INTEVAC INC
Form 10-Q
July 29, 2014
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended June 28, 2014

OR

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

For the transition period from to

Commission file number 0-26946

INTEVAC, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-3125814**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**

3560 Bassett Street

Santa Clara, California 95054

(Address of principal executive office, including Zip Code)

Registrant s telephone number, including area code: (408) 986-9888

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

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 x	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

On July 25, 2014, 23,625,343 shares of the Registrant s Common Stock, $0.001 par value, were outstanding.

Table of Contents

INTEVAC, INC.

INDEX

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. ***Financial Statements***

INTEVAC, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

	June 28, 2014	December 31, 2013
	(Unaudited)	
	(In thousands, except par value)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 25,059	$ 20,121
Short-term investments	33,173	48,975
Trade and other accounts receivable, net of allowances of $0 at both June 28, 2014 and at December 31, 2013	9,265	15,037
Inventories	22,613	22,762
Prepaid expenses and other current assets	1,443	1,237
Total current assets	91,553	108,132
Long-term investments	17,064	12,318
Restricted cash	1,000	
Property, plant and equipment, net	13,316	12,945
Intangible assets, net of amortization of $3,953 at June 28, 2014 and $3,485 at December 31, 2013	4,434	4,902
Deferred income taxes and other long-term assets	9,873	9,979
Total assets	$ 137,240	$ 148,276
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 4,256	$ 4,011
Accrued payroll and related liabilities	4,237	5,034
Other accrued liabilities	2,836	3,263
Customer advances	2,114	3,743
Deferred income taxes	939	939
Total current liabilities	14,382	16,990
Other long-term liabilities	2,175	1,715
Stockholders equity:		
Common stock, $0.001 par value	24	24
Additional paid-in capital	158,490	156,359
Treasury stock, 437 shares at June 28, 2014 and 241 shares at December 31, 2013	(3,157)	(1,688)
Accumulated other comprehensive income	703	725
Accumulated deficit	(35,377)	(25,849)
Total stockholders equity	120,683	129,571

Total liabilities and stockholders equity	$ 137,240	$ 148,276

Note: Amounts as of December 31, 2013 are derived from the December 31, 2013 audited consolidated financial statements.

See accompanying notes to the condensed consolidated financial statements.

Table of Contents

INTEVAC, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(Unaudited) (In thousands, except per share amounts)			
Net revenues:				
Systems and components	$ 12,038	$ 13,234	$ 25,358	$ 22,120
Technology development	2,677	3,749	6,372	7,845
Total net revenues	14,715	16,983	31,730	29,965
Cost of net revenues:				
Systems and components	7,540	10,173	17,276	16,480
Technology development	1,964	2,981	4,433	6,142
Total cost of net revenues	9,504	13,154	21,709	22,622
Gross profit	5,211	3,829	10,021	7,343
Operating expenses:				
Research and development	4,558	5,584	8,831	11,943
Selling, general and administrative	5,899	5,235	11,160	11,206
Total operating expenses	10,457	10,819	19,991	23,149
Loss on divestiture				(208)
Loss from operations	(5,246)	(6,990)	(9,970)	(16,014)
Interest income and other, net	120	92	192	172
Loss before income taxes	(5,126)	(6,898)	(9,778)	(15,842)
Benefit from income taxes	119	486	250	1,166
Net loss	$ (5,007)	$ (6,412)	$ (9,528)	$ (14,676)
Net loss per share:				
Basic and diluted	$ (0.21)	$ (0.27)	$ (0.40)	$ (0.62)
Weighted average common shares outstanding:				
Basic and diluted	23,927	23,785	23,892	23,724

See accompanying notes to the condensed consolidated financial statements.

Table of Contents

INTEVAC, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(Unaudited) (In thousands)			
Net loss	$ (5,007)	$ (6,412)	$ (9,528)	$ (14,676)
Other comprehensive income (loss), before tax:				
Change in unrealized net loss on available-for-sale investments	(11)	(74)	(6)	(89)
Foreign currency translation gains (losses)	15	(4)	(16)	(10)
Other comprehensive income (loss), before tax	4	(78)	(22)	(99)
Income tax benefit related to items in other comprehensive income				
Other comprehensive income (loss), net of tax	4	(78)	(22)	(99)
Comprehensive loss	$ (5,003)	$ (6,490)	$ (9,550)	$ (14,775)

See accompanying notes to the condensed consolidated financial statements.

Table of Contents

INTEVAC, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six months ended	
	June 28, 2014	**June 29, 2013**
	(Unaudited)	
	(In thousands)	
Operating activities		
Net loss	$ (9,528)	$ (14,676)
Adjustments to reconcile net loss to net cash and cash equivalents used in operating activities:		
Depreciation and amortization	2,336	2,093
Net amortization of investment premiums and discounts	358	431
Equity-based compensation	1,363	1,082
Change in the fair value of acquisition-related contingent consideration	97	(209)
Deferred income taxes	(316)	(1,324)
Loss on divestiture		208
Changes in operating assets and liabilities	3,066	8,242
Total adjustments	6,904	10,523
Net cash and cash equivalents used in operating activities	(2,624)	(4,153)
Investing activities		
Purchases of investments	(23,878)	(24,384)
Proceeds from sales and maturities of investments	35,076	25,727
Proceeds from sale of DeltaNu assets		500
Increase in restricted cash	(1,000)	
Purchases of leasehold improvements and equipment	(2,240)	(835)
Net cash and cash equivalents provided by investing activities	7,958	1,008
Financing activities		
Net proceeds from issuance of common stock	1,178	1,144
Common stock repurchases	(1,559)	
Net cash and cash equivalents provided by (used in) financing activities	(381)	1,144
Effect of exchange rate changes on cash and cash equivalents	(15)	(10)
Net increase (decrease) in cash and cash equivalents	4,938	(2,011)
Cash and cash equivalents at beginning of period	20,121	24,261
Cash and cash equivalents at end of period	$ 25,059	$ 22,250

See accompanying notes to the condensed consolidated financial statements.

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation

In the opinion of management, the unaudited interim condensed consolidated financial statements of Intevac, Inc. and its subsidiaries (Intevac or the Company) included herein have been prepared on a basis consistent with the December 31, 2013 audited consolidated financial statements and include all material adjustments, consisting of normal recurring adjustments, necessary to fairly present the information set forth therein. These unaudited interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in Intevac s Annual Report on Form 10-K for the fiscal year ended December 31, 2013 (2013 Form 10-K). Intevac s results of operations for the six months ended June 28, 2014 are not necessarily indicative of future operating results.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make judgments, estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ materially from those estimates.

2. Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606) which provides guidance for revenue recognition. This ASU affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets. This ASU will supersede the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. This ASU also supersedes some cost guidance included in Subtopic 605-35, Revenue Recognition-Construction-Type and Production-Type Contracts. The standard s core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under today s guidance. These may include 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 separate performance obligation. The standard will be effective for Intevac in the first quarter of fiscal 2017 using one of two retrospective application methods. Early adoption is not permitted. We are currently evaluating the impact of the adoption of this accounting standard update on our consolidated financial statements.

In April 2014, the FASB issued authoritative guidance that raises the threshold for a disposal transaction to qualify as a discontinued operation and requires additional disclosures about discontinued operations and disposals of individually significant components that do not qualify as discontinued operations. The authoritative guidance becomes effective prospectively for Intevac in the first quarter of fiscal 2015. Early adoption is permitted, but only for disposals that have not been reported in financial statements previously issued.

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

3. Inventories

Inventories are stated at the lower of average cost or market and consist of the following:

	June 28, 2014	December 31, 2013
	(In thousands)	
Raw materials	$ 12,517	$ 13,005
Work-in-progress	8,596	8,196
Finished goods	1,500	1,561
	$ 22,613	$ 22,762

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

4. Equity-Based Compensation

At June 28, 2014, Intevac had equity-based awards outstanding under the 2012 Equity Incentive Plan and the 2004 Equity Incentive Plan (the Plans) and the 2003 Employee Stock Purchase Plan (the ESPP). Intevac s stockholders approved all of these plans. The Plans permit the grant of incentive or non-statutory stock options, restricted stock, stock appreciation rights, restricted stock units (RSUs, also referred to as performance units) and performance shares.

The ESPP provides that eligible employees may purchase Intevac s common stock through payroll deductions at a price equal to 85% of the lower of the fair market value at the beginning of the applicable offering period or at the end of each applicable purchase interval. Offering periods are generally two years in length, and consist of a series of six-month purchase intervals. Eligible employees may join the ESPP at the beginning of any six-month purchase interval. Under the terms of the ESPP, employees can choose to have up to 15% of their base earnings withheld to purchase Intevac common stock.

Compensation Expense

The effect of recording equity-based compensation for the three and six months ended June 28, 2014 and June 29, 2013 was as follows:

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(In thousands)			
Equity-based compensation by type of award:				
Stock options	$ 153	$ 104	$ 394	$ 277
RSUs	376	108	668	184
Employee stock purchase plan	137	307	301	621
Total equity-based compensation	$ 666	$ 519	$ 1,363	$ 1,082

Tax benefit recognized	$ 3	$ 5	$ 6	$ 10

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Equity-based compensation expense is based on awards ultimately expected to vest and such amount has been reduced for estimated forfeitures. Forfeitures were estimated based on Intevac s historical experience, which Intevac believes to be indicative of Intevac s future experience.

Stock Options and ESPP

The fair value of stock options and ESPP awards is estimated at the grant date using the Black-Scholes option valuation model. The determination of fair value of stock options and ESPP awards on the date of grant using an option-pricing model is affected by Intevac s stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards and actual employee stock option exercise behavior.

Option activity as of June 28, 2014 and changes during the six months ended June 28, 2014 were as follows:

	Shares	Weighted Average Exercise Price
Options outstanding at December 31, 2013	2,637,969	$ 8.53
Options granted	460,735	$ 7.35
Options cancelled and forfeited	(89,082)	$ 8.48
Options exercised	(83,113)	$ 4.45
Options outstanding at June 28, 2014	2,926,509	$ 8.46
Vested and expected to vest at June 28, 2014	2,687,654	$ 8.63
Options exercisable at June 28, 2014	1,565,514	$ 10.01

Intevac issued 224,000 shares under the ESPP during the six months ended June 28, 2014.

Intevac estimated the weighted-average fair value of stock options and employee stock purchase rights using the following weighted-average assumptions:

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
Stock Options:				
Weighted-average fair value of grants per share	$ 3.02	$ 2.11	$ 3.14	$ 2.10
Expected volatility	52.11%	58.04%	52.38%	57.95%
Risk free interest rate	1.30%	1.18%	1.36%	1.16%
Expected term of options (in years)	4.2	4.5	4.3	4.4
Dividend yield	None	None	None	None

	Six Months Ended	
	June 28, 2014	June 29, 2013
Stock Purchase Rights:		

Weighted-average fair value of grants per share	$ 2.15	$ 1.60
Expected volatility	43.40%	52.42%
Risk free interest rate	0.11%	0.26%
Expected term of purchase rights (in years)	0.74	1.85
Dividend yield	None	None

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The computation of the expected volatility assumptions used in the Black-Scholes calculations for new stock option grants and purchase rights is based on the historical volatility of Intevac s stock price, measured over a period equal to the expected term of the stock option grant or purchase right. The risk-free interest rate is based on the yield available on U.S. Treasury Strips with an equivalent remaining term. The expected term of employee stock options represents the weighted-average period that the stock options are expected to remain outstanding and was determined based on historical experience of similar awards, giving consideration to the contractual terms of the equity-based awards and vesting schedules. The expected term of purchase rights represents the period of time remaining in the current offering period. The dividend yield assumption is based on Intevac s history of not paying dividends and the assumption of not paying dividends in the future.

