

VICOR CORP
Form 10-Q
July 31, 2017
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2017

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

For the transition period from _____

Commission File Number 0-18277

VICOR CORPORATION

(Exact name of registrant as specified in its charter)

Delaware **04-2742817**
(State of Incorporation) **(I.R.S. Employer Identification No.)**
25 Frontage Road, Andover, Massachusetts 01810

(Address of Principal Executive Office)

(978) 470-2900

(Registrant's telephone number)

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

Indicate by check mark whether the registrant 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, a smaller reporting company, or an emerging growth company. See the definitions of large accelerated filer, accelerated filer, smaller reporting company, and emerging growth company in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares outstanding of each of the issuer's classes of Common Stock as of **July 25, 2017** was:

| | |
|---------------------------------------|------------|
| Common Stock, \$.01 par value | 27,495,033 |
| Class B Common Stock, \$.01 par value | 11,758,218 |

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Part I Financial Information

Item 1 Financial Statements

Condensed Consolidated Balance Sheets

(In thousands)

(Unaudited)

| | June 30, 2017 | December 31, 2016 |
|--|-------------------|-------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 51,425 | \$ 56,170 |
| Accounts receivable, less allowance of \$161 in 2017 and \$153 in 2016 | 34,092 | 25,216 |
| Inventories, net | 30,514 | 27,136 |
| Other current assets | 3,867 | 3,250 |
| Total current assets | 119,898 | 111,772 |
| Long-term deferred tax assets, net | 21 | 38 |
| Long-term investments, net | 2,565 | 2,508 |
| Property, plant and equipment, net | 38,927 | 37,574 |
| Other assets | 2,204 | 2,175 |
| Total assets | \$ 163,615 | \$ 154,067 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 10,542 | \$ 7,588 |
| Accrued compensation and benefits | 9,925 | 8,965 |
| Accrued expenses | 2,475 | 2,179 |
| Income taxes payable | 86 | 92 |
| Deferred revenue | 7,738 | 3,403 |
| Total current liabilities | 30,766 | 22,227 |
| Long-term deferred revenue | 339 | 374 |
| Contingent consideration obligations | 142 | 253 |
| Long-term income taxes payable | 189 | 196 |
| Other long-term liabilities | 87 | |
| Total liabilities | 31,523 | 23,050 |
| Commitments and contingencies (Note 9) | | |
| Equity: | | |
| Vicor Corporation stockholders' equity: | | |

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| | | |
|--|------------|------------|
| Class B Common Stock | 118 | 118 |
| Common Stock | 399 | 397 |
| Additional paid-in capital | 178,661 | 176,344 |
| Retained earnings | 92,005 | 93,438 |
| Accumulated other comprehensive loss | (414) | (561) |
| Treasury stock, at cost | (138,927) | (138,927) |
| Total Vicor Corporation stockholders' equity | 131,842 | 130,809 |
| Noncontrolling interest | 250 | 208 |
| Total equity | 132,092 | 131,017 |
| Total liabilities and equity | \$ 163,615 | \$ 154,067 |

See accompanying notes.

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VICOR CORPORATION

Condensed Consolidated Statements of Operations

(In thousands, except per share amounts)

(Unaudited)

| | Three Months | | Six Months Ended | |
|---|-------------------|-----------|------------------|------------|
| | Ended June 30, | | June 30, | |
| | 2017 | 2016 | 2017 | 2016 |
| Net revenues | \$ 57,709 | \$ 52,941 | \$ 112,171 | \$ 98,968 |
| Cost of revenues | 31,779 | 28,470 | 62,589 | 55,181 |
| Gross margin | 25,930 | 24,471 | 49,582 | 43,787 |
| Operating expenses: | | | | |
| Selling, general and administrative | 14,536 | 14,315 | 28,559 | 28,331 |
| Research and development | 11,932 | 10,757 | 22,939 | 21,486 |
| Total operating expenses | 26,468 | 25,072 | 51,498 | 49,817 |
| Loss from operations | (538) | (601) | (1,916) | (6,030) |
| Other income (expense), net: | | | | |
| Total unrealized gains on available-for-sale securities, net | 39 | 26 | 57 | 53 |
| Portion of gains recognized in other comprehensive income (loss) | (36) | (23) | (51) | (46) |
| Net credit gains recognized in earnings | 3 | 3 | 6 | 7 |
| Other income (expense), net | 357 | 61 | 679 | 132 |
| Total other income (expense), net | 360 | 64 | 685 | 139 |
| Loss before income taxes | (178) | (537) | (1,231) | (5,891) |
| Less: Provision for income taxes | 267 | 13 | 168 | 35 |
| Consolidated net loss | (445) | (550) | (1,399) | (5,926) |
| Less: Net income (loss) attributable to noncontrolling interest | 14 | (6) | 34 | (31) |
| Net loss attributable to Vicor Corporation | \$ (459) | \$ (544) | \$ (1,433) | \$ (5,895) |
| Net loss per common share attributable to Vicor Corporation: | | | | |
| Basic | \$ (0.01) | \$ (0.01) | \$ (0.04) | \$ (0.15) |
| Diluted | \$ (0.01) | \$ (0.01) | \$ (0.04) | \$ (0.15) |
| Shares used to compute net loss per common share attributable to Vicor Corporation: | | | | |
| Basic | 39,172 | 38,801 | 39,121 | 38,798 |

