McGladrey

Independent Auditor's Review Report

To the Audit Committee
Costar Technologies, Inc.
Coppell, Texas

Report on the Financial Statements

We have reviewed the accompanying consolidated balance sheet of Costar Technologies, Inc. and subsidiaries as of September 30, 2014, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the three-month and nine-month periods then ended. The consolidated statements of operations, changes in stockholders' equity and cash flows of Costar Technologies, Inc. and subsidiaries for the three-month and nine-month period ended September 30, 2013, were compiled by other accountants whose report dated November 14, 2013, did not express an opinion or provide any assurance on those statements. The accompanying consolidated statements of operations, changes in stockholders' equity and cash flows of Costar Technologies, Inc. and subsidiaries for the three-month and nine-month periods ended September 30, 2013 were not reviewed by us, and accordingly, we do not express any form of assurance on those statements. The consolidated balance sheet of the Company as of December 31, 2013, and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for the year then ended (not presented herein), were reviewed by other accountants whose report dated March 31, 2014, stated that they were not aware of any material modifications that should be made to the financial statements in order for them to be in conformity with accounting principles generically accepted in the United States of America.

Management's Responsibility

The Company's management is responsible for the preparation and fair presentation of the interim financial information in accordance with accounting principles generally accepted in the United States of America; this responsibility includes the design, implementation, and maintenance of internal control sufficient to provide a reasonable basis for the preparation and fair presentation of interim financial information in accordance with generally accepted accounting principles.

Auditor's Responsibility

Our responsibility is to conduct our review in accordance with auditing standards generally accepted in the United States of America applicable to reviews of interim financial information. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the financial information. Accordingly, we do not express such an opinion.

Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim financial information for it to be in accordance with accounting principles generally accepted in the United States of America.

McGladrey LLP

Dallas, Texas
November 14, 2014

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES

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COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(AMOUNTS SHOWN IN THOUSANDS)

	September 30, 2014	December 31, 2013
ASSETS		
Current assets		
Cash	$ 166	$ 1,637
Accounts receivable, less allowance for doubtful accounts of $75 in 2014 and 2013	5,797	2,136
Inventories, net of reserve for obsolescence of $286 and $379 in 2014 and 2013, respectively	7,605	7,180
Promissory note - current		86
Prepaid expenses	298	207
Total current assets	13,866	11,246
Non-current assets		
Property and equipment, net	442	69
Deferred financing costs, net	111	
Trade names, net	2,523	925
Distribution agreement, net	862	918
Customer relationships, net	1,181	80
Covenant not to compete	20	14
Goodwill	1,921	
Total assets	$ 20,926	$ 13,252
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 1,953	$ 2,448
Accrued expenses and other	1,373	832
Line of credit	1,766	
Short-term debt	600	
Contingent purchase price	333	
Total current liabilities	6,025	3,280
Long-Term liabilities		
Deferred tax liability	79	
Long-term debt	2,250	
Total long-term liabilities	2,329	
Total liabilities	8,354	3,280
Stockholders' Equity		
Preferred stock		
Common stock	3	3
Additional paid in capital	156,041	155,912
Accumulated deficit	(138,951)	(141,422)
Less common stock held in treasury	(4,521)	(4,521)
Total stockholders' equity	12,572	9,972
Total liabilities and stockholders' equity	$ 20,926	$ 13,252

See independent accountants' review report and notes to consolidated financial statements.

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(AMOUNTS SHOWN IN THOUSANDS)

	For the Three Months Ended September 30, 2014	2013	For the Nine Months Ended September 30, 2014	2013
Net revenues	$ 8,976	$ 8,617	$ 25,559	$ 22,145
Cost of revenues	5,343	6,051	15,990	15,601
Gross profit	3,633	2,566	9,569	6,544
Selling, general and administrative expenses	2,413	1,506	5,805	4,435
Engineering and development expense	606		734	
Transaction and related expense	153		397	
	3,172	1,506	6,936	4,435
Income from operations	461	1,060	2,633	2,109
Other income (expenses)				
Interest expense	(44)		(54)	(51)
Other income and expense, net		4	3	40
Total other income (expenses), net	(44)	4	(51)	(11)
Income before taxes	417	1,064	2,582	2,098
Current income tax provision		14	32	14
Deferred income tax provision	8		79	
Net income	$ 409	$ 1,050	$ 2,471	$ 2,084
Net income per share:				
Basic	$ 0.28	$ 0.72	$ 1.69	$ 1.43
Diluted	$ 0.26	$ 0.69	$ 1.59	$ 1.38
Weighted average shares outstanding				
Basic	1,462	1,457	1,462	1,453
Diluted	1,550	1,518	1,550	1,514

See independent accountants' review report and notes to consolidated financial statements.