RSUs

A summary of the RSU activity is as follows:

	Shares	Weighted Average Grant Date Fair Value
Non-vested RSUs at December 31, 2013	237,859	$ 5.34
Granted	226,373	$ 7.29
Vested	(69,650)	$ 5.39
Cancelled and forfeited	(13,909)	$ 5.68
Non-vested RSUs at June 28, 2014	380,673	$ 6.48

RSUs are converted into shares of Intevac common stock upon vesting on a one-for-one basis. RSUs typically are scheduled to vest over four years. Vesting of RSUs is subject to the grantee s continued service with Intevac. The compensation expense related to these awards is determined using the fair market value of Intevac common stock on the date of the grant, and the compensation expense is recognized over the vesting period. In fiscal 2014, the annual bonus for participants in the Company s annual incentive plan will be settled with RSUs with one year vesting. The Company accrued for the payment of bonuses at the expected company-wide payout percentage amount at June 28, 2014, which amounts were less than the target bonus amounts for each participant. The bonus accrual is classified as a liability until the number of shares is determined on the date the awards are granted, at which time the Company classifies the awards into equity. The Company recorded equity-based compensation expense related to the annual incentive plan of $161,000 and $322,000, respectively for the three and six months ended June 28, 2014.

Performance-based RSUs (performance-based awards) granted in fiscal 2013 to certain executive officers are also subject to the achievement of specified performance goals. These performance-based awards become eligible to vest only if performance goals are achieved and then actually will vest only if the grantee remains employed by Intevac through each applicable vesting date. The fair value of these performance-based awards is estimated on the date of grant and assumes that the specified performance goals will be achieved. If the goals are achieved, these awards vest over a specified remaining service period, provided that the grantee remains employed by Intevac through each scheduled vesting date. If the performance goals are not met, no compensation expense is recognized and any previously recognized compensation expense is reversed. The expected cost of each award is reflected over the service period and is reduced for estimated forfeitures. For performance-based awards granted during fiscal 2013, the performance goals require the achievement of targeted revenues and adjusted annual operating profit levels measured at the end of two and three-year periods.

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

5. Purchased Intangible Assets

Details of finite-lived intangible assets by segment as of June 28, 2014, are as follows.

	June 28, 2014		
	Gross Carrying Amount	Accumulated Amortization (In thousands)	Net Carrying Amount
Equipment	$ 7,172	$ (3,220)	$ 3,952
Photonics	1,215	(733)	482
	$ 8,387	$ (3,953)	$ 4,434

Total amortization expense of finite-lived intangibles for the three and six months ended June 28, 2014 was $234,000 and $468,000.

As of June 28, 2014, future amortization expense is expected to be as follows.

(In thousands)	
2014	$ 468
2015	853
2016	853
2017	756
2018	615
Thereafter	889
	$ 4,434

6. Acquisition-Related Contingent Consideration

In connection with the acquisition of Solar Implant Technologies, Inc. (SIT), Intevac agreed to pay to the selling shareholders in cash a revenue earnout on Intevac s net revenue from commercial sales of certain products over a specified period up to an aggregate of $9.0 million. Intevac estimated the fair value of this contingent consideration on June 28, 2014 based on probability-based forecasted revenues reflecting Intevac s own assumptions concerning future revenue from such products. As of June 28, 2014, payments made associated with the revenue earnout obligation have not been significant.

The fair value measurement of contingent consideration is based on significant inputs not observed in the market and thus represents a Level 3 measurement. Any change in fair value of the contingent consideration subsequent to the acquisition date is recognized in operating income within the statement of operations. The following table represents a reconciliation of the change in the fair value measurement of the contingent consideration liability for the three and six month periods ended June 28, 2014 and June 29, 2013:

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(In thousands)			
Opening balance	$ 1,435	$ 5,262	$ 1,384	$ 5,151
Changes in fair value	46	(320)	97	(209)
Closing balance	$ 1,481	$ 4,942	$ 1,481	$ 4,942

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The following table displays the balance sheet classification of the contingent consideration liability account at June 28, 2014 and at December 31, 2013:

	June 28, 2014	December 31, 2013
	(In thousands)	
Other accrued liabilities	$ 140	$ 164
Other long-term liabilities	1,341	1,220
Total acquisition-related contingent consideration	$ 1,481	$ 1,384

The following table represents the quantitative range of the significant unobservable inputs used in the calculation of fair value of the continent consideration liability as of June 28, 2014. Significant increases or decreases in any of these inputs in isolation would result in a significantly lower (higher) fair value measurement.

	Quantitative Information about Level 3 Fair Value Measurements at June 28, 2014			
	Fair Value	Valuation Technique	Unobservable Input	Range (Weighted Average)
	(In thousands, except for percentages)			
Revenue Earnout	$ 1,481	Discounted cash flow	Weighted average cost of capital	17.2%
			Probability weighting of achieving revenue forecasts	20.0% - 55.0% (33.0%)

7. Divestiture

Sale of DeltaNu

On March 29, 2013, the Company sold certain assets, including existing tangible and intangible assets, which comprised its Raman spectroscopy instruments product line, also known as DeltaNu, for consideration not to exceed $1.5 million. Under the terms of the agreement, the acquirer also assumed certain liabilities related to the purchased assets. Payment terms included $500,000 which was paid on the closing date, with the remaining balance to be paid in the form of an earnout of 5% of the acquirer s Raman spectroscopy instrument sales for 5 years following the closing date which will be due and payable on or before each anniversary of the closing date or a minimum earnout payment of $100,000 annually, whichever is higher. The maximum earnout payments during the payment period shall not exceed $1.0 million.

As the earnout is collected over an extended period of time and in management s judgment the degree of collectibility is uncertain, Intevac did not recognize the minimum earnout payments upon closing, but instead will record income in the period when the minimum earnout payments can be reasonably estimated for that period and payment is assured. The first earnout payment in the amount of $75,000 was received in the second quarter of fiscal 2014 and was reported in interest and other income, net on the condensed consolidated statement of operations.

The following table summarizes the components of the loss (in thousands):

Cash proceeds	$ 500
Assets sold:	
Accounts receivable	147
Inventories	320
Other current assets	27
Property, plant and equipment	159
Trade name	90
Total assets sold	743
Liabilities divested:	
Accounts payable	59
Other accrued expenses	6
Total liabilities divested	65
Transaction and other costs	30
Loss on sale	$ (208)

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

8. Warranty

Intevac provides for the estimated cost of warranty when revenue is recognized. Intevac s warranty is per contract terms, and for systems sold directly the warranty typically ranges between 12 and 24 months from customer acceptance. For systems sold through a distributor, Intevac offers a 3 month warranty. The remainder of any warranty period is the responsibility of the distributor. During this warranty period any defective non-consumable parts are replaced and installed at no charge to the customer. The warranty period on consumable parts is limited to their reasonable usable lives. Intevac uses estimated repair or replacement costs along with its historical warranty experience to determine its warranty obligation. Intevac generally provides a twelve month warranty on its Photonics products. The provision for the estimated future costs of warranty is based upon historical cost and product performance experience. Intevac exercises judgment in determining the underlying estimates.

On the condensed consolidated balance sheets, the short-term portion of the warranty provision is included in other accrued liabilities, while the long-term portion is included in other long-term liabilities. The expense associated with product warranties issued or adjusted is included in cost of net revenues on the condensed consolidated statements of operations.

The following table displays the activity in the warranty provision account for the three and six months ended June 28, 2014 and June 29, 2013:

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(In thousands)			
Opening balance	$ 1,331	$ 2,225	$ 1,647	$ 2,349
Expenditures incurred under warranties	(217)	(210)	(523)	(464)
Accruals for product warranties issued during the reporting period	219	329	504	538
Adjustments to previously existing warranty accruals	(177)	(257)	(472)	(336)
Closing balance	$ 1,156	$ 2,087	$ 1,156	$ 2,087

The following table displays the balance sheet classification of the warranty provision account at June 28, 2014 and at December 31, 2013:

	June 28, 2014	December 31, 2013
	(In thousands)	
Other accrued liabilities	$ 989	$ 1,546
Other long-term liabilities	167	101
Total warranty provision	$ 1,156	$ 1,647

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

9. Guarantees

Officer and Director Indemnifications

As permitted or required under Delaware law and to the maximum extent allowable under that law, Intevac has certain obligations to indemnify its current and former officers and directors for certain events or occurrences while the officer or director is, or was serving, at Intevac s request in such capacity. These indemnification obligations are valid as long as the director or officer acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the Company and, with respect to any criminal action or proceeding, had no reasonable cause to believe his or her conduct was unlawful. The maximum potential amount of future payments Intevac could be required to make under these indemnification obligations is unlimited; however, Intevac has a director and officer insurance policy that mitigates Intevac s exposure and enables Intevac to recover a portion of any future amounts paid. As a result of Intevac s insurance policy coverage, Intevac believes the estimated fair value of these indemnification obligations is not material.

Other Indemnifications

As is customary in Intevac s industry, many of Intevac s contracts provide remedies to certain third parties such as defense, settlement, or payment of judgments for intellectual property claims related to the use of its products. Such indemnification obligations may not be subject to maximum loss clauses. Historically, payments made related to these indemnifications have been immaterial.

10. Cash, Cash Equivalents and Investments

Cash and cash equivalents, short-term investments and long-term investments consist of:

	June 28, 2014			
	Amortized Cost	Unrealized Holding Gains	Unrealized Holding Losses	Fair Value
	(In thousands)			
Cash and cash equivalents:				
Cash	$ 7,467	$	$	$ 7,467
Money market funds	17,592			17,592
Total cash and cash equivalents	$ 25,059	$	$	$ 25,059
Short-term investments:				
Certificate of deposit	$ 1,000	$	$	$ 1,000
Commercial paper	499			499
Corporate bonds and medium-term notes	22,977	18	1	22,994
Municipal bonds	4,669	5		4,674
U.S. treasury and agency securities	4,003	3		4,006
Total short-term investments	$ 33,148	$ 26	$ 1	$ 33,173
Long-term investments:				
Corporate bonds and medium-term notes	$ 5,272	$	$ 3	$ 5,269
Municipal bonds	1,797	3	1	1,799
U.S. treasury and agency securities	9,992	6	2	9,996

Total long-term investments	$ 17,061	$	9	$	6	$ 17,064
Total cash, cash equivalents, and investments	$ 75,268	$	35	$	7	$ 75,296

14

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

	December 31, 2013			
	Amortized Cost	Unrealized Holding Gains	Unrealized Holding Losses	Fair Value
	(In thousands)			
Cash and cash equivalents:				
Cash	$ 5,819	$	$	$ 5,819
Money market funds	14,302			14,302
Total cash and cash equivalents	$ 20,121	$	$	$ 20,121
Short-term investments:				
Commercial paper	$ 1,998	$ 1	$	$ 1,999
Corporate bonds and medium-term notes	27,181	13	3	27,191
Municipal bonds	6,108	4		6,112
U.S. treasury and agency securities	13,506	7		13,513
Variable rate demand notes (VRDNs)	160			160
Total short-term investments	$ 48,953	$ 25	$ 3	$ 48,975
Long-term investments:				
Corporate bonds and medium-term notes	$ 8,811	$ 12	$	$ 8,823
Municipal bonds	3,495	2	2	3,495
Total long-term investments	$ 12,306	$ 14	$ 2	$ 12,318
Total cash, cash equivalents, and investments	$ 81,380	$ 39	$ 5	$ 81,414

The contractual maturities of available-for-sale securities at June 28, 2014 are presented in the following table.