| | | | | |
|---------|--------|--------|--------|--------|
| Diluted | 39,172 | 38,801 | 39,121 | 38,798 |
|---------|--------|--------|--------|--------|

See accompanying notes.

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VICOR CORPORATION

Condensed Consolidated Statements of Comprehensive Income (Loss)

(In thousands)

(Unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|----------|------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Consolidated net loss | \$ (445) | \$ (550) | \$ (1,399) | \$ (5,926) |
| Foreign currency translation (losses) gains, net of tax (1) | (40) | 244 | 104 | 417 |
| Unrealized gains on available-for-sale securities, net of tax (1) | 36 | 23 | 51 | 46 |
| Other comprehensive (loss) income | (4) | 267 | 155 | 463 |
| Consolidated comprehensive loss | (449) | (283) | (1,244) | (5,463) |
| Less: Comprehensive income attributable to noncontrolling interest | 11 | 13 | 42 | 1 |
| Comprehensive loss attributable to Vicor Corporation | \$ (460) | \$ (296) | \$ (1,286) | \$ (5,464) |

- (1) The deferred tax assets associated with cumulative foreign currency translation gains and cumulative unrealized gains on available for sale securities are completely offset by a tax valuation allowance as of June 30, 2017 and 2016. Therefore, there is no income tax benefit (provision) recognized for the three and six months ended June 30, 2017 and 2016.

See accompanying notes.

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VICOR CORPORATION

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

| | Six Months Ended June 30, | |
|--|------------------------------|------------------|
| | 2017 | 2016 |
| Operating activities: | | |
| Consolidated net loss | \$ (1,399) | \$ (5,926) |
| Adjustments to reconcile consolidated net loss to net cash used for operating activities: | | |
| Depreciation and amortization | 4,346 | 4,311 |
| Stock-based compensation expense, net | 541 | 669 |
| Increase in other assets | | (505) |
| Increase in other long-term liabilities | 87 | |
| Decrease in long-term deferred revenue | (35) | (58) |
| (Gain) loss on disposal of equipment | (23) | 4 |
| Deferred income taxes | 17 | (51) |
| Provision (benefit) for doubtful accounts | 8 | (23) |
| Decrease in long-term income taxes payable | (7) | (12) |
| Credit gain on available-for-sale securities | (6) | (7) |
| Change in current assets and liabilities, net | (4,232) | (2,407) |
| Net cash used for operating activities | (703) | (4,005) |
| Investing activities: | | |
| Additions to property, plant and equipment | (5,631) | (4,646) |
| Proceeds from sale of equipment | 23 | 2 |
| (Increase) decrease in other assets | (80) | 57 |
| Net cash used for investing activities | (5,688) | (4,587) |
| Financing activities: | | |
| Proceeds from issuance of Common Stock | 1,769 | 129 |
| Payment of contingent consideration obligations | (111) | (25) |
| Acquisition of noncontrolling interest | | (372) |
| Net cash provided by (used for) financing activities | 1,658 | (268) |
| Effect of foreign exchange rates on cash | (12) | 33 |
| Net decrease in cash and cash equivalents | (4,745) | (8,827) |
| Cash and cash equivalents at beginning of period | 56,170 | 62,980 |
| Cash and cash equivalents at end of period | \$ 51,425 | \$ 54,153 |

See accompanying notes.

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VICOR CORPORATION

Notes to Condensed Consolidated Financial Statements

June 30, 2017

(unaudited)

1. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements of Vicor Corporation and its consolidated subsidiaries (collectively, the Company) have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, these interim financial statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for any other interim period or the year ending December 31, 2017. The balance sheet at December 31, 2016 presented herein has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2016 filed by the Company with the Securities and Exchange Commission on March 7, 2017.

