

INTEVAC INC
Form 10-Q/A
May 10, 2005

On June 26, 2004, 20,038,814 shares of the Registrant's Common Stock, no par value, were outstanding.

INTEVAC, INC.

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EXPLANATORY NOTE

This Amendment No. 1 to Intevac, Inc.'s (the "Company") Quarterly Report on Form 10-Q for the quarter ended June 26, 2004 is being filed to reflect the restatement of the Company's condensed consolidated financial statements for that period. The restatement relates to revenue on various technology development contracts that was not recognized per contract terms or per accounting principles generally accepted in the United States of America. Also included in this restatement are two timing inaccuracies in reported cost of sales and a revision to the amount of other comprehensive income reported. See Note 2 to the Company's unaudited condensed consolidated financial statements for additional discussion. This Form 10-Q/A does not reflect events occurring after the filing of the original Form 10-Q, or modify or update the disclosures therein in any way other than as required to reflect the amendment set forth in Note 2.

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****INTEVAC, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**
(In thousands)

| | June 26, 2004 (Unaudited) Restated | December 31, 2003 |
|--|---|----------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 21,880 | \$ 19,507 |
| Short term investments | 15,632 | |
| Trade and other accounts receivable, net of allowances of \$24 and \$22 at June 26, 2004 and December 31, 2003 | 15,317 | 14,016 |
| Inventories | 39,000 | 13,108 |
| Prepaid expenses and other current assets | 737 | 1,113 |
| Total current assets | 92,566 | 47,774 |
| Property, plant and equipment, net | 5,848 | 5,796 |
| Long term investments | 12,187 | |
| Investment in 601 California Avenue LLC | 2,431 | 2,431 |
| Other long term assets | 3 | 4 |
| Total assets | \$ 113,035 | \$ 55,975 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| Current liabilities: | | |
| Convertible notes | \$ | \$ 1,025 |
| Accounts payable | 7,222 | 3,396 |
| Accrued payroll and related liabilities | 1,687 | 1,610 |
| Other accrued liabilities | 3,104 | 2,643 |
| Customer advances | 30,635 | 16,432 |
| Total current liabilities | 42,648 | 25,106 |
| Shareholders' equity: | | |
| Common stock, no par value | 94,189 | 51,982 |
| Accumulated other comprehensive income | 217 | 223 |
| Accumulated deficit | (24,019) | (21,336) |

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| | | |
|--|------------|-----------|
| Total shareholders' equity | 70,387 | 30,869 |
| Total liabilities and shareholders' equity | \$ 113,035 | \$ 55,975 |

See accompanying notes.

Table of Contents**INTEVAC, INC.**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME (LOSS)**
(In thousands, except per share amounts)
(Unaudited)

| | Three Months Ended | | Six Months Ended | |
|--|---------------------------|--------------------------|------------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 | June 26, 2004 | June 28, 2003 |
| | Restated | | Restated | |
| Net revenues: | | | | |
| Systems and components | \$ 15,626 | \$ 2,677 | \$ 19,819 | \$ 13,241 |
| Technology development | 2,138 | 1,910 | 4,380 | 3,361 |
| Total net revenues | 17,764 | 4,587 | 24,199 | 16,602 |
| Cost of net revenues: | | | | |
| Systems and components | 10,183 | 1,711 | 12,826 | 11,032 |
| Technology development | 1,654 | 1,435 | 3,321 | 2,559 |
| Inventory provisions | 247 | 322 | 753 | 732 |
| Total cost of net revenues | 12,084 | 3,468 | 16,900 | 14,323 |
| Gross profit | 5,680 | 1,119 | 7,299 | 2,279 |
| Operating expenses: | | | | |
| Research and development | 3,083 | 3,114 | 6,141 | 5,743 |
| Selling, general and administrative | 2,223 | 2,146 | 4,393 | 4,071 |
| Total operating expenses | 5,306 | 5,260 | 10,534 | 9,814 |
| Operating profit (loss) | 374 | (4,141) | (3,235) | (7,535) |
| Interest expense | | (508) | (12) | (1,025) |
| Interest income and other, net | 303 | (148) | 552 | (243) |
| Income (loss) before income taxes | 677 | (4,797) | (2,695) | (8,803) |
| Benefit from income taxes | | | (12) | |
| Net income (loss) | \$ 677 | \$ (4,797) | (2,683) | \$ (8,803) |
| Other comprehensive income: | | | | |
| Foreign currency translation adjustments | (7) | 10 | (6) | 4 |
| Total comprehensive income (loss) | \$ 670 | \$ (4,787) | \$ (2,689) | \$ (8,799) |
| Basic income (loss) per share: | | | | |