	Amortized Cost	Fair Value
	(In thousands)	
Due in one year or less	$ 48,735	$ 48,761
Due after one through two years	19,066	19,068
	$ 67,801	$ 67,829

The following table provides the fair market value of Intevac s investments with unrealized losses that are not deemed to be other-than temporarily impaired as of June 28, 2014.

	June 28, 2014	
	In Loss Position for Less than 12 Months	In Loss Position for Greater than 12 Months
	Fair Value	Fair Value

		Gross Unrealized Losses		Gross Unrealized Losses
		(In thousands)		
Corporate bonds and medium-term notes	$ 8,829	$ 4	$	$
Municipal bonds	2,771	1		
U.S. treasury and agency securities	1,998	2		
	$ 13,598	$ 7	$	$

All prices for the fixed maturity securities including U.S. Treasury and agency securities, certificates of deposit, commercial paper, corporate bonds, VRDNs and municipal bonds are received from independent pricing services

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

utilized by Intevac s outside investment manager. This investment manager performs a review of the pricing methodologies and inputs utilized by the independent pricing services for each asset type priced by the vendor. In addition, on at least an annual basis, the investment manager conducts due diligence visits and interviews with each pricing vendor to verify the inputs utilized for each asset class. The due diligence visits include a review of the procedures performed by each vendor to ensure that pricing evaluations are representative of the price that would be received to sell a security in an orderly transaction. Any pricing where the input is based solely on a broker price is deemed to be a Level 3 price. Intevac uses the pricing data obtained from its outside investment manager as the primary input to make its assessments and determinations as to the ultimate valuation of the above-mentioned securities and has not made, during the periods presented, any material adjustments to such inputs.

The following table represents the fair value hierarchy of Intevac s available-for-sale securities measured at fair value on a recurring basis as of June 28, 2014.

	Fair Value Measurements at June 28, 2014		
	Total	Level 1	Level 2
		(In thousands)	
Recurring fair value measurements:			
Available-for-sale securities			
Money market funds	$ 17,592	$ 17,592	$
U.S. treasury and agency securities	14,002	8,997	5,005
Certificate of deposit	1,000		1,000
Commercial paper	499		499
Corporate bonds and medium-term notes	28,263		28,263
Municipal bonds	6,473		6,473
Total recurring fair value measurements	$ 67,829	$ 26,589	$ 41,240

11. Derivative Instruments

The Company uses foreign currency forward contracts to mitigate variability in gains and losses generated from the re-measurement of certain monetary assets and liabilities denominated in foreign currencies. These hedges do not qualify for special hedge accounting treatment. These derivatives are carried at fair value with changes recorded in interest income and other, net in the condensed consolidated statements of operations. Changes in the fair value of these derivatives are largely offset by re-measurement of the underlying assets and liabilities. Cash flows from such derivatives are classified as operating activities. The derivatives have maturities of approximately one month. The notional amount of Company s foreign currency derivatives was $474,000 at June 28, 2014 and $894,000 at December 31, 2013.

12. Equity

Stock Repurchase Program

On November 21, 2013, Intevac s Board of Directors approved a stock repurchase program authorizing up to $30.0 million in repurchases. At June 28, 2014, $26.8 million remains available for future stock repurchases under the repurchase program.

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The following table summarizes Intevac s stock repurchases:

	Three Months Ended	Six Months Ended
	June 28, 2014 (In thousands, except per share amounts)	
Shares of common stock repurchased	58	195
Cost of stock repurchased	$ 419	$ 1,469
Average price paid per share	$ 7.21	$ 7.49

Intevac records treasury stock purchases under the cost method using the first-in, first-out (FIFO) method. Upon reissuance of treasury stock, amounts in excess of the acquisition cost are credited to additional paid in capital. If Intevac reissues treasury stock at an amount below its acquisition cost and additional paid in capital associated with prior treasury stock transactions is insufficient to cover the difference between the acquisition cost and the reissue price, this difference is recorded against retained earnings.

Accumulated Other Comprehensive Income

The changes in accumulated other comprehensive income by component for the three and six months ended June 28, 2014 and June 29, 2013, are as follows.

	Three Months Ended			Six Months Ended		
	June 28, 2014					
	Foreign currency	Unrealized holding gains on available-for-sale investments	Total	Foreign currency	Unrealized holding gains on available-for-sale investments	Total
	(In thousands)					
Beginning balance	$ 660	$ 39	$ 699	$ 691	$ 34	$ 725
Other comprehensive income (loss) before reclassification	15	(11)	4	(16)	(6)	(22)
Amounts reclassified from other comprehensive income						
Net current-period other comprehensive income (loss)	15	(11)	4	(16)	(6)	(22)
Ending balance	$ 675	$ 28	$ 703	$ 675	$ 28	$ 703

Table of Contents

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

	Three Months Ended			Six Months Ended		
			June 29, 2013			
	Foreign currency	Unrealized holding gains on available-for-sale investments	Total	Foreign currency	Unrealized holding gains on available-for-sale investments	Total
			(In thousands)			
Beginning balance	$ 688	$ 60	$ 748	$ 694	$ 75	$ 769
Other comprehensive loss before reclassification	(4)	(74)	(78)	(10)	(89)	(99)
Amounts reclassified from other comprehensive income						
Net current-period other comprehensive loss	(4)	(74)	(78)	(10)	(89)	(99)
Ending balance	$ 684	$ (14)	$ 670	$ 684	$ (14)	$ 670

13. Net Loss Per Share

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

	Three Months Ended		Six Months Ended	
	June 28 2014	June 29, 2013	June 28 2014	June 29, 2013
	(In thousands, except per share amounts)			
Net loss	$ (5,007)	$ (6,412)	$ (9,528)	$ (14,676)
Weighted-average shares basic	23,927	23,785	23,892	23,724
Effect of dilutive potential common shares				
Weighted-average shares diluted	23,927	23,785	23,892	23,724
Net loss per share basic and diluted	$ (0.21)	$ (0.27)	$ (0.40)	$ (0.62)
Antidilutive shares based on employee awards excluded	1,977	2,690	1,911	2,696

Potentially dilutive common shares consist of shares issuable upon exercise of employee stock options and vesting of RSUs and are excluded from the calculation of diluted EPS when their effect would be anti-dilutive.

14. Segment Reporting

Intevac s two reportable segments are: Equipment and Photonics. Intevac s chief operating decision-maker has been identified as the President and CEO, who reviews operating results to make decisions about allocating resources and assessing performance for the entire Company. Segment information is presented based upon Intevac s management organization structure as of June 28, 2014 and the distinctive nature of each segment. Future changes to this internal financial structure may result in changes to the reportable segments disclosed.

Each reportable segment is separately managed and has separate financial results that are reviewed by Intevac s chief operating decision-maker. Each reportable segment contains closely related products that are unique to the particular segment. Segment operating profit is determined based upon internal performance measures used by the chief operating decision-maker.

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Intevac derives the segment results from its internal management reporting system. The accounting policies Intevac uses to derive reportable segment results are substantially the same as those used for external reporting purposes. Management measures the performance of each reportable segment based upon several metrics, including orders, net revenues and operating income. Management uses these results to evaluate the performance of, and to assign resources to, each of the reportable segments. Intevac manages certain operating expenses separately at the corporate level. Intevac allocates certain of these corporate expenses to the segments in an amount equal to 3% of net revenues. Segment operating income excludes interest income/expense and other financial charges and income taxes according to how a particular reportable segment s management is measured. Management does not consider impairment charges, gains and losses on divestitures and sales of intellectual property, and unallocated costs in measuring the performance of the reportable segments.

The Equipment segment designs, develops and markets vacuum process equipment solutions for high-volume manufacturing of small substrates with precise thin film properties for hard drive and solar cell manufacturers as well as other adjacent thin film deposition applications.

The Photonics segment develops compact, cost-effective, high-sensitivity digital-optical products for the capture and display of low-light images and the optical analysis of materials. Intevac provides sensors, cameras and systems for government applications such as night vision and long-range target identification.

Information for each reportable segment for the three and six months ended June 28, 2014 and June 29, 2013 is as follows:

Net Revenues

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(In thousands)			
Equipment	$ 3,762	$ 9,164	$ 12,809	$ 14,532
Photonics	10,953	7,819	18,921	15,433
Total segment net revenues	$ 14,715	$ 16,983	$ 31,730	$ 29,965

Operating Income (Loss)

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	(In thousands)			
Equipment	$ (5,667)	$ (5,841)	$ (9,808)	$ (13,183)
Photonics	2,567	253	3,475	62
Total income (loss) from segment operations	(3,100)	(5,588)	(6,333)	(13,121)
Unallocated costs	(2,146)	(1,402)	(3,637)	(2,685)
Loss on divestiture				(208)

Loss from operations	(5,246)	(6,990)	(9,970)	(16,014)
Interest income and other, net	120	92	192	172
Loss before income taxes	$ (5,126)	$ (6,898)	$ (9,778)	$ (15,842)

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Total assets for each reportable segment as of June 28, 2014 and December 31, 2013 are as follows:

Assets

	June 28, 2014	December 31, 2013
	(In thousands)	
Equipment	$ 30,515	$ 33,428
Photonics	18,334	21,120
Total segment assets	48,849	54,548
Cash, cash equivalents and investments	75,296	81,414
Restricted cash	1,000	
Deferred income taxes	9,921	9,605
Other current assets	988	982
Common property, plant and equipment	1,186	1,302
Other assets		425
Consolidated total assets	$ 137,240	$ 148,276

15. Restructuring Charges

During the first quarter of fiscal 2014, Intevac substantially completed implementation of the 2014 cost reduction plan (the Plan), which was intended to reduce expenses and reduce its workforce by 6 percent. The cost of implementing the Plan was reported under cost of net revenues and operating expenses in the condensed consolidated statements of operations. Substantially all cash outlays in connection with the Plan occurred in the first half of fiscal 2014. Implementation of the Plan is expected to reduce salary, wages and other employee-related expenses by approximately $2.1 million on an annual basis.

On February 1, 2013, Intevac announced the 2013 cost reduction plan (the 2013 Plan) to reduce expenses including a reduction in its workforce. Implementation of the 2013 Plan was substantially completed in the first half of fiscal 2013 and the Company reduced its workforce by 18 percent. The cost of implementing the 2013 Plan was reported under cost of net revenues and operating expenses in the condensed consolidated statement of operations. Substantially all cash outlays in connection with the 2013 Plan occurred in the first half of fiscal 2013. As of June 28, 2014, activities related to the 2013 Plan were complete.

