

INTEVAC INC
Form 10-Q
April 30, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended March 30, 2013

OR

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

For the transition period from to

Commission file number 0-26946

INTEVAC, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

94-3125814
(IRS Employer Identification No.)

3560 Bassett Street

Santa Clara, California 95054

(Address of principal executive office, including Zip Code)

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

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

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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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer 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 Act). Yes No

On April 30, 2013, 23,778,779 shares of the Registrant's Common Stock, \$0.001 par value, were outstanding.

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INTEVAC, INC.

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

	March 30, 2013	December 31, 2012
	(Unaudited)	
	(In thousands, except par value)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 24,842	\$ 24,261
Short-term investments	42,630	40,591
Trade and other accounts receivable, net of allowances of \$0 at both March 30, 2013 and at December 31, 2012	10,342	19,822
Inventories	25,943	26,193
Prepaid expenses and other current assets	2,111	2,120
Total current assets	105,868	112,987
Property, plant and equipment, net	12,672	13,426
Long-term investments	26,154	27,317
Intangible assets, net of amortization of \$2,743 at March 30, 2013 and \$2,887 at December 31, 2012	5,642	5,868
Deferred income taxes and other long-term assets	13,620	12,905
Total assets	\$ 163,956	\$ 172,503
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 3,308	\$ 4,479
Accrued payroll and related liabilities	4,571	4,194
Other accrued liabilities	7,783	8,489
Customer advances	1,438	2,193
Deferred income taxes	1,281	1,281
Total current liabilities	18,381	20,636
Other long-term liabilities	9,532	9,232
Stockholders' equity:		
Common stock, \$0.001 par value	24	23
Additional paid-in capital	153,688	151,996
Accumulated other comprehensive income	748	769
Accumulated deficit	(18,417)	(10,153)
Total stockholders' equity	136,043	142,635
Total liabilities and stockholders' equity	\$ 163,956	\$ 172,503

Note: Amounts as of December 31, 2012 are derived from the December 31, 2012 audited consolidated financial statements.

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See accompanying notes.

Table of Contents**INTEVAC, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

	Three months ended	
	March 30,	March 31,
	2013	2012
	(Unaudited)	
	(In thousands, except per share amounts)	
Net revenues:		
Systems and components	\$ 8,885	\$ 14,768
Technology development	4,097	2,547
Total net revenues	12,982	17,315
Cost of net revenues:		
Systems and components	6,307	8,819
Technology development	3,161	1,672
Total cost of net revenues	9,468	10,491
Gross profit	3,514	6,824
Operating expenses:		
Research and development	6,358	9,213
Selling, general and administrative	5,971	6,773
Total operating expenses	12,329	15,986
Gain (loss) on divestitures	(208)	2,207
Loss from operations	(9,023)	(6,955)
Interest income and other, net	80	372
Loss before income taxes	(8,943)	(6,583)
Benefit from income taxes	679	3,422
Net loss	\$ (8,264)	\$ (3,161)
Net loss per share:		
Basic and Diluted	\$ (0.35)	\$ (0.14)
Weighted average common shares outstanding:		
Basic and Diluted	23,663	23,218

See accompanying notes.

Table of Contents**INTEVAC, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

	Three months ended	
	March 30,	March 31,
	2013	2012
	(Unaudited)	
	(In thousands)	
Net loss	\$ (8,264)	\$ (3,161)
Other comprehensive income (loss), before tax		
Change in unrealized net loss on available-for-sale investments	(15)	130
Foreign currency translation gains (losses)	(6)	12
Other comprehensive income (loss), before tax	(21)	142
Income tax provision related to items in other comprehensive income (loss)		45
Other comprehensive income (loss), net of tax	(21)	97
Comprehensive loss	\$ (8,285)	\$ (3,064)

See accompanying notes.