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(AMOUNTS SHOWN IN THOUSANDS)

For the Nine Months Ended September 30, 2014 and 2013

	Common Stock		Additional Paid - In	Treasury Stock		Accumulated	Total Stockholders'
	Shares	Amount	Capital	Shares	Amount	Deficit	Equity
Balances at December 31, 2012	1,680	$ 2	$ 155,893	233	$ (4,523)	$ (143,329)	$ 8,043
Net income						2,084	2,084
Liquidation of treasury stock				(7)	2		2
Exercise of stock options	4	1	4				5
Stock based compensation			13				13
Balances at September 30, 2013	1,684	$ 3	$ 155,910	226	$ (4,521)	$ (141,245)	$ 10,147
Balances at December 31, 2013	1,684	$ 3	$ 155,912	226	$ (4,521)	$ (141,422)	$ 9,972
Net income						2,471	2,471
Exercise of stock options	6		21				21
Stock based compensation			108				108
Balances at September 30, 2014	1,690	$ 3	$ 156,041	226	$ (4,521)	$ (138,951)	$ 12,572

See independent accountants' review report and notes to consolidated financial statements.

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(AMOUNTS SHOWN IN THOUSANDS)

For the Nine Months Ended September 30,	2014	2013
Cash flows from operating activities		
Net income	$ 2,471	$ 2,084
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock based compensation	108	13
Depreciation and amortization	239	113
Amortization of deferred financing costs	14	
Provision for obsolete inventory	(93)	8
Deferred tax liability	79	
Changes in operating assets and liabilities, net of acquisition:		
Accounts receivable, net	(1,555)	(1,222)
Inventories, net	3,227	97
Promissory note	86	151
Prepaid expenses	123	(312)
Accounts payable	(928)	837
Accrued expenses and other	315	700
Net cash provided by operating activities	4,086	2,469
Cash flows from investing activities		
Purchase of property and equipment	(45)	(2)
Long term note related to the sale of Sielox, LLC assets		172
Acquisition of CohuHD	(9,886)	
Net cash used in investing activities	(9,931)	170
Cash flows from financing activities		
Deferred financing costs	(125)	
Contingent purchase price	(137)	
Proceeds (repayment) on lines of credit	1,766	(170)
Proceeds from term debt	3,000	
Payments toward term debt	(150)	
Common stock		1
Exercise of stock options	20	4
Liquidation of Treasury Stock		2
Net cash provided by (used in) financing activities	4,374	(163)
Net increase (decrease) in cash	(1,471)	2,476
Cash, beginning of period	1,637	114
Cash, end of period	$ 166	$ 2,590
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	$ 54	$ 51
Cash paid during the period for taxes	$ 41	$ 41

See independent accountants' review report and notes to consolidated financial statements.

1. Nature of operations

Costar Technologies, Inc. (“Costar Technologies”) was incorporated in the State of Delaware in February 1997 under the name “Fairmarket, Inc.”. Costar Technologies, and its wholly owned subsidiaries, Costar Video Systems, LLC (“Costar”) and LQ Corporation (“LQ”) (collectively the “Company”), develops, designs and distributes a range of security solution products such as surveillance cameras, lenses, digital video recorders and high speed domes. The Company also develops, designs and distributes industrial vision products to observe repetitive production and assembly lines, thereby increasing efficiency by detecting faults in the production process.

Effective June 6, 2014, the Company and its newly formed, wholly owned subsidiary, Sirius Acquisition, LLC purchased CohuHD, the camera products and video solutions division of Cohu, Inc. On June 13, 2014, the name of Sirius Acquisition, LLC was changed to CohuHD Costar, LLC (“CohuHD Costar”). CohuHD Costar is a leading provider of video cameras and related products, specializing in IP video solutions for traffic monitoring, security, surveillance and military applications; and accessories such as cables, camera mounts, lenses and data storage devices (See Note 3).

2. Summary of significant accounting policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and include the accounts of Costar Technologies and its wholly owned subsidiaries. All material intercompany transactions have been eliminated in consolidation.

These consolidated financial statements were approved by management and available for issuance on November 14, 2014. Subsequent events have been evaluated through this date.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents

The Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. As of September 30, 2014 and December 31, 2013, the Company had no such cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded at net realizable values. The Company maintains an allowance for estimated losses resulting from the failure of customers to make required payments and for anticipated returns. The allowance is based on specific facts and circumstances surrounding individual customers as well as historical experience. Provisions for losses on receivables and returns are charged to income to maintain the allowance at a level considered adequate to cover losses and future returns. Receivables are charged off against the reserve when they are deemed uncollectible and returns are charged off against the reserve when the actual returns are incurred.