The changes in restructuring reserves associated with the Plans for the three and six months ended June 28, 2014 and June 29, 2013 are as follows.

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
	Severance and other employee-			

		related costs (In thousands)		
Beginning balance	$	$ 41	$	$
Provision for restructuring reserves	61	240	288	742
Cash payments made	(61)	(281)	(288)	(742)
Ending balance	$	$	$	$

16. Income Taxes

Intevac recorded income tax benefits of $119,000 and $250,000 for the three and six months ended June 28, 2014, respectively. Intevac recorded income tax benefits of $486,000 and $1.2 million for the three and six months ended June 29, 2013, respectively. The income tax provisions for the three and six month periods are based

INTEVAC, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

upon estimates of annual income (loss), annual permanent differences and statutory tax rates in the various jurisdictions in which Intevac operates. Intevac did not recognize a benefit on the U.S. net operating loss for the three and six months ended June 28, 2014 and June 29, 2013 due to having full valuation allowances on the U.S. deferred tax assets. Intevac s tax rate differs from the applicable statutory rates due primarily to establishment of a valuation allowance, the utilization of deferred and current credits and the effect of permanent differences and adjustments of prior permanent differences. Intevac s future effective income tax rate depends on various factors including, the level of Intevac s projected earnings, the geographic composition of worldwide earnings, tax regulations governing each region, net operating loss carryforwards, availability of tax credits and the effectiveness of Intevac s tax planning strategies. Management carefully monitors these factors and timely adjusts the effective income tax rate.

17. Contingencies

From time to time, Intevac may have certain contingent liabilities that arise in the ordinary course of its business activities. Intevac accounts for contingent liabilities when it is probable that future expenditures will be made and such expenditures can be reasonably estimated.

Leases

Intevac leases certain facilities under non-cancelable operating leases that expire at various times up to March 2024 and has options to renew most leases, with rentals to be negotiated. Certain of Intevac s leases contain provisions for rental adjustments. Included in other long-term liabilities on the consolidated balance sheets is $241,000 of deferred rent as of June 28, 2014 related to the effective rent on Intevac s long-term lease for Intevac s Santa Clara, California facility. The terms of the Company s lease of its Santa Clara, California facility include a tenant improvement allowance of up to $1.7 million. Tenant improvement allowances are reimbursements received from the landlord for initial construction costs and are amortized on a straight-line basis over the lease term as a reduction in rent. The tenant improvement allowances are recorded when the Company has completed its obligations and the tenant improvement allowance is receivable. In addition, Intevac is required to maintain a standby letter of credit for $1.0 million for this lease. This standby letter of credit is secured with $1.0 million of restricted cash. The facility leases require Intevac to pay for all normal maintenance costs. Gross rental expense was $1.1 million and $1.8 million for the three and six months ended June 28, 2014, respectively.

As of June 28, 2014, future minimum lease payments are as follows.

(In thousands)	
2014	$ 1,023
2015	3,195
2016	3,101
2017	2,646
2018	2,630
Thereafter	15,149
	$ 27,744

Table of Contents

Item 2. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

This Quarterly Report on Form 10-Q contains forward-looking statements, which involve risks and uncertainties. Words such as believes, expects, anticipates and the like indicate forward-looking statements. These forward-looking statements include comments related to Intevac s shipments, projected revenue recognition, product costs, gross margin, operating expenses, interest income, income taxes, cash balances and financial results in 2014 and beyond; projected customer requirements for Intevac s new and existing products, and when, and if, Intevac s customers will place orders for these products; Intevac s ability to proliferate its Photonics technology into major military programs; the timing of delivery and/or acceptance of the systems and products that comprise Intevac s backlog for revenue and the Company s ability to achieve cost savings. Intevac s actual results may differ materially from the results discussed in the forward-looking statements for a variety of reasons, including those set forth under Risk Factors and in other documents we file from time to time with the Securities and Exchange Commission, including our Annual Report on Form 10-K filed on February 20, 2014, and our periodic Form 10-Q s and Form 8-K s.

Overview

Intevac provides process manufacturing equipment solutions to the hard disk drive industry and offers high-productivity, thin film processing systems to the photovoltaic (PV) industry and to adjacent markets for thin film deposition applications. Intevac also provides sensors, cameras and systems for government applications such as night vision and long-range target identification. Intevac s customers include manufacturers of hard disk drives and PV cells as well as the U.S. government and its agencies and contractors. Intevac reports two segments: Equipment and Photonics.

Product development and manufacturing activities occur in North America and Asia. Intevac has field offices in Asia to support its equipment customers. Intevac s equipment and service products are highly technical and are sold primarily through Intevac s direct sales force. Intevac also sells its products through distributors in Japan and China.

Intevac s results are driven by worldwide demand for hard disk drives, which in turn depends on the growth in digital data creation and storage, the rate of areal density improvements, the end-user demand for personal computers, enterprise data storage, including on-line, cloud storage and near-line applications, personal audio and video players and video game platforms that include such drives. Demand for Intevac s equipment is impacted by Intevac s customers relative market share positions and production capacity needs. Intevac continues to execute its strategy of equipment diversification into new markets by introducing new products for PV solar cell manufacturing and most recently a thin film physical vapor deposition (PVD) application for protective coating for touch screen cover glass manufacturing. Intevac believes that expansion into these markets, which Intevac believes are significantly larger than the hard disk drive deposition equipment market, will result in incremental equipment revenues for Intevac and decrease Intevac s dependence on the hard disk drive industry. Intevac s equipment business is subject to cyclical industry conditions, as demand for manufacturing equipment and services can change depending on supply and demand for hard disk drives, PV cells, and cell phones as well as other factors such as global economic conditions and technological advances in fabrication processes.

Table of Contents

The following table presents certain significant measurements for the three and six months ended June 28, 2014 and June 29, 2013:

	Three months ended			Six months ended		
	June 28, 2014	**June 29, 2013**	**Change over prior period**	**June 28, 2014**	**June 29, 2013**	**Change over prior period**
	(In thousands, except percentages and per share amounts)					
Net revenues	$ 14,715	$ 16,983	$ (2,268)	$ 31,730	$ 29,965	$ 1,765
Gross profit	$ 5,211	$ 3,829	$ 1,382	$ 10,021	$ 7,343	$ 2,678
Gross margin percent	35.4%	22.5%	12.9 points	31.6%	24.5%	7.2 points
Loss from operations	$ (5,246)	$ (6,990)	$ 1,744	$ (9,970)	$ (16,014)	$ 6,044
Net loss	$ (5,007)	$ (6,412)	$ 1,405	$ (9,528)	$ (14,676)	$ 5,148
Loss per diluted share	$ (0.21)	$ (0.27)	$ 0.06	$ (0.40)	$ (0.62)	$ 0.22

Net revenues decreased for the second quarter of fiscal 2014 compared to the same period in the prior year primarily due to lower equipment sales to disk manufacturers and lower Photonics contract research and development (R&D), offset in part by higher Photonics product sales. In the second quarter of 2013, Intevac recognized revenue on its first production system for its solar implant ENERG*i* product. The net loss for the second quarter fiscal 2014 decreased compared to the same period in the prior year due to higher gross margins and by lower operating expenses as a result of cost reduction efforts, offset in part by lower revenues and increased costs associated with a contested Board of Directors election.

Net revenues increased for the first six months for fiscal 2014 compared to the same period in the prior year primarily due to higher Photonics product sales offset in part by lower equipment sales to disk manufacturers and lower Photonics contract R&D. Intevac recognized revenue on one 200 Lean system in the first half of fiscal 2014 and did not recognize revenue on any 200 Lean systems in the first half of fiscal 2013. The net loss for the first six months of fiscal 2014 decreased compared to the same period in the prior year due to higher revenues, higher gross margins and lower operating expenses as a result of cost reduction efforts offset in part by increased costs associated with a contested Board of Directors election.

In fiscal 2014, Intevac expects that demand for and growth in hard disk media may increase, but this demand will not exceed the existing capacity during the year. The Company therefore expects that shipments of Intevac equipment to hard disk drive manufacturers will be approximately at the same levels as 2013. In 2014, Intevac expects higher sales of new thin-film equipment products. For fiscal 2014, Intevac expects that Photonics business levels will increase from 2013 as Photonics delivers production shipments of the pilot night vision system for the Apache helicopter.

Intevac s trademarks, include the following: 200 Lean®, AccuLuber , EBAPS®, ENERG*i* , I-Port , LithoPrime®, INTEVAC, INTEVAC MATRIX , MicroVista®, NightVista® and Night Port.

Table of Contents

Results of Operations

Net revenues

	Three months ended				Six months ended	
	June 28, 2014	June 29, 2013	Change over prior period	June 28, 2014	June 29, 2013	Change over prior period
			(In thousands)			
Equipment	$ 3,762	$ 9,164	$ (5,402)	$ 12,809	$ 14,532	$ (1,723)
Photonics:						
Products	8,276	4,070	4,206	12,549	7,588	4,961
Contract R&D	2,677	3,749	(1,072)	6,372	7,845	(1,473)
	10,953	7,819	3,134	18,921	15,433	3,488
Total net revenues	$ 14,715	$ 16,983	$ (2,268)	$ 31,730	$ 29,965	$ 1,765

Equipment revenue for the three and six months ended June 28, 2014 decreased over the same periods in the prior year as a result of lower sales of technology upgrades, service and spare parts. During the second quarter of 2014 Intevac recognized revenue on disk equipment technology upgrades, spare parts and service. During the second quarter of 2013 Intevac recognized revenue on one solar implant ENERG*i* system, disk equipment technology upgrades, spare parts and service. Equipment revenue for the six months ended June 28, 2014 included revenue recognition for one 200 Lean system, upgrades and spare parts. Equipment revenue for the six months ended June 29, 2013 included revenue recognition for one solar implant ENERG*i* system, two AccuLuber systems, upgrades and spare parts.

Photonics revenue for the three and six month periods ended June 28, 2014 increased over the same periods in the prior year as a result of increased product sales offset in part by lower contract R&D work. The decrease in contract R&D revenue was the result of completion of the program to design the Apache pilot night viewing system during mid-2013. The increase in product sales resulted from the transition to production deliveries for the Apache pilot night viewing camera at the end of 2013. On March 29, 2013, Intevac sold certain assets comprising its Raman spectroscopy instruments product line, also known as DeltaNu, and no longer offers Raman spectroscopy products.

Backlog

	June 28, 2014	December 31, 2013	June 29, 2013
		(In thousands)	
Equipment	$ 8,613	$ 13,565	$ 29,295
Photonics	37,772	46,319	48,295
Total backlog	$ 46,385	$ 59,884	$ 77,590

Equipment backlog at June 28, 2014 included one PV deposition system and one PVD touch screen cover glass coating system. Equipment backlog at December 31, 2013 included one 200 Lean system and one PV deposition system. Equipment backlog at June 29, 2013 included three 200 Lean systems. Photonics backlog at June 28, 2014 includes $28.8 million in revenue that will be earned in one year and $9.0 million in revenue that will be earned beyond one year.

