

VICOR CORP
Form 10-Q
November 08, 2006

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-Q

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

For the quarterly period ended September 30, 2006

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

For the transition period from _____

Commission File Number 0-18277

VICOR CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State of Incorporation)

04-2742817
(I.R.S. Employer Identification No.)

25 Frontage Road, Andover, Massachusetts 01810
(Address of Principal Executive Office)

(978) 470-2900
(Registrant's telephone number)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer Accelerated Filer Non-accelerated filer

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

The number of shares outstanding of each of the issuer's classes of common stock as of October 31, 2006 was:

Common Stock, \$.01 par value	29,707,583
Class B Common Stock, \$.01 par value	11,854,952

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PAGE 1**Item 1 Financial Statements**VICOR CORPORATION
Condensed Consolidated Balance Sheets
(In thousands)
(Unaudited)

	September 30, 2006	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	\$ 28,376	\$ 34,024
Short-term investments	87,971	88,692
Accounts receivable, less allowance of \$693 in 2006 and \$635 in 2005	30,101	28,072
Inventories, net	20,931	17,168
Deferred tax assets	2,673	2,673
Other current assets	2,359	2,518
Total current assets	172,411	173,147
Long-term investments		3,348
Property, plant and equipment, net	53,358	59,114
Other assets	8,329	10,146
	\$ 234,098	\$ 245,755

Liabilities and Stockholders Equity

Current liabilities:

Accounts payable	\$ 7,728	\$ 8,741
Accrued compensation and benefits	4,839	4,583
Accrued expenses	3,762	3,016
Income taxes payable	1,692	6,279
Deferred revenue	131	143
Total current liabilities	18,152	22,762
Deferred income taxes	3,259	3,172
Minority interests	3,448	3,031

Stockholders equity:

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Preferred Stock		
Class B Common Stock	119	119
Common Stock	382	377
Additional paid-in capital	157,782	151,698
Retained earnings	172,729	175,660
Accumulated other comprehensive income(loss)	54	(72)
Treasury stock, at cost	(121,827)	(110,992)
Total stockholders' equity	209,239	216,790
	\$ 234,098	\$ 245,755

See accompanying notes.

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Condensed Consolidated Statements of Operations
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Net revenues	\$ 46,932	\$ 45,298	\$ 144,014	\$ 133,057
Cost of revenues	26,981	26,284	81,852	81,419
Gross margin	19,951	19,014	62,162	51,638
Operating expenses:				
Selling, general and administrative	11,225	10,144	33,796	30,385
Research and development	7,961	7,590	23,531	22,066
Gain from litigation-related settlement, net				(2,250)
Total operating expenses	19,186	17,734	57,327	50,201
Income from operations	765	1,280	4,835	1,437
Other income (expense), net	1,318	261	3,787	938
Income before income taxes	2,083	1,541	8,622	2,375
(Benefit) provision for income taxes	(379)	(167)	210	539
Net income	\$ 2,462	\$ 1,708	\$ 8,412	\$ 1,836
Net income per common share:				
Basic	\$ 0.06	\$ 0.04	\$ 0.20	\$ 0.04
Diluted	\$ 0.06	\$ 0.04	\$ 0.20	\$ 0.04
Shares used to compute net income per share:				
Basic	41,703	41,912	41,932	41,896
Diluted	41,771	42,093	42,212	42,049
Cash dividends declared per share			\$ 0.27	\$ 0.12

See accompanying notes.

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Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine Months Ended	
	September 30, 2006	September 30, 2005
Operating activities:		
Net income	\$ 8,412	\$ 1,836
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	10,621	12,794
Stock compensation expense	523	
Minority interest in net income of subsidiaries	417	659
Amortization of bond premium	14	462
(Gain) loss on disposal of equipment	(75)	10
Change in current assets and liabilities, net	(8,852)	4,542
Net cash provided by operating activities	11,060	20,303
Investing activities:		
Purchases of short-term investments	(105,107)	(70,682)
Sales and maturities of short-term and long-term investments	109,398	73,596
Additions to property, plant and equipment	(4,242)	(6,571)
Increase in other assets	(148)	(442)
Net cash used in investing activities	(99)	(4,099)
Financing activities:		
Proceeds from issuance of Common Stock	5,566	1,724
Common Stock dividends paid	(11,343)	(5,025)
Acquisitions of treasury stock	(10,835)	(3,277)
Net cash used in financing activities	(16,612)	(6,578)
Effect of foreign exchange rates on cash	3	185
Net (decrease) increase in cash and cash equivalents	(5,648)	9,811

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Cash and cash equivalents at beginning of period	34,024		36,277
Cash and cash equivalents at end of period	\$ 28,376	\$	46,088

See accompanying notes.

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VICOR CORPORATION
 Notes to Condensed Consolidated Financial Statements
 September 30, 2006
 (Unaudited)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for any other interim period or the year ending December 31, 2006. The balance sheet at December 31, 2005 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto contained in the Company's annual report on Form 10-K for the year ended December 31, 2005 (File No. 0-18277) filed by Vicor Corporation (the Company or Vicor) with the Securities and Exchange Commission.