Table of Contents**INTEVAC, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Three months ended	
	March 30,	March 31,
	2013	2012
	(Unaudited)	
	(In thousands)	
Operating activities		
Net loss	\$ (8,264)	\$ (3,161)
Adjustments to reconcile net loss to net cash and cash equivalents provided by (used in) operating activities:		
Depreciation and amortization	1,032	1,241
Net amortization of investment premiums and discounts	228	395
Equity-based compensation	563	1,054
Change in the fair value of acquisition-related contingent consideration	111	278
Deferred income taxes	(768)	(3,258)
Loss (gain) on divestitures	208	(2,207)
Changes in operating assets and liabilities	7,267	(196)
Total adjustments	8,641	(2,693)
Net cash and cash equivalents provided by (used in) operating activities	377	(5,854)
Investing activities		
Purchases of investments	(15,783)	(16,091)
Proceeds from sales and maturities of investments	14,664	13,405
Proceeds from sale of DeltaNu assets	500	
Proceeds from sale of mainframe technology		3,000
Purchases of leasehold improvements and equipment	(301)	(852)
Net cash and cash equivalents used in investing activities	(920)	(538)
Financing activities		
Proceeds from issuance of common stock	1,130	863
Net cash and cash equivalents provided by financing activities	1,130	863
Effect of exchange rate changes on cash and cash equivalents	(6)	12
Net increase (decrease) in cash and cash equivalents	581	(5,517)
Cash and cash equivalents at beginning of period	24,261	23,560
Cash and cash equivalents at end of period	\$ 24,842	\$ 18,043

See accompanying notes.

Table of Contents**INTEVAC, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****1. Basis of Presentation**

In the opinion of management, the unaudited interim condensed consolidated financial statements of Intevac, Inc. and its subsidiaries (Intevac or the Company) included herein have been prepared on a basis consistent with the December 31, 2012 audited consolidated financial statements and include all material adjustments, consisting of normal recurring adjustments, necessary to fairly present the information set forth therein. These unaudited interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in Intevac's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 (2012 Form 10-K). Intevac's results of operations for the three months ended March 30, 2013 are not necessarily indicative of future operating results.

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

2. Inventories

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

	March 30, 2013	December 31, 2012
	(In thousands)	
Raw materials	\$ 14,143	\$ 14,921
Work-in-progress	4,571	5,526
Finished goods	7,229	5,746
	\$ 25,943	\$ 26,193

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

3. Equity-Based Compensation

At March 30, 2013, Intevac had equity-based awards outstanding under the 2012 Equity Incentive Plan and the 2004 Equity Incentive Plan (the Plans) and the 2003 Employee Stock Purchase Plan (the ESPP). Intevac's stockholders approved all of these plans. The Plans permit the grant of incentive or non-statutory stock options, restricted stock, stock appreciation rights, restricted stock units (RSUs) also referred to as performance units) and performance shares.

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

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

The effect of recording equity-based compensation for the three-month periods ended March 30, 2013 and March 31, 2012 was as follows:

	Three Months Ended	
	March 30, 2013	March 31, 2012
	(In thousands)	
Equity-based compensation by type of award:		
Stock options	\$ 173	\$ 733
RSUs	76	6
Employee stock purchase plan	314	315
Total equity-based compensation	563	1,054
Tax effect on equity-based compensation	(5)	(279)
Net effect on net loss	\$ 558	\$ 775

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

Stock Options and ESPP

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

Option activity as of March 30, 2013 and changes during the three months ended March 30, 2013 were as follows:

	Shares	Weighted Average Exercise Price
Options outstanding at December 31, 2012	3,128,408	\$ 11.52
Options granted	14,500	\$ 4.71
Options cancelled and forfeited	(435,625)	\$ 12.82
Options exercised	(64,813)	\$ 3.91
Options outstanding at March 30, 2013	2,642,470	\$ 11.45
Vested and expected to vest at March 30, 2013	2,548,559	\$ 11.53
Options exercisable at March 30, 2013	1,926,833	\$ 12.12

Intevac issued 246,000 shares under the ESPP during the three months ended March 30, 2013.

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

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

	Three Months Ended	
	March 30, 2013	March 31, 2012
Stock Options:		
Weighted-average fair value of grants per share	\$ 1.97	\$ 4.53
Expected volatility	55.57%	65.25%
Risk free interest rate	0.52%	1.10%
Expected term of options (in years)	3.9	5.2
Dividend yield	None	None
Stock Purchase Rights:		
Weighted-average fair value of grants per share	\$ 1.60	\$ 3.49
Expected volatility	52.42%	61.77%
Risk free interest rate	0.26%	0.33%
Expected term of purchase rights (in years)	1.85	1.56
Dividend yield	None	None

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

RSUs

A summary of the RSU activity is as follows:

	Shares	Weighted Average
		Grant Date Fair Value
Non-vested RSUs at December 31, 2012	100,461	\$ 7.33
Granted	9,125	\$ 4.76
Vested	(2,500)	\$ 8.24
Cancelled and forfeited	(8,133)	\$ 7.55
Non-vested RSUs at March 30, 2013	98,953	\$ 7.05

RSUs are converted into shares of Intevac common stock upon vesting on a one-for-one basis. RSUs typically are scheduled to vest over four years. Vesting of RSUs is subject to the grantee's continued service with Intevac. The compensation expense related to these awards is determined using the fair market value of Intevac common stock on the date of the grant, and the compensation expense is recognized over the vesting period.

