

AEHR TEST SYSTEMS
Form 10-Q
October 14, 2015

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

FORM 10-Q

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

For the quarterly period ended August 31, 2015

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: 000-22893

AEHR TEST SYSTEMS
(Exact name of Registrant as specified in its charter)

California
(State or other jurisdiction of
incorporation or organization)

94-2424084
(I.R.S. Employer Identification No.)

400 Kato Terrace
Fremont, CA
(Address of principal
executive offices)

94539
(Zip Code)

(510) 623-9400
(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 as the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant 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

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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.

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 Exchange Act).

Yes No

Number of shares of the registrant’s common stock, \$0.01 par value, outstanding as of September 30, 2015 was 12,991,278.

AEHR TEST SYSTEMS

FORM 10-Q

FOR THE QUARTER ENDED AUGUST 31, 2015

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PART I. FINANCIAL INFORMATION

Item 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

AEHR TEST SYSTEMS
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

(unaudited)

	August 31, 2015	May 31, 2015 (1)
ASSETS		
Current assets:		
Cash and cash equivalents	\$3,653	\$5,527
Accounts receivable, net	2,628	1,383
Inventories	7,258	7,123
Prepaid expenses and other	465	262
Total current assets	14,004	14,295
Property and equipment, net	465	478
Other assets	94	95
Total assets	\$14,563	\$14,868
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$1,848	\$724
Accrued expenses	1,557	1,045
Customer deposits and deferred revenue, short-term	1,819	4,750
Total current liabilities	5,224	6,519
Long-term debt, net of debt issuance costs	3,828	3,791
Income taxes payable	--	8
Deferred revenue, long-term	127	--
Total liabilities	9,179	10,318
Aehr Test Systems shareholders' equity:		
Common stock, \$0.01 par value: Authorized: 75,000; Issued and outstanding: 12,987 shares and 12,857 shares at August 31, 2015 and May 31, 2015, respectively	130	129
Additional paid-in capital	57,068	56,547
Accumulated other comprehensive income	2,249	2,231
Accumulated deficit	(54,045)	(54,339)
Total Aehr Test Systems shareholders' equity	5,402	4,568
Noncontrolling interest	(18)	(18)

Total shareholders' equity	5,384	4,550
Total liabilities and shareholders' equity	\$14,563	\$14,868

(1) The condensed consolidated balance sheet at May 31, 2015 has been derived from the audited consolidated financial statements at that date.

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

AEHR TEST SYSTEMS
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended August 31,	
	2015	2014
Net sales	\$6,633	\$3,558
Cost of sales	3,250	1,948
Gross profit	3,383	1,610
Operating expenses:		
Selling, general and administrative	1,845	1,624
Research and development	1,062	959
Total operating expenses	2,907	2,583
Income (loss) from operations	476	(973)
Interest expense	(135)	(14)
Other (expense) income, net	(24)	31
Income (loss) before income tax (expense) benefit	317	(956)
Income tax (expense) benefit	(23)	49
Net income (loss)	294	(907)
Less: Net income attributable to the noncontrolling interest	--	--
Net income (loss) attributable to Aehr Test Systems common shareholders	\$294	\$(907)
Net income (loss) per share		
Basic and Diluted	\$0.02	\$(0.08)
Shares used in per share calculations:		
Basic	12,963	11,391
Diluted	13,814	11,391

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

AEHR TEST SYSTEMS
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
 (in thousands, unaudited)

	Three Months Ended August 31,	
	2015	2014
Net income (loss)	\$294	\$(907)
Other comprehensive income (loss), net of tax:		
Net change in cumulative translation adjustments	18	(36)
Total comprehensive income (loss)	312	(943)
Less: Comprehensive income attributable to the noncontrolling interest	--	1
Comprehensive income (loss), attributable to Aehr Test Systems	\$312	\$(944)

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

AEHR TEST SYSTEMS
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (in thousands)
 (unaudited)

