

MICROVISION INC  
Form 10-Q  
May 10, 2012

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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

For the quarterly period ended March 31, 2012

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 0-21221

[MicroVision, Inc.](#)

(Exact name of Registrant as Specified in its Charter)

**Delaware**

(State or Other Jurisdiction of Incorporation or Organization)

**91-1600822**

(I.R.S. Employer Identification Number)

6222 185th Avenue NE  
Redmond, Washington 98052

(Address of Principal Executive Offices, including Zip Code)

(425) 936-6847

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(Registrant's Telephone Number, including Area Code)

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 reports), and (2) has been subject to such filing requirements for the past 90 days. 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). 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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). YES  NO

As of May 7, 2012, 17,047,000 shares of the Company's common stock, \$0.001 par value, were outstanding.

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MicroVision, Inc.  
Consolidated Balance Sheets  
(In thousands, except per share data)  
(Unaudited)

|  | March 31,<br>2012 | December 31,<br>2011 |
|--|-------------------|----------------------|
| <b>Assets</b>  |                   |                      |
| Current assets   |                   |                      |
| Cash and cash equivalents  | \$ 6,808          | \$ 13,075            |
| Investment securities, available-for-sale  | 13                | 8                    |
| Accounts receivable, net of allowances of \$318 and \$243  | 389               | 463                  |
| Costs and estimated earnings in excess of billings on uncompleted contracts                                | 63                | 70                   |
| Inventory  | 1,119             | 4,254                |
| Other current assets   | 925               | 785                  |
| Total current assets   | 9,317             | 18,655               |
| Property and equipment, net  | 1,984             | 2,347                |
| Restricted investments   | 436               | 786                  |
| Intangible assets  | 2,002             | 2,048                |
| Other assets   | 34                | 34                   |
| Total assets   | \$ 13,773         | \$ 23,870            |
| <b>Liabilities and Shareholders' Equity</b>  |                   |                      |
| Current liabilities  |                   |                      |
| Accounts payable   | \$ 6,406          | \$ 7,341             |
| Accrued liabilities  | 5,031             | 5,113                |
| Billings in excess of costs and estimated earnings on uncompleted contracts                                | 602               | 156                  |
| Current portion of capital lease obligations   | 41                | 39                   |
| Current portion of long-term debt  | 95                | 93                   |
| Total current liabilities  | 12,175            | 12,742               |
| Capital lease obligations, net of current portion  | 60                | 72                   |
| Long-term debt, net of current portion   | 42                | 67                   |
| Deferred rent, net of current portion  | 119               | 187                  |
| Total liabilities  | 12,396            | 13,068               |
| Commitments and contingencies  |                   |                      |
| Shareholders' Equity   |                   |                      |
| Preferred stock, par value \$.001; 25,000 shares authorized; 0 and 0 shares issued and outstanding         | -                 | -                    |
| Common stock, par value \$.001; 100,000 shares authorized; 17,027 and 17,019 shares issued and outstanding | 17                | 17                   |
| Additional paid-in capital   | 426,031           | 425,658              |
| Accumulated other comprehensive loss   | (30)              | (35)                 |
| Accumulated deficit  | (424,641)         | (414,838)            |
| Total shareholders' equity   | 1,377             | 10,802               |
| Total liabilities and shareholders' equity   | \$ 13,773         | \$ 23,870            |

The accompanying notes are an integral part of these financial statements.

MicroVision, Inc.  
Consolidated Statements of Operations  
(In thousands, except per share data)  
(Unaudited)

|   | Three Months Ended |            |
|---|--------------------|------------|
|   | March 31,          |            |
|   | 2012               | 2011       |
| Product revenue   | \$ 1,529           | \$ 886     |
| Contract revenue  | 201                | 233        |
| Total revenue   | 1,730              | 1,119      |
| Cost of product revenue                                 | 4,175              | 2,240      |
| Cost of contract revenue                                | 155                | 299        |
| Total cost of revenue                                   | 4,330              | 2,539      |
| Gross margin  | (2,600)            | (1,420)    |
| Research and development expense                        | 3,940              | 4,327      |
| Sales, marketing, general and administrative expense    | 3,288              | 3,299      |
| Gain on disposal of fixed assets                        | -                  | (7)        |
| Total operating expenses                                | 7,228              | 7,619      |
| Loss from operations                                    | (9,828)            | (9,039)    |
| Interest income   | 10                 | 15         |
| Interest expense  | (9)                | (13)       |
| Other income  | 24                 | -          |
| Net loss  | \$ (9,803)         | \$ (9,037) |
| Net loss per share - basic and diluted                  | \$ (0.58)          | \$ (0.70)  |
| Weighted-average shares outstanding - basic and diluted | 17,027             | 12,837     |

The accompanying notes are an integral part of these financial statements.

MicroVision, Inc.  
Consolidated Statements of Comprehensive Loss  
(In thousands)  
(Unaudited)

|  | Three Months Ended<br>March 31, |            |
|--|---------------------------------|------------|
|  | 2012                            | 2011       |
| Net loss   | \$ (9,803)                      | \$ (9,037) |
| Other comprehensive gain (loss):                                       |                                 |            |
| Unrealized gain (loss) on investment securities,<br>available-for-sale | 5                               | (1)        |
| Comprehensive loss   | \$ (9,798)                      | \$ (9,038) |

The accompanying notes are an integral part of these financial statements.

MicroVision, Inc.  
Consolidated Statements of Cash Flows  
(In thousands)  
(Unaudited)

|   | Three Months Ended<br>March 31, |            |
|---|---------------------------------|------------|
|   | 2012                            | 2011       |
| Cash flows from operating activities  |                                 |            |
| Net loss  | \$ (9,803)                      | \$ (9,037) |
| Adjustments to reconcile net loss to net cash used in operations:           |                                 |            |
| Depreciation  | 613                             | 518        |
| Amortization of intangible assets   | 46                              | 47         |
| Gain on disposal of property and equipment                                  | -                               | (7)        |
| Non-cash stock-based compensation expense                                   | 373                             | 401        |
| Inventory write-downs   | 1,094                           | 461        |
| Non-cash deferred rent  | (44)                            | (69)       |
| Change in:  |                                 |            |
| Accounts receivable, net  | 74                              | 236        |
| Costs and estimated earnings in excess of billings on uncompleted contracts | 7                               | 14         |
| Inventory   | 2,041                           | 191        |
| Other current assets  | (140)                           | 87         |
| Other assets  | -                               | (12)       |
| Accounts payable  | (792)                           | (985)      |
| Accrued liabilities   | (106)                           | 142        |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 446                             | (34)       |
| Other long-term liabilities   | -                               | (94)       |
| Net cash used in operating activities                                       | (6,191)                         | (8,141)    |
| Cash flows from investing activities  |                                 |            |
| Decrease in restricted investment   | 350                             | 170        |
| Proceeds on sale of property and equipment                                  | -                               | 7          |
| Purchases of property and equipment   | (393)                           | (64)       |
| Net cash provided by (used in) investing activities                         | (43)                            | 113        |
| Cash flows from financing activities  |                                 |            |
| Principal payments under capital leases                                     | (10)                            | (12)       |
| Principal payments under long-term debt                                     | (23)                            | (20)       |
| Net proceeds from issuance of common stock and warrants                     | -                               | 3,116      |
| Net cash provided by (used in) financing activities                         | (33)                            | 3,084      |
| Net decrease in cash and cash equivalents                                   | (6,267)                         | (4,944)    |
| Cash and cash equivalents at beginning of period                            | 13,075                          | 19,413     |
| Cash and cash equivalents at end of period                                  | \$ 6,808                        | \$ 14,469  |
| Supplemental disclosure of cash flow information                            |                                 |            |
| Cash paid for interest  | \$ 9                            | \$ 13      |
| Supplemental schedule of non-cash investing and financing activities        |                                 |            |
| Other non-cash additions to property and equipment                          | \$ 86                           | \$ 229     |

The accompanying notes are an integral part of these financial statements.

