Shares used in calculation of net income per share: |               |               |               |
| Basic   | 15,229,000    | 15,589,000    | 15,139,000    |
| Diluted   | 15,512,000    | 16,925,000    | 15,846,000    |
| Cash dividends declared per common share:           | \$ 2.00       | \$ 0.00       | \$ 0.00       |

*See accompanying notes to financial statements.*

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**Insignia Systems, Inc.**  
STATEMENTS OF SHAREHOLDERS' EQUITY

|                                       | Common Stock<br>Shares | Common Stock<br>Amount | Additional<br>Paid-In<br>Capital | Retained<br>Earnings<br>(Accumulated<br>Deficit) | Total         |
|---------------------------------------|------------------------|------------------------|----------------------------------|--|---------------|
| <b>Balances at December 31, 2008</b>  | 15,069,000             | \$ 151,000             | \$ 31,881,000                    | \$ (24,761,000)                                  | \$ 7,271,000  |
| Issuance of common stock, net         | 112,000                | 1,000                  | 160,000                          |  | 161,000       |
| Value of stock-based compensation     |                        |                        | 537,000                          |  | 537,000       |
| Net income                            |                        |                        |                                  | 3,716,000  | 3,716,000     |
| <b>Balances at December 31, 2009</b>  | 15,181,000             | 152,000                | 32,578,000                       | (21,045,000)                                     | 11,685,000    |
| Issuance of common stock, net         | 751,000                | 8,000                  | 727,000                          |  | 735,000       |
| Repurchase of common stock, net       | (85,000)               | (1,000)                | (468,000)                        |  | (469,000)     |
| Value of stock-based compensation     |                        |                        | 711,000                          |  | 711,000       |
| Net income                            |                        |                        |                                  | 6,596,000  | 6,596,000     |
| <b>Balances at December 31, 2010</b>  | 15,847,000             | 159,000                | 33,548,000                       | (14,449,000)                                     | 19,258,000    |
| Issuance of common stock, net         | 1,556,000              | 15,000                 | 3,111,000                        |  | 3,126,000     |
| Repurchase of common stock, net       | (3,773,000)            | (38,000)               | (17,331,000)                     |  | (17,369,000)  |
| Value of stock-based compensation     |                        |                        | 721,000                          |  | 721,000       |
| Dividends paid                        |                        |                        |                                  | (31,335,000)                                     | (31,335,000)  |
| Excess tax benefit from stock options |                        |                        | 2,369,000                        |  | 2,369,000     |
| Net income                            |                        |                        |                                  | 51,089,000                                       | 51,089,000    |
| <b>Balances at December 31, 2011</b>  | 13,630,000             | \$ 136,000             | \$ 22,418,000                    | \$ 5,305,000                                     | \$ 27,859,000 |

*See accompanying notes to financial statements.*

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**Insignia Systems, Inc.**  
STATEMENTS OF CASH FLOWS

| Year Ended December 31  | 2011          | 2010          | 2009         |
|---|---------------|---------------|--------------|
| <b>Operating Activities:</b>  |               |               |              |
| Net income  | \$ 51,089,000 | \$ 6,596,000  | \$ 3,716,000 |
| Adjustments to reconcile net income to net cash provided by operating activities: |               |               |              |
| Depreciation and amortization   | 694,000       | 339,000       | 405,000      |
| Deferred income tax expense (benefit)   | 5,545,000     | (5,702,000)   |              |
| Stock-based compensation  | 721,000       | 711,000       | 537,000      |
| Changes in operating assets and liabilities:                                      |               |               |              |
| Accounts receivable   | 564,000       | (337,000)     | (123,000)    |
| Inventories   | 93,000        | (25,000)      | 53,000       |
| Prepaid expenses and other  | (862,000)     | (151,000)     | (158,000)    |
| Accounts payable  | 109,000       | 82,000        | (496,000)    |
| Accrued liabilities   | (172,000)     | 297,000       | (1,417,000)  |
| Income tax payable  | 3,117,000     |               |              |
| Accrued income taxes  | 424,000       |               |              |
| Excess tax benefit from stock options   | (2,369,000)   |               |              |
| Deferred revenue  | (43,000)      | (971,000)     | (53,000)     |
| Net cash provided by operating activities   | 58,910,000    | 839,000       | 2,464,000    |
| <b>Investing Activities:</b>  |               |               |              |
| Purchases of property and equipment   | (2,195,000)   | (387,000)     | (278,000)    |
| Acquisition of selling arrangement  | (4,000,000)   |               |              |
| Purchases of investments  |               | (3,800,000)   | (6,300,000)  |
| Proceeds from sale of investments   | 500,000       | 7,700,000     | 1,900,000    |
| Net cash provided by (used in) investing activities                               | (5,695,000)   | 3,513,000     | (4,678,000)  |
| <b>Financing Activities:</b>  |               |               |              |
| Payment of long-term liabilities  |               | (219,000)     | (202,000)    |
| Excess tax benefit from stock options   | 2,369,000     |               |              |
| Dividends paid  | (31,335,000)  |               |              |
| Proceeds from issuance of common stock, net                                       | 3,126,000     | 735,000       | 161,000      |
| Repurchase of common stock, net   | (17,369,000)  | (469,000)     |              |
| Net cash provided by (used in) financing activities                               | (43,209,000)  | 47,000        | (41,000)     |
| Increase (decrease) in cash and cash equivalents                                  | 10,006,000    | 4,399,000     | (2,255,000)  |
| Cash and cash equivalents at beginning of year                                    | 13,196,000    | 8,797,000     | 11,052,000   |
| Cash and cash equivalents at end of year  | \$ 23,202,000 | \$ 13,196,000 | \$ 8,797,000 |
| <b>Supplemental disclosures for cash flow information:</b>                        |               |               |              |
| Cash paid during the year for income taxes  | \$ 21,762,000 | \$ 62,000     | \$ 67,000    |
| Cash paid during the year for interest  |               | 110,000       | 72,000       |
| <b>Non-cash investing and financing activities:</b>                               |               |               |              |
| Cashless exercise of options and warrants   | \$ 800,000    | \$ 3,363,000  | \$           |
| <i>See accompanying notes to financial statements.</i>                            |               |               |              |

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**Insignia Systems, Inc.**  
**Notes to Financial Statements**

1. **Summary of Significant Accounting Policies.**

**Description of Business.** Insignia Systems, Inc. (the Company) markets in-store advertising products, programs and services to retailers and consumer packaged goods manufacturers. The Company's products include the Insignia Point-of-Purchase Services (POPS) in-store advertising program, thermal sign card supplies for the Company's SIGNright and Impulse systems, Stylus software and laser printable cardstock and label supplies.