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| | | | | |
|----------------------------------|---------|-----------|-----------|-----------|
| Net income (loss) | \$ 0.03 | \$ (0.39) | \$ (0.14) | \$ (0.72) |
| Shares used in per share amounts | 20,010 | 12,187 | 19,373 | 12,176 |
| Diluted income (loss) per share: | | | | |
| Net income (loss) | \$ 0.03 | \$ (0.39) | \$ (0.14) | \$ (0.72) |
| Shares used in per share amounts | 20,678 | 12,187 | 19,373 | 12,176 |

See accompanying notes.

Table of Contents**INTEVAC, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

| | Six months ended | |
|--|--------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 |
| | Restated | |
| Operating activities | | |
| Net loss | \$ (2,683) | \$ (8,803) |
| Adjustments to reconcile net loss to net cash and cash equivalents used in operating activities: | | |
| Depreciation and amortization | 1,131 | 950 |
| Inventory provisions | 753 | 732 |
| Loss on disposal of equipment | 1 | 642 |
| Changes in operating assets and liabilities | (8,993) | (234) |
| Total adjustments | (7,108) | 2,090 |
| Net cash and cash equivalents used in operating activities | (9,791) | (6,713) |
| Investing activities | | |
| Purchases of investments | (27,895) | |
| Purchases of leasehold improvements and equipment | (1,108) | (1,680) |
| Net cash and cash equivalents used in investing activities | (29,003) | (1,680) |
| Financing activities | | |
| Proceeds from issuance of common stock | 42,207 | 186 |
| Payoff of convertible notes due 2004 | (1,025) | |
| Net cash and cash equivalents provided by financing activities | 41,182 | 186 |
| Effect of exchange rate changes on cash | (15) | (7) |
| Net increase (decrease) in cash and cash equivalents | 2,373 | (8,214) |
| Cash and cash equivalents at beginning of period | 19,507 | 28,457 |
| Cash and cash equivalents at end of period | \$ 21,880 | \$ 20,243 |
| Supplemental Schedule of Cash Flow Information | | |
| Cash paid (received) for: | | |
| Interest | \$ 33 | \$ 993 |
| Income tax refund | \$ | \$ (214) |

See accompanying notes.

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INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Business Activities and Basis of Presentation

We are the world's leading provider of thin-film disk sputtering equipment for the thin-film disk industry and a developer of leading technology for extreme low light imaging sensors, cameras and systems. We operate two businesses: Equipment and Imaging.

Our Equipment business designs, manufactures, markets and services complex capital equipment used in the sputtering, or deposition, of highly engineered thin films of material onto disks which are used in hard disk drives. Hard disk drives are the primary storage medium for digital data and function by magnetically storing data on thin-film disks. These thin-film disks are created in a sophisticated manufacturing process involving many steps, including plating, annealing, polishing, texturing, sputtering and lubrication.

Our Imaging business develops and manufactures electro-optical sensors, cameras, and systems that permit highly sensitive detection of photons in the visible and near infrared portions of the spectrum, allowing imaging in extreme low light situations. These efforts are aimed at creating new products for both military and commercial applications.

The financial information at June 26, 2004 and for the three- and six-month periods ended June 26, 2004 and June 28, 2003 is unaudited, but includes all adjustments (consisting only of normal recurring accruals) that we consider necessary for a fair presentation of the financial information set forth herein, in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, it does not include all of the information and footnotes required by U.S. GAAP for annual financial statements. For further information, refer to the Consolidated Financial Statements and footnotes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2003.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements. Our critical accounting policies are summarized in Item 2 of this Form 10-Q.

We evaluate the collectibility of trade receivables on an ongoing basis and provide reserves against potential losses when appropriate.

The results for the three- and six-month periods ended June 26, 2004 are not considered indicative of the results to be expected for any future period or for the entire year.