MicroVision, Inc.  
Notes to Consolidated Financial Statements  
March 31, 2012  
(Unaudited)

1. MANAGEMENT'S STATEMENT AND PRINCIPLES OF CONSOLIDATION

Management's Statement

The Consolidated Balance Sheet as of March 31, 2012, the Consolidated Statements of Operations and Comprehensive Loss for the three months ended March 31, 2012 and 2011, and Consolidated Statements of Cash Flows for the three months ended March 31, 2012 and 2011 have been prepared by MicroVision, Inc. ("we" or "us") and have not been audited. In the opinion of management, all adjustments necessary to state fairly the financial position at March 31, 2012 and the results of operations, comprehensive loss and cash flows for all periods presented have been made and consist of normal recurring adjustments. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules of the Securities and Exchange Commission (the "SEC"). The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. You should read these condensed consolidated financial statements in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011. The results of operations for the three months ended March 31, 2012 are not necessarily indicative of the operating results that may be attained for the entire fiscal year.

We have incurred significant losses since inception. We have funded operations to date primarily through the sale of common stock, convertible preferred stock, warrants, the issuance of convertible debt and, to a lesser extent, from development contract revenues and product sales. At March 31, 2012, we had \$6.8 million in cash, cash equivalents and investment securities available-for-sale and a working capital deficit of \$2.9 million. In May 2012, we signed a definitive agreement with private investors to raise approximately \$5.0 million from the sale of our common stock and warrants to purchase our common stock. The investment is subject to customary closing conditions and is expected to be completed by May 29, 2012. See Note 10 for more information.

Based on our current operating plan, we anticipate that we have sufficient cash and cash equivalents to fund our operations through June 2012. With the additional \$5.0 million we expect to raise in May 2012, we anticipate that we would have sufficient cash and cash equivalents to fund our operations through October 2012. We will require additional cash to fund our operating plan past that time. We are introducing new technology into an emerging market which creates significant uncertainty about our ability to accurately project revenue, costs and cash flows. If the level of sales anticipated by our financial plan is not achieved or our working capital requirements are higher than planned, we will need to raise additional cash sooner or take actions to reduce operating expenses. We plan to obtain additional cash through the issuance of equity or debt securities and through the monetization of select patents that we believe are not core to our business. There can be no assurance that additional cash will be available or that, if available, it will be available on terms acceptable to us on a timely basis. If adequate funds are not available on a timely basis, we intend to consider limiting our operations substantially to extend our funds as we pursue other financing opportunities and business relationships. This limitation of operations would include significant reductions in staff and operating costs.

We have received a report from our independent public accounting firm regarding the consolidated financial statements for the year ended December 31, 2011 that includes an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern. Our consolidated financial statements have been prepared on a going concern basis.





A one-for-eight reverse stock split of MicroVision's common stock became effective on February 17, 2012. All of the share and per share amounts discussed and shown in the consolidated financial statements and notes have been adjusted to reflect the effect of this reverse split.

### Principles of Consolidation

Our consolidated financial statements include the accounts of MicroVision, Inc. and MicroVision Innovations Singapore Pte. Ltd. ("MicroVision Singapore"), a wholly owned foreign subsidiary. MicroVision Singapore was incorporated in April 2011 and is engaged in operational support functions for MicroVision, Inc. There were no material intercompany accounts and transactions during the three months ended March 31, 2012.

## 2. NET LOSS PER SHARE

Basic net loss per share is calculated using the weighted-average number of common shares outstanding during the reporting periods. Diluted net loss per share is calculated using the weighted-average number of common shares outstanding and taking into account the dilutive effect of all potentially dilutive securities, including common stock equivalents and convertible securities outstanding. Potentially dilutive common stock equivalents primarily consist of warrants, employee stock options and nonvested equity shares. Diluted net loss per share for the three months ended March 31, 2012 and 2011 is equal to basic net loss per share because the effect of all potential common stock outstanding during the periods, including options, warrants and nonvested equity shares is anti-dilutive. The components of basic and diluted net loss per share were as follows (in thousands, except loss per share data):

|  | Three Months Ended |            |
|--|--------------------|------------|
|  | March 31,          |            |
|  | 2012               | 2011       |
| Numerator:   |                    |            |
| Net loss available for common shareholders - basic and diluted | \$ (9,803)         | \$ (9,037) |
| Denominator:   |                    |            |
| Weighted-average common shares outstanding - basic and diluted | 17,027             | 12,837     |
| Net loss per share - basic and diluted                         | \$ (0.58)          | \$ (0.70)  |

On March 31, 2012 and 2011, we excluded the following convertible securities from diluted net loss per share, as the effect of including them would have been anti-dilutive: publicly traded warrants exercisable for 753,000 and 753,000 shares of common stock, respectively, options and private warrants exercisable into a total of 2,471,000 and 1,334,000 shares of common stock, respectively, and 127,000 and 122,000 shares of nonvested equity shares, respectively.

## 3. CASH EQUIVALENTS, INVESTMENT SECURITIES AVAILABLE-FOR-SALE AND FAIR VALUE MEASUREMENTS

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between informed market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the authoritative guidance establishes a three level fair value inputs hierarchy, and requires an entity to maximize the use of observable valuation inputs and minimize the use of unobservable inputs. When estimating fair values, we use market data, assumptions and risks we believe market participants would use in measuring the fair value of the asset or liability, including the risks inherent in the inputs and the valuation techniques.

Our cash equivalents and investment securities available-for-sale are comprised of money market savings accounts and equity securities. The corporate equity securities are valued using inputs and common methods with sufficient levels of transparency and observability to be classified at Level 2.



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The valuation inputs hierarchy classification for our assets measured at fair value on a recurring basis are summarized below as of March 31, 2012 and December 31, 2011. This table does not include cash held in our money market savings accounts. We did not have any liabilities measured at fair value on a recurring basis as of March 31, 2012 or December 31, 2011.

| As of March 31, 2012:       | Level 1 | Level 2   | Level 3 | Total     |
|-----------------------------|---------|-----------|---------|-----------|
| <b>Assets</b>               |         |           |         |           |
| Corporate equity securities | -       | \$ 13,000 | -       | \$ 13,000 |
|                             | \$ -    | \$ 13,000 | \$ -    | \$ 13,000 |
| <br>                        |         |           |         |           |
| As December 31, 2011:       | Level 1 | Level 2   | Level 3 | Total     |
| <b>Assets</b>               |         |           |         |           |
| Corporate equity securities | -       | \$ 8,000  | -       | \$ 8,000  |
|                             | \$ -    | \$ 8,000  | \$ -    | \$ 8,000  |

#### 4. INVENTORY

Inventory consists of the following:

|                | March 31,<br>2012 | December 31,<br>2011 |
|----------------|-------------------|----------------------|
| Raw materials  | \$ 128,000        | \$ 2,741,000         |
| Finished goods | 991,000           | 1,513,000            |
|                | \$ 1,119,000      | \$ 4,254,000         |

The inventory at March 31, 2012 and December 31, 2011 consisted of raw materials primarily for our accessory pico projectors and PicoP display engine, and finished goods primarily composed of our accessory pico projectors. Inventory for the three months ended March 31, 2012 also included net write downs of \$1.1 million to adjust our inventory value to reflect our lowered sales forecast of pico projectors resulting from our decision to reduce marketing activities for our first-generation PicoP technology products as availability of our next-generation PicoP technology approaches. Inventory is stated at the lower of cost or market, with cost determined on net realizable value basis. Management periodically assesses the need to provide for obsolescence of inventory and adjusts the carrying value of inventory to its net realizable value when required. In addition, we reduce the value of our inventory to our estimated scrap value when management determines that it is not probable that the inventory will be consumed through normal production during the next twelve months.