(AMOUNTS SHOWN IN THOUSANDS)

2. Summary of significant accounting policies (continued)

Inventories

Inventories are recorded on the first in first out basis and are stated at the lower of average cost, standard cost, or market. A provision is made to reduce excess or obsolete inventories to their net realizable value. The reserve for inventory obsolescence was $286 and $379 as of 2014 and 2013, respectively.

	September 30, 2014		December 31, 2013	
Parts, components, and materials	$	1,847		
Work-in-process		732		
Finished products		5,026	$	7,180
Total Inventory	$	7,605	$	7,180

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is computed using the straight-line method over estimated useful lives of 3-5 years as follows.

Computer hardware and software	3 years
Furniture and fixtures	5 years
Leasehold improvements	Shorter of lease term or asset useful life

Intangible Assets

In accordance with GAAP, intangible assets with indefinite lives are not amortized, but instead tested for impairment. Intangible assets are reviewed for impairment at least annually or whenever events or changes in circumstances indicate the carrying value of the assets may not be recoverable. Impairment losses are recognized if the fair value of the intangible asset is less than its carrying value.

Intangible assets with finite lives are amortized over their estimated useful lives. These intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. A loss is recognized in the consolidated statements of operations if it is determined that an impairment exists based on expected future undiscounted cash flows. The amount of the impairment is the excess of the carrying amount of the impaired asset over its fair value.

Goodwill

Goodwill is tested annually for impairment, or sooner when circumstances indicate an impairment may exist. The Company has elected to first perform a qualitative assessment, based on the entity's events and circumstances, to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The results of this qualitative assessment determine whether it is necessary to perform the two-step impairment test. No indicators warranting reevaluation arose during the three months ended September 30, 2014.

2. Summary of significant accounting policies (continued)

Long-Lived Assets

In accordance with GAAP, the Company reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. A loss is recognized on the consolidated statements of operations if it is determined that an impairment exists based on expected future undiscounted cash flows. The amount of the impairment is the excess of the carrying amount of the impaired asset over its fair value.

Fair Value Measurements

During the second quarter of 2014, the Company adopted FASB ASC 820, Fair Value Measurements and Disclosures, which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. This accounting standard does not require any new fair value measurements. The Company applies fair value accounting for all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis. The Company defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, which are required to be recorded at fair value, the Company considers the principal or most advantageous market in which the Company would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions and credit risk. (See Note 4)

Revenue Recognition

The Company ships and invoices its sales in accordance with signed purchase orders. The Company only recognizes revenue when it is realized and earned when the following criteria are met: there is evidence of an agreement; delivery has occurred; the selling price is fixed or determinable; and collectability is reasonably assured. The Company considers criteria to have been met when goods are shipped in accordance with signed purchase orders. Any software imbedded in the products sold is considered incidental to the product being sold.

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), to supersede nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity is expected to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than required under existing U.S. GAAP, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each performance obligation. ASU 2014-09 is effective for the Company in the first quarter of fiscal year 2017 using either of two methods: (a) retrospective to each prior reporting period presented with the option to elect certain practical expedients as defined within ASU 2014-09; or (b) retrospective with the cumulative effect of initially applying ASU 2014-09 recognized at the date of initial application and providing certain additional disclosures as defined in ASU 2014-09. The Company has not yet selected a transition method and is currently evaluating the impact of the pending adoption of ASU 2014-09 on the consolidated financial statements.

(AMOUNTS SHOWN IN THOUSANDS)

2. Summary of significant accounting policies (continued)

Research and Development

Expenditures for research, development and engineering of software and hardware products, that are included in selling, general and administrative expenses in the consolidated statements of operations, are expensed as incurred.

Stock Based Compensation (per share amounts shown in whole numbers)

The Company complies with the accounting and reporting requirements of the Accounting for Stock Based Compensation guidelines which require companies to record compensation expense for share-based awards issued to employees in exchange for services provided. The amount of the compensation expense is based on the estimated fair value of the awards on their grant dates and is generally recognized over the applicable vesting period.

The fair value of stock options is determined using an option-pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock, expected dividends, and the risk free interest rate over the expected life of the option.

During the nine months ended September 30, 2014 the Company recognized $108 in stock based compensation expense in its consolidated financial statements relating to the issuance of stock options. The Company recorded $13 in stock based compensation expense during the nine months ended September 30, 2013 relating to the issuance of stock options.