2. Stock-Based Compensation

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (FAS 123R), which is a revision of FAS No. 123, Accounting for Stock-Based Compensation. FAS 123(R) supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and amends SFAS No. 95, Statement of Cash Flows. Generally, the approach in FAS 123(R) is similar to the approach described in FAS 123. However, FAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values at the date of grant. Pro forma disclosure is no longer an alternative.

The Company is using the modified prospective method as permitted under FAS 123(R). Under this transition method, compensation cost recognized in the first nine months of fiscal 2006 includes: (a) compensation cost for all share-based payments granted prior to but not yet vested as of December 31, 2005, based on the grant-date fair value estimated in accordance with the provisions of FAS 123, and (b) compensation cost for all share-based payments granted subsequent to December 31, 2005, based on the grant-date fair value estimated in accordance with the provisions of FAS 123(R). In accordance with the modified prospective method of adoption, Vicor's results of operations and financial position for prior periods have not been restated.

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VICOR CORPORATION
 Notes to Condensed Consolidated Financial Statements (Continued)
 September 30, 2006
 (Unaudited)

2. Stock-Based Compensation (Continued)

Vicor currently grants stock options under the following equity compensation plans that are shareholder-approved: *Amended and Restated 2000 Stock Option and Incentive Plan (the 2000 Plan)* The 2000 Plan permits the grant of share options to its employees and other key persons, including non-employee directors, for up to 4 million shares of common stock.

1998 Stock Option and Incentive Plan (the 1998 Plan) The 1998 Plan permits the grant of share options to its employees and other key persons, including non-employee directors for up to 2 million shares of common stock.

1993 Stock Option Plan (the 1993 Plan) The 1993 Plan permits the grant of share options to its employees and non-employee directors for up to 4 million shares of common stock.

Picor Corporation (Picor), a privately held majority owned subsidiary of Vicor, currently grants stock options under the following equity compensation plan that has been approved by its Board of Directors:

2001 Stock Option and Incentive Plan, as amended (the 2001 Picor Plan) The 2001 Picor Plan, permits the grant of share options to its employees and other key persons, including non-employee directors and full or part-time officers, for up to 10 million shares of common stock.

All option awards are granted at an exercise price equal to or greater than the market price for Vicor at the date of the grant, and are granted at the fair market value for Picor at the date of grant. Options vest at various periods of up to five years and may be exercised for up to ten years from the date of grant, which is the maximum contractual term.

As a result of adopting FAS 123(R), the Company recorded \$173,000 of non-cash stock-based compensation expense for the three months ended September 30, 2006 and \$523,000 for the nine months ended September 30, 2006. The stock-based compensation included \$16,000 in cost of revenues, \$92,000 in selling, general and administrative expense and \$65,000 in research and development expense for the three months ended September 30, 2006 and \$65,000, \$271,000, and \$187,000, respectively, for the nine months ended September 30, 2006. The compensation expense did not have a material impact on basic or diluted net income per share.

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September 30, 2006
(Unaudited)**2. Stock-Based Compensation (Continued)**

Had expense been recognized using the fair value method described in FAS 123, using the Black-Scholes option pricing model, the following pro forma results of operations would have been reported (in thousands except for per share information):

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net income as reported	\$ 1,708	\$ 1,836
Stock-based employee compensation cost, net of related tax effects	(199)	(675)
Pro forma net income	\$ 1,509	\$ 1,161
Net income per share, as reported:		
Basic	\$ 0.04	\$ 0.04
Diluted	\$ 0.04	\$ 0.04
Pro forma net income per share:		
Basic	\$ 0.04	\$ 0.03
Diluted	\$ 0.04	\$ 0.03

The above table includes compensation expense for Picor options of \$28,000 and \$77,000 for the three and nine months ended September 30, 2005. The three and nine months ended September 30, 2005 expenses has been revised to include these Picor amounts. The fair value of Picor common stock was estimated by obtaining an independent valuation of Picor.

The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	Vicor		Picor		Vicor		Picor	
	2006	2005	2006	2005	2006	2005	2006	2005
Risk-free interest rate	4.8%	3.9%	5.1%	4.4%	4.7%	3.9%	5.1%	4.4%
Expected dividend yield	1.8%	.9%			1.5%	.2%		

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Expected volatility	.52	.57	.48	.43	.53	.59	.48	.43
Expected term (years)	4.1	4.5	6.5	6.5	3.8	3.9	6.5	6.5

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Notes to Condensed Consolidated Financial Statements (Continued)
September 30, 2006
(Unaudited)**2. Stock-Based Compensation (Continued)***Risk-free interest rate:*

Vicor The Company uses the yield on zero-coupon U.S. Treasury Strip securities for a period that is commensurate with the expected term assumption for each vesting period.

Picor The Company uses the yield to maturity of a ten-year treasury bond, since all of Picor's options expire ten years after they are granted.