#### 5. SHARE-BASED COMPENSATION

We use the straight-line attribution method to allocate the fair value of share-based compensation awards over the requisite service period for each award. The following table shows the amount of stock-based employee compensation expense included in the consolidated statements of operations:

|  | Three Months Ended<br>March 31, |            |
|--|---------------------------------|------------|
|  | 2012                            | 2011       |
| Cost of contract revenue                             | \$ 6,000                        | \$ 10,000  |
| Cost of product revenue                              | 20,000                          | 10,000     |
| Research and development expense                     | 137,000                         | 174,000    |
| Sales, marketing, general and administrative expense | 215,000                         | 192,000    |
| Total share-based employee compensation expense      | \$ 378,000                      | \$ 386,000 |

## Options Activity and Positions

The following table summarizes shares, weighted average exercise price, weighted average remaining contractual term and aggregate intrinsic value of options outstanding and options exercisable as of March 31, 2012:

| Options                          | Shares  | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term<br>(years) | Aggregate<br>Intrinsic<br>Value |
|----------------------------------|---------|--|--|---------------------------------|
| Outstanding as of March 31, 2012 | 940,000 | \$ 23.99                                 | 5.0  | \$ 1,785                        |
| Exercisable as of March 31, 2012 | 739,000 | \$ 26.25                                 | 4.4  | \$ 1,483                        |

As of March 31, 2012, our unamortized share-based employee compensation was \$1.7 million which we plan to amortize over the next 2.2 years and our unamortized nonvested equity share-based employee compensation was \$557,000 which we plan to amortize over the next 1.7 years.

## 6. LONG-TERM NOTES

Tenant Improvement Loan Agreement

During 2006, we entered into a loan agreement with the lessor of our corporate headquarters in Redmond, Washington to finance \$536,000 in tenant improvements. The loan carries a fixed interest rate of 9% per annum, is repayable over the initial term of the lease, which expires in 2013, and is secured by a letter of credit. The balance of the loan was \$137,000 at March 31, 2012.

## 7. COMMITMENTS AND CONTINGENCIES

## Litigation

We are subject to various claims and pending or threatened lawsuits in the normal course of business. We are not currently party to any legal proceedings that management believes are reasonably possible to have a material adverse effect on our consolidated financial position, results of operations or cash flows.

## Adverse purchase commitments

We have periodically entered into noncancelable purchase contracts in order to ensure the availability of materials to support production of our PicoP based products. We periodically assess the need to provide for impairment on these purchase contracts and record a loss on purchase commitments when required. As of December 31, 2011 and March 31, 2012 we had approximately \$134,000 accrued for adverse purchase commitments related to these purchase contracts.

## 8. RECEIVABLES FROM RELATED PARTIES

Our accounts receivable balance at December 31, 2011 and March 31, 2012 includes \$159,000 from a sale of PicoP engines to Walsin Lihwa Corporation which integrated the engines into its product sold in China during 2011. Based on filings with the SEC as of March 31, 2012, Walsin Lihwa beneficially owns approximately 7.3% of our common stock as determined in accordance with SEC rules, through its wholly owned subsidiary Max Display Enterprises Limited.

## 9. NEW ACCOUNTING PRONOUNCEMENTS

In June 2011, the FASB issued a new accounting standard on the presentation of comprehensive income. The new standard requires the presentation of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. We have adopted this portion of the guidance with no material impact on our financial statements. The new standard also requires presentation of adjustments for items that are reclassified from other comprehensive income to net income in the statement where the components of net income and the components of other comprehensive income are presented. However, in December 2011 the FASB issued further guidance which indefinitely defers the guidance related to the presentation of reclassification adjustments.

## 10. SUBSEQUENT EVENTS

In April 2012, we reduced our workforce to align with our ingredient brand business model and expect to record expense of approximately \$304,000 related to the severance agreements for these employees in the second quarter of 2012.

In May 2012, we signed a definitive agreement with private investors to raise approximately \$5.0 million from the sale of 3.3 million shares of our common stock and warrants to purchase 1.0 million shares of our common stock. The warrants have an exercise price of \$2.125, are exercisable six months after the issuance date and have a three year term. The investment is subject to customary closing conditions and is expected to be completed by May 29, 2012.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Forward-Looking Statements

The information set forth in this report in Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," and Item 3, "Quantitative and Qualitative Disclosure about Market Risk," includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and is subject to the safe harbor created by that section. Such statements may include, but are not limited to, projections of revenues, income or loss, capital expenditures, plans for product development and cooperative arrangements, future operations, financing needs or plans of MicroVision, as well as assumptions relating to the foregoing. The words "anticipate," "believe," "estimate," "expect," "goal," "may," "plan," "project," "will," and similar expressions identify forward-looking statements, which speak only as of the date the statement was made. Factors that could cause actual results to differ materially from those projected in our forward-looking statements include the following: our ability to obtain financing; market acceptance of our technologies and products; our financial and technical resources relative to those of our competitors; our ability to keep up with rapid technological change; government regulation of our technologies; our ability to enforce our intellectual property rights and protect our proprietary technologies; the ability to obtain additional contract awards and to develop partnership opportunities; the timing of commercial product launches; the ability to achieve key technical milestones in key products; and other risk factors identified in this report under the caption "Item 1A - Risk Factors."

### Overview

We are developing high-resolution miniature laser display and imaging engines based upon our proprietary PicoP® display engine technology. Our PicoP technology utilizes our widely patented expertise in two dimensional Micro-Electrical Mechanical Systems (MEMS), lasers, optics and electronics to create a high quality video or still image from a small form factor device with lower power needs than conventional display technologies. Our strategy is to develop and supply PicoP display engines directly or through licensing of our patents and sale of key components

to original equipment manufacturers (OEMs) that would embed them into a variety of consumer, automotive, enterprise and industrial products. In markets requiring high volume production of the PicoP display engine components or subsystems that are to be integrated with other components, we plan to provide designs for components, subsystems and systems to OEMs under licensing arrangements.

The primary objective for consumer applications is to provide users of mobile consumer devices such as smartphones, media players, tablet PCs, and other consumer electronic products with a large screen viewing experience produced by a small embedded projector. These potential products would allow users to watch movies and videos, play video games, display images and other data onto a variety surfaces, freeing users from the limitations of a small, palm-sized screen. The current PicoP technology could be modified to be embedded into a pair of glasses to provide the mobile user with a see-through or occluded personal display to view movies, play games or access other content.