**Revenue Recognition.** Revenues are recognized by the Company when persuasive evidence of an arrangement exists, shipment has occurred, the price is fixed, and collectability is reasonably assured. The Company recognizes revenue from Insignia POPSigns ratably over the period of service. The Company recognizes revenue related to equipment, software and sign card sales at the time the products are shipped to customers. Revenue associated with maintenance agreements is recognized ratably over the life of the contract. Revenue that has been billed and not yet earned is reflected as deferred revenue on the Balance Sheet.

**Cash and Cash Equivalents.** The Company considers all highly liquid investments with an original maturity date of three months or less to be cash equivalents. Cash equivalents are stated at cost, which approximates fair value. At December 31, 2011, \$5,963,000 was invested in an overnight repurchase account and \$15,000,000 was invested in certificates of deposit. At December 31, 2010, \$5,001,000 was invested in an overnight repurchase account and \$7,400,000 was invested in certificates of deposit. The balances in cash accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents. Amounts held in checking accounts during the years ended December 31, 2011 and 2010, were fully insured under the Federal government's Temporary Liquidity Guarantee Program. Amounts held in repurchase accounts during the years ended December 31, 2011 and 2010, were invested in Ginnie Mae mortgage securities which were backed by the full faith and credit guaranty of the United States government. Bank certificates of deposit at December 31, 2011 and 2010, were held at various institutions with amounts at each institution at or below the \$250,000 insured limit of the Federal Deposit Insurance Corporation.

**Short-Term Investments.** Short-term investments consist of short-term bank certificates of deposit with original maturities of between three and twelve months. These short-term investments are classified as held to maturity and are valued at cost which approximates fair value. Bank certificates of deposit at December 31, 2010, were held at various institutions with amounts at each institution at or below the \$250,000 insured limit of the Federal Deposit Insurance Corporation.

**Fair Value of Financial Instruments.** The financial statements include the following financial instruments: cash and cash equivalents, short-term investments, accounts receivable, and accounts payable. The financial instruments approximate fair value because of the short-term nature of these instruments.

**Accounts Receivable.** The majority of the Company's accounts receivable is due from companies in the consumer packaged goods industry. Credit is extended based on evaluation of a customer's financial condition and, generally, collateral is not required. Accounts receivable are due within 30-90 days and are stated at amounts due from customers net of an allowance for doubtful accounts. Accounts receivable outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes-off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

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Changes in the Company's allowance for doubtful accounts are as follows:

| December 31          | 2011      | 2010     | 2009     |
|----------------------|-----------|----------|----------|
| Beginning balance    | \$ 8,000  | \$ 8,000 | \$ 7,000 |
| Bad debt provision   | 7,000     |          | 9,000    |
| Accounts written-off | (3,000)   |          | (8,000)  |
| Ending balance       | \$ 12,000 | \$ 8,000 | \$ 8,000 |

**Inventories.** Inventories are primarily comprised of parts and supplies for Impulse and SIGNright machines, sign cards, and roll stock. Inventory is valued at the lower of cost or market using the first-in, first-out (FIFO) method, and consists of the following:

| December 31     | 2011       | 2010       |
|-----------------|------------|------------|
| Raw materials   | \$ 74,000  | \$ 132,000 |
| Work-in-process | 12,000     | 25,000     |
| Finished goods  | 235,000    | 257,000    |
|                 | \$ 321,000 | \$ 414,000 |

**Property and Equipment.** Property and equipment is recorded at cost. Significant additions or improvements extending asset lives are capitalized, while repairs and maintenance are charged to expense when incurred. Depreciation is provided in amounts sufficient to relate the cost of assets to operations over their estimated useful lives. The straight-line method of depreciation is used for financial reporting purposes and accelerated methods are used for tax purposes. Estimated useful lives of the assets are as follows:

|                                 |           |
|---------------------------------|-----------|
| Production tooling              | 1-3 years |
| Machinery and equipment         | 5-6 years |
| Office furniture and fixtures   | 3 years   |
| Computer equipment and software | 3 years   |

Leasehold improvements are amortized over the shorter of the remaining term of the lease or estimated life of the asset.

**Impairment of Long-Lived Assets.** The Company records impairment losses on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. Impaired assets are then recorded at their estimated fair market value. There were no impairments during the years ended December 31, 2011, 2010 and 2009.

**Income Taxes.** Income taxes are accounted for under the liability method. Deferred income taxes are provided for temporary differences between the financial reporting and tax basis of assets and liabilities. Deferred taxes are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax asset will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of the enactment. It is the Company's policy to provide for uncertain tax positions and the related interest and penalties based upon management's assessment of whether a tax benefit is more likely than not to be sustained upon examination by tax authorities.

**Stock-Based Compensation.** The Company measures and recognizes compensation expense for all stock-based payments at fair value. We use the Black-Scholes option pricing model to determine the weighted average fair value of options and employee stock purchase plan rights. The determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as by assumptions regarding a number of complex and subjective variables. These variables include, but are not limited to, the expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

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The expected terms of the options and employee stock purchase plan rights are based on evaluations of historical and expected future employee exercise behavior. The risk-free interest rate is based on the U.S. Treasury rates at the date of grant with maturity dates approximately equal to the expected life at grant date. Volatility is based on historical and expected future volatility of the Company's stock. The Company has not historically issued any dividends, beyond the one-time special dividend declared on February 22, 2011, and paid on May 2, 2011, and does not expect to in the future. Forfeitures are estimated at the time of the grant and revised, if necessary, in subsequent periods if actual forfeitures differ from estimates.