2. Restatement of Financial Statements

In connection with our preparation of the consolidated financial statements for the fiscal year ended December 31, 2004, we determined that the previously issued financial statements contained in the Quarterly Reports on Form 10-Q for the quarters ended March 27, 2004, June 26, 2004 and September 25, 2004 should be restated to correct errors in those financial statements. The decision to restate these financial statements was made based on the following information:

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We determined during the course of our year-end audit that projected, rather than approved, billing rates were used to calculate revenue for cost-plus-fixed-fee technology development contracts. An adjustment was made at year-end to reflect the correct revenue recognition, but the previously reported quarterly revenue numbers were misstated.

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INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A series of proposed adjustments, which were not material by themselves, became material when combined with the restatement of revenue described above.

A revision to the amount of other comprehensive income reported was made to move certain amounts unrelated to foreign currency adjustments to other income.

The following is a summary of the effect of these changes on our condensed consolidated balance sheet as of June 26, 2004 and our condensed consolidated statement of operations for the three- and six-month periods ended June 26, 2004 (in thousands, except per share data):

| | Condensed Consolidated Balance Sheet | | |
|--|---|--------------------|------------------------|
| | As Previously Reported | Adjustments | As Restated |
| June 26, 2004 | | | |
| Trade and other accounts receivable | \$ 15,597 | \$ (280) | \$ 15,317 |
| Inventories | 38,907 | 93 | 39,000 |
| Total current assets | 92,753 | (187) | 92,566 |
| Total assets | 113,222 | (187) | 113,035 |
| Other accrued liabilities | 3,134 | (30) | 3,104 |
| Total current liabilities | 42,678 | (30) | 42,648 |
| Accumulated other comprehensive income | 216 | 1 | 217 |
| Accumulated deficit | (23,681) | (158) | (24,019) |
| Total shareholder's equity | 70,544 | (157) | 70,387 |

| | Condensed Consolidated Statement of Operations | | |
|---|---|--------------------|------------------------|
| | As Previously Reported | Adjustments | As Restated |
| Three months ended June 26, 2004 | | | |
| Net revenues | \$ 17,980 | \$ (216) | \$ 17,764 |
| Cost of net revenues | 12,189 | (105) | 12,084 |
| Gross profit | 5,791 | (111) | 5,680 |
| Interest income and other, net | 307 | (4) | 303 |
| Net income (loss) | 792 | (115) | 677 |
| Net income (loss) per share - basic | 0.04 | (0.01) | 0.03 |
| Net income (loss) per share - diluted | 0.04 | (0.01) | 0.03 |

| | Condensed Consolidated Statement of Operations | | |
|---------------------------------------|---|--------------------|------------------------|
| | As Previously Reported | Adjustments | As Restated |
| Six months ended June 26, 2004 | | | |
| Net revenues | \$ 24,479 | \$ (280) | \$ 24,199 |
| Cost of net revenues | 17,023 | (123) | 16,900 |
| Gross profit | 7,456 | (157) | 7,299 |
| Interest income and other, net | 553 | (1) | 552 |
| Net income (loss) | (2,525) | (158) | (2,683) |

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| | | | |
|---------------------------------------|--------|--------|--------|
| Net income (loss) per share - basic | (0.13) | (0.01) | (0.14) |
| Net income (loss) per share - diluted | (0.13) | (0.01) | (0.14) |

Table of Contents**INTEVAC, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. Concentrations**

Our largest customers tend to change from period to period. Historically, a significant portion of our revenues in any particular period have been attributable to sales to a limited number of customers. Our order backlog at June 26, 2004 included orders for nine 200 Lean systems from one customer.

4. Inventories

Inventories are priced using standard costs, which approximate first-in, first-out. The components of inventory consist of the following:

| | June 26, 2004 | December 31, 2003 |
|------------------|------------------------------|----------------------------------|
| | (In thousands) | |
| | Restated | |
| Raw materials | \$ 8,044 | \$ 3,306 |
| Work-in-progress | 2,670 | 4,371 |
| Finished goods | 28,286 | 5,431 |
| | \$ 39,000 | \$ 13,108 |

Finished goods inventory consists primarily of completed systems at customer sites that are undergoing installation and acceptance testing.