The fair value of the 2014 stock options was estimated on the date of grant using the Black-Scholes valuation model based on the following assumptions:

	Nine Months Ended September 30, 2014
Expected dividend yield	0.00%
Expected stock price volatility	71.80% -84.05%
Risk-free interest rate	2.00%
Expected life in years	10 years
Weighted-average fair value of options granted	$9.41

Basic and Diluted Net Income per Share (per share amounts shown in whole numbers)

Basic income per share is computed by dividing income attributable to common shareholders by the weighted average number of common shares outstanding for the period. Diluted income per share reflects the dilution of common stock equivalents such as options to the extent the impact is dilutive. As the Company incurred net income for the three and nine months ended September 30, 2014, potentially dilutive securities have been included in the diluted net income per share computations and any potentially anti-dilutive shares have been excluded and are shown below.

(AMOUNTS SHOWN IN THOUSANDS)

2. Summary of significant accounting policies (continued)

Basic and Diluted Net Income per Share (per share amounts shown in whole numbers)(continued)

The following table reconciles the number of shares utilized in the net income per share calculations for three and nine months ended September 30, 2014 and 2013:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income	$ 409	$ 1,050	$ 2,471	$ 2,084
Shares				
Weighted average shares outstanding - basic	1,462	1,457	1,462	1,453
Weighted average dilutive share equivalents from stock options	88	61	88	61
Weighted average shares outstanding - diluted	1,550	1,518	1,550	1,514
Net income per share - basic	$ 0.28	$ 0.72	$ 1.69	$ 1.43
Net income per share - diluted	$ 0.26	$ 0.69	$ 1.59	$ 1.38

The number of potentially dilutive shares from stock options excluded from the diluted net income per share calculation as of September 30, 2014 and September 30, 2013 was 2 and 41, respectively.

Income Taxes

The Company complies with GAAP which requires an asset and liability approach to financial reporting for income taxes. Deferred income tax assets and liabilities are computed for differences between the consolidated financial statement and tax basis of assets and liabilities that will result in future taxable or deductible amounts, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred income tax assets to the amount expected to be realized.

The determination of the Company's provision for income taxes requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. Significant judgment is required in assessing the timing and amounts of deductible and taxable items and the probability of sustaining uncertain tax positions. The benefits of uncertain tax positions are recorded in the Company's consolidated financial statements only after determining a more-likely-than-not probability that the uncertain tax positions will withstand challenge, if any, from tax authorities. When facts and circumstances change, the Company reassesses these probabilities and records any changes in the consolidated financial statements as appropriate. Accrued interest and penalties related to income tax matters are classified as a component of income tax expense.

In accordance with GAAP, the Company is required to determine whether a tax position is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The Company files an income tax return in the U.S. federal jurisdiction, and may file income tax returns in various U.S. states and foreign jurisdictions. The tax benefit recognized is measured as the largest amount of benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. De-recognition of a tax benefit previously recognized results in the Company recording a tax liability that increases the accumulated deficit. Generally, the Company is no longer subject to income tax examination by major taxing authorities for the years before 2010.

(AMOUNTS SHOWN IN THOUSANDS)

3. Acquisition

Effective June 6, 2014, the Company and its newly formed, wholly owned subsidiary, Sirius Acquisition, LLC, completed the acquisition (the “Acquisition”) of substantially all of the assets of CohuHD, a division of the camera products and video solutions division of Cohu, Inc., pursuant to the transactions contemplated by the Asset Purchase Agreement (“Purchase Agreement”), dated as of June 3, 2014, by and among the Costar Technologies, Inc., Sirius Acquisition, LLC, and Cohu, Inc. On June 13, 2014, the name of Sirius Acquisition, LLC was changed to CohuHD Costar, LLC (“CohuHD Costar”). Results from operations for CohuHD Costar have been included in the Company’s consolidated financial statements.

CohuHD Costar is a leading provider of video cameras and related products, specializing in IP video solutions for traffic monitoring, security, surveillance and military applications; and accessories such as cables, camera mounts, lenses and data storage devices. Estimated total consideration for the Acquisition is up to approximately $10,315, consisting of a cash payment of $9,886 (including an estimated working capital adjustment of $386) less a final working capital adjustment of $41 and deferred consideration of up to $500 in cash, contingent upon CohuHD Costar shipping and receiving payment for specified purchase orders within twelve months of close, for which the fair value was estimated to be $470 and was recorded as a short term liability.

The Company acquired CohuHD Costar for its leadership in the traffic market, complementary products, unique customer base, cross selling opportunities, and its additive value to the Company’s profits. CohuHD Costar provides a new customer base and a new sales channel to the Company.