If factors change and we employ different assumptions in the valuation of grants in future periods, the compensation expense that we record may differ significantly from what we have recorded in the current periods.

**Advertising Costs.** Advertising costs are charged to operations as incurred. Advertising expenses were approximately \$18,000, \$3,000 and \$11,000 during the years ended December 31, 2011, 2010 and 2009.

**Net Income Per Share.** Basic net income per share is computed by dividing net income by the weighted average shares outstanding and excludes any dilutive effects of options and warrants. Diluted net income per share gives effect to all diluted potential common shares outstanding during the year. Options to purchase approximately 764,000, 551,000 and 1,852,000 shares of common stock with weighted average exercise prices of \$6.04, \$7.44 and \$4.53 were outstanding at December 31, 2011, 2010 and 2009 and were not included in the computation of common stock equivalents because their exercise prices were higher than the average fair market value of the common shares during the reporting periods.

Weighted average common share outstanding for the years ended December 31, 2011, 2010 and 2009 were as follows:

| <b>Year ended December 31</b>   | <b>2011</b> | <b>2010</b> | <b>2009</b> |
|---|-------------|-------------|-------------|
| Denominator for basic net income per share -weighted average shares             | 15,229,000  | 15,589,000  | 15,139,000  |
| Effect of dilutive securities:  |             |             |             |
| Stock options and warrants  | 283,000     | 1,336,000   | 707,000     |
| Denominator for diluted net income per share - adjusted weighted average shares | 15,512,000  | 16,925,000  | 15,846,000  |

**Use of Estimates.** The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.



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***New Accounting Pronouncements.*** In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update ( ASU ) No. 2009-13, *Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force*, that provides amendments to the criteria for separating consideration in multiple-deliverable arrangements. As a result of these amendments, multiple-deliverable revenue arrangements will be separated in more circumstances than under previous U.S. GAAP. The ASU does this by establishing a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence ( VSOE ) if available, third-party evidence if VSOE is not available, or estimated selling price if neither VSOE nor third-party evidence is available. A vendor will be required to determine its best estimate of selling price in a manner that is consistent with that used to determine the price to sell the deliverable on a standalone basis. This ASU also eliminates the residual method of allocation and will require that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method, which allocates any discount in the overall arrangement proportionally to each deliverable based on its relative selling price. This standard became effective for the Company in January 2011 and did not have a material impact on the Company's results of operations or financial condition.

In October 2009, the FASB issued ASU 2009-14, *Certain Revenue Arrangements That Include Software Elements a consensus of the FASB Emerging Issues Task Force*. This ASU removes tangible products containing software components and nonsoftware components that function together to deliver the tangible product's essential functionality from the scope of the software revenue guidance in Subtopic 985-605 of the Codification. Additionally, ASU 2009-14 provides guidance on how a vendor should allocate arrangement consideration to deliverables in an arrangement that includes both tangible products and software that is not essential to the product's functionality. This standard became effective for the Company in January 2011 and did not have a material impact on the Company's results of operations or financial condition.

In December 2009, the FASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures Topic 820 Improving Disclosures about Fair Value Measurements*. This ASU requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement as set forth in Codification Subtopic 820-10. The FASB's objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Some of the new disclosures are effective for reporting periods beginning after December 15, 2009, with the remaining new disclosures effective for reporting periods beginning after December 15, 2010. The adoption of this ASU did not have a material impact on our financial statements.

In July 2010, the FASB issued ASU No. 2010-20, *Receivables Topic 310 Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, to enhance the disclosures required for financing receivables (for example, loans, trade accounts receivable, notes receivable, and receivables relating to a lessor's leveraged, direct financing, and sales-type leases) and allowances for credit losses. The amended disclosures are designed to provide more information to financial statement users regarding the credit quality of a creditor's financing receivables and the adequacy of its allowance for credit losses. The amended guidance is effective for period-end balances beginning with the first interim or annual reporting period ending on or after December 15, 2010. The amended guidance is effective for activity during a reporting period beginning on or after December 15, 2010. The Company adopted the amended guidance and it did not have a significant impact on the Company's financial statements.

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820) Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. This ASU provides a consistent definition of fair value between U.S. GAAP and International Financial Reporting Standards. Additionally, the ASU changes certain fair value measurement principles and expands the disclosures for fair value measurements. ASU 2011-04 is effective for interim and annual periods beginning after December 15, 2011 and is to be applied prospectively. The adoption of this ASU is not expected to have a material impact on the Company's financial statements.

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2. **Selling Arrangement.** In February 2011, the Company paid News America Marketing In-Store, LLC (News America) \$4,000,000 in exchange for a 10-year arrangement to sell signs with price into News America's network of retailers as News America's exclusive agent. The \$4,000,000 is being amortized on a straight-line basis over the 10-year term of the arrangement. Amortization expense, which was \$283,000 for the year ended December 31, 2011 and is expected to be \$400,000 per year over the next five years, is recorded within Cost of Services in the Company's Statements of Operations. The net carrying amount of the selling arrangement is recorded within Other Assets on the Company's Balance Sheets. A summary of the carrying amount of this selling arrangement is as follows as of December 31, 2011:

| Description         | Gross Cost   | Accumulated Amortization | Net Balance  |
|---------------------|--------------|--------------------------|--------------|
| Selling Arrangement | \$ 4,000,000 | \$ (283,000)             | \$ 3,717,000 |

3. **Property and Equipment.** Property and equipment consists of the following at December 31:

|   | 2011         | 2010         |
|---|--------------|--------------|
| <b>Property and Equipment:</b>              |              |              |
| Production tooling, machinery and equipment | \$ 3,908,000 | \$ 2,344,000 |
| Office furniture and fixtures               | 260,000      | 258,000      |
| Computer equipment and software             | 1,008,000    | 936,000      |
| Web site                                    | 38,000       | 38,000       |
| Leasehold improvements                      | 595,000      | 351,000      |
|   | 5,809,000    | 3,927,000    |
| Accumulated depreciation and amortization   | (3,050,000)  | (2,952,000)  |
| Net Property and Equipment                  | \$ 2,759,000 | \$ 975,000   |

Depreciation expense for the years ended December 31, 2011, 2010 and 2009 was \$411,000, \$339,000 and \$405,000, respectively.