Inventory reserves included in the above numbers were \$10.8 million and \$10.2 million at June 26, 2004 and December 31, 2003, respectively. Each quarter, we analyze our inventory (raw materials, work-in-progress and finished goods) against the forecast demand for the next 12 months. Parts with no forecast requirements in that period are considered excess and inventory provisions are established to write those parts down to zero net book value. During this process, some inventory is identified as having no future use or value to us and is disposed of against the reserves. During the six months ended June 26, 2004, \$753,000 was added to inventory reserves based on the quarterly analysis and \$261,000 of inventory was disposed of and charged to the reserve. During the six months ended June 28, 2003, \$732,000 was added to inventory reserves based on the quarterly analysis and \$4,000 of inventory was disposed of and charged to the reserve.

5. Employee Stock Plans

At June 26, 2004, we had two stock-based employee compensation plans. We account for those plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. We do not plan to adopt the fair value requirements of SFAS 123 for reporting purposes, unless it is mandated by GAAP.

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The following table illustrates the effects on net income and earnings per share if Intevac had applied the fair value-recognition provisions of FASB Statement No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation.

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INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

| | Three Months Ended | | Six Months Ended | |
|---|-------------------------------|--------------------------|------------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 | June 26, 2004 | June 28, 2003 |
| | (in thousands) | | | |
| | Restated | | Restated | |
| Net income (loss), as reported | \$ 677 | \$ (4,797) | \$ (2,683) | \$ (8,803) |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | (341) | (155) | (609) | (267) |
| Pro forma net income (loss) | \$ 336 | \$ (4,952) | \$ (3,292) | \$ (9,070) |
| Basic and diluted loss per share: | | | | |
| As reported | \$ 0.03 | \$ (0.39) | \$ (0.14) | \$ (0.72) |
| Pro forma | \$ 0.02 | \$ (0.41) | \$ (0.17) | \$ (0.74) |

6. Warranty

Our typical warranty is 12 months from customer acceptance. In some cases we market extended warranty periods beyond 12 months to our customers. The warranty period on used systems is generally shorter than 12 months. During this warranty period any necessary non-consumable parts are supplied and installed. The warranty period on consumable parts is limited to their reasonable usable life. A provision for the estimated warranty cost is recorded at the time revenue is recognized.

The following table displays the activity in the warranty provision account, which is included in other accrued liabilities on our balance sheet, for the three and six-month periods ending June 26, 2004 and June 28, 2003:

| | Three Months Ended | | Six Months Ended | |
|--|-------------------------------|--------------------------|------------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 | June 26, 2004 | June 28, 2003 |
| | (in thousands) | | | |
| | Restated | | Restated | |
| Beginning balance | \$ 386 | \$ 644 | \$ 534 | \$ 845 |
| Expenditures incurred under warranties | (53) | (46) | (109) | (607) |
| Accruals for product warranties issued during the reporting period | 456 | 32 | 493 | 191 |
| Adjustments to previously existing warranty accruals | (135) | 34 | (264) | 235 |
| Ending balance | \$ 654 | \$ 664 | \$ 654 | \$ 664 |

7. Guarantees

We have entered into agreements with customers and suppliers that include limited intellectual property indemnification obligations that are customary in the industry. These guarantees generally require us to compensate the other party for certain damages and costs incurred as a result of third party intellectual property claims arising from these transactions. The nature of the intellectual property indemnification obligations prevents us from making a reasonable estimate of the maximum potential amount we could be required to pay our customers and suppliers. Historically, we have not made any significant indemnification payments under such agreements and no amount has been accrued in the accompanying consolidated financial statements with respect to these indemnification obligations.

Table of Contents**INTEVAC, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****8. Cash, Cash Equivalents and Investments in Debt Securities**

Our investment portfolio consists of cash, cash equivalents and investments in debt securities. We consider all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Investments in debt securities consists principally of highly rated debt instruments with maturities generally between one and 25 months.

In accordance with Statement of Accounting Standards No. 115 Accounting for Certain Investments in Debt and Equity Securities, and based on our intentions regarding these instruments, we have classified our investments in debt securities as held-to-maturity and account for these investments at amortized cost. Interest income is recorded using an effective interest rate, with the associated premium or discount amortized to interest income. Realized gains and losses are included in earnings. The table below presents the amortized principal amount, major security type and maturities for our investments in debt securities. The amortized principal amount approximates fair value at June 26, 2004.