	Three Months Ended August 31,	
	2015	2014
Cash flows from operating activities:		
Net income (loss)	\$294	\$(907)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Stock-based compensation expense	319	197
Provision for (recovery of) doubtful accounts	19	(20)
Amortization of debt issuance costs	37	--
Depreciation and amortization	37	29
Changes in operating assets and liabilities:		
Accounts receivable	(1,257)	1,272
Inventories	(156)	(156)
Prepaid expenses and other	(201)	(46)
Accounts payable	1,113	(270)
Accrued expenses	505	38
Customer deposits and deferred revenue	(2,804)	(294)
Income taxes payable	(2)	(53)
Deferred rent	--	(8)
Net cash used in operating activities	(2,096)	(218)
Cash flows from investing activities:		
Purchases of property and equipment	(21)	(21)
Net cash used in investing activities	(21)	(21)
Cash flows from financing activities:		
Line of credit borrowings, net	--	223
Proceeds from issuance of common stock under employee plans	223	315
Net cash provided by financing activities	223	538
Effect of exchange rates on cash	20	(33)
Net (decrease) increase in cash and cash equivalents	(1,874)	266
Cash and cash equivalents, beginning of period	5,527	1,809
Cash and cash equivalents, end of period	\$3,653	\$2,075
Supplemental disclosure of non-cash flow information:		
Net change in capitalized share-based compensation	\$(20)	\$27

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

AEHR TEST SYSTEMS
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying financial information has been prepared by Aehr Test Systems, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission, or SEC. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States (GAAP) have been condensed or omitted pursuant to such rules and regulations.

In the opinion of management, the unaudited condensed consolidated financial statements for the interim periods presented have been prepared on a basis consistent with the May 31, 2015 audited consolidated financial statements and reflect all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the condensed consolidated financial position and results of operations as of and for such periods indicated. These unaudited condensed consolidated financial statements and notes thereto should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended May 31, 2015. Results for the interim periods presented herein are not necessarily indicative of results which may be reported for any other interim period or for the entire fiscal year.

PRINCIPLES OF CONSOLIDATION. The condensed consolidated financial statements include the accounts of Aehr Test Systems and its subsidiaries (collectively, the "Company," "we," "us," and "our"). All significant intercompany balances have been eliminated in consolidation. For the majority owned subsidiary, we reflected the noncontrolling interest of the portion we do not own on our Consolidated Balance Sheets in Shareholders' Equity and in the Consolidated Statements of Operations.

ACCOUNTING ESTIMATES. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are used to account for revenue adjustments, the allowance for doubtful accounts, inventory reserves, income taxes, stock-based compensation expenses, and product warranties, among others. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ materially from those estimates.

SIGNIFICANT ACCOUNTING POLICIES. The Company's significant accounting policies are disclosed in the Company's Annual Report on Form 10-K for the year ended May 31, 2015. There have been no changes in our significant accounting policies during the three months ended August 31, 2015.

2. STOCK-BASED COMPENSATION

Stock-based compensation expense consists of expenses for stock options and employee stock purchase plan, or ESPP, shares. Stock-based compensation cost is measured at each grant date, based on the fair value of the award using the Black-Scholes option valuation model, and is recognized as expense over the employee's requisite service period. This model was developed for use in estimating the value of publicly traded options that have no vesting restrictions and are fully transferable. The Company's employee stock options have characteristics significantly different from those of publicly traded options. All of the Company's stock-based compensation is accounted for as an equity instrument. See Notes 12 and 13 in the Company's Annual Report on Form

10-K for fiscal 2015 filed on August 28, 2015 for further information regarding the stock option plan and the ESPP.

The following table summarizes compensation costs related to the Company's stock-based compensation for the three months ended August 31, 2015 and 2014 (in thousands):

	Three Months Ended August 31,	
	2015	2014
Stock-based compensation in the form of employee stock options and ESPP shares, included in:		
Cost of sales	\$22	\$14
Selling, general and administrative	238	148
Research and development	59	35
Total stock-based compensation	\$319	\$197

As of August 31, 2015, there were no stock-based compensation costs capitalized as part of inventory. Stock-based compensation costs of \$51,000 were capitalized as part of inventory at August 31, 2014.