4. **Commitments and Contingencies.**

**Operating Leases.** The Company conducts its operations in a leased facility. On March 27, 2008, the Company entered into an operating lease for its current facility which is in effect from August 2008 through February 2016. The Company had also previously leased equipment under operating lease agreements effective through September 2009. Rent expense under all of these leases, excluding operating costs, was approximately \$445,000, \$446,000 and \$451,000 for the years ended December 31, 2011, 2010 and 2009.

Minimum future lease obligations under these leases, excluding operating costs, are approximately as follows for the years ending December 31:

|      |            |
|------|------------|
| 2012 | \$ 465,000 |
| 2013 | 474,000    |
| 2014 | 484,000    |
| 2015 | 492,000    |
| 2016 | 82,000     |

**Retailer Agreements.** The Company has contracts in the normal course of business with various retailers, some of which provide for fixed or store-based payments rather than sign placement-based payments. During the years ended December 31, 2011, 2010 and 2009, the Company incurred \$1,371,000, \$3,324,000 and \$3,017,000 of costs related to fixed and store-based payments. The amounts are recorded in Cost of Services in the Company's Statements of Operations.



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Aggregate commitment amounts under agreements with retailers are approximately as follows for the years ending December 31:

|      |            |
|------|------------|
| 2012 | \$ 807,000 |
| 2013 | 791,000    |
| 2014 | 256,000    |

On an ongoing basis the Company negotiates renewals of various retailer agreements. Upon the completion of future contract renewals, the annual commitment amounts for 2012 and thereafter could be in excess of the amounts above.

**Legal.** On February 9, 2011, the Company and News America entered into a settlement agreement to resolve the antitrust and false advertising lawsuit that had been outstanding for several years. Pursuant to the Settlement Agreement, News America paid the Company \$125,000,000, and the Company paid News America \$4,000,000 in exchange for a 10-year arrangement to sell signs with price into News America's network of retailers as News America's exclusive agent (see Note 2).

A reconciliation of the settlement proceeds to the gain from litigation settlement recognized in the Company's Statements of Operations is as follows:

| Year Ended December 31               | 2011           | 2010 | 2009 |
|--------------------------------------|----------------|------|------|
| Settlement proceeds                  | \$ 125,000,000 | \$   | \$   |
| Less contingent attorney's fees      | (31,250,000)   |      |      |
| Less bonuses paid to employees       | (3,988,000)    |      |      |
| Gain from litigation settlement, net | \$ 89,762,000  | \$   | \$   |

In March 2009, the Company settled its claim against its directors and officers liability and general liability insurer and received a payment of \$1,387,000 as part of the settlement. The Company recorded the payment as Insurance Settlement Proceeds in the Statements of Operations for the year ended December 31, 2009, and the litigation with the insurers is now finished.

During the years ended December 31, 2011, 2010 and 2009, the Company incurred legal fees of \$1,588,000, \$2,081,000 and \$1,839,000. Legal fees and expenses are expensed as incurred and are included in general and administrative expenses in the Company's Statements of Operations.

The Company is subject to various other legal proceedings in the normal course of business. Management believes the outcome of these proceedings will not have a material adverse effect on the Company's financial position or results of operations.

#### 5. Shareholders' Equity.

**Warrants.** On July 2, 2007, the Company issued a warrant to purchase 800,000 shares of the Company's common stock to Valassis Sales and Marketing Services, Inc. (Valassis) at a price of \$4.04 for a term of five years. On September 1, 2010, the entire warrant was exercised using the cashless exercise alternative provided for in the warrant and 281,511 shares of common stock were issued to Valassis.

**Stock-Based Compensation.** The Company's stock-based compensation plans are administered by the Compensation Committee of the Board of Directors, which selects persons to receive awards and determines the number of shares subject to each award and the terms, conditions, performance measures and other provisions of the award.

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The following table summarizes the stock-based compensation expense which was recognized in the Company's Statements of Operations for the years ended December 31, 2011, 2010 and 2009:

| Year ended December 31     | 2011       | 2010       | 2009       |
|----------------------------|------------|------------|------------|
| Cost of sales              | \$ 135,000 | \$ 131,000 | \$ 103,000 |
| Selling                    | 190,000    | 180,000    | 120,000    |
| Marketing                  | 90,000     | 88,000     | 63,000     |
| General and administrative | 306,000    | 312,000    | 251,000    |
|                            | \$ 721,000 | \$ 711,000 | \$ 537,000 |

The Company uses the Black-Scholes option-pricing model to estimate fair value of stock-based awards with the following weighted average assumptions:

|                                     | 2011  | 2010  | 2009  |
|-------------------------------------|-------|-------|-------|
| <i>Stock Options:</i>               |       |       |       |
| Expected life (years)               | 4.51  | 3.54  | 3.57  |
| Expected volatility                 | 70%   | 55%   | 77%   |
| Dividend yield                      | 0%    | 0%    | 0%    |
| Risk-free interest rate             | 1.60% | 1.28% | 1.31% |
| <br>                                |       |       |       |
| <i>Stock Purchase Plan Options:</i> |       |       |       |
| Expected life (years)               | 1.0   | 1.0   | 1.0   |
| Expected volatility                 | 30%   | 55%   | 90%   |
| Dividend yield                      | 0%    | 0%    | 0%    |
| Risk-free interest rate             | 0.30% | 0.45% | 0.40% |

The Company uses the straight-line attribution method to recognize expense for unvested options. The amount of share-based compensation recognized during a period is based on the value of the awards that are ultimately expected to vest. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The Company will re-evaluate the forfeiture rate annually and adjust it as necessary.