Expected dividend yield:

Vicor The Company determines the expected dividend yield by annualizing the most recent prior cash dividends declared by the Company's Board of Directors and dividing that result by the closing stock price on the date of that dividend declaration. Because the Company historically has not paid regular periodic dividends and has not committed to do so in the future, the Company annualizes the most recent prior cash dividends based on its expectations at the time regarding the frequency of dividends to be declared over the next twelve months. Dividends are not paid on options.

Picor Picor has not and does not expect to declare and pay dividends in the foreseeable future. Therefore, the expected dividend yield is not applicable.

Expected volatility:

Vicor Under FAS 123, Vicor used historical volatility to estimate the grant-date fair value of the options. Under FAS 123(R), Vicor has elected to continue to use historical volatility, using the expected term for the period over which to calculate the volatility (see below). The Company does not expect its future volatility to differ from its historical volatility. The computation of the Company's volatility is based on a simple average calculation of monthly volatilities over the expected term.

Picor As Picor is a nonpublic entity, historical volatility information is not available. As permitted under FAS 123(R), an industry sector index of approximately 40 publicly traded fabless semiconductor firms was developed for calculating historical volatility for Picor. Historical prices for each of the companies in the index based on the market price of the shares on each day of trading over the expected term were used to determine the historical volatility.

Expected term:

Vicor The Company uses historical employee exercise and option expiration data to estimate the expected term assumption for the Black-Scholes grant-date valuation. The Company believes that this historical data is currently the best estimate of the expected term of options, and that generally all groups of our employees exhibit similar exercise behavior.

Picor Due to the lack of historical information, the simplified method prescribed by the Securities and Exchange Commission's Staff Accounting Bulletin No. 107 was used to determine the expected term.

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Notes to Condensed Consolidated Financial Statements (Continued)
September 30, 2006
(Unaudited)**2. Stock-Based Compensation (Continued)***Forfeiture rate*

Vicor The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. FAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term forfeitures is distinct from cancellations or expirations and represents only the unvested portion of the surrendered option. The Company currently expects, based on an analysis of its historical forfeitures, that approximately 84% of its options will actually vest, and therefore has applied an annual forfeiture rate of 9.4% to all unvested options as of September 30, 2006. This analysis will be re-evaluated quarterly and the forfeiture rate will be adjusted as necessary. Ultimately, the actual expense recognized over the vesting period will only be for those shares that vest.

Picor Since the compensation expense for the three and nine months ended September 30, 2006 was immaterial, the Company did not apply an estimated forfeiture rate to the compensation expense.

A summary of the activity under Vicor's stock option plans as of September 30, 2006 and changes during the three and nine month periods then ended, is presented below (in thousands except for share and weighted-average data):

	Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Outstanding at June 30, 2006	1,766,992	\$18.94		
Granted	7,000	\$11.56		
Forfeited and expired	(65,119)	\$30.50		
Exercised	(14,542)	\$ 7.45		
Outstanding at September 30, 2006	1,694,331	\$18.56	3.09	\$760
Exercisable at September 30, 2006	1,456,239	\$19.16	2.60	\$609
Vested or expected to vest at September 30, 2006				
(1)	1,660,747	\$18.61	3.01	\$747

(1) In addition to the vested options, the Company expects a

portion of the
unvested
options to vest
at some point in
the future.

Options
expected to vest
is calculated by
applying an
estimated
forfeiture rate to
the unvested
options.

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September 30, 2006
(Unaudited)2. Stock-Based Compensation (Continued)

	Options Outstanding	Weighted- Average Exercise Price
Outstanding at December 31, 2005	2,260,248	\$18.14
Granted	103,860	\$18.57
Forfeited and expired	(235,337)	\$25.08
Exercised	(434,440)	\$12.80
Outstanding at September 30, 2006	1,694,331	\$18.56

During the three and nine months ended September 30, 2006, under all plans, the total intrinsic value of Vicor options exercised (i.e. the difference between the market price at exercise and the price paid by the employee to exercise the options) was \$77,000 and \$3,043,000, respectively, and the total amount of cash received from exercise of these options was \$109,000 and \$5,559,000, respectively. The total grant-date fair value of stock options that vested during the three and nine months ended September 30, 2006 was approximately \$125,000 and \$1,236,000, respectively.

As of September 30, 2006, there was \$883,000 of total unrecognized compensation cost related to unvested share-based awards for Vicor. That cost is expected to be recognized over a weighted-average period of 1.62 years for all Vicor awards.

A summary of the activity under Vicor's stock option plan as of September 30, 2006 and changes during the three and nine month periods then ended, is presented below (in thousands except for share and weighted-average data):

	Options Outstanding	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Outstanding at June 30, 2006	4,057,140	\$0.53		
Granted	255,000	\$0.88		
Forfeited and expired	(9,600)	\$0.33		
Exercised				
Outstanding at September 30, 2006	4,302,540	\$0.55	7.17	\$1,402
Exercisable at September 30, 2006	1,950,904	\$0.38	6.02	\$ 980

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Vested or expected to vest at September 30, 2006	4,302,540	\$0.55	7.17	\$1,402
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