| | June 26, 2004 | December 31, 2003 |
|--|------------------------------|----------------------------------|
| | (in thousands) | |
| Amortized Principal Amount: | | |
| Debt securities issued by US government agencies | \$ 22,096 | \$ |
| Corporate debt securities | 5,723 | |
| Total investments in debt securities | \$ 27,819 | \$ |
| Short-term investments | \$ 15,632 | \$ |
| Long-term investments | 12,187 | |
| Total investments in debt securities | \$ 27,819 | \$ |

9. Net Income (Loss) Per Share

The following table sets forth the computation of basic and diluted earnings (loss) per share:

| | Three Months Ended | | Six Months Ended | |
|------------|-------------------------------|--------------------------|------------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 | June 26, 2004 | June 28, 2003 |
| | (in thousands) | | | |
| | Restated | | Restated | |
| Numerator: | | | | |

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| | | | | |
|---|--------|------------|------------|------------|
| Numerator for basic income (loss) per share - loss available to common stockholders | \$ 677 | \$ (4,797) | \$ (2,683) | \$ (8,803) |
| Effect of dilutive securities: 6 1/2% convertible notes (1) | | | | |
| Numerator for diluted income (loss) per share - loss available to common stockholders after assumed conversions | \$ 677 | \$ (4,797) | \$ (2,683) | \$ (8,803) |

Table of Contents**INTEVAC, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

| | | | | |
|---|------------------|--------|--------|--------|
| Denominator: | | | | |
| Denominator for basic income (loss) per share | weighted-average | | | |
| shares | | 20,010 | 12,187 | 19,373 |
| | | | | 12,176 |
| Effect of dilutive securities: | | | | |
| Employee stock options (2) | | 668 | | |
| 6 1/2% convertible notes (1) | | | | |
| Dilutive potential common shares | | 668 | | |
| Denominator for diluted income (loss) per share | adjusted | 20,678 | 12,187 | 19,373 |
| | | | | 12,164 |

- (1) Diluted EPS for the three- and six-month periods ended June 26, 2004 and June 28, 2003 exclude as converted treatment of the convertible notes, as their inclusion would be anti-dilutive. The number of as converted shares excluded for the six-month period ended June 26, 2004 was 17,137 and the number of as converted shares excluded for the three- and six-month periods ended June 28, 2003 was 4,269,983.
- (2) Potentially dilutive securities, consisting of shares issuable upon exercise of employee stock options, are excluded from the calculation of diluted EPS as their effect would be anti-dilutive. The weighted average number of employee stock options excluded for the three-month periods ended June 26, 2004 and June 28, 2003 was 247,102 and 1,793,950, respectively, and the number of employee stock options excluded for the six-month periods ended June 26, 2004 and June 28, 2003 was 1,486,205 and 1,792,059, respectively.

10. Segment Reporting*Segment Description*

We have two reportable operating segments: Equipment and Imaging. Our Equipment business designs, manufactures, markets and services complex capital equipment used in the sputtering, or deposition, of highly engineered thin films of material onto thin-film disks which are used in hard disk drives. Our Imaging business develops and manufactures electro-optical sensors, cameras and systems that permit highly sensitive detection of photons in the visible and near infrared portions of the spectrum, allowing imaging in extreme low light situations.

Included in corporate activities are general corporate expenses, less an allocation of corporate expenses to operating units equal to 3% of net revenues. Assets of corporate activities include unallocated cash and short-term investments, deferred income tax assets (which are fully reserved) and other assets.

Business Segment Net Revenues

| | | | |
|---------------------|-----------------|-------------------------|-----------------|
| Three Months | | Six Months Ended | |
| Ended | | June | |
| June | June 28, | June | June 28, |
| 26, | | 26, | |

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| | 2004 | 2003 | 2004 | 2003 |
|-----------|-----------------|-------------|-----------------------|-------------|
| | | | (in thousands) | |
| | Restated | | Restated | |
| Equipment | \$ 15,403 | \$ 2,396 | \$ 19,556 | \$ 12,813 |
| Imaging | 2,361 | 2,191 | 4,643 | 3,789 |
| Total | \$ 17,764 | \$ 4,587 | \$ 24,199 | \$ 16,602 |