Table of Contents**INTEVAC, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****4. Goodwill and Purchased Intangible Assets**

Goodwill and indefinite-lived intangible assets are tested for impairment on an annual basis or more frequently upon the occurrence of circumstances that indicate that goodwill and indefinite-lived intangible assets may be impaired.

Intevac performed its annual goodwill impairment test in the fourth quarter of fiscal 2012, and, based on step one of the impairment analysis, Intevac determined that the fair values of both its Equipment and Intevac Photonics reporting units were less than their carrying value and potential impairment existed. Intevac completed the second step of the goodwill impairment analysis and determined that there would be no remaining implied value attributable to goodwill in either reporting unit and accordingly, Intevac wrote off all of the goodwill in both its Equipment and Intevac Photonics reporting units. In the second half of 2012, the Company experienced a significant decline in its stock price which resulted in the Company's market capitalization falling significantly below the recorded value of its consolidated net assets.

As of March 30, 2013, indefinite-lived intangible assets consist of in-process technology in the amount of \$4.0 million in the Equipment segment, which will be subject to amortization upon commercialization. If an in-process technology is abandoned, the acquired technology will be written-off.

Details of finite-lived intangible assets by segment as of March 30, 2013, are as follows.

	Gross Carrying Amount	March 30, 2013 Accumulated Amortization (In thousands)	Net Carrying Amount
Equipment	\$ 3,170	\$ (2,142)	\$ 1,028
Intevac Photonics	1,215	(601)	614
	\$ 4,385	\$ (2,743)	\$ 1,642

Total amortization expense of finite-lived intangibles for the three months ended March 30, 2013 was \$136,000.

As of March 30, 2013, future amortization expense is expected to be as follows.

(In thousands)	
2013	\$ 407
2014	363
2015	283
2016	281
2017	186
Thereafter	122
	\$ 1,642

5. Acquisition-Related Contingent Consideration

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In connection with the acquisition of Solar Implant Technologies, Inc. (SIT), Intevac agreed to pay up to an aggregate of \$7.0 million in cash to the selling shareholders if certain milestones were achieved over a specified period. Intevac has made payments to the selling shareholders for achievement of the first, second and third milestones. The fourth and final milestone was not achieved on the targeted date outlined in the acquisition agreement and will not be paid. There is no remaining contingent consideration obligation associated with the milestone payments at March 30, 2013.

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

In connection with the acquisition of SIT, Intevac also agreed to pay to the selling shareholders in cash a revenue earnout on Intevac's net revenue from commercial sales of certain products over a specified period up to an aggregate of \$9.0 million. Intevac estimated the fair value of this contingent consideration on March 30, 2013 based on probability-based forecasted revenues reflecting Intevac's own assumptions concerning future revenue from such products. As of March 30, 2013, Intevac has not made any payments associated with the revenue earnout obligation.

The fair value measurement of contingent consideration is based on significant inputs not observed in the market and thus represents a Level 3 measurement. Any change in fair value of the contingent consideration subsequent to the acquisition date is recognized in operating income within the statement of operations. The following table represents a reconciliation of the change in the fair value measurement of the contingent consideration liability for the three-month periods ended March 30, 2013 and March 31, 2012:

	Three months ended	
	March 30,	March 31,
	2013	2012
	(In thousands)	
Opening balance	\$ 5,151	\$ 8,715
Changes in fair value	111	278
Closing balance	\$ 5,262	\$ 8,993

The following table displays the balance sheet classification of the contingent consideration liability account at March 30, 2013 and at December 31, 2012:

	March 30,	December 31,
	2013	2012
	(In thousands)	
Other accrued liabilities	\$ 147	\$ 265
Other long-term liabilities	5,115	4,886
Total acquisition-related contingent consideration	\$ 5,262	\$ 5,151

The following table represents the quantitative range of the significant unobservable inputs used in the calculation of fair value of the contingent consideration liability as of March 30, 2013. Significant increases or decreases in any of these inputs in isolation would result in a significantly lower (higher) fair value measurement.