Table of Contents

Revenue by geographic region

	Three months ended			Six months ended		
	June 28, 2014	June 29, 2013	Change over prior period	June 28, 2014	June 29, 2013	Change over prior period
	(In thousands)					
United States	$ 10,843	$ 9,714	$ 1,129	$ 25,351	$ 17,047	$ 8,304
Asia	2,937	5,881	(2,944)	4,417	10,366	(5,949)
Europe	935	1,388	(453)	1,962	2,552	(590)
Total net revenues	$ 14,715	$ 16,983	$ (2,268)	$ 31,730	$ 29,965	$ 1,765

International sales include products shipped to overseas operations of U.S. companies. The increase in U.S. sales in 2014 versus 2013 was primarily due to delivery of a 200 Lean system to a U.S. customer, higher camera sales and the initial production shipments of the pilot night vision camera for the Apache helicopter. The decrease in sales to the Asia region in 2014 versus 2013 was primarily due to lower net revenues from solar implant systems, disk lubrication systems and technology upgrades. The decrease in sales to the Europe region in 2014 versus 2013 was primarily due to lower sales of Photonics digital night-vision cameras to a NATO customer.

Gross profit

	Three months ended			Six months ended		
	June 28, 2014	June 29, 2013	Change over prior period	June 28, 2014	June 29, 2013	Change over prior period
	(In thousands, except percentages)					
Equipment gross profit	$ 312	$ 1,352	$ (1,040)	$ 2,317	$ 2,554	$ (237)
% of Equipment net revenues	8.3%	14.8%		18.1%	17.6%	
Photonics gross profit	$ 4,899	$ 2,477	$ 2,422	$ 7,704	$ 4,789	$ 2,915
% of Photonics net revenues	44.7%	31.7%		40.7%	31.0%	
Total gross profit	$ 5,211	$ 3,829	$ 1,382	$ 10,021	$ 7,343	$ 2,678
% of net revenues	35.4%	22.5%		31.6%	24.5%	

Cost of net revenues consists primarily of purchased materials and costs attributable to contract research and development, and also includes fabrication, assembly, test and installation labor and overhead, customer-specific engineering costs, warranty costs, royalties, provisions for inventory reserves and scrap.

Equipment gross margin was 8.3% in the three months ended June 28, 2014 compared to 14.8% in the three months ended June 29, 2013 and was 18.1% in the six months ended June 28, 2014 compared to 17.6% in the six months ended June 29, 2013. The lower gross margin for the three months ended June 28, 2014 was due primarily to lower systems and spares shipments, offset in part by lower inventory provisions and the lower system margin on the first solar implant ENERG*i* system for which revenue was recognized in second quarter of 2013. The higher gross margin for the six months ended June 28, 2014 was due primarily to lower factory costs as a result of cost containment efforts, lower inventory provisions and the lower system margin on the first solar implant ENERG*i* system for which revenue was recognized in second quarter of 2013. Gross margins in the Equipment business will vary depending on a number of factors, including product mix, product cost, system configuration and pricing, factory utilization, and provisions for excess and obsolete inventory.

Photonics gross margin increased to 44.7% in the three months ended June 28, 2014 compared to 31.7% in the three months ended June 29, 2013 and increased to 40.7% in the six months ended June 28, 2014 compared to 31.0% in the six months ended June 29, 2013. The higher gross margin for the three months ended June 28, 2014 was due to higher margins on both products and contract R&D and lower inventory provisions. The higher gross margin for the six months ended June 28, 2014 was due to higher margins on contract R&D, lower warranty costs and lower inventory provisions. Gross margins in the Photonics business will vary depending on a number of factors, including sensor yield, product mix, product cost, pricing, factory utilization, provisions for warranty and inventory reserves.

Table of Contents

Research and development

	Three months ended			Six months ended		
	June 28, 2014	**June 29, 2013**	**Change over prior period**	**June 28, 2014**	**June 29, 2013**	**Change over prior period**
			(In thousands)			
Research and development expense	$ 4,558	$ 5,584	$ (1,026)	$ 8,831	$ 11,943	$ (3,112)

Research and development spending decreased in Equipment and in Photonics during the three and six month periods ended June 28, 2014 as compared to the same periods in the prior year. The decrease in Equipment spending was due primarily to decreased PV development and from cost reduction initiatives. Photonics research and development spending during the first half of fiscal 2013 included costs from DeltaNu which did not re-occur in the first half of fiscal 2014 as DeltaNu was sold on March 29, 2013. Research and development expenses do not include costs of $2.0 million and $4.4 million for the three and six months ended June 28, 2014 respectively, or $3.0 million and $6.1 million for the three and six months ended June 29, 2013, respectively, which are related to customer-funded contract R&D programs at Photonics and therefore included in cost of net revenues.

Selling, general and administrative

	Three months ended			Six months ended		
	June 28, 2014	**June 29, 2013**	**Change over prior period**	**June 28, 2014**	**June 29, 2013**	**Change over prior period**
			(In thousands)			
Selling, general and administrative expense	$ 5,899	$ 5,235	$ 664	$ 11,160	$ 11,206	$ (46)

Selling, general and administrative expense consists primarily of selling, marketing, customer support, financial and management costs. The increase in selling, general and administrative spending in the three months ended June 28, 2014 was primarily the result of increased professional service costs associated with a contested Board of Directors election, higher charges associated with the change in the fair value of the contingent consideration obligations related to the SIT acquisition, offset in-part by lower variable compensation program expense and savings from cost reduction initiatives.

Cost reduction plans

During the first quarter of fiscal 2014, Intevac substantially completed implementation of the 2014 cost reduction plan (the Plan), which was intended to reduce expenses and reduce its workforce by 6 percent. The total cost of implementing the Plan was $288,000 of which $43,000 was reported under cost of net revenues and $245,000 was reported under operating expenses. Substantially all cash outlays in connection with the Plan occurred in the first half of fiscal 2014. Implementation of the Plan is expected to reduce salary, wages and other employee-related expenses by approximately $2.1 million on an annual basis.

During the first quarter of fiscal 2013, Intevac announced the 2013 cost reduction plan (the 2013 Plan) to reduce expenses including a reduction in its workforce. Implementation of the Plan was substantially completed in the first half of fiscal 2013 and the workforce was reduced by 18 percent. During the first half of 2013, Intevac recognized employee-related costs of $742,000 of which $315,000 was reported under cost of net revenues and $427,000 was reported under operating expenses in connection with the 2013 Plan. All cash outlays in connection with the 2013 Plan occurred in the first half of fiscal 2013. As of June 28, 2014, activities related to the 2013 Plan were complete.

Table of Contents

Loss on divestiture

On March 29, 2013, the Company sold certain assets, including existing tangible and intangible assets, which comprised its Raman spectroscopy instruments product line, also known as DeltaNu, for consideration not to exceed $1.5 million, of which $500,000 was received in cash upon closing, and recorded a loss of $208,000. The first earnout payment in the amount of $75,000 was received in the second quarter of fiscal 2014 and was reported in interest and other income, net on the condensed consolidated statement of operations. See Note 7 Divestiture in the notes to the condensed consolidated financial statements for additional information related to the loss on divestiture.

Interest income and other, net

	Three months ended			Six months ended		
	June 28, 2014	June 29, 2013	Change over prior period	June 28, 2014	June 29, 2013	Change over prior period
	(In thousands)					
Interest income and other, net	$ 120	$ 92	$ 28	$ 192	$ 172	$ 20

Interest income and other, net is comprised of interest income and realized gains and losses on sales of investments, foreign currency gains and losses, and other income and expense such as gains and losses on sales of fixed assets and earnout income from divestitures.

Income tax benefit

	Three months ended			Six months ended		
	June 28, 2014	June 29, 2013	Change over prior period	June 28, 2014	June 29, 2013	Change over prior period
	(In thousands)					
Income tax benefit	$ 119	$ 486	$ (367)	$ 250	$ 1,166	$ (916)

Intevac recorded income tax benefits of $119,000 and $250,000 for the three and six months ended June 28, 2014, respectively. Intevac recorded income tax benefits of $486,000 and $1.2 million for the three and six months ended June 29, 2013, respectively. The income tax provisions for the three and six month periods are based upon estimates of annual income (loss), annual permanent differences and statutory tax rates in the various jurisdictions in which Intevac operates. Intevac did not recognize a benefit on the U.S. net operating loss for the three and six months ended June 28, 2014 and June 29, 2013 due to having full valuation allowances on the U.S. deferred tax assets. Intevac s tax rate differs from the applicable statutory rates due primarily to establishment of a valuation allowance, the utilization of deferred and current credits and the effect of permanent differences and adjustments of prior permanent differences. Intevac s future effective income tax rate depends on various factors including, the level of Intevac s projected earnings, the geographic composition of worldwide earnings, tax regulations governing each region, net operating loss carryforwards, availability of tax credits and the effectiveness of Intevac s tax planning strategies. Management carefully monitors these factors and timely adjusts the effective income tax rate.

Liquidity and Capital Resources

At June 28, 2014, Intevac had $75.3 million in cash, cash equivalents, and investments compared to $81.4 million at December 31, 2013. During the first six months of 2014, cash, cash equivalents and investments decreased by $6.1 million due primarily to cash used by operating activities, purchases of fixed assets, repurchases of common stock and increases in restricted cash partially offset by cash received from the sale of Intevac common stock to Intevac s employees through Intevac s employee benefit plans.

Table of Contents

Cash, cash equivalents and investments consist of the following:

	June 28, 2014	December 31, 2013
	(In thousands)	
Cash and cash equivalents	$ 25,059	$ 20,121
Short-term investments	33,173	48,975
Long-term investments	17,064	12,318
Total cash, cash equivalents and investments	$ 75,296	$ 81,414

Operating activities used cash of $2.6 million during the first six months of 2014 and used cash of $4.2 million during the first six months of 2013. The decrease in cash used by operating activities was due primarily to a smaller net loss and to reductions in working capital during the first six months of 2014, offset in part by the payment of annual bonuses.

Accounts receivable totaled $9.3 million at June 28, 2014, compared to $15.0 million at December 31, 2013. The decrease of $5.8 million in the receivable balance was due primarily to decreased revenue levels and improved collections. Total net inventories decreased slightly to $22.6 million at June 28, 2014, compared to $22.8 million at December 31, 2013. Accounts payable increased slightly to $4.3 million at June 28, 2014 compared to $4.0 million at December 31, 2013 in line with business levels. Accrued payroll and related liabilities decreased to $4.2 million at June 28, 2014 compared to $5.0 million at December 31, 2013 primarily related to the payment for prior year bonuses. Customer deposits decreased to $2.1 million at June 28, 2014 compared to $3.7 million at December 31, 2013.

Investing activities generated cash of $8.0 million during the first six months of 2014. Proceeds from sales of investments net of purchases totaled $11.2 million. Intevac is required to maintain a standby letter of credit for $1.0 million for the Santa Clara, California campus lease. This standby letter of credit is secured with $1.0 million of restricted cash. Capital expenditures for the six months ended June 28, 2014 were $2.2 million.

Financing activities in the first six months of 2014 used cash of $381,000. The sale of Intevac common stock to Intevac s employees through Intevac s employee benefit plans generated cash $1.2 million. Cash used to repurchase shares of common stock under the Company s stock repurchase program totaled $1.6 million for the six months ended June 28, 2014.