Table of Contents**INTEVAC, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)***Business Segment Profit & Loss*

| | Three Months Ended | | Six Months Ended | |
|-----------------------------------|-------------------------------|--------------------------|------------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 | June 26, 2004 | June 28, 2003 |
| | (in thousands) | | | |
| | Restated | | Restated | |
| Equipment | \$ 1,520 | \$ (1,937) | \$ (680) | \$ (3,157) |
| Imaging | (942) | (1,394) | (1,831) | (3,021) |
| Corporate activities | (204) | (810) | (724) | (1,357) |
| Operating income (loss) | 374 | (4,141) | (3,235) | (7,535) |
| Interest expense | | (508) | (12) | (1,025) |
| Interest income | 148 | 88 | 232 | 165 |
| Other income and expense, net | 155 | (236) | 320 | (408) |
| Income (loss) before income taxes | \$ 677 | \$ (4,797) | \$ (2,695) | \$ (8,803) |

Business Segment Assets

| | June 26, 2004 | December 31, 2003 |
|----------------------|--------------------------|----------------------------------|
| | (in thousands) | |
| | Restated | |
| Equipment | \$ 53,252 | \$ 25,462 |
| Imaging | 6,999 | 7,702 |
| Corporate activities | 52,784 | 22,811 |
| Total | \$ 113,035 | \$ 55,975 |

Geographic Area Net Trade Revenues

| | Three Months Ended | | Six Months Ended | |
|--|-------------------------------|--------------------------|------------------------------|--------------------------|
| | June 26, 2004 | June 28, 2003 | June 26, 2004 | June 28, 2003 |

| | | (in thousands) | | |
|---------------|-----------------|-----------------------|-----------------|-----------|
| | Restated | | Restated | |
| United States | \$ 11,030 | \$ 2,521 | \$ 13,826 | \$ 4,608 |
| Far East | 6,454 | 2,060 | 10,093 | 11,988 |
| Europe | 280 | | 280 | |
| Rest of World | | 6 | | 6 |
| Total | \$ 17,764 | \$ 4,587 | \$ 24,199 | \$ 16,602 |

11. Income Taxes

We did not accrue a tax provision for the three-month period ended June 26, 2004 as the profits for this period were offset by net operating loss carry-forwards. We did not accrue a tax benefit for either the six-month period ended June 26, 2004 or the three- and six-month periods ended June 28, 2003, due to the inability to realize additional refunds from loss carry-backs. The \$12,000 credit to income tax expense during the six-month period ended June 26, 2004 related to a revised estimate of 2003 taxes owed by our Singapore subsidiary. Our \$17.6 million deferred tax asset is fully offset by a \$17.6 million valuation allowance, resulting in a net deferred tax asset of zero at June 26, 2004.

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INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Capital Transactions

During the six-month period ending June 26, 2004, we completed a public offering of 4,750,000 shares of our common stock, of which 2,969,000 were newly issued and outstanding shares sold by us for net proceeds of \$41.6 million. A selling shareholder sold 1,781,000 shares in the offering. We also sold stock to our employees under Intevac's Stock Option and Employee Stock Purchase Plans. A total of 116,350 shares were issued under these plans during the six-month period ending June 26, 2004, for which Intevac received \$647,000.

13. Financial Presentation

Certain prior year amounts in the Condensed Consolidated Financial Statements have been reclassified to conform to 2004 presentation.

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Item 4. Controls and Procedures

Evaluation of disclosure controls and procedures. We maintain a set of disclosure controls and procedures that are designed to ensure that information relating to Intevac, Inc. required to be disclosed in periodic filings under Securities Exchange Act of 1934, or Exchange Act, is recorded, processed, summarized and reported in a timely manner under the Exchange Act. In connection with the original filing of Form 10-Q for the quarter ended June 26, 2004, as required under Rule 13a-15(b) of the Exchange Act, an evaluation was carried out under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of June 26, 2004 to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

Subsequent to the period covered by this report, in connection with our preparation of the consolidated financial statements for the fiscal year ended December 31, 2004, management of the Company determined that the previously issued financial statements contained in the Company's Quarterly Reports on Form 10-Q for the quarter ended March 27, 2004, June 26, 2004 and September 25, 2004 should be restated to correct errors in those financial statements. This restatement is further discussed in Note 2, Restatement of Financial Statements to the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q/A.