The PicoP technology could be embedded into a vehicle or integrated into a portable aftermarket device to create a high-resolution head-up display (HUD) that could project point-by-point navigation, critical operational, safety and other information important to the vehicle operator.

The enterprise products employing our technology would allow users in field-based professions such as service repair or sales to view and share information such as schematics for equipment repair and sales data and orders within CRM applications on a larger, more user-friendly interface. We also see potential for embedding the PicoP laser display engine in industrial products where our displays could be used for 3D measuring and digital signage, enhancing the overall user experience of these applications.

We currently market and sell our SHOWWX™ line of accessory pico projectors that use our Pico display engine through a network of global distributors. We continue to enter into a limited number of development agreements with commercial and U.S. government customers to develop advanced prototypes and demonstration units based on our light scanning technologies.

In February 2012, we announced our plan to transition to an "Image by PicoP" ingredient brand business model under which we will pursue commercialization of our PicoP display engine technology by licensing our technology and selling key components to OEMs who would design and build products using the PicoP technology. We expect to make our next-generation HD PicoP display engine technology based on direct green lasers (PicoP Gen2) available to OEMs this year.

## Results of Operations

### Product revenue

| (in thousands)              | 2012     | 2011   | \$ change | % change |
|-----------------------------|----------|--------|-----------|----------|
| Three months ended March 31 | \$ 1,529 | \$ 886 | \$ 643    | 72.6     |

Our product sales generally include acceptance provisions. We recognize product revenue upon acceptance of the product by the customer or expiration of the contractual acceptance period, after which there are no rights of return. We have entered into agreements with resellers and distributors. Sales made to resellers and distributors are recognized using either the sell-through method or upon expiration of the contractually agreed-upon acceptance period, depending on our ability to reasonably estimate returns. Some of the agreements with resellers and distributors contain price-protection clauses, and revenue is recognized net of these amounts. Provisions are made for warranties at the time revenue is recorded. Warranty expense was not material for any periods presented.

Our quarterly revenue may vary substantially due to the timing of product orders from customers, production constraints and availability of components and raw materials. We plan to continue to sell our existing inventory of SHOWWX products through the second quarter of 2012.

Product revenue was higher during the three months ended March 31, 2012 than the same period in 2011, due to increased sales of our PicoP display engines compared to the prior period. The backlog of product orders at March 31, 2012 was approximately \$305,000, compared to \$591,000 at March 31, 2011. The product backlog is scheduled for



delivery within one year.

## Contract revenue.

| (in thousands)              | 2012   | 2011   | \$ change | % change |
|-----------------------------|--------|--------|-----------|----------|
| Three months ended March 31 | \$ 201 | \$ 233 | \$ (32)   | (13.7)   |

We earn contract revenue from performance on development contracts with the U.S. government and commercial customers and from the sale of prototype units and evaluation kits based on our PicoP display engine. Our contract revenue from development contracts in a particular period is dependent upon when we enter into a contract, the value of the contracts we have entered into, and the availability of technical resources to perform work on the contracts. Our contract revenue from sales of prototype units and evaluation kits may vary substantially due to the timing of orders from customers and potential constraints on resources.

We recognize contract revenue as work progresses on long-term, cost plus fixed fee, and fixed price contracts using the percentage-of-completion method, which relies on estimates of total expected contract revenue and costs. We have developed processes that allow us to make reasonable estimates of the cost to complete a contract. When we begin work on the contract and at the end of each accounting period, we estimate the costs required to complete the contract and compare these estimates to costs incurred to date. Since our contracts generally require some level of technology development, the actual costs required to complete a contract can vary from our estimates. Recognized revenues are subject to revisions as actual cost becomes certain. Revisions in revenue estimates are reflected in the period in which the facts that give rise to the revision become known. In the future, revisions in these estimates could significantly impact recognized revenue in any one reporting period.

We recognize contract revenue on the sale of prototype units and evaluation kits, upon acceptance of the deliverables by the customer or expiration of the contractual acceptance period, after which there are no rights of return. While we anticipate future revenue from these units, quarterly revenue may vary substantially due to the timing of orders from customers and potential constraints on resources.

Contract revenue was lower during the three months ended March 31, 2012 than the same periods in 2011, due to the sale of fewer prototype units and evaluation kits in 2012, compared to the prior year.

Our backlog of development contracts, including orders for prototype units and evaluation kits, at March 31, 2012 was \$1.2 million compared to \$895,000 at March 31, 2011, all of which is scheduled for completion during the next twelve months.

## Cost of product revenue

| (in thousands)              | 2012     | % of product revenue | 2011     | % of product revenue | \$ change | % change |
|-----------------------------|----------|----------------------|----------|----------------------|-----------|----------|
| Three months ended March 31 | \$ 4,175 | 273.1                | \$ 2,240 | 252.8                | \$ 1,935  | 86.4     |

Our costs to produce pico projectors during the three months ended March 31, 2012 were substantially higher than product revenue. Cost of product revenue includes the direct and allocated indirect cost of manufacturing products sold to customers. Direct costs include labor, materials and other costs incurred directly in the manufacture of these products. Indirect costs include labor and other costs associated with operating our manufacturing capabilities and capacity. Our overhead, which includes the costs of procuring, inspecting and storing material, and facility and depreciation costs, is allocated to cost of product revenue based on the proportion of direct material purchased to support production. In the event that we maintain capacity in excess of production requirements, cost of product revenue may also include manufacturing overhead associated with the excess capacity. During the three months ended March 31, 2012 we expensed approximately \$244,000 of manufacturing overhead associated with production capacity in excess of production requirements, compared to \$340,000 during the three months ended March 31, 2011.



During the three months ended March 31, 2012, cost of product revenue included a net write down of \$1.1 million for inventory in stock at the end of the quarter. The write down included adjustments to our inventory value to reflect our lowered sales forecast of pico projectors as a result of our decision to reduce marketing activities for our first-generation PicoP technology products as availability of our next-generation PicoP technology approaches. The increase in cost of product revenue for the three months ended March 31, 2012, compared to the same period in 2011, was primarily a result of increased sales of pico projectors and higher inventory write downs compared to the same period a year ago.

During the three months ended March 31, 2012, we sold inventory which had been previously written down to the lower of cost or market. Accordingly, cost of product revenue for the three months ended March 31, 2012 did not include approximately \$1.1 million of previously recognized write downs associated with this inventory.

The cost of product revenue as a percentage of product revenue can fluctuate significantly from period to period, depending on the product mix and volume, the level of overhead expense and the volume of direct material purchased. The increase in the cost of product revenue as a percentage of product revenue in 2012, compared to the same period in 2011, was primarily attributed to lower of cost or market adjustments comprising a larger proportion of total cost of product revenue.

#### Cost of contract revenue

| (in thousands)              | 2012   | % of contract revenue | 2011   | % of contract revenue | \$ change | % change |
|-----------------------------|--------|-----------------------|--------|-----------------------|-----------|----------|
| Three months ended March 31 | \$ 155 | 77.1                  | \$ 299 | 128.3                 | \$ (144)  | (48.2)   |

Cost of contract revenue includes both the direct and allocated indirect costs of performing on development contracts and producing prototype units and evaluation kits. Direct costs include labor, materials and other costs incurred directly in performing on a contract or producing prototype units and evaluation kits. Indirect costs include labor and other costs associated with operating our research and development department and building our technical capabilities and capacity. Cost of contract revenue is determined by the level of direct and indirect costs incurred, which can fluctuate substantially from period to period.