Certain expenses were incurred related to the Acquisition in the amount of $153 for the three months ended September 30, 2014. For the nine months ended September 30, 2014 the Company incurred approximately $397 in expenses related to the Acquisition.

The Acquisition of these assets meets the definition of a business combination under GAAP. The purchase accounting has not been finalized, therefore, the following table presents a summary of the provisional fair value of assets acquired and liabilities assumed as of June 6, 2014.

Assets acquired:		
Accounts receivable	$	2,065
Inventories		3,559
Prepaid expenses		214
Property and equipment		393
Trade name		1,657
Customer relationships		1,145
Covenant not to compete		20
Goodwill		1,921
Total assets acquired		10,974
Liabilities assumed:		
Accounts payable		433
Accrued expenses		226
Total liabilities assumed		659
Total assets acquired and liabilities assumed, net	$	10,315

(AMOUNTS SHOWN IN THOUSANDS)

3. Acquisition

Included in the consolidated statement of operations are CohuHD Costar revenues and net income of $5,972 and $1,062, respectively, for the nine-months ended September 30, 2014 and $4,244 and $511, respectively, for the three-months ended September 30, 2014. The following proforma information gives effect to the acquisition as if it had occurred on the first day of each of the three and nine month periods ended September 30, 2014 and 2013.

	For the Three Months Ended September 30,				For the Nine Months Ended September 30,			
	2014		2013		2014		2013	
Total revenue	$	8,976	$	12,636	$	31,019	$	34,371
Net income	$	409	$	1,506	$	1,939	$	3,199

4. Fair value measurements

The Company defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, which are required to be recorded at fair value, the Company considers the principal or most advantageous market in which the Company would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions and credit risk.

The Company applies the following fair value hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

Level 1: Quoted prices in active markets for identical assets or liabilities that the entity has the ability to access.

Level 2: Observable inputs other than prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated with observable market data.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. This includes certain pricing models, discounted cash flow methodologies, and similar techniques that use significant unobservable inputs.

Contingent consideration

As of September 30, 2014, the Company had obligations to transfer $333 in contingent purchase price to Cohu, Inc. in conjunction with the Acquisition, if specified future operational objectives are met over the next year. The Company recorded the acquisition-date fair value of these contingent liabilities, based on the likelihood of contingent earn-out payments, as part of the consideration transferred. The earn-out payments are subsequently remeasured to fair value each reporting date. For contingent purchase price to be settled in cash, the Company used a discounted cash flow method using internal models. The Company classified the financial liabilities to be settled in cash as Level 3, due to the lack of relevant observable inputs and market activity. The original fair value measurement was estimated to be $470. The Company made an earn-out payment of $137 in the three months ended September 30, 2014, with a $333 remaining balance.

(AMOUNTS SHOWN IN THOUSANDS)

4. Fair value measurements (continued)

The following table summarizes financial liabilities measured at fair value on a recurring basis as of September 30, 2014, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

		Fair Value Measurement at Reporting Date Using		
Description	As of September 30, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Liabilities:				
Contingent purchase price	$ 333			$ 333

The following table reflects the activity for liabilities measured at fair value using Level 3 inputs as of September 30, 2014:

Balance as of December 31, 2013	$ -
Issuances of contingent purchase price	$ 470
Payments made on contingent purchase price	(137)
Balance as of September 30, 2014	$ 333

5. Property and equipment

Property and equipment at September 30, 2014 and December 31, 2013, were as follows:

	2014	2013
Office furniture and equipment	$ 833	$ 395
Less accumulated depreciation	(391)	(326)
Total property and equipment, net	$ 442	$ 69

Depreciation expense for the three months ended September 30, 2014 and 2013 was $19 and $20 and for the nine months ended September 30, 2014 and 2013 was $66 and $30, respectively.

(AMOUNTS SHOWN IN THOUSANDS)

6. Intangible assets

The following is a summary of amortized and unamortized intangible assets September 30, 2014 and December 31, 2013.