As a result, we are implementing a change in our internal controls over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) to remediate internal control deficiencies that led to the restatements noted above. Management has concluded that these internal control deficiencies constitute material weaknesses in our internal control over financial reporting. A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Management identified the following material weaknesses in its assessment of the effectiveness of the Company's internal control over financial reporting. As of December 31, 2004, we concluded that we did not maintain effective controls over (1) aspects of the Imaging Business, (2) approval of inventory cycle count adjustments, and (3) documentation related to our quarterly review and approval of excess and obsolete inventory reserves. The Company's evaluation was as follows:

Imaging Business - We determined during the course of our year-end audit that projected, rather than approved, billing rates were used to calculate revenue for cost-plus-fixed-fee technology development contracts. In addition, journal entries for revenue recognition and the related documentation were not subjected to adequate review and approval.

We also determined during the course of our year-end audit that firm fixed-price technology development contracts were not being accounted for in accordance with U.S. GAAP for firm fixed-price contracts. This would have resulted in an overstatement of revenue and operating profit had it not been discovered prior to the public release of our 2004 earnings. During the first quarter of 2005, we retrained our accounting staff in proper application of revenue recognition policies and implemented policies regarding analyzing contracts for proper revenue recognition accounting.

We determined during the course of our year-end audit that a receivable greater than one year old had not been reserved as a bad debt. During the fourth quarter of 2004, we implemented a bad debt policy that required receivables aged more than one year to be fully reserved. Our review did not include unbilled receivables and we did not establish

the appropriate bad debt reserve. This would have resulted in an understatement of bad debt expense and an overstatement of operating profit had it not been discovered prior to the public release of our earnings. We have changed our process for evaluating accounts receivable to ensure that all balances are reviewed for collectibility on a regular basis.

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Approval of Inventory Cycle Count Adjustments We routinely cycle count our stockroom inventories and make corrections to our inventory balances as a result of those cycle counts. We determined late in 2004 that the cycle count adjustments were being made, but without written approval by management as required by our internal control policies. Management authorization of cycle count adjustments is necessary to reduce the potential of an employee using a cycle count adjustment to conceal a theft of inventory. The requirement for the appropriate management approval of all cycle count adjustments was re-emphasized in December of 2004.

Documentation of Excess and Obsolete Inventory Reserve Calculation Review and Approval We determine, on a quarterly basis, the level of reserves required related to excess and obsolete inventory. Excess and obsolete inventory reserves are an estimate which requires significant judgment on the part of management. Our Chief Financial Officer reviews and approves these estimates on a quarterly basis. Given the significant nature of the estimate, we determined during the course of our internal controls evaluations that improved documentation of those reviews was needed. We will document the quarterly management reviews of excess and obsolete calculations beginning with the reviews performed in the first quarter of 2005.

Because of these material weaknesses, management has concluded that the Company did not maintain effective internal control over financial reporting at December 31, 2004, as well as at June 26, 2004, based on the criteria set forth in the COSO *Internal Control-Integrated Framework*.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2004 has been audited by Grant Thornton LLP, an independent registered public accounting firm, as stated in their report which is included in our Annual Report on Form 10-K for the year ended December 31, 2004.

Changes in internal controls. There was no change in our internal controls over financial reporting which was identified in connection with the evaluation required by Rule 13(a)-15(d) of the Exchange Act that occurred during our second quarter ended June 26, 2004 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

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PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) The following exhibits are filed herewith:

| Number | Exhibit Description |
|---------------|--|
| 31.1 | Certification of President and Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Vice President, Finance and Administration, Chief Financial Officer, Treasurer and Secretary Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification Pursuant to U.S.C. 1350 adopted Pursuant to Section 906 of the Sarbanes- Oxley Act of 2002. |

(b) Reports on Form 8-K:

- (1) On April 23, 2004, we filed a report on Form 8-K regarding the issuance of a press release announcing our results for the three months ended March 27, 2004.
- (2) On May 18, 2004, we filed a report on Form 8-K regarding a business presentation provided to investors.
- (3) On July 13, 2004, we filed a report on Form 8-K regarding the issuance of a press release announcing our results for the three months ended June 26, 2004.

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SIGNATURES

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

INTEVAC, INC.

Date: May 10, 2005

By: /s/ KEVIN FAIRBAIRN
Kevin Fairbairn
President, Chief Executive Officer and
Director (Principal Executive Officer)

Date: May 10, 2005

By: /s/ CHARLES B. EDDY III
Charles B. Eddy III
Vice President, Finance and
Administration, Chief Financial Officer,
Treasurer and Secretary (Principal
Financial and Accounting Officer)

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