As of December 31, 2011, there was \$672,000 of total unrecognized compensation costs related to the outstanding stock options which is expected to be recognized over a weighted average period of 1.2 years.

**Stock Options.** Prior to 2003 the Company had a stock option plan (the 1990 Plan) for its employees and directors under which substantially all of the shares reserved for issuance had been issued. During May 2003, the Company's shareholders approved the 2003 Incentive Stock Option Plan (the 2003 Plan), which replaced the 1990 Plan. In May 2011, the Company's shareholders voted to increase the common shares reserved for issuance from 2,875,000 to 3,175,000. Options granted under the 1990 Plan will remain in effect until they are exercised or expire according to their terms. All current option grants are made under the 2003 Plan.

Under the terms of the stock option plans, the Company grants incentive or non-qualified stock options to employees and directors generally at an exercise price at or above 100% of fair market value at the close of business on the date of grant. The stock options expire ten years after the date of grant and generally vest over three years. The Company issues new shares with stock options are exercised.

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The following table summarizes activity under the option plans:

|                              | Plan Shares<br>Available for<br>Grant | Plan Options<br>Outstanding | Weighted<br>Average<br>Exercise<br>Price Per | Aggregate<br>Intrinsic<br>Value |
|------------------------------|---------------------------------------|-----------------------------|--|---------------------------------|
| Balance at January 1, 2009   | 264,004                               | 2,497,711                   | \$ 3.50                                      |                                 |
| Reserved                     | 250,000                               |                             |  |                                 |
| Granted                      | (353,500)                             | 353,500                     | 2.88   |                                 |
| Exercised                    |                                       | (51,866)                    | 2.36   | \$ 103,000                      |
| Cancelled - 2003 Plan        | 1,101                                 | (1,101)                     | 3.88   |                                 |
| Cancelled - 1990 Plan        |                                       | (150,000)                   | 8.35   |                                 |
| Balance at December 31, 2009 | 161,605                               | 2,648,244                   | \$ 3.17                                      |                                 |
| Reserved                     | 250,000                               |                             |  |                                 |
| Granted                      | (334,500)                             | 334,500                     | 5.49   |                                 |
| Exercised                    |                                       | (350,250)                   | 2.21   | \$ 1,155,000                    |
| Cancelled - 2003 Plan        | 12,700                                | (12,700)                    | 5.48   |                                 |
| Cancelled - 1990 Plan        |                                       | (21,870)                    | 6.95   |                                 |
| Balance at December 31, 2010 | 89,805                                | 2,597,924                   | \$ 3.55                                      |                                 |
| Reserved                     | 300,000                               |                             |  |                                 |
| Granted                      | (416,450)                             | 416,450                     | 3.85   |                                 |
| Exercised                    |                                       | (1,634,671)                 | 2.31   | \$ 7,094,000                    |
| Cancelled - 2003 Plan        | 26,666                                | (26,666)                    | 4.82   |                                 |
| Cancelled - 1990 Plan        |                                       | (118,300)                   | 7.84   |                                 |
| Balance at December 31, 2011 | 21                                    | 1,234,737                   | \$ 4.87                                      |                                 |

The number of options exercisable under the option plans was:

|                   |           |
|-------------------|-----------|
| December 31, 2009 | 1,988,202 |
| December 31, 2010 | 1,994,945 |
| December 31, 2011 | 562,488   |

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The following table summarizes information about the stock options outstanding at December 31, 2011:

| Range of Exercise Prices |          | Options Outstanding |  |   | Options Exercisable |   |
|--------------------------|----------|---------------------|--|---|---------------------|---|
|                          |          | Number Outstanding  | Weighted Average Remaining Contractual | Weighted Average Exercise Price Per Share | Number Exercisable  | Weighted Average Exercise Price Per Share |
| \$ 1.92                  | \$ 2.80  | 305,055             | 7.23 years                             | \$ 2.46                                   | 175,872             | \$ 2.37                                   |
| 3.02                     | 3.79     | 101,299             | 7.58 years                             | 3.48                                      | 49,633              | 3.75                                      |
| 4.22                     |          | 321,750             | 8.83 years                             | 4.22                                      | 20,000              | 4.22                                      |
| 4.66                     |          | 3,333               | 7.94 years                             | 4.66                                      | 1,667               | 4.66                                      |
| 5.49                     |          | 287,000             | 7.83 years                             | 5.49                                      | 99,016              | 5.49                                      |
| 5.80                     | 11.36    | 216,300             | 0.58 years                             | 9.05                                      | 216,300             | 9.05                                      |
| \$ 1.92                  | \$ 11.36 | 1,234,737           | 6.65 years                             | \$ 4.87                                   | 562,488             | \$ 5.68                                   |

Options outstanding under the Option Plans expire at various dates during the period February 2012 through December 2021. Options outstanding at December 31, 2011 had a weighted average remaining life of 6.65 years and an aggregate intrinsic value of \$7,000. Options exercisable at December 31, 2011 had a weighted average remaining life of 4.60 years and an aggregate intrinsic value of \$7,000. The weighted average grant-date fair value of options granted during the years ended December 31, 2011, 2010 and 2009, were \$2.12, \$2.23 and \$1.55.

**Employee Stock Purchase Plan.** The Company has an Employee Stock Purchase Plan (the Plan) that enables employees to contribute up to 10% of their base compensation toward the purchase of the Company's common stock at 85% of its market value on the first or last day of the year. During the years ended December 31, 2011, 2010 and 2009, employees purchased 39,907, 143,493 and 59,634 shares under the Plan. At December 31, 2011, 86,176 shares are reserved for future employee purchases of common stock under the Plan. For the years ended December 31, 2011, 2010 and 2009, the Company recognized \$42,000, \$80,000 and \$77,000 of stock-based compensation expense related to the Plan.