Cost of contract revenue for the three months ended March 31, 2011 included a provision for estimated losses on uncompleted contracts of \$85,000. The losses resulted from excess material cost associated with minimum order quantities for materials required to complete the statement of work.

Cost of contract revenue was lower during the three months ended March 31, 2012 than the same period in 2011 as a result of lower contract activity and no provision for estimated losses compared to the prior period. The cost of contract revenue as a percentage of contract revenue was lower in the three months ended March 31, 2012, than in the comparable periods in 2012 primarily as a result of the provision for estimated losses recognized in the prior period.

The cost of revenue as a percentage of revenue can fluctuate significantly from period to period, depending on the contract cost mix and the levels of direct and indirect costs incurred.

#### Research and development expense.

| (in thousands)              | 2012     | 2011     | \$ change | % change |
|-----------------------------|----------|----------|-----------|----------|
| Three months ended March 31 | \$ 3,940 | \$ 4,327 | \$ (387)  | (8.9)    |

Research and development expense consists of compensation related costs of employees and contractors engaged in internal research and product development activities, direct material to support development programs, laboratory operations, outsourced development and processing work, and other operating expenses. We allocate our research and development resources based on the business opportunity of the available projects, the skill mix of the resources

available and the contractual commitments we have made to customers.

The decrease in research and development expense during the three months ended March 31, 2012, compared to the same period in 2011, is primarily attributable to decreased payroll costs associated with reductions in staffing levels compared to the prior year.

We believe that under the ingredient brand business model we will lower our research and development spending substantially in the future. We expect that continuing research and development expense will be required to advance the PicoP technology and support our customers to integrate our technology into their products under the ingredient brand business model.

Sales, marketing, general and administrative expense.

| (in thousands)              | 2012     | 2011     | \$ change | % change |
|-----------------------------|----------|----------|-----------|----------|
| Three months ended March 31 | \$ 3,288 | \$ 3,299 | \$ (11)   | (0.3)    |

Sales, marketing, general and administrative expense includes compensation and support costs for marketing, sales, management and administrative staff, and for other general and administrative costs, including legal and accounting services, consultants and other operating expenses. We believe that under the ingredient brand business model we will lower our sales, marketing, general and administrative spending in the future.

Interest income.

| (in thousands)              | 2012  | 2011  | \$ change | % change |
|-----------------------------|-------|-------|-----------|----------|
| Three months ended March 31 | \$ 10 | \$ 15 | \$ (5)    | (33.3)   |

The decrease in interest income for the three ended March 31, 2012 compared to the same period in 2011 resulted primarily from lower average cash, investment securities balances, and interest rates.

Interest expense.

| (in thousands)              | 2012 | 2011  | \$ change | % change |
|-----------------------------|------|-------|-----------|----------|
| Three months ended March 31 | \$ 9 | \$ 13 | \$ (4)    | (30.8)   |

The decrease in interest expense for the three months ended March 31, 2012 compared to the same period in 2011 resulted primarily from lower average balances on our capital leases and our outstanding loan for leasehold improvements.

### Liquidity and Capital Resources

We have incurred significant losses since inception. We have funded our operations to date primarily through the sale of equity and debt securities and, to a lesser extent, from development contract revenues and product sales. At March 31, 2012, we had \$6.8 million in cash, cash equivalents and investment securities, available-for-sale and a working capital deficit of \$2.9 million. In May 2012, we signed a definitive agreement with private investors to raise approximately \$5.0 million from the sale of our common stock and warrants to purchase our common stock. The investment is subject to customary closing conditions and is expected to be completed by May 29, 2012. See Item 5 of this report for more information.

Based on our current operating plan, we anticipate that we have sufficient cash and cash equivalents to fund our operations through June 2012. With the additional \$5.0 million we expect to raise in May 2012, we anticipate that we would have sufficient cash and cash equivalents to fund our operations through October 2012. We will require additional cash to fund our operating plan past that time. We are introducing new technology into an emerging market which creates significant uncertainty about our ability to accurately project revenue, costs and cash flows. If the level of sales anticipated by our financial plan is not achieved or our working capital requirements are higher than planned, we will need to raise additional cash sooner or take actions to reduce operating expenses. We plan to obtain additional cash through the issuance of equity or debt securities and through the monetization of select patents that we believe are not core to our business. There can be no assurance that additional cash will be available or that, if available, it will be available on terms acceptable to us on a timely basis. If adequate funds are not available on a timely basis, we intend to consider limiting our operations substantially to extend our funds as we pursue other financing opportunities and business relationships. This limitation of operations would include significant reductions in staff and operating costs.

We received a report from our independent public accounting firm regarding the consolidated financial statements for the year ended December 31, 2011 that includes an explanatory paragraph expressing substantial doubt about our ability to continue as a going concern. Our consolidated financial statements have been prepared on a going concern basis.

In April 2012, we implemented measures designed to significantly reduce our cash used in operations in the second half of 2012 compared to the levels expected for the first half of 2012 to align with our ingredient brand business model.

Cash used in operating activities totaled \$6.2 million during the three months ended March 31, 2012, compared to \$8.1 million during the same period in 2011. During the three months ended March 31, 2012, the decrease in net cash used in operating activities was primarily driven by lower inventory purchases for commercialization of PicoP-based products.

Net cash used in investing activities totaled \$43,000 for the three months ended March 31, 2012 compared to net cash provided by investing activities of \$113,000 during the three months ended March 31, 2011. During the three months ended March 31, 2012, the change in net cash used in investing activities was primarily driven by the expiration of a letter of credit that was outstanding under a supplier agreement resulting in a decrease of our restricted investments offset by purchases of production equipment. During the three months ended March 31, 2012, we used cash of \$393,000 for capital expenditures, compared to \$64,000 during the same period in 2011.

Net cash used in financing activities totaled \$33,000 for the three months ended March 31, 2012 compared to net cash provided by financing activities of \$3.1 million during the same period in 2011. In March 2011, we raised \$3.1 million, before placement agent and other issuance costs, from the sale of approximately 313,000 shares of our common stock.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

#### Interest Rate and Market Liquidity Risks

As of March 31, 2012, all of our cash, cash equivalents and investment securities available-for-sale have variable interest rates or are equity investments traded in active markets. Therefore, we believe our exposure to the market and interest rate risk is not material.

Our investment policy generally directs that the investment managers should select investments to achieve the following goals: principal preservation, adequate liquidity and return.





The values of cash equivalents and investment securities, available-for-sale by maturity date as of March 31, 2012, are as follows:

| (amount in thousands)     | <b>Amount</b> | <b>Percent</b> |
|---------------------------|---------------|----------------|
| Cash and cash equivalents | \$ 6,808      | 99.81 %        |
| Less than one year        | 13            | 0.19 %         |
| One to two years          | -             | -              |
| Greater than five years   | -             | -              |
|                           | \$ 6,821      | 100.00 %       |

#### Foreign Exchange Rate Risk

All of our development contract payments are made in U.S. dollars. However, in the future we may enter into additional development contracts in foreign currencies that may subject us to foreign exchange rate risk. We have purchase orders and supply agreements in foreign currencies and may enter into such arrangements from time to time in the future. We believe our exposure to currency fluctuations related to these arrangements is not material. We intend to enter into foreign currency hedges to offset material exposure to currency fluctuations when we can adequately determine the timing and amounts of the exposure.