Intevac s investment portfolio consists principally of investment grade money market mutual funds, U.S. Treasury and agency securities, certificates of deposit, commercial paper, municipal bonds and corporate bonds. Intevac regularly monitors the credit risk in its investment portfolio and takes measures, which may include the sale of certain securities, to manage such risks in accordance with its investment policies.

As of June 28, 2014, approximately $10.2 million of cash and cash equivalents were domiciled in foreign tax jurisdictions. Intevac expects a significant portion of these funds to remain off shore in the short term. If the Company chose to repatriate these funds to the United States, it would be required to accrue and pay additional taxes on any portion of the repatriation where no United States income tax had been previously provided.

Intevac believes that its existing cash, cash equivalents and investments will be sufficient to meet its cash requirements for the foreseeable future. Intevac intends to undertake approximately $3.5 million to $4.0 million in capital expenditures during the remainder of 2014.

Table of Contents

Contractual Obligations

The following table summarizes Intevac s contractual obligations as of June 28, 2014:

	Total	< 1 Year	1 3 Years	3-5 Years	> 5 Years
			Payments due by period (in thousands)		
Operating lease obligations	$ 27,744	$ 1,023	$ 6,296	$ 5,276	$ 15,149
Purchase obligations and commitments [1]	6,044	6,044			
Other long-term liabilities [2, 4]	409	409			
Total [3, 4]	$ 34,197	$ 7,476	$ 6,296	$ 5,276	$ 15,149

1 Purchase obligations include agreements to purchase goods or services that are enforceable and legally binding on Intevac and that specify all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Purchase obligations exclude agreements that are cancelable without penalty. These purchase obligations are related principally to inventory and other items.

2 Intevac is unable to reliably estimate the timing of future payments related to uncertain tax positions; therefore, $425,000 of unrecognized tax benefits has been excluded from the table above.

3 Total excludes contractual obligations already recorded on the condensed consolidated balance sheet as current liabilities (except other long-term liabilities) and certain purchase obligations.

4 Total excludes contingent consideration that may be paid pursuant to asset purchases or business combinations.

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America (US GAAP) requires management to make judgments, assumptions and estimates that affect the amounts reported. Intevac s significant accounting policies are described in Note 1 to the consolidated financial statements included in Item 8 of Intevac s Annual Report on Form 10-K filed on February 20, 2014. Certain of these significant accounting policies are considered to be critical accounting policies, as defined below.

A critical accounting policy is defined as one that is both material to the presentation of Intevac s financial statements and requires management to make difficult, subjective or complex judgments that could have a material effect on Intevac s financial conditions and results of operations. Specifically, critical accounting estimates have the following attributes: 1) Intevac is required to make assumptions about matters that are highly uncertain at the time of the estimate; and 2) different estimates Intevac could reasonably have used, or changes in the estimate that are reasonably likely to occur, would have a material effect on Intevac s financial condition or results of operations.

Estimates and assumptions about future events and their effects cannot be determined with certainty. Intevac bases its estimates on historical experience and on various other assumptions believed to be applicable and reasonable under the circumstances. These estimates may change as new events occur, as additional information is obtained and as Intevac s operating environment changes. These changes have historically been minor and have been included in the consolidated financial statements as soon as they become known. In addition, management is periodically faced with uncertainties, the outcomes of which are not within its control and will not be known for prolonged periods of time. Many of these uncertainties are discussed in the section below entitled Risk Factors. Based on a critical assessment of Intevac s accounting policies and the underlying judgments and uncertainties affecting the application of those policies, management believes that Intevac s consolidated financial statements are fairly stated in accordance with US GAAP, and provide a meaningful presentation of Intevac s financial condition and results of operation.

Table of Contents

For further information about Intevac s other critical accounting policies, see the discussion of critical accounting policies in Intevac s 2013 Form 10-K. Management believes that there has been no significant change during the six months ended June 28, 2014 to the items identified as critical accounting policies in Intevac s 2013 Form 10-K.

Item 3. ***Quantitative and Qualitative Disclosures About Market Risk***

Interest rate risk. Intevac s exposure to market risk for changes in interest rates relates primarily to its investment portfolio. Intevac does not use derivative financial instruments in Intevac s investment portfolio. The Company has adopted an investment policy and established guidelines relating to credit quality, diversification and maturities of its investments in order to preserve principal and maintain liquidity. All investment securities in Intevac s portfolio have an investment grade credit rating. Investments typically consist of certificates of deposit, commercial paper, obligations of the U.S. government and its agencies, corporate debt securities and municipal bonds.

The table below presents principal amounts and related weighted-average interest rates by year of expected maturity for Intevac s investment portfolio at June 28, 2014.

	2014	2015	2016	Total	Fair Value
		(In thousands, except percentages)			
Cash equivalents					
Variable rate amounts	$ 17,592			$ 17,592	$ 17,592
Weighted-average rate	0.03%				
Short-term investments					
Fixed rate amounts	$ 13,173	$ 15,968		$ 29,141	$ 29,164
Weighted-average rate	1.18%	2.96%			
Variable rate amounts	$ 4,007			$ 4,007	$ 4,009
Weighted-average rate	0.75%				
Long-term investments					
Fixed rate amounts		$ 2,798	$ 14,263	$ 17,061	$ 17,064
Weighted-average rate		1.89%	1.47%		
Total investment portfolio	$ 34,772	$ 18,766	$ 14,263	$ 67,801	$ 67,829

Foreign exchange risk. From time to time, Intevac enters into foreign currency forward exchange contracts to hedge certain of its anticipated foreign currency re-measurement exposures. The objective of these contracts is to minimize the impact of foreign currency exchange rate movements on Intevac s operating results. The notional amount of Company s foreign currency derivatives was $474,000 at June 28, 2014.

Item 4. ***Controls and Procedures***

Evaluation of disclosure controls and procedures

Intevac maintains 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 the 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 filing of this Form 10-Q for the quarter ended June 28, 2014, 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 Intevac s disclosure controls and procedures as of the end of the period covered by this quarterly report. Based on this evaluation, Intevac s Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of June 28, 2014.

Attached as exhibits to this Quarterly Report are certifications of the CEO and the CFO, which are required in accordance with Rule 13a-14 of the Exchange Act. This Controls and Procedures section includes the information concerning the controls evaluation referred to in the certifications, and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

Definition of disclosure controls

Disclosure Controls are controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms. Disclosure Controls are also designed to ensure that such information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Our Disclosure Controls include components of our internal control over financial reporting, which consists of control processes designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles in the U.S. To the extent that components of our internal control over financial reporting are included within our Disclosure Controls, they are included in the scope of our quarterly controls evaluation.

Limitations on the effectiveness of controls

Intevac s management, including the CEO and CFO, does not expect that Intevac s Disclosure Controls or Intevac s internal control over financial reporting will prevent all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system s objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within Intevac have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Changes in internal controls over financial reporting

There were no changes in our internal controls over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, Intevac s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. ***Legal Proceedings***

From time to time, Intevac is involved in claims and legal proceedings that arise in the ordinary course of business. Intevac expects that the number and significance of these matters will increase as Intevac s business expands. Any claims or proceedings against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time, result in the diversion of significant operational resources, or require us to enter into royalty or licensing agreements which, if required, may not be available on terms favorable to us or at all. Intevac is not presently a party to any lawsuit or proceeding that, in Intevac s opinion, is likely to seriously harm Intevac s business.

Table of Contents

Item 1A. ***Risk Factors***

The following factors could materially affect Intevac s business, financial condition or results of operations and should be carefully considered in evaluating the Company and its business, in addition to other information presented elsewhere in this report.

The industries we serve are cyclical, volatile and unpredictable.

The majority of our revenue is derived from the sale of equipment used to manufacture commodity technology products such as disk drives, PV solar cells and cell phones. This subjects us to business cycles, the timing, length and volatility of which can be difficult to predict. When demand for commodity technology products exceeds production capacity, then demand for new capital equipment such as ours tends to be amplified. Conversely, when supply of commodity technology products exceeds demand, then demand for new capital equipment such as ours tends to be depressed. For example, sales of systems for magnetic disk production were depressed from late 2007 through 2009. The number of new systems delivered increased in 2010 as customers increased their production capacity in response to increased demand for data storage, but decreased in 2011, 2012, 2013, and through the first half of 2014 as the hard disk drive industry did not add the same level of capacity that it did in 2010. We cannot predict with any certainty when these cycles will begin or end. We believe that our sales will continue to be depressed through 2014.

Our equipment represents only a portion of the capital expenditure that our customers incur when they upgrade or add production capacity. Accordingly, our customers generally commit to making large capital expenditures far in excess of the cost of our systems alone when they decide to purchase our systems. The magnitude of these capital expenditures requires our customers to have access to large amounts of capital. Our customers generally reduce their level of capital investment during downturns in the overall economy or during a downturn in their industries.

We must effectively manage our resources and production capacity to meet rapidly changing demand. Our business experiences rapid growth and contraction, which stresses our infrastructure, internal systems and managerial resources. During periods of increasing demand for our products, we must have sufficient manufacturing capacity and inventory to meet customer demand; attract, retain and motivate a sufficient number of qualified individuals; and effectively manage our supply chain. During periods of decreasing demand for our products, we must be able to align our cost structure with prevailing market conditions; motivate and retain key employees and effectively manage our supply chain.

Sales of our equipment are primarily dependent on our customers upgrade and capacity expansion plans and whether our customers select our equipment.

We have no control over our customers upgrade and capacity expansion plans, and we cannot be sure they will select, or continue to select, our equipment when they upgrade or expand their capacity. The sales cycle for our equipment systems can be a year or longer, involving individuals from many different areas of Intevac and numerous product presentations and demonstrations for our prospective customers. Our sales process also commonly includes production of samples, customization of our products, and installation of evaluation systems in the factories of our prospective customers. We do not enter into long-term contracts with our customers, and until an order is actually submitted by a customer there is no binding commitment to purchase our systems.

The Photonics business is also subject to long sales cycles because many of its products, such as our military imaging products, often must be designed into the customers end products, which are often complex state-of-the-art products. These development cycles are typically multi-year, and our sales are contingent on our customers successfully integrating our product into their product, completing development of their product and then obtaining production orders for their product from the U.S. government or its allies.

Sales of new manufacturing systems are also dependent on obsolescence and replacement of the installed base of our customers existing equipment with newer, more capable equipment. If upgrades are developed that extend the useful life of the installed base of systems, then we tend to sell more upgrade products and fewer new systems, which can significantly reduce total revenue. For example, some of our 200 Lean customers continue to use legacy systems for the production of perpendicular media, which delayed the replacement of such systems with new 200 Lean systems.

Our 200 Lean customers also experience competition from companies that produce alternative storage technologies like flash memory, which offer smaller size, lower power consumption and more rugged designs. These storage technologies are being used increasingly in enterprise applications and smaller form factors such as tablets, smart-phones, ultra-books, and notebook personal computers instead of hard disk drives. Tablet computing devices and smart-phones have never contained, nor are they likely in the future to contain, a disk drive. Products using alternative technologies, such as flash memory, optical storage and other storage technologies are becoming increasingly common and could become a significant source of competition to particular applications of the products of our 200 Lean customers, which could adversely affect our results of operations. If alternative technologies, such as flash memory, replace hard disk drives as a significant method of digital storage, then demand for our hard disk manufacturing products would decrease.