During the three months ended August 31, 2015 and 2014, the Company recorded stock-based compensation related to stock options of \$286,000 and \$162,000, respectively.

As of August 31, 2015, the total compensation cost related to unvested stock-based awards under the Company's 1996 Stock Option Plan and 2006 Equity Incentive Plan, but not yet recognized, was approximately \$1,610,000, which is net of estimated forfeitures of \$4,000. This cost will be amortized on a straight-line basis over a weighted average period of approximately 2.7 years.

During the three months ended August 31, 2015 and 2014, the Company recorded stock-based compensation related to the ESPP of \$33,000 and \$35,000, respectively.

As of August 31, 2015, the total compensation cost related to purchase rights under the ESPP but not yet recognized was approximately \$101,000. This cost will be amortized on a straight-line basis over a weighted average period of approximately 1.2 years.

Valuation Assumptions

Valuation and Amortization Method. The Company estimates the fair value of stock options granted using the Black-Scholes option valuation model and a single option award approach. The fair value under the single option approach is amortized on a straight-line basis over the requisite service periods of the awards, which is generally the vesting period.

Expected Term. The Company's expected term represents the period that the Company's stock-based awards are expected to be outstanding and was determined based on historical experience, giving consideration to the contractual terms of the stock-based awards, vesting schedules and expectations of future employee behavior as evidenced by changes to the terms of its stock-based awards.

Expected Volatility. Volatility is a measure of the amounts by which a financial variable such as stock price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. The Company uses the historical volatility for the past four or five years, which matches the expected term of most of the option grants, to estimate expected volatility. Volatility for each of the ESPP's four time periods of six months, twelve months, eighteen

months, and twenty-four months is calculated separately and included in the overall stock-based compensation cost recorded.

Dividends. The Company has never paid any cash dividends on its common stock and does not anticipate paying any cash dividends in the foreseeable future. Consequently, the Company uses an expected dividend yield of zero in the Black-Scholes option valuation model.

Risk-Free Interest Rate. The Company bases the risk-free interest rate used in the Black-Scholes option valuation model on the implied yield in effect at the time of option grant on U.S. Treasury zero-coupon issues with a remaining term equivalent to the expected term of the stock awards including the ESPP.

Estimated Forfeitures. When estimating forfeitures, the Company considers voluntary termination behavior as well as analysis of actual option forfeitures.

Fair Value. The fair value of the Company's stock options granted to employees for the three months ended August 31, 2014 were estimated using the following weighted average assumptions in the Black-Scholes option valuation model:

	August 31, 2014	
Option plan shares		
Expected term (in years)	4	
Volatility	0.91	
Expected dividend	\$0.00	
Risk-free interest rate	1.28	%
Estimated forfeiture rate	0.25	%
Weighted average grant date fair value	\$1.71	

There were no stock options granted to employees for the three months ended August 31, 2015.

During the three months ended August 31, 2015, Restricted Stock Units (RSUs) were granted for 35,000 shares. The market value on the date of the grant was \$2.16 per share. The RSUs are performance based and immediately vest upon attainment of goals established.

There were no ESPP purchase rights granted to employees for the three months ended August 31, 2015 and 2014.