	September 30, 2014	
	Gross Amount	Accumulated Amortization
Amortized intangible assets		
Customer relations - Southern Imaging	$ 1,599	$ 1,599
Distribution agreement - Southern Imaging	1,468	605
Customer relations – IVS	125	61
Covenant not to compete – IVS	50	49
Trade name – CohuHD	1,657	59
Customer relationships – CohuHD	1,145	29
Covenant not to compete – CohuHD	20	1
Total amortized intangible assets	6,064	2,403
Unamortized intangible assets		
Trade name - Costar	800	
Trade name - IVS	125	
Goodwill – CohuHD	1,921	
Total unamortized intangible assets	2,846	
Total intangible assets	$ 8,910	$ 2,403

	December 31, 2013	
	Gross Amount	Accumulated Amortization
Amortized intangible assets		
Customer relations - Southern Imaging	$ 1,599	$ 1,599
Distribution agreement - Southern Imaging	1,468	550
Customer relations – IVS	125	45
Covenant not to compete – IVS	50	36
Total amortized intangible assets	3,242	2,230
Unamortized intangible assets		
Trade name - Costar	800	
Trade name - IVS	125	
Total unamortized intangible assets	925	
Total intangible assets	$ 4,167	$ 2,230

The weighted average amortization period for the Company's intangible assets is 8 years. The estimated useful lives for customer relationships, distribution agreements and covenant not to compete are 6, 20 and 3 years, respectively. The intangibles gained from the CohuHD Costar acquisition are trade name, customer relationships, and noncompete agreement which have estimated useful lives of 7, 10, and 5 years respectively.

(AMOUNTS SHOWN IN THOUSANDS)

6. Intangible assets (continued)

Amortization expense for the three months ended September 30, 2014 and 2013 was $116 and $27 and for the nine months ended September 30, 2014 and 2013 was $173 and $83, respectively. Future amortization expense, as of September 30, 2014, is as follows:

Year Ending September 30,	
2015	451
2016	449
2017	449
2018	430
Thereafter	1,882
Total future amortization expense	$ 3,661

7. Lines of credit and long-term debt

Effective as of September 23, 2011, Costar entered into a Loan and Security Agreement with Briar Capital L.P. (“Briar”). The Loan and Security Agreement allows for up to $3,500 in revolving lines of credit, with a three year maturity. The obligations under the Costar Loan and Security Agreement with Briar are secured by a lien on substantially all accounts receivable, inventory, equipment, general intangibles, including intellectual property, chattel paper, instruments and documents of Costar, as set forth in the Loan and Security Agreement with Briar. The Company is a guarantor of Costar’s obligations under the Costar Loan and Security Agreement with Briar pursuant to the guaranty made by the Company in favor of Briar. Borrowings under the Loan and Security Agreement accrue interest at a rate equal to the 30-day LIBOR rate plus 8.25% per annum.

The Costar Loan and Security Agreement with Briar contains customary representations and warranties, events of default and covenants, including, among other things, covenants that restrict the ability of Costar to incur certain additional indebtedness or to issue equity interests. The Costar Loan and Security Agreement with Briar also contain financial covenants restricting capital expenditures of Costar and requiring Costar and the Company to maintain a specific Tangible Net Worth. As of September 30, 2014 and December 31, 2013, $0 was owed to Briar.

Effective April 1, 2013, Costar entered into a Loan and Security Agreement (“Facility”) with BOKF, NA dba Bank of Texas (“Bank of Texas”). The Facility allows for up to $1,000 in a revolving line of credit, with a one year maturity. The obligation under the Facility with Bank of Texas is secured by a lien on substantially all accounts receivable, inventory, and equipment. The Company is a guarantor of Costar’s obligation under the Facility with Bank of Texas pursuant to the guaranty made by the Company in favor of Bank of Texas. Borrowings under the Facility accrue interest at a rate equal to Bank of Texas Prime, currently 4.0% per annum. With the execution of the new Bank of Texas Facility, the Briar loan was paid in full and closed.

The Facility with Bank of Texas contains customary representations and warranties, events of default and covenants, including, among other things, covenants that restrict the ability of Costar to incur certain additional indebtedness or to issue equity interests. The Facility with Bank of Texas also contains financial covenants calculated on a consolidated basis requiring the Company to maintain a certain Debt Service Coverage Ratio, Minimum Profitability, and a Minimum Tangible Net Worth.

(AMOUNTS SHOWN IN THOUSANDS)

7. Lines of credit and long-term debt (continued)

Effective March 31, 2014, Costar entered into a Change in Terms Agreement with Bank of Texas extending the maturity date of the Facility to May 31, 2014. The amount owed on the Facility as of March 31, 2014 and May 31, 2014 was $0.

Effective May 31, 2014, Costar entered into a Change in Terms Agreement with Bank of Texas extending the maturity date of the Facility to June 30, 2014. The amount owed on the Facility as of May 31, 2014 and June 30, 2014 was $0.

Effective June 3, 2014, the Company entered into an Amended Loan and Security Agreement ("Accord") with Bank of Texas. The Accord allows for up to $7,000 in a revolving line of credit and a $3,000 term loan with maturities of June 3, 2016 and June 3, 2019, respectively. The obligation under the Accord with Bank of Texas is secured by a lien on substantially all accounts receivable, inventory, and equipment. As of September 30, 2014, the Company was paying interest at the BOKF prime rate (3.25%). With the execution of the new Accord, the Bank of Texas $1,000 Facility was closed.