**Dividends.** As of December 31, 2010, the Company had never paid a cash dividend on its common stock. On February 22, 2011, the Board declared a one-time special dividend of \$2.00 per share to shareholders of record as of April 1, 2011, paid May 2, 2011. Since this special dividend exceeded 25% of the Company's stock price, in accordance with applicable NASDAQ rules, the ex-dividend date was May 3, 2011, one day following the payment date. Outside of this special dividend, the Board of Directors presently intends to retain all earnings for use in the Company's business and does not anticipate paying cash dividends in the foreseeable future.

**Stock Repurchase Plan.** On February 23, 2010, the Board of Directors authorized the repurchase of up to \$2,000,000 of the Company's common stock on or before January 31, 2011. The plan did not obligate the Company to repurchase any particular number of shares, and may have been suspended at any time at the Company's discretion. At December 31, 2010, 85,000 shares had been repurchased under this plan.

On February 22, 2011, the Board of Directors authorized the repurchase of up to \$15,000,000 of the Company's common stock on or before January 31, 2012, under a new plan. On May 25, 2011, the Board amended the plan to increase the maximum share purchase amount from \$15,000,000 to \$20,000,000. The plan does not obligate the Company to repurchase any particular number of shares, and may be suspended at any time at the Company's discretion. As of January 31, 2012, the Company has repurchased a total of 3,877,000 shares totaling \$17,562,000.

During the year ended December 31, 2011, the Company repurchased shares of stock from certain executive officers and employees of the Company. These share repurchases qualify as related party transactions. The Company repurchased a total of approximately 738,000 shares from these individuals at a total amount of \$1,590,000.

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6. **Income Taxes.** The provision (benefit) for income taxes consists of the following:

| <b>Year Ended December 31</b>                  | <b>2011</b>   | <b>2010</b>    | <b>2009</b> |
|--|---------------|----------------|-------------|
| Current taxes - Federal                        | \$ 22,678,000 | \$             | \$ 86,000   |
| Current taxes - State                          | 2,383,000     | 28,000         | 29,000      |
| Deferred taxes - Federal                       | 5,226,000     | 1,086,000      | 645,000     |
| Deferred taxes - State                         | 319,000       | 95,000         | 56,000      |
| Benefit from adjustment of valuation allowance |               | (6,883,000)    | (701,000)   |
| Provision (benefit) for income taxes           | \$ 30,606,000 | \$ (5,674,000) | \$ 115,000  |

Significant components of the deferred taxes are as follows:

| <b>As of December 31</b>   | <b>2011</b>  | <b>2010</b>  |
|--|--------------|--------------|
| <b>Current Deferred Tax Assets:</b>                                    |              |              |
| Accrued compensation   | \$ 304,000   | \$           |
| Accrued expenses   | 147,000      | 119,000      |
| Inventory reserve  | 27,000       | 29,000       |
| Other  | 5,000        | 3,000        |
| Current deferred tax assets before valuation allowance                 | 483,000      | 151,000      |
| Less valuation allowance   |              |              |
| Current deferred tax assets  | \$ 483,000   | \$ 151,000   |
| <b>Long-Term Deferred Tax Assets (Liabilities):</b>                    |              |              |
| Accrued compensation   | \$ 304,000   | \$           |
| Net operating loss carryforwards                                       | 36,000       | 6,291,000    |
| Depreciation   | (692,000)    | 55,000       |
| Stock options  | 26,000       | 107,000      |
| Alternative minimum tax credits  |              | 125,000      |
| Other  |              | 3,000        |
| Long-term deferred tax assets (liabilities) before valuation allowance | (326,000)    | 6,581,000    |
| Less valuation allowance   |              | (1,030,000)  |
| Long-term deferred tax assets (liabilities)                            | \$ (326,000) | \$ 5,551,000 |

At December 31, 2010, the Company had federal net operating loss carryforwards of approximately \$18,744,000, which were fully utilized in 2011. The Company had previously determined that these carryforwards are not subject to the limitations of Internal Revenue Code Section 382 which provides limitations on the availability of net operating losses to offset current taxable income if an ownership change has occurred.

At December 31, 2010, the Company had indefinite-lived alternative minimum tax credit carryforwards of \$125,000, which were fully utilized in 2011.



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During the year ended December 31, 2010, the Company recorded a \$6,883,000 net release of the valuation allowance. The release was due to the taxable income generated from the News America lawsuit settlement on February 9, 2011. During the year ended December 31, 2009, the Company recorded a \$701,000 net release of the valuation allowance related to the utilization of loss carryforwards and determined that it was still more likely than not that none of the remaining deferred tax assets would be realized. The Company evaluates all significant available positive and negative evidence, including the existence of losses in recent years and its forecast of future taxable income, in assessing the need for a valuation allowance. The underlying assumptions the Company uses in forecasting future taxable income require significant judgment and take into account the Company's recent performance.

The tax benefit related to the partial release of the valuation allowance against deferred tax assets for the year ended December 31, 2010 was \$5,674,000. Included as part of the Company's net operating loss carryforwards at December 31, 2010 were approximately \$2,700,000 in tax deductions that resulted from the exercise of stock options. When these tax deductions were realized in 2011, the corresponding income tax benefit of the change in the valuation allowance was recorded as additional paid-in capital.

The actual tax expense attributable to income from continuing operations differs from the expected tax expense (benefit) computed by applying the U.S. federal corporate income tax rate of 35% to the net income as follows:

| Year Ended December 31            | 2011  | 2010     | 2009   |
|-----------------------------------|-------|----------|--------|
| Federal statutory rate            | 35.0% | 34.0%    | 34.0%  |
| Change in valuation allowance     |       | (674.9)  | (35.3) |
| Stock options                     | (0.2) | 19.6     | 3.0    |
| State taxes                       | 2.0   | 2.6      | 0.5    |
| Meals and entertainment           |       | 3.6      | 0.8    |
| Impact of uncertain tax positions | 0.5   |          |        |
| Other                             | 0.2   | (0.3)    |        |
| Effective federal income tax rate | 37.5% | (615.4)% | 3.0%   |

The Company has recorded a liability of \$424,000 for uncertain tax positions taken in tax returns during the year ended December 31, 2011. This liability is reflected as Accrued Income Taxes on the Company's Balance Sheets. The Company files income tax returns in the United States and numerous state and local tax jurisdictions. Tax years that are open for examination and assessment by the Internal Revenue Service are 2008 and forward. With limited exceptions, tax years prior to 2008 are no longer open in major state and local tax jurisdictions. The Company does not anticipate that the total unrecognized tax benefits will change significantly prior to December 31, 2012.