The following table summarizes the stock option transactions during the three months ended August 31, 2015 (in thousands, except per share data):

	Available Shares	Outstanding Options		
		Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value
Balances, May 31, 2015	845	3,686	\$ 1.66	\$2,946
Options granted	--	--	--	
Options terminated	122	(122)	\$2.04	
Options exercised	--	(130)	\$1.72	
Balances, August 31, 2015	967	3,434	\$ 1.63	\$2,587

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Options fully vested and expected to vest at August 31, 2015	3,366	\$1.63	\$2,535
Options exercisable at August 31, 2015	2,174	\$1.41	\$2,062

The options outstanding and exercisable at August 31, 2015 were in the following exercise price ranges (in thousands, except per share data):

Range of Exercise Prices	Number Outstanding Shares	Options Outstanding at August 31, 2015		Number Exercisable Shares	Options Exercisable at August 31, 2015		Aggregate Intrinsic Value
		Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price		Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	
\$0.59-\$0.97	670	3.60	\$ 0.70	627	3.62	\$ 0.71	
\$1.09-\$1.40	1,257	3.75	\$ 1.28	921	3.47	\$ 1.28	
\$1.73-\$2.06	267	5.43	\$ 1.88	216	5.49	\$ 1.90	
\$2.10-\$2.71	1,240	6.12	\$ 2.45	410	5.85	\$ 2.53	
\$0.59-\$2.71	3,434	4.71	\$ 1.63	2,174	4.16	\$ 1.41	\$2,062

The total intrinsic value of options exercised during the three months ended August 31, 2015 was \$60,000. The total intrinsic value of options exercised during the three months ended August 31, 2014 was \$407,000. The weighted average remaining contractual life of the options exercisable and expected to be exercisable at August 31, 2015 was 4.7 years.

3. EARNINGS PER SHARE

Basic earnings per share is determined using the weighted average number of common shares outstanding during the period. Diluted earnings per share is determined using the weighted average number of common shares and potential common shares (representing the dilutive effect of stock options, and employee stock purchase plan shares) outstanding during the period using the treasury stock method.

The following table presents the computation of basic and diluted net loss per share attributable to AeHR Test Systems common shareholders (in thousands, except per share data):

	Three Months Ended August 31,	
	2015	2014
Numerator: Net income (loss)	\$294	\$(907)
Denominator for basic net income (loss) per share:		
Weighted-average shares outstanding	12,963	11,391
Shares used in basic net income (loss) per share calculation	12,963	11,391
Effect of dilutive securities	851	--
Denominator for diluted net income (loss) per share	13,814	11,391
Basic net income (loss) per share	\$0.02	\$(0.08)
Diluted net income (loss) per share	\$0.02	\$(0.08)

For the purpose of computing diluted earnings per share, weighted average potential common shares do not include stock options with an exercise price greater than the average fair value of the Company's common stock for the period, as the effect would be anti-dilutive. Stock options to purchase 1,371,000 shares of common stock and ESPP rights to purchase 175,000 ESPP shares were outstanding for the three months ending August 31, 2015, but were not included

in the computation of diluted net loss per share, because the inclusion

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of such shares would be anti-dilutive. Stock options to purchase 3,323,000 shares of common stock and ESPP rights to purchase 131,000 ESPP shares were outstanding on August 31, 2014, but were not included in the computation of diluted net loss per share, because the inclusion of such shares would be anti-dilutive.

4. FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company's financial instruments are measured at fair value consistent with authoritative guidance. This authoritative guidance defines fair value, establishes a framework for using fair value to measure assets and liabilities, and disclosures required related to fair value measurements.

The guidance establishes a fair value hierarchy based on inputs to valuation techniques that are used to measure fair value that are either observable or unobservable. Observable inputs reflect assumptions market participants would use in pricing an asset or liability based on market data obtained from independent sources while unobservable inputs reflect a reporting entity's pricing based upon their own market assumptions. The fair value hierarchy consists of the following three levels:

Level 1 - instrument valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets.

Level 2 - instrument valuations are obtained from readily-available pricing sources for comparable instruments.

Level 3 - instrument valuations are obtained without observable market values and require a high level of judgment to determine the fair value.

The following table summarizes the Company's financial assets and liabilities measured at fair value on a recurring basis as of August 31, 2015 (in thousands):

Balance as of August 31, 2015	Level 1	Level 2
----------------------------------	---------	---------