Our growth depends on development of technically advanced new products and processes.

We have invested heavily, and continue to invest, in the development of new products, such as our 200 Lean and other PVD systems, our solar systems for PV applications, our digital night-vision products and our near-eye display products. Our success in developing and selling new products depends upon a variety of factors, including our ability to: predict future customer requirements, make technological advances, achieve a low total cost of ownership for our products, introduce new products on schedule, manufacture products cost-effectively including transitioning production to volume manufacturing; commercialize and attain customer acceptance of our products; and achieve acceptable and reliable performance of our new products in the field. Our new product decisions and development commitments must anticipate continuously evolving industry requirements significantly in advance of sales. In addition, we are attempting to expand into new or related markets, including the PV and cell phone cover lens markets. Our expansion into the PV market is dependent upon the success of our customers development plans. To date we have not recognized material revenue from such products. Failure to correctly assess the size of the markets, to successfully develop cost effective products to address the markets or to establish effective sales and support of the new products would have a material adverse effect on future revenues and profits.

Rapid technological change in our served markets requires us to rapidly develop new technically advanced products. Our future success depends in part on our ability to develop and offer new products with improved capabilities and to continue to enhance our existing products. If new products have reliability or quality problems, our performance may be impacted by reduced orders, higher manufacturing costs, delays in acceptance and payment for new products and additional service and warranty expenses.

We are exposed to risks associated with a highly concentrated customer base.

Historically, a significant portion of our revenue in any particular period has been attributable to sales of our disk sputtering systems to a limited number of customers. This concentration of customers, when combined with changes in the customers specific capacity plans and market share shifts can lead to extreme variability in our revenue and financial results from period to period.

The concentration of our customer base may enable our customers to demand pricing and other terms unfavorable to Intevac, and makes us more vulnerable to changes in demand by a given customer. Orders from a relatively limited number of manufacturers have accounted for, and will likely continue to account for, a substantial portion of our revenues. The loss of one of these large customers, or delays in purchasing by them, could have a material and adverse effect on our revenues.

We operate in an intensely competitive marketplace, and our competitors have greater resources than we do.

In the market for our disk sputtering systems, we experience competition primarily from Canon Anelva, which has sold a substantial number of systems worldwide. In the PV equipment market, Intevac faces competition from large established competitors including Applied Materials, Centrotherm Photovoltaics, Amtech, Jusung and Von Ardenne. In the market for our military imaging products we experience competition from companies such as Exelis and L-3 Communications. Some of our competitors have substantially greater financial, technical, marketing, manufacturing and other resources than we do, especially in the PV equipment market. Our competitors may develop enhancements to, or future generations of, competitive products that offer superior price or performance features, and new competitors may enter our markets and develop such enhanced products. Moreover, competition for our customers is intense, and our competitors have historically offered substantial pricing concessions and incentives to attract our customers or retain their existing customers.

Our operating results fluctuate significantly from quarter to quarter, which can lead to volatility in the price of our common stock.

Our quarterly revenues and common stock price have fluctuated significantly. We anticipate that our revenues, operating margins and common stock price will continue to fluctuate for a variety of reasons, including: (1) changes in the demand, due to seasonality, cyclicality and other factors in the markets for computer systems, storage subsystems and consumer electronics containing disks our customers produce with our systems; (2) delays or problems in the introduction and acceptance of our new products, or delivery of existing products; (3) timing of orders, acceptance of new systems by our customers or cancellation of those orders; (4) new products, services or technological innovations by our competitors or us; (5) changes in our manufacturing costs and operating expense; (6) changes in general economic, political, stock market and industry conditions; and (7) any failure of our operating results to meet the expectations of investment research analysts or investors.

Any of these, or other factors, could lead to volatility and/or a rapid change in the trading price of our common shares. In the past, securities class action litigation has been instituted against companies following periods of volatility in the market price of their securities. Any such litigation, if instituted against Intevac, could result in substantial costs and diversion of management time and attention.

Adverse economic conditions and volatility and disruption of the capital and credit markets may negatively impact our revenues and our ability to access financing.

Economic conditions worldwide have contributed to decreased spending by our customers and a slowdown in the hard disk drive industry. These factors have adversely impacted our operating results and have caused us to be cautious about our future outlook. Our customers also continue to remain cautious about the economy. Negative macroeconomic and global recessionary factors, further volatility or disruption in the capital and credit markets or further uncertainty or weakening in key markets could negatively impact spending for our products and may materially adversely affect our business, operating results and financial condition.

In addition, while we intend to finance operations with existing cash and cash flow from operations, if necessary, we may require financing to support our continued operations. Due to the existing uncertainty in the capital and credit markets, our access to capital may not be available on terms acceptable to us or at all.

We may not be able to obtain export licenses from the U.S. government permitting delivery of our products to international customers.

Many of our products, especially Photonics products, require export licenses from U.S. government agencies under the Export Administration Act, the Trading with the Enemy Act of 1917, the Arms Export Act of 1976 or the International Traffic in Arms Regulations. These regulations limit the potential market for some of our products. We can give no assurance that we will be successful in obtaining all the licenses necessary to export our products. Heightened government scrutiny of export licenses for defense related products has resulted in lengthened review periods for our license applications. Exports to countries that are not considered by the U.S. government to be allies are likely to be prohibited, and even sales to U.S. allies may be limited. Failure to comply with export control laws, including identification and reporting of all exports and re-exports of controlled technology or exports made without correct license approval or improper license use could result in severe penalties and revocation of licenses. Failure to obtain export licenses, delays in obtaining licenses, or revocation of previously issued licenses would prevent us from selling the affected products outside the United States and could negatively impact our results of operations.

The Photonics business is dependent on U.S. government contracts, which are subject to fixed pricing, immediate termination and a number of procurement rules and regulations.

We sell our Photonics products and services directly to the U.S. government, as well as to prime contractors for various U.S. government programs. The U.S government is considering significant changes in the level of existing, follow-on or replacement programs. We cannot predict the impact of potential changes in priorities due to military transformations and/or the nature of future war-related activities. A shift of government priorities to programs in which we do not participate and/or reductions in funding for or the termination of programs in which we do participate, unless offset by other programs and opportunities, could have a material adverse effect on our financial position, results of operations, or cash flows.

Funding of multi-year government programs is subject to congressional appropriations, and there is no guarantee that the U.S. government will make further appropriations, particularly given the U.S. government s recent focus on spending in other areas and spending reductions. Sales to the U.S. government and its prime contractors may also be affected by changes in procurement policies, budget considerations and political developments in the United States or abroad. For example, if the U.S. government is less focused on defense spending or there is a decrease in hostilities, demand for our products could decrease. The loss of funding for a government program would result in a loss of future revenues attributable to that program. The influence of any of these factors, which are beyond our control, could negatively impact our results of operations.

A significant portion of our U.S. government revenue is derived from fixed-price development and production contracts. Under fixed-price contracts, unexpected increases in the cost to develop or manufacture a product, whether due to inaccurate estimates in the bidding process, unanticipated increases in material costs, reduced production volumes, inefficiencies or other factors, are borne by us. We have experienced cost overruns in the past that have resulted in losses on certain contracts, and may experience additional cost overruns in the future. We are required to recognize the total estimated impact of cost overruns in the period in which they are first identified. Such cost overruns could have a material adverse effect on our results of operations.

Generally, government contracts contain provisions permitting termination, in whole or in part, without prior notice at the government s convenience upon the payment of compensation only for work done and commitments made at the time of termination. We cannot ensure that one or more of the government contracts under which we, or our customers, operate will not be terminated under these circumstances. Also, we cannot ensure that we, or our customers, would be able to procure new government contracts to offset the revenues lost as a result of any termination of existing contracts, nor can we ensure that we, or our customers, will continue to remain in good standing as federal contractors.

As a U.S. government contractor we must comply with specific government rules and regulations and are subject to routine audits and investigations by U.S. government agencies. If we fail to comply with these rules and regulations, the results could include: (1) reductions in the value of our contracts; (2) reductions in amounts previously billed and recognized as revenue; (3) contract modifications or termination; (4) the assessment of penalties and fines; and (5) suspension or debarment from government contracting or subcontracting for a period of time or permanently.

Our success depends on international sales and the management of global operations.

The majority of our revenues come from regions outside the United States. Most of our international sales are to customers in Asia, which includes products shipped to overseas operations of U.S. companies. We currently have manufacturing facilities in California and Singapore and international customer support offices in Singapore, China, and Malaysia. We expect that international sales will continue to account for a significant portion of our total revenue in future years. Certain of our suppliers are also located outside the United States.

Managing our global operations presents challenges including, but not limited to, those arising from: (1) global trade issues; (2) variations in protection of intellectual property and other legal rights in different countries; (3) concerns of U.S. governmental agencies regarding possible national commercial and/or security issues posed by growing manufacturing business in Asia; (4) fluctuation of interest rates, raw material costs, labor and operating

Table of Contents

costs, and exchange rates, including the weakening relative position of the U.S. dollar; (5) variations in the ability to develop relationships with suppliers and other local businesses; (6) changes in the laws and regulations of the United States, including export restrictions, and other countries, as well as their interpretation and application; (7) the need to provide technical and spares support in different locations; (8) political and economic instability; (9) cultural differences; (10) varying government incentives to promote development; (11) shipping costs and delays; (12) adverse conditions in credit markets; (13) variations in tariffs, quotas, tax codes and other market barriers; and (14) barriers to movement of cash.

We must regularly assess the size, capability and location of our global infrastructure and make appropriate changes to address these issues.

Changes to our effective tax rate affect our results of operations.

As a global company, we are subject to taxation in the United States, Singapore and various other countries. Significant judgment is required to determine and estimate worldwide tax liabilities. Our future effective tax rate could be affected by: (1) changes in tax laws; (2) the allocation of earnings to countries with differing tax rates; (3) changes in worldwide projected annual earnings in current and future years: (4) accounting pronouncements; or (5) changes in the valuation of our deferred tax assets and liabilities. Although we believe our tax estimates are reasonable, there can be no assurance that any final determination will not be different from the treatment reflected in our historical income tax provisions and accruals, which could result in additional payments by Intevac.

We booked significant tax benefits in 2008, 2009, 2011 and 2013 based on our belief that we could both carry back losses and tax credits to years Intevac paid income taxes and carry forward losses and tax credits to future years where we believed we would generate taxable income. In 2012, the Company established a $23.4 million non-cash valuation allowance against certain of its U.S. deferred tax assets based upon an evaluation of all available objectively verifiable evidence, including but not limited to the cumulative loss incurred over the three-year period ended December 31, 2012 by the Company s U.S. operations. For the year ended December 31, 2013, a $7.2 million valuation allowance increase for the U.S. federal deferred tax asset was recorded. The establishment of the non-cash valuation allowance on the Company s U.S. deferred tax assets did not have any impact on its cash, nor does such an allowance preclude the Company from utilizing its tax losses, tax credits or other deferred tax assets in future periods.

Intevac will need to generate approximately $52.1 million of taxable income in Singapore in order to fully realize the foreign deferred tax assets recorded as of June 28, 2014. If our expectations of future income are incorrect, we could be required to establish additional valuation allowance against some or all of the entire remaining deferred tax assets which are attributable to our Singapore operation.