#### ITEM 4.

#### **CONTROLS AND PROCEDURES**

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934) as of the end of the period covered by this report and, based on this evaluation, our principal executive officer and principal financial officer have concluded that these disclosure controls and procedures are effective. There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Securities Exchange Act of 1934) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### PART II

#### OTHER INFORMATION

#### ITEM 1A

#### **- RISK FACTORS**

#### Risk Factors Relating to the MicroVision Business

We have a history of operating losses and expect to incur significant losses in the future.

We have had substantial losses since our inception. We cannot assure you that we will ever become or remain profitable.

- As of March 31, 2012, we had an accumulated deficit of \$424.6 million.
- We incurred consolidated net losses of \$331.5 million from inception through 2009, \$47.5 in 2010, \$35.8 million in 2011, and a net loss of \$9.8 million in the three months ended March 31, 2012.

The likelihood of our success must be considered in light of the expenses, difficulties and delays frequently encountered by companies formed to develop and market new technologies. In particular, our operations to date have focused primarily on research and development of our technology platform and development of demonstration units.

We are unable to accurately estimate future revenues and operating expenses based upon historical performance.

We cannot be certain that we will succeed in obtaining additional development contracts or that we will be able to obtain substantial customer orders for our products. In light of these factors, we expect to continue to incur substantial losses and negative cash flow at least through 2012 and likely thereafter. We cannot be certain that we will achieve positive cash flow at any time in the future.

We will require additional capital to fund our operations and to implement our business plan. If we do not obtain additional capital, we may be required to curtail our operations substantially. Raising additional capital may dilute the value of current shareholders' shares.

Based on our current operating plan, we anticipate that we have sufficient cash and cash equivalents to fund our operations through June 2012. In May 2012, we signed a definitive agreement with private investors to raise approximately \$5.0 million from the sale of our common stock and warrants to purchase our common stock which we expect to be completed by May 29, 2012. See Item 5 of this report for more information. With the additional \$5.0 million we expect to raise in May 2012, we anticipate that we would have sufficient cash and cash equivalents to fund our operations through October 2012. We will require additional cash to fund our operating plan past that time. We are introducing new technology into an emerging market which creates significant uncertainty about our ability to accurately project revenue, costs and cash flows. If the level of sales anticipated by our financial plan is not achieved or our working capital requirements are higher than planned, we will need to raise additional cash sooner or take actions to reduce operating expenses. We plan to obtain additional cash through the issuance of equity or debt securities and through the monetization of select patents that we believe are not core to our business.

Our capital requirements will depend on many factors, including, but not limited to, the rate at which we can, directly or through arrangements with original equipment manufacturers, introduce products incorporating the PicoP display engine and image capture technologies and the market acceptance and competitive position of such products. If revenues are less than we anticipate, if the mix of revenues varies from anticipated amounts or if expenses exceed the amounts budgeted, we may require additional capital earlier than expected to fund our operations. In addition, our operating plan provides for the development of strategic relationships with systems and equipment manufacturers that may require additional investments by us.

Additional capital may not be available to us, or if available, on terms acceptable to us or on a timely basis. Raising additional capital may involve issuing securities with rights and preferences that are senior to our common stock and may dilute the value of current shareholders' shares. If adequate funds are not available on a timely basis we intend to consider limiting our operations substantially to extend out funds as we pursue other financing opportunities and business relationships. This limitation of operations would include significant reductions in staff and operating costs.

We are dependent on third parties in order to develop, manufacture, sell and market our products.

Our strategy for commercializing our technology and products incorporating the PicoP display engine technology includes entering into cooperative development, manufacturing, sales and marketing arrangements with corporate partners, original equipment manufacturers and other third parties. We cannot be certain that we will be able to negotiate arrangements on acceptable terms, if at all, or that these arrangements will be successful in yielding commercially viable products. If we cannot establish these arrangements, we would require additional capital to undertake such activities on our own and would require extensive manufacturing, sales and marketing expertise that we do not currently possess and that may be difficult to obtain. In addition, we could encounter significant delays in introducing the PicoP display engine technology or find that the development, manufacture or sale of products incorporating the PicoP display engine would not be feasible. To the extent that we enter into cooperative development, sales and marketing or other joint venture arrangements, our revenues will depend upon the performance of third parties. We cannot be certain that any such arrangements will be successful.

We cannot be certain that our technology platform or products incorporating our PicoP display engine will achieve market acceptance. If products incorporating the PicoP display engine do not achieve market acceptance, our revenues may not grow.

Our success will depend in part on customer acceptance of the PicoP display engine. The PicoP display engine may not be accepted by manufacturers who use display technologies in their products, by systems integrators who incorporate our products into their products or by end users of these products. To be accepted, the PicoP display

engine must meet the expectations of our potential customers in the consumer, automotive, industrial, and medical markets. If our technology fails to achieve market acceptance, we may not be able to continue to develop our technology platform.

Future products based on our PicoP technology are dependent on advances in technology by other companies.

Our PicoP technology will continue to rely on technologies, such as light sources, MEMS and optical components that are developed and produced by other companies. The commercial success of certain future products based on our technology will depend in part on advances in these and other technologies by other companies. We may, from time to time, contract with and support companies developing key technologies in order to accelerate the development of them for our or our customers' specific uses. There are no guarantees that such activities will result in useful technologies or components for us.

We are dependent on a small number of customers for our revenue. Our quarterly performance may vary substantially and this variance, as well as general market conditions, may cause our stock price to fluctuate greatly and potentially expose us to litigation.

Since 2010, most of our revenues have been generated from product sales to a limited number of customers and distribution partners. Our quarterly operating results may vary significantly based on:

- commercial acceptance of our PicoP-based products;
- the rate at which our distributors can achieve sell through of our products;
- changes in evaluations and recommendations by any securities analysts following our stock or our industry generally;
- announcements by other companies in our industry;
- changes in business or regulatory conditions;
- announcements or implementation by our competitors of technological innovations or new products;
- the status of particular development programs and the timing of performance under specific development agreements;
- economic and stock market conditions; or
- other factors unrelated to our company or industry.

In one or more future quarters, our results of operations may fall below the expectations of securities analysts and investors and the trading price of our common stock may decline as a consequence. In addition, following periods of volatility in the market price of a company's securities, shareholders often have instituted securities class action litigation against that company. If we become involved in a class action suit, it could divert the attention of management, and, if adversely determined, could require us to pay substantial damages.

We or our customers may fail to perform under open orders, which could adversely affect our operating results and cash flows.

Our backlog of open orders totaled \$1.5 million as of March 31, 2012. We may be unable to meet the performance requirements, including performance specifications or delivery dates, required by such purchase orders. Further, our customers may be unable or unwilling to perform their obligations there under on a timely basis or at all if, among other reasons, our products and technologies do not achieve market acceptance, our customers' products and technologies do not achieve market acceptance or our customers otherwise fail to achieve their operating goals. To the extent we are unable to perform under such purchase orders or to the extent customers are unable or unwilling to perform, our operating results and cash flows could be adversely affected.

It may become more difficult to sell our stock in the public market or maintain our listing on the NASDAQ Global Market.