7. **Employee Benefit Plans.** The Company sponsors a Retirement Profit Sharing and Savings Plan under Section 401(k) of the Internal Revenue Code. The plan allows employees to defer up to 50% of their wages, subject to Federal limitations, on a pre-tax basis through contributions to the plan. During the years ended December 31, 2011, 2010 and 2009, the Company made a matching contribution of \$87,000, \$84,000 and \$77,000, respectively.
8. **Concentrations.**  
**Major Customers.** During the year ended December 31, 2011, two customers accounted for 33% and 12% of the Company's total net sales. At December 31, 2011, these two customers represented 30% and 12% of the Company's total accounts receivable. During the year ended December 31, 2010, three customers accounted for 20%, 19% and 15% of the Company's total net sales. At December 31, 2010, these three customers represented 11%, 26%, and 6% of the Company's total accounts receivable. During the year ended December 31, 2009, two customers each accounted for 20% of the Company's total net sales.

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Although there are a number of customers that the Company sells to, the loss of a major customer could adversely affect operating results. Additionally, the loss of a major retailer from the Company's retail network could adversely affect operating results.

**Export Sales.** Export sales accounted for less than 1% of total net sales during the years ended December 31, 2011, 2010 and 2009.

9. **Quarterly Financial Data.** (Unaudited)

Quarterly data for the years ended December 31, 2011 and 2010 was as follows:

| <b>Year Ended December 31, 2011</b> | <b>1st Quarter</b> | <b>2nd Quarter</b> | <b>3rd Quarter</b> | <b>4th Quarter</b> |
|-------------------------------------|--------------------|--------------------|--------------------|--------------------|
| Net sales                           | \$ 4,947,000       | \$ 5,026,000       | \$ 3,060,000       | \$ 4,200,000       |
| Gross profit                        | 2,036,000          | 1,938,000          | 170,000            | 674,000            |
| Net income (loss)                   | 53,873,000         | (675,000)          | (1,721,000)        | (388,000)          |
| Net income (loss) per share:        |                    |                    |                    |                    |
| Basic                               | \$ 3.37            | \$ (0.04)          | \$ (0.11)          | \$ (0.03)          |
| Diluted                             | \$ 3.17            | \$ (0.04)          | \$ (0.11)          | \$ (0.03)          |
| <b>Year Ended December 31, 2010</b> | <b>1st Quarter</b> | <b>2nd Quarter</b> | <b>3rd Quarter</b> | <b>4th Quarter</b> |
| Net sales                           | \$ 5,883,000       | \$ 8,326,000       | \$ 8,517,000       | \$ 7,281,000       |
| Gross profit                        | 2,930,000          | 4,345,000          | 4,475,000          | 3,421,000          |
| Net income (loss)                   | (435,000)          | 654,000            | 932,000            | 5,445,000          |
| Net income (loss) per share:        |                    |                    |                    |                    |
| Basic                               | \$ (0.03)          | \$ 0.04            | \$ 0.06            | \$ 0.34            |
| Diluted                             | \$ (0.03)          | \$ 0.04            | \$ 0.05            | \$ 0.32            |

10. **Subsequent Events.** On March 1, 2012, the Company enacted a plan to restructure its operations, including workforce reductions, salary adjustments and other cost-saving initiatives. The Company expects to pay approximately \$450,000 related to the restructuring in March 2012.

**Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosures**

Not applicable.

**Item 9A. Controls and Procedures**

**Disclosure Controls and Procedures**

The Company's management carried out an evaluation, under the supervision and with the participation of the Company's Chief Executive Officer (principal executive officer) and the Company's Chief Financial Officer (principal financial officer), of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of December 31, 2011, pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Company's Chief Executive Officer and the Company's Chief Financial Officer concluded that the Company's disclosure controls and procedures as of December 31, 2011 were effective. Disclosure controls and procedures ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and are designed to ensure that information required to be disclosed by us in these reports is accumulated and communicated to our management, as appropriate to allow timely decisions regarding disclosures.

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**Management's Annual Report on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate control over financial reporting, as such term is defined in Rule 13a-15(f) of the Exchange Act. Under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2011. In conducting its evaluation, our management used the criteria set forth by the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation management believes our internal control over financial reporting was effective as of December 31, 2011.

Baker Tilly Virchow Krause, LLP, an independent registered public accounting firm, has issued an attestation report on our internal control over financial reporting as of December 31, 2011. The attestation report of Baker Tilly Virchow Krause, LLP, on our internal control over financial reporting as of December 31, 2011 is included in Part II, Item 8 under Reports of Independent Registered Public Accounting Firm and is incorporated by reference herein.

**Changes in Internal Control Over Financial Reporting**

No changes in the Company's internal control over financial reporting have occurred during the fourth quarter of 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None.

**PART III.**

Item 10. Directors, Executive Officers and Corporate Governance

The information required by Item 10 concerning the directors and executive officers of the Company and corporate governance is incorporated herein by reference to the Company's proxy statement for its 2012 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed.

Item 11. Executive Compensation

The information required by Item 11 is incorporated herein by reference to the Company's proxy statement for its 2012 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by Item 12 is incorporated herein by reference to the Company's proxy statement for its 2012 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed.

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Item 13. Certain Relationships and Related Transactions and Director Independence

The information required by Item 13 is incorporated herein by reference to the Company's proxy statement for its 2012 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed.

Item 14. Principal Accountant Fees and Services

The information required by Item 14 is incorporated herein by reference to the Company's proxy statement for its 2012 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed.