We may be subject to additional impairment charges due to potential declines in the fair value of our assets.

As a result of our acquisitions, we have significant intangible assets and had significant goodwill on our balance sheet. We test these assets for impairment on a periodic basis as required, and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The events or changes that could require us to test our intangible assets for impairment include: a significant reduction in our stock price, and as a result market capitalization, changes in our estimated future cash flows, as well as changes in rates of growth in our industry or in any of our reporting units. In the fourth quarter of 2012, as a result of a decline in our market capitalization and a reduction in our revenue expectations we recorded a goodwill impairment charge in the amount of $18.4 million. We will continue to evaluate the carrying value of our intangible assets and if we determine in the future that there is a potential further impairment, we may be required to record additional charges to earnings which could materially adversely affect our financial results and could also materially adversely affect our business. See Note 5 Purchased Intangible Assets in the notes to the condensed consolidated financial statements for additional information related to impairment of intangible assets.

Table of Contents

Our success is dependent on recruiting and retaining a highly talented work force.

Our employees are vital to our success, and our key management, engineering and other employees are difficult to replace. We do not maintain key person life insurance on any of our employees. The expansion of high technology companies worldwide has increased demand and competition for qualified personnel, and has made companies increasingly protective of prior employees. It may be difficult for us to locate employees who are not subject to non-competition agreements and other restrictions.

The majority of our U.S. operations are located in California where the cost of living and of recruiting employees is high. Our operating results depend, in large part, upon our ability to retain and attract qualified management, engineering, marketing, manufacturing, customer support, sales and administrative personnel. Furthermore, we compete with industries such as the hard disk drive, semiconductor, and solar industries for skilled employees. Failure to retain existing key personnel, or to attract, assimilate or retain additional highly qualified employees to meet our needs in the future, could have a material and adverse effect on our business, financial condition and results of operations.

We are dependent on certain suppliers for parts used in our products.

We are a manufacturing business. Purchased parts constitute the largest component of our product cost. Our ability to manufacture depends on the timely delivery of parts, components and subassemblies from suppliers. We obtain some of the key components and subassemblies used in our products from a single supplier or a limited group of suppliers. If any of our suppliers fail to deliver quality parts on a timely basis, we may experience delays in manufacturing, which could result in delayed product deliveries, increased costs to expedite deliveries or develop alternative suppliers, or require redesign of our products to accommodate alternative suppliers. Some of our suppliers are thinly capitalized and may be vulnerable to failure given recent economic conditions.

Our business depends on the integrity of our intellectual property rights.

The success of our business depends upon the integrity of our intellectual property rights, and we cannot ensure that: (1) any of our pending or future patent applications will be allowed or that any of the allowed applications will be issued as patents or will issue with claims of the scope we sought; (2) any of our patents will not be invalidated, deemed unenforceable, circumvented or challenged; (3) the rights granted under our patents will provide competitive advantages to us; (4) other parties will not develop similar products, duplicate our products or design around our patents; or (5) our patent rights, intellectual property laws or our agreements will adequately protect our intellectual property or competitive position.

From time to time, we have received claims that we are infringing third parties   intellectual property rights or seeking to invalidate our rights. We cannot ensure that third parties will not in the future claim that we have infringed current or future patents, trademarks or other proprietary rights relating to our products. Any claims, with or without merit, could be time-consuming, result in costly litigation, cause product shipment delays or require us to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to us.

We could be involved in litigation.

From time to time we may be involved in litigation of various types, including litigation alleging infringement of intellectual property rights and other claims. Litigation is expensive, subjects us to the risk of significant damages and requires significant management time and attention and could have a material and adverse effect on our business, financial condition and results of operations.

We could be negatively affected as a result of a proxy contest and the actions of activist stockholders.

A proxy contest with respect to election of our directors, or other activist stockholder activities, could adversely affect our business because: (i) responding to a proxy contest and other actions by activist stockholders can be costly and time-consuming, disruptive to our operations and divert the attention of management and our employees; (ii) perceived uncertainties as to our future direction caused by activist activities may result in the loss of potential business opportunities, and may make it more difficult to attract and retain qualified personnel and business partners; and (iii) if individuals are elected to our Board of Directors with a specific agenda, it may adversely affect our ability to effectively and timely implement our strategic plans.

Table of Contents

Difficulties in integrating past or future acquisitions could adversely affect our business.

We have completed a number of acquisitions and dispositions during our operating history. For example, in 2007, we acquired certain assets of DeltaNu, LLC and certain assets of Creative Display Systems, LLC, in 2008 we acquired certain assets of OC Oerlikon Balzers Ltd., in 2010 we acquired the outstanding shares of SIT, in 2012 we completed the sale of certain semiconductor mainframe technology assets and in 2013 we completed the sale of the assets of DeltaNu. We have spent and may continue to spend significant resources identifying and pursuing future acquisition opportunities. Acquisitions involve numerous risks including: (1) difficulties in integrating the operations, technologies and products of the acquired companies; (2) the diversion of our management s attention from other business concerns; and (3) the potential loss of key employees of the acquired companies. Failure to achieve the anticipated benefits of the prior and any future acquisitions or to successfully integrate the operations of the companies we acquire could have a material and adverse effect on our business, financial condition and results of operations. Any future acquisitions could also result in potentially dilutive issuance of equity securities, acquisition or divestiture-related write-offs or the assumption of debt and contingent liabilities. In addition, we have made and will continue to consider making strategic divestitures. With any divestiture, there are risks that future operating results could be unfavorably impacted if targeted objectives, such as cost savings, are not achieved or if other business disruptions occur as a result of the divestiture or activities related to the divestiture.

We are subject to risks of non-compliance with environmental and other governmental regulations.

We are subject to a variety of governmental regulations relating to the use, storage, discharge, handling, emission, generation, manufacture, treatment and disposal of toxic or otherwise hazardous substances, chemicals, materials or waste. If we fail to comply with current or future regulations, such failure could result in suspension of our operations, alteration of our manufacturing process, remediation costs or substantial civil penalties or criminal fines against us or our officers, directors or employees. Additionally, these regulations could require us to acquire expensive remediation or abatement equipment or to incur substantial expenses to comply with them.

We are also subject to a variety of other governmental regulations and may incur significant costs associated with the compliance with these regulations. For example rules adopted by the SEC to implement the Dodd-Frank Wall Street Reform and Consumer Protection Act impose diligence and disclosure requirements regarding the use of conflict minerals mined from the Democratic Republic of Congo and adjoining countries in the products we manufacture. Compliance with these regulations is likely to result in additional costs and expenses or may affect the sourcing and availability of the components used in the products we manufacture.

Business interruptions could adversely affect our operations.

Our operations are vulnerable to interruption by fire, earthquake, floods or other natural disaster, quarantines or other disruptions associated with infectious diseases, national catastrophe, terrorist activities, war, disruptions in our computing and communications infrastructure due to power loss, telecommunications failure, human error, physical or electronic security breaches and computer viruses, and other events beyond our control. We do not have a detailed disaster recovery plan. Despite our implementation of network security measures, our tools and servers may be vulnerable to computer viruses, break-ins and similar disruptions from unauthorized tampering with our computer systems and tools located at customer sites. Political instability could cause us to incur increased costs in transportation, make such transportation unreliable, increase our insurance costs or cause international currency markets to fluctuate. All these unforeseen disruptions and instabilities could have the same effects on our suppliers and their ability to timely deliver their products. In addition, we do not carry sufficient business interruption insurance to compensate us for all losses that may occur, and any losses or damages incurred by us could have a material adverse effect on our business and results of operations. For example, we self-insure earthquake risks because we believe this is the prudent financial decision based on the high cost of the limited coverage available in the earthquake insurance market. An earthquake could significantly disrupt our operations, most of which are conducted in California. It could also significantly delay our research and engineering effort on new products, most of which is also conducted in California. We take steps to minimize the damage that would be caused by business interruptions, but there is no certainty that our efforts will prove successful.

Table of Contents

We are required to evaluate our internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act of 2002, and any adverse results from such evaluation could result in a loss of investor confidence in our financial reports and have an adverse effect on our stock price.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, our management must perform evaluations of our internal control over financial reporting. Beginning in 2004, our Form 10-K has included a report by management of their assessment of the adequacy of such internal control. Additionally, our independent registered public accounting firm must publicly attest to the effectiveness of our internal control over financial reporting.

We have completed the evaluation of our internal controls over financial reporting as required by Section 404 of the Sarbanes-Oxley Act. Although our assessment, testing, and evaluation resulted in our conclusion that as of December 31, 2013, our internal controls over financial reporting were effective, we cannot predict the outcome of our testing in future periods. Ongoing compliance with this requirement is complex, costly and time-consuming. If Intevac fails to maintain effective internal control over financial reporting; our management does not timely assess the adequacy of such internal control; or our independent registered public accounting firm does not deliver an unqualified opinion as to the effectiveness of our internal control over financial reporting, then we could be subject to restatement of previously reported financial results, regulatory sanctions and a decline in the public s perception of Intevac, which could have a material and adverse effect on our business, financial condition and results of operations.

Item 2. ***Unregistered Sales of Equity Securities and Use of Proceeds***

The following table provides information as of June 28, 2014 with respect to the shares of common stock repurchased by Intevac during the second quarter of fiscal 2014.

	Total Number of Shares Purchased	Average Price Paid per Share	Aggregate Price Paid	Total Number of Shares Purchased as Part of Publicly Announced Program*	Maximum Dollar Value of Shares That May Yet be Purchased Under the Program*
	(in thousands, except per share data)				
Month #1					
March 30, 2014 to April 26, 2014		$	$		$ 27,262
Month #2					
April 27, 2014 to May 24, 2014	24	$ 7.19	$ 177	24	$ 27,085
Month #3					
May 25, 2014 to June 28, 2014	33	$ 7.22	$ 242	33	$ 26,843

* On November 21, 2013, the Board of Directors approved a stock repurchase program authorizing up to $30.0 million in repurchases.

Item 3. ***Defaults upon Senior Securities***

None.

Table of Contents

Item 4. ***Mine Safety Disclosures***

Not applicable.

Item 5. ***Other Information***

None.

Item 6. ***Exhibits***

The following exhibits are filed herewith:

Exhibit Number	Description
10.1	The Registrant s 2003 Employee Stock Purchase Plan, as amended +
10.2	The Registrant s 2012 Equity Incentive Plan, as amended +
10.3	Agreement, dated as of May 11, 2014, by and among Intevac, Inc., J. Daniel Plants, Marc T. Giles, Voce Catalyst Partners LP and Voce Capital Management LLC (1)
31.1	Certification of President and Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Executive Vice President, Finance and Administration, Chief Financial Officer, Treasurer and Secretary Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certifications Pursuant to U.S.C. 1350 Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Previously filed as an exhibit to the Company s Report on Form 8-K filed May 15, 2014.

\+ Management compensatory plan or arrangement required to be filed as an exhibit.

Table of Contents

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: July 29, 2014	By:	/s/ WENDELL BLONIGAN Wendell Blonigan President and Chief Executive Officer (Principal Executive Officer)
Date: July 29, 2014	By:	/s/ JEFFREY ANDRESON Jeffrey Andreson Executive Vice President, Finance and Administration, Chief Financial Officer, Treasurer and Secretary (Principal Financial and Accounting Officer)

41