Our common stock is listed for quotation on The NASDAQ Global Market. To keep our listing on this market, we must meet NASDAQ's listing maintenance standards. If we are unable to continue to meet NASDAQ's listing maintenance standards, our common stock could be delisted from The NASDAQ Global Market. If our common stock were delisted, we likely would seek to list the common stock on the NASDAQ Capital Market, the American Stock Exchange or on a regional stock exchange. Listing on such other market or exchange could reduce the liquidity of our common stock. If our common stock were not listed on the NASDAQ Capital Market or an exchange, trading of our common stock would be conducted in the over-the-counter market on an electronic bulletin board established for unlisted securities or directly through market makers in our common stock. If our common stock were to trade in the over-the-counter market, an investor would find it more difficult to dispose of, or to obtain accurate quotations for the price of, the common stock. A delisting from The NASDAQ Global Market and failure to obtain listing on such other market or exchange would subject our securities to so-called penny stock rules that impose additional sales practice and market-making requirements on broker-dealers who sell or make a market in such securities. Consequently, removal from The NASDAQ Global Market and failure to obtain listing on another market or exchange could affect the ability or willingness of broker-dealers to sell or make a market in our common stock and the ability of purchasers of our common stock to sell their securities in the secondary market. In addition, when the market price of our common stock is less than \$5.00 per share, we become subject to penny stock rules even if our common stock is still

listed on The NASDAQ Global Market. While the penny stock rules should not affect the quotation of our common stock on The NASDAQ Global Market, these rules may further limit the market liquidity of our common stock and the ability of investors to sell our common stock in the secondary market. The market price of our stock has mostly traded below \$5.00 per share during 2011, 2010, and 2009. On May 7, 2012, the closing price of our stock was \$1.76.

Our lack of financial and technical resources relative to our competitors may limit our revenues, potential profits, overall market share or value.

Our current products and potential future products will compete with established manufacturers of existing products and companies developing new technologies. Many of our competitors have substantially greater financial, technical and other resources than we have. Because of their greater resources, our competitors may develop products or technologies that are superior to our own. The introduction of superior competing products or technologies could result in reduced revenues, lower margins or loss of market share, any of which could reduce the value of our business.

We may not be able to keep up with rapid technological change and our financial results may suffer.

The information display industry has been characterized by rapidly changing technology, accelerated product obsolescence and continuously evolving industry standards. Our success will depend upon our ability to further develop our technology platform and to cost effectively introduce new products and features in a timely manner to meet evolving customer requirements and compete with competitors' product advances.

We may not succeed in these efforts because of:

- delays in product development;
- lack of market acceptance for our products; or
- lack of funds to invest in product development and marketing.

The occurrence of any of the above factors could result in decreased revenues, market share and value.

We could face lawsuits related to our use of the PicoP display engine or other technologies. Defending these suits would be costly and time consuming. An adverse outcome in any such matter could limit our ability to commercialize our technology and products, reduce our revenues and increase our operating expenses.

We are aware of several patents held by third parties that relate to certain aspects of light scanning displays and image capture products. These patents could be used as a basis to challenge the validity, limit the scope or limit our ability to obtain additional or broader patent rights of our patents or patents we have licensed. A successful challenge to the validity of our patents or patents we have licensed could limit our ability to commercialize our technology and the PicoP display engine and, consequently, materially reduce our revenues. Moreover, we cannot be certain that patent holders or other third parties will not claim infringement by us with respect to current and future technology. Because U.S. patent applications are held and examined in secrecy, it is also possible that presently pending U.S. applications will eventually be issued with claims that will be infringed by our products or our technology. The defense and prosecution of a patent suit would be costly and time consuming, even if the outcome were ultimately favorable to us. An adverse outcome in the defense of a patent suit could subject us to significant costs, to require others and us to cease selling products that incorporate the PicoP display engine, to cease licensing our technology or to require disputed rights to be licensed from third parties. Such licenses, if available, would increase our operating expenses. Moreover, if claims of infringement are asserted against our future co-development partners or customers, those partners or customers may seek indemnification from us for damages or expenses they incur.

If we fail to manage expansion effectively, our revenue and expenses could be adversely affected.

Our ability to successfully offer products and implement our business plan in a rapidly evolving market requires an effective planning and management process. The growth in business and relationships with customers and other third parties has placed, and will continue to place, a significant strain on our management systems and resources. We will need to continue to improve our financial and managerial controls, reporting systems and procedures and will need to continue to train and manage our work force.

Our products may be subject to future health and safety regulations that could increase our development and production costs.

Products incorporating the PicoP display engine could become subject to new health and safety regulations that would reduce our ability to commercialize the PicoP display engine. Compliance with any such new regulations would likely increase our cost to develop and produce products using the PicoP display engine and adversely affect our financial results.



Our dependence on sales to distributors increases the risks of managing our supply chain and may result in excess inventory or inventory shortages.

We expect the majority of our distributor relationships for our accessory pico projector and its accessories to involve the distributor taking inventory positions and reselling to multiple customers. With these distributor relationships, we would not recognize revenue until the distributors sell the product through to their end user customers. Our distributor relationships may reduce our ability to forecast sales and increases risks to our business. Since our distributors would act as intermediaries between us and the end user customers, we would be required to rely on our distributors to accurately report inventory levels and production forecasts. This may require us to manage a more complex supply chain and monitor the financial condition and credit worthiness of our distributors and the end user customers. Our failure to manage one or more of these risks could result in excess inventory or shortages that could adversely impact our operating results and financial condition.

Our operating results may be adversely impacted by worldwide political and economic uncertainties and specific conditions in the markets we address.

In the recent past, general worldwide economic conditions have experienced a downturn due to slower economic activity, concerns about inflation, increased energy costs, decreased consumer confidence, reduced corporate profits and capital spending, and adverse business conditions. Any continuation or worsening of the current global economic and financial conditions could materially adversely affect (i) our ability to raise, or the cost of, needed capital, (ii) demand for our current and future products and (iii) our ability to commercialize products. We cannot predict the timing, strength, or duration of any economic slowdown or subsequent economic recovery, worldwide, or in the display industry.

Because we plan to continue using foreign contract manufacturers, our operating results could be harmed by economic, political, regulatory and other factors in foreign countries.

We currently use foreign manufacturers to manufacture future products, where appropriate. These international operations are subject to inherent risks, which may adversely affect us, including:

- political and economic instability;
- high levels of inflation, historically the case in a number of countries in Asia;
- burdens and costs of compliance with a variety of foreign laws;
- foreign taxes;
- changes in tariff rates or other trade and monetary policies; and
- changes or volatility in currency exchange rates.

If we have to qualify a new contract manufacturer or foundry for our products, we may experience delays that result in lost revenues and damaged customer relationships.

We rely on single suppliers to manufacture our PicoP display engine, our SHOWWX products and our MEMS chips in wafer form. The lead time required to establish a relationship with a new contract manufacturer or foundry is long, and it takes time to adapt a product's design to a particular manufacturer's processes. Accordingly, there is no readily available alternative source of supply for these products and components in high volumes. This could cause significant delays in shipping products if we have to change our source of supply and manufacture quickly, which may result in lost revenues and damaged customer relationships.

If we experience delays or failures in developing commercially viable products, we may have lower revenues.

We have begun sales of units incorporating the PicoP display engine. However, we must undertake additional research, development and testing before we are able to develop additional products for commercial sale. Product development delays by us or our potential product development partners, or the inability to enter into relationships

with these partners, may delay or prevent us from introducing products for commercial sale.

Our success will depend, in part, on our ability to secure significant third-party manufacturing resources.