Table of Contents**PART IV.**Item 15. Exhibits and Financial Statement Schedules

The following financial statements of Insignia Systems, Inc. are included in Item 8:

Reports of Independent Registered Public Accounting Firms  
Balance Sheets as of December 31, 2011 and 2010  
Statements of Operations for the years ended December 31, 2011, 2010 and 2009  
Statements of Shareholders' Equity for the years ended December 31, 2011, 2010 and 2009  
Statements of Cash Flows for the years ended December 31, 2011, 2010 and 2009  
Notes to Financial Statements

## (a) Exhibits

| Exhibit Number | Description   | Incorporation By Reference To   |
|----------------|---|---|
| 3.1            | Articles of Incorporation of Registrant, as amended to date   | Exhibit 3.1 of the Registrant's Registration Statement on Form S-18, Reg. No. 33-40765C   |
| 3.2            | Bylaws, as amended to date  | Exhibit 3.1 of the Registrant's Form 8-K filed February 23, 2007  |
| 4.1            | Specimen Common Stock Certificate of Registrant   | Exhibit 4.1 of the Registrant's Registration Statement on Form S-18, Reg. No. 33-40765C   |
| 10.1           | The Company's 1990 Stock Plan, as amended   | Exhibit 10.3 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2001  |
| 10.2           | Employee Stock Purchase Plan, as amended  | Exhibit 4.2 of the Registrant's Registration Statement on Form S-8, Reg. No. 333-161311   |
| 10.3           | The Company's 2003 Incentive Stock Option Plan, as amended  | Exhibit 4.1 of the Registrant's Registration Statement on Form S-8, Reg. No. 333-168715   |
| 10.4           | Amended Change in Control Severance Agreement with Scott F. Drill dated May 26, 2010  | Exhibit 10.1 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2010   |
| 10.5           | Amended Change in Control Severance Agreement with Justin W. Shireman dated May 26, 2010  | Exhibit 10.2 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2010   |
| 10.6           | Exclusive Reseller Agreement between Valassis Sales & Marketing Services, Inc. and the Company entered into as of June 12, 2006                               | Exhibit 10.1 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2006 (Confidential treatment has been requested for portions of the Agreement pursuant to Rule 24b-2.) |
| 10.7           | Amendment #1 dated December 6, 2006 to the Exclusive Reseller Agreement dated June 12, 2006 between Valassis Sales & Marketing Services, Inc. and the Company | Exhibit 10.1 of the Registrant's Form 10-K/A for the year ended December 31, 2008 (Confidential treatment has been requested for portions of the Amendment pursuant to Rule 24b-2.)       |
| 10.8           | Amended Change in Control Severance Agreement with Scott J. Simcox dated May 26, 2010   | Exhibit 10.3 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2010   |

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| Exhibit Number | Description   | Incorporation By Reference To   |
|----------------|---|---|
| 10.9           | Amended Change in Control Severance Agreement with Alan Jones dated May 26, 2010  | Exhibit 10.4 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2010   |
| 10.10          | Amended Change in Control Severance Agreement with A. Thomas Lucas dated May 26, 2010   | Exhibit 10.5 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2010   |
| 10.11          | Amendment #2 dated July 2, 2007 to Exclusive Reseller Agreement dated June 12, 2006 between Valassis Sales & Marketing Services, Inc. and the Company   | Exhibit 10.1 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2007 (Confidential treatment has been requested for portions of the Amendment pursuant to Rule 24b-2.) |
| 10.12          | Form of Warrant dated July 2, 2007 to purchase shares of common stock issued to Valassis Sales & Marketing Services, Inc. by the Company per Amendment #2 to the Exclusive Reseller Agreement | Exhibit 10.2 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2007   |
| 10.13          | Lease Agreement between the Company and the Landlord (Opus Northwest L.L.C.) dated March 27, 2008 (Exhibits Omitted)  | Exhibit 10.22 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2007   |
| 10.14          | 2010 Executive Officer Incentive Bonus Plan   | Exhibit 99.1 of the Registrant's Form 8-K filed June 2, 2010  |
| 10.15          | Change in Control Severance Agreement with John C. Gonsior dated June 13, 2011  | Exhibit 10.1 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2011   |
| 10.16          | Exclusive Agreement for Sale and Implementation of Specified Signs with Price approved June 6, 2011 (confidential treatment requested)  | Exhibit 10.2 of the Registrant's Form 10-Q for the quarterly period ended June 30, 2011   |
| 10.17          | Settlement Agreement and Release with News America Marketing In-Store, LLC, dated February 9, 2011, including exhibits (confidential treatment requested)                                     | Exhibit 10.1 of the Registrant's Form 10-Q for the quarterly period ended March 31, 2011  |
| 14             | Code of Ethics  | Exhibit 14 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2003  |
| 23.1           | Consent of Independent Registered Public Accounting Firm  | Filed herewith  |
| 23.2           | Consent of Independent Registered Public Accounting Firm  | Filed herewith  |
| 31.1           | Certification of Principal Executive Officer  | Filed herewith  |
| 31.2           | Certification of Principal Financial Officer  | Filed herewith  |
| 32             | Section 1350 Certification  | Filed herewith  |

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**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.

By: /s/ Scott F. Drill  
Scott F. Drill  
President and CEO

Dated: March 7, 2012

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

| Signature                                  | Title   | Date          |
|--|---|---------------|
| /s/ Scott F. Drill<br>Scott F. Drill       | President, Chief Executive Officer (principal executive officer) Secretary and Director                       | March 7, 2012 |
| /s/ John C. Gonsior<br>John C. Gonsior     | Vice President of Finance, Chief Financial Officer (principal financial and accounting officer) and Treasurer | March 7, 2012 |
| /s/ David L. Boehnen<br>David L. Boehnen   | Director  | March 7, 2012 |
| /s/ Peter V. Derycz<br>Peter V. Derycz     | Director  | March 7, 2012 |
| /s/ Donald J. Kramer<br>Donald J. Kramer   | Director  | March 7, 2012 |
| /s/ Reid V. MacDonald<br>Reid V. MacDonald | Director  | March 7, 2012 |
| /s/ Gordon F. Stofer<br>Gordon F. Stofer   | Director  | March 7, 2012 |