Quantitative Information about Level 3 Fair Value Measurements at March 30, 2013			
	Fair Value	Valuation Technique	Unobservable Input
			Range (Weighted Average)
			(In thousands, except for percentages)
Revenue Earnout	\$ 5,262	Discounted cash flow	Weighted average cost of capital Probability weighting of achieving revenue forecasts
			14.8% 2.0% - 43.0% (29.5%)

6. Divestitures

Sale of DeltaNu

On March 29, 2013, the Company sold certain assets, including existing tangible and intangible assets, which comprised its Raman spectroscopy instruments product line, also known as DeltaNu, for consideration not to exceed

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

\$1.5 million. Under the terms of the agreement, the acquirer also assumed certain liabilities related to the purchased assets. Payment terms included \$500,000 which was paid on the closing date, with the remaining balance to be paid in the form of an earnout of 5% of the acquirer's Raman spectroscopy instrument sales for 5 years following the closing date which will be due and payable on or before each anniversary of the closing date or a minimum earnout payment of \$100,000 annually, whichever is higher. The maximum earnout payments during the payment period shall not exceed \$1.0 million.

As the earnout is collected over an extended period of time and in management's judgment the degree of collectibility is uncertain, Intevac did not recognize the minimum earnout payments upon closing, but instead will record income in the period when the minimum earnout payments can be reasonably estimated for that period and payment is assured.

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

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

Sale of Mainframe Technology

On January 6, 2012, the Company sold certain assets including intellectual property and residual assets which comprised its semiconductor mainframe technology to Brooks Automation Inc.

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

Cash proceeds	\$ 3,000
Assets sold:	
Inventories	589
Property, plant and equipment	178

Transaction and other costs	26
Gain on sale	\$ 2,207

7. Warranty

Intevac provides for the estimated cost of warranty when revenue is recognized. Intevac's warranty is per contract terms, and for systems sold directly the warranty typically ranges between 12 and 24 months from customer acceptance. For systems sold through a distributor, Intevac offers a 3 month warranty. The remainder of any warranty period is the responsibility of the distributor. During this warranty period any defective non-consumable

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

parts are replaced and installed at no charge to the customer. The warranty period on consumable parts is limited to their reasonable usable lives. Intevac uses estimated repair or replacement costs along with its historical warranty experience to determine its warranty obligation. Intevac generally provides a twelve month warranty on its Intevac Photonics products. The provision for the estimated future costs of warranty is based upon historical cost and product performance experience. Intevac exercises judgment in determining the underlying estimates.

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

The following table displays the activity in the warranty provision account for the three-month periods ended March 30, 2013 and March 31, 2012:

	Three months ended	
	March 30,	March 31,
	2013	2012
	(In thousands)	
Opening balance	\$ 2,349	\$ 2,724
Expenditures incurred under warranties	(253)	(781)
Accruals for product warranties issued during the reporting period	208	428
Adjustments to previously existing warranty accruals	(79)	123
Closing balance	\$ 2,225	\$ 2,494

The following table displays the balance sheet classification of the warranty provision account at March 30, 2013 and at December 31, 2012:

	March 30,	December 31,
	2013	2012
	(In thousands)	
Other accrued liabilities	\$ 2,135	\$ 2,259
Other long-term liabilities	90	90
Total warranty provision	\$ 2,225	\$ 2,349

8. Guarantees***Officer and Director Indemnifications***

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

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exposure and enables Intevac to recover a portion of any future amounts paid. As a result of Intevac's insurance policy coverage, Intevac believes the estimated fair value of these indemnification obligations is not material.

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

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

9. Cash, Cash Equivalents and Investments

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

	Amortized Cost	March 30, 2013 Unrealized Holding Gains Unrealized Holding Losses (in thousands)		Fair Value
Cash and cash equivalents:				
Cash	\$ 10,758	\$	\$	\$ 10,758
Money market funds	14,084			14,084
Total cash and cash equivalents	\$ 24,842	\$	\$	\$ 24,842
Short-term investments:				
Commercial paper	\$ 3,497	\$ 1	\$	\$ 3,498
Corporate bonds and medium-term notes	18,212	30	9	18,233
Municipal bonds	1,202			1,202
U.S. treasury and agency securities	19,476	26		19,502
Variable rate demand notes (VRDNs)	195			195
Total short-term investments	\$ 42,582	\$ 57	\$ 9	\$ 42,630
Long-term investments:				
Corporate bonds and medium-term notes	\$ 17,132	\$ 10	\$ 8	\$ 17,134
Municipal bonds	1,000	5		1,005
U.S. treasury and agency securities	8,010	5		8,015
Total long-term investments	\$ 26,142	\$ 20	\$ 8	\$ 26,154