Future principal payments for the term loan, as of September 30, 2014, are as follows:

Year Ending September 30,	
2015	600
2016	600
2017	600
2018	600
2019	450
Total term loan principal payments	$ 2,850

The Accord with Bank of Texas contains customary representations and warranties, events of default and covenants, including, among other things, covenants that restrict the ability of Costar to incur certain additional indebtedness or to issue equity interests. The Accord with Bank of Texas also contains financial covenants calculated on a consolidated basis requiring the Company to maintain a certain Debt Service Coverage Ratio, Minimum Profitability, and a Minimum Tangible Net Worth. As of September 30, 2014 and December 31, 2013, $1,766 and $0 was owed to Bank of Texas on the revolving line of credit and $2,850 and $0 was owed to Bank of Texas on the term loan, respectively.

The Company paid approximately $125 in various fees associated with securing the new accord. The fees are treated as a deferred financing costs assets and will be amortized over the life of the accord using the straight-line method for the revolving line of credit portion and the effective-interest method for the term note portion.

8. Deferred income taxes

Deferred tax assets are determined based on the difference between financial statement and tax bases using enacted tax rates in effect for the year in which the differences are expected to reverse. As of December 31, 2013, the Company had approximately $148,900 in net operating loss carry forwards. Of that amount, approximately $130,000 relate to LQ Corporation, which was acquired by the Company in a 2007 merger. The Company believes an ownership change occurred under IRC Section 382, which will limit the Company's ability to utilize these losses. The Company also believes that the remainder of the NOLs are not impaired under IRC Section 382 and that it can utilize approximately $20,700, if the Company is able to generate taxable income before the losses expire between the years 2019 and 2030.

The Company's management determined that it was more likely than not that the benefit of the net deferred tax asset would not be realized. In assessing the Company's ability to utilize these assets, management considered whether it was more likely than not that some portion or all of the deferred tax asset would not be realized. The realization of the deferred tax asset is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considered the scheduled reversal of deferred tax liabilities and the projected future taxable income in making this assessment. Based upon the level of projected future taxable income over the period of expiration of the net operating loss carry forwards when temporary differences that give rise to the deferred tax assets are deductible, management provided a valuation allowance to the uncertainty of realizing these benefits at September 30, 2014.

The Company has certain deferred tax liabilities created by indefinite lived intangible assets that could not be used to offset the deferred tax assets. As of September 30, 2014, the Company has recognized a deferred tax liability of approximately $79 related to these indefinite lived intangible assets.

9. Stockholders' equity (shown in whole amounts)

At September 30, 2014 and December 31, 2013, the authorized capital stock of the Company consisted of (i) 10,000,000 shares of voting common stock with a par value of $0.001 per share and (ii) 10,000,000 shares of preferred stock with a par value of $0.001 per share. As of September 30, 2014 and December 31, 2013, there was no preferred stock issued and outstanding. The Company's Board has the authority to determine the voting powers, designations, preferences, privileges and restrictions of the preferred shares. As of September 30, 2014, there were 1,464,659 shares of common stock outstanding and 1,690,025 shares of common stock issued. As of December 31, 2013, there were 1,458,659 shares of common stock outstanding and 1,684,425 shares of common stock issued.

10. Stock option plan (shown in whole amounts)

The Company's 2000 Stock Option and Incentive Plan (the "2000 Incentive Plan") provides for awards in the form of incentive stock options, non-qualified stock options, restricted stock awards and other forms of awards to officers, directors, employees and consultants of the Company. At September 30, 2014 there were 137,982 share options issued under this plan. At September 30, 2014, there were 122,354 shares available for issuance under the 2000 Incentive Plan.

The Board of Directors of the Company determines the term of each option, the option price, and the number of shares for which each option is granted and the times at which each option vests. For holders of 10% or more of the Company's outstanding common stock, incentive stock options may not be granted at less than 110% of the fair market value of the common stock at the date of grant.