Our success depends, in part, on our ability to provide our components and future products in commercial quantities at competitive prices. Accordingly, we will be required to obtain access, through business partners or contract manufacturers, to manufacturing capacity and processes for the commercial production of our expected future products. We cannot be certain that we will successfully obtain access to sufficient manufacturing resources. Future manufacturing limitations of our suppliers could result in a limitation on the number of products incorporating our technology that we are able to produce.

If our licensors and we are unable to obtain effective intellectual property protection for our products and technology, we may be unable to compete with other companies.

Intellectual property protection for our products is important and uncertain. If we do not obtain effective intellectual property protection for our products, processes and technology, we may be subject to increased competition. Our commercial success will depend in part on our ability and the ability of our licensors to maintain the proprietary nature of the PicoP display and other key technologies by securing valid and enforceable patents and effectively maintaining unpatented technology as trade secrets. We try to protect our proprietary technology by seeking to obtain United States and foreign patents in our name, or licenses to third-party patents, related to proprietary technology, inventions, and improvements that may be important to the development of our business. However, our patent position and the patent position of our licensors involve complex legal and factual questions. The standards that the United States Patent and Trademark Office and its foreign counterparts use to grant patents are not always applied predictably or uniformly and can change. Additionally, the scope of patents are subject to interpretation by courts and their validity can be subject to challenges and defenses, including challenges and defenses based on the existence of prior art. Consequently, we cannot be certain as to the extent to which we will be able to obtain patents for our new products and technology or the extent to which the patents that we already own or license from others protect our products and technology. Reduction in scope of protection or invalidation of our licensed or owned patents, or our inability to obtain new patents, may enable other companies to develop products that compete with ours on the basis of the same or similar technology.

We also rely on the law of trade secrets to protect unpatented know-how and technology to maintain our competitive position. We try to protect this know-how and technology by limiting access to the trade secrets to those of our employees, contractors and partners with a need to know such information and by entering into confidentiality agreements with parties that have access to it, such as our employees, consultants and business partners. Any of these parties could breach the agreements and disclose our trade secrets or confidential information, or our competitors might learn of the information in some other way. If any trade secret not protected by a patent were to be disclosed to or independently developed by a competitor, our competitive position could be materially harmed.

We could be exposed to significant product liability claims that could be time-consuming and costly, divert management attention and adversely affect our ability to obtain and maintain insurance coverage.

We may be subject to product liability claims if any of our product applications are alleged to be defective or cause harmful effects. For example, because some of our PicoP displays are designed to scan a low power beam of colored light into the user's eye, the testing, manufacture, marketing and sale of these products involve an inherent risk that product liability claims will be asserted against us. Product liability claims or other claims related to our products, regardless of their outcome, could require us to spend significant time and money in litigation, divert management time and attention, require us to pay significant damages, harm our reputation or hinder acceptance of our products. Any successful product liability claim may prevent us from obtaining adequate product liability insurance in the future on commercially desirable or reasonable terms. An inability to obtain sufficient insurance coverage at an acceptable cost or otherwise to protect against potential product liability claims could prevent or inhibit the commercialization of our products.

Our development agreements have long sales cycles, which make it difficult to plan our expenses and forecast our revenues.

Our development agreements have lengthy sales cycles that involve numerous steps including determination of a product application, exploring the technical feasibility of a proposed product, evaluating the costs of manufacturing a product and manufacturing or contracting out the manufacturing of the product. Our long sales cycle, which can last several years, makes it difficult to predict the quarter in which contract signing and revenue recognition will occur. Delays in entering into development agreements could cause significant variability in our revenues and operating results for any particular quarterly period.

Our development contracts may not lead to products that will be profitable.

Our development contracts, including without limitation those discussed in this document, are exploratory in nature and are intended to develop new types of products for new applications. These efforts may prove unsuccessful and these relationships may not result in the development of products that will be profitable.

If we lose our rights under our third-party technology licenses, our operations could be adversely affected.

Our business depends in part on technology rights licensed from third parties. We could lose our exclusivity or other rights to use the technology under our licenses if we fail to comply with the terms and performance requirements of the licenses. In addition, certain licensors may terminate a license upon our breach and have the right to consent to sublicense arrangements. If we were to lose our rights under any of these licenses, or if we were unable to obtain required consents to future sublicenses, we could lose a competitive advantage in the market, and may even lose the ability to commercialize certain products completely. Either of these results could substantially decrease our revenues.

Loss of any of our key personnel could have a negative effect on the operation of our business.

Our success depends on our executive officers and other key personnel and on the ability to attract and retain qualified new personnel. Achievement of our business objectives will require substantial additional expertise in the areas of sales and marketing, research and product development and manufacturing. Competition for qualified personnel in these fields is intense, and the inability to attract and retain additional highly skilled personnel, or the loss of key personnel, could reduce our revenues and adversely affect our business.

#### ITEM 5. Other Information

On May 9, 2012, we entered into a Securities Purchase Agreement (the "Purchase Agreement") with Shmuel Farhi and Salvatore Pacifico and Silvana Pacifico, jointly (the "Investors"). Under the terms of the Purchase Agreement, the investors have agreed to purchase at a closing (the "Closing") to be held no later than May 29, 2012, 3,346,048 shares (the "Shares") of our common stock at a price of \$1.494 per share. At the Closing, we have agreed to issue the Investors warrants (the "Warrants") to purchase a total of 1 million shares of our common stock at an exercise price of \$2.125 per share, exercisable until the third anniversary of the Closing. The aggregate purchase price payable by the Investors for the Shares and Warrants is approximately \$5 million in cash. The Closing is subject to customary closing conditions. The Shares and the Warrants would be issued in a transaction not involving any public offering pursuant to Section 4(2) of the Securities Act of 1933, as amended.

The Purchase Agreement requires us to also enter into a Registration Rights Agreement at Closing, pursuant to which we would agree to use our commercially reasonable efforts to file a registration statement (the "Registration Statement") with respect to the Shares and the shares of our common stock issuable under the Warrant as soon as practicable and in no event later than 60 days after the Closing, and to use our commercially reasonable efforts to cause the Registration Statement to become effective as soon as practicable thereafter, and in no event later than 120 days from the Closing.

Statements above relating to the consummation of the described investment are forward-looking statements that involve a number of risks and uncertainties. Factors that could cause actual results to differ materially from those projected in our forward-looking statements include our ability to satisfy the conditions to Closing in the Purchase Agreement and the risk that the Investors may not perform their obligations to purchase the Shares and Warrants. Except as expressly required by federal securities laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changes in circumstances or any other reason.



ITEM 6. Exhibits

- 31.1 Chief Executive Officer Certification Pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Chief Financial Officer Certification Pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Chief Executive Officer Certification pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Chief Financial Officer Certification pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as 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
- 101.DEF\* XBRL Taxonomy Extension Definition Linkbase
- 101.LAB\* XBRL Taxonomy Extension Label Linkbase
- 101.PRE\* XBRL Taxonomy Extension Presentation Linkbase

\* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability.

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.

MICROVISION, INC.

Date: May 10, 2012

BY: /s/ Alexander Y. Tokman

Alexander Y. Tokman

Chief Executive Officer

(Principal Executive Officer)

Date: May 10, 2012

BY: /s/ Jeff Wilson

Jeff Wilson

Chief Financial Officer

(Principal Financial Officer, Principal Accounting Officer)



## EXHIBIT INDEX

The following documents are filed herewith.

| <u>Exhibit<br/>Number</u> | <u>Description</u>  |
|---------------------------|---|
| 31.1                      | <u>Chief Executive Officer Certification Pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>   |
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