(AMOUNTS SHOWN IN THOUSANDS)

10. Stock option plan (shown in whole amounts) (continued)

The following table summarizes information about stock options outstanding at September 30, 2014:

Options Outstanding				Options Fully Vested and Exercisable	
Range of Exercise Price Per Share	Number Outstanding	Weighted Average Remaining Contractual Life (In Years)	Weighted Average Exercise Price Per Share	Number Exercisable	Weighted Average Exercise Price Per Share
$0.725-$14.70	137,982	6.46	$5.28	99,075	$4.58

Stock option activity for the nine months ended September 30, 2014 and 2013 is as follows:

	2014		2013	
	Number of Shares	Weighted Average Exercise Price Per Share	Number of Shares	Weighted Average Exercise Price Per Share
Outstanding at beginning of year	111,749	$3.38	120,612	$4.31
Granted	31,833	$11.68	19,333	$2.53
Exercised	5,600	$3.72		
Canceled			8,196	$6.86
Outstanding at period end	137,982	$5.28	131,749	$3.89
Options exercisable at period end	99,075	$4.58	101,853	$4.49
Weighted average fair value of options granted during the period at fair value		$9.41		$1.72

During the nine months ended September 30, 2014 the Company recognized approximately $108,000 in stock based compensation expense in its consolidated financial statements relating to the issuance of stock options. The Company recorded approximately $13,000 in stock based compensation expense during the nine months ended September 30, 2013.

11. Lease agreements

On January 31, 2011 the Company entered into a new lease agreement for certain facilities that will expire in 2018. Rent expense under the agreement for the years ended September 30, 2014 and 2013 were approximately $259 and $95, respectively.

(AMOUNTS SHOWN IN THOUSANDS)

11. Lease agreements (continued)

Additionally, in connection with the completion of the Acquisition, effective June 6, 2014 the Company signed a three year lease with Cohu, Inc. in Poway, CA for the CohuHD Costar business.

Future minimum annual rent payments are approximately as follows:

Year Ending September 30,	
2015	622
2016	673
2017	544
2018	110
Total future minimum lease commitments	1,878

12. Risk concentrations

Concentration of Cash

The Company maintains its cash balances in financial institutions. These balances are insured by the Federal Deposit Insurance Corporation up to $250 per institution. The Company is subject to credit risk to the extent any financial institution with which it conducts business is unable to fulfill contractual obligations on its behalf. Management monitors the financial condition of such financial institutions and does not anticipate any losses from these financial institutions.

Concentration of Customers

The Company's security surveillance product line customers include traditional "large box" national retailers and distributors. The Company's industrial vision product line customers include manufacturers that assemble products using automated production lines; these customers use the Company's video systems to monitor activity on the production line. For the nine months ended September 30, 2014 and 2013, the Company's two largest customers, Wal-Mart Stores, Inc. and Diebold, Inc., accounted for approximately $12,464 and $14,311, or 48.8% and 64.6% of the Company's total revenue, respectively. Amounts owed by two main customers accounted for $1,367, or 23.6%, and three main customers accounted for $1,219, or 57.0% of the outstanding accounts receivable balance, as of September 30, 2014 and December 31, 2013, respectively.

Concentration of Suppliers

For the nine months ended September 30, 2014 and 2013, the Company made purchases from two main suppliers of approximately 26.4% and 51.6% of total purchases, respectively. Amounts owed to one main supplier accounted for 17.4% and two main suppliers accounted for 79.2% of the total accounts payable balance, as of September 30, 2014 and December 31, 2013, respectively.

13. Sale of Assets (Promissory Note)

During December 2010, the Company entered into an agreement to sell certain assets and liabilities of Sielox, LLC ("Sielox"), an indirect wholly owned subsidiary. One of the agreed conditions of the sale was that Costar would continue to sell its range of security solution products through the Sielox network of approved business partners. The terms and conditions that govern the sale of Costar products are stated in the Master Distribution Agreement (the "Agreement") entered into between Costar and HGW Acquisition Company ("HGW"). The term of the Agreement commences on January 1, 2011, and ends on December 31, 2013. During the term of the Agreement, HGW has agreed to purchase Costar products in the minimum amount of $5,000. Actual purchases will be measured against a schedule of semi-annual purchase commitments (the "Purchase Commitment"). In furtherance of the Purchase Commitment, HGW delivered to Costar a secured promissory note with an original principal balance in the amount of $500 and bearing interest on the unpaid balance at a rate equal to 7% per annum. The promissory note is secured by a first priority security interest in HGW's accounts receivable. In the event that HGW fails to purchase Costar products in an amount equal to the Purchase Commitment as of the end of an applicable semi-annual period, HGW will have a period of 30 days to remedy the purchase default. That remedy will be in the form of a payment to Costar, of an amount equal to 25% of the shortfall, plus interest. The balance of the note at September 30, 2014 and December 31, 2013 was approximately $0 and $86, respectively.

Effective January 1, 2014 Costar entered into a new, two year Master Distribution Agreement with Sielox. Sielox will continue to sell Costar's range of security solution products through the Sielox network of approved business partners.