2. Long-Term Investments

As of June 30, 2017 and December 31, 2016, the Company held one auction rate security with a par value of \$3,000,000, purchased through and held in custody by a broker-dealer affiliate of Bank of America, N.A., that has experienced failed auctions (the Failed Auction Security) since February 2008. The Failed Auction Security held by the Company is Aaa/AA+ rated by major credit rating agencies, is collateralized by student loans, and is guaranteed by the U.S. Department of Education under the Federal Family Education Loan Program. Management is not aware of any reason to believe the issuer of the Failed Auction Security is presently at risk of default. Through June 30, 2017, the Company has continued to receive interest payments on the Failed Auction Security in accordance with the terms of its indenture. Management believes the Company ultimately should be able to liquidate the Failed Auction Security without significant loss primarily due to the overall quality of the issue held and the collateral securing the substantial majority of the underlying obligation. However, current conditions in the auction rate securities market have led management to conclude the recovery period for the Failed Auction Security exceeds 12 months. As a result, the Company continued to classify the Failed Auction Security as long-term as of June 30, 2017.

The following is a summary of available-for-sale securities (in thousands):

| | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|-------------------------|----------|------------------------------|-------------------------------|----------------------------|
| June 30, 2017 | | | | |
| Failed Auction Security | \$ 3,000 | \$ | \$ 435 | \$ 2,565 |

| December 31, 2016 | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|-------------------------|----------|------------------------------|-------------------------------|----------------------------|
| Failed Auction Security | \$ 3,000 | \$ | \$ 492 | \$ 2,508 |

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June 30, 2017

(unaudited)

As of June 30, 2017, the Failed Auction Security had been in an unrealized loss position for greater than 12 months.

Based on the fair value measurements described in Note 3, the fair value of the Failed Auction Security on June 30, 2017, with a par value of \$3,000,000, was estimated by the Company to be approximately \$2,565,000. The gross unrealized loss of \$435,000 on the Failed Auction Security consists of two types of estimated loss: an aggregate credit loss of \$53,000 and an aggregate temporary impairment of \$382,000. In determining the amount of credit loss, the Company compared the present value of cash flows expected to be collected to the amortized cost basis of the security, considering credit default risk probabilities and changes in credit ratings as significant inputs, among other factors (See Note 3).

The following table represents a rollforward of the activity related to the credit loss recognized in earnings on the Failed Auction Security for the six months ended June 30 (in thousands):

| | 2017 | 2016 |
|--|-------|-------|
| Balance at the beginning of the period | \$ 59 | \$ 72 |
| Reductions in the amount related to credit gain for which other-than- temporary impairment was not previously recognized | (6) | (7) |
| Balance at the end of the period | \$ 53 | \$ 65 |

At this time, the Company has no intent to sell the impaired Failed Auction Security and does not believe it is more likely than not the Company will be required to sell this security. If current market conditions deteriorate further, the Company may be required to record additional unrealized losses. If the credit rating of the security deteriorates, the Company may be required to adjust the carrying value of the investment through impairment charges recorded in the Condensed Consolidated Statements of Operations, and any such impairment adjustments may be material.

Based on the Company's ability to access cash and cash equivalents and its expected operating cash flows, management does not anticipate the current lack of liquidity associated with the Failed Auction Security held will affect the Company's ability to execute its current operating plan.

3. Fair Value Measurements

The Company accounts for certain financial assets at fair value, defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions market participants would use in pricing

an asset or liability. A three-level hierarchy is used to show the extent and level of judgment used to estimate fair value measurements.

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June 30, 2017

(unaudited)

Assets and liabilities measured at fair value on a recurring basis included the following as of June 30, 2017 (in thousands):

| | Quoted Prices in Active Markets (Level 1) | Using Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value as of June 30, 2017 |
|--------------------------------------|--|---|--|--|
| Cash equivalents: | | | | |
| Money market funds | \$ 9,614 | \$ | \$ | \$ 9,614 |
| Long-term investments: | | | | |
| Failed Auction Security | | | 2,565 | 2,565 |
| Liabilities: | | | | |
| Contingent consideration obligations | | | (142) | (142) |

Assets and liabilities measured at fair value on a recurring basis included the following as of December 31, 2016 (in thousands):

| | Quoted Prices in Active Markets (Level 1) | Using Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value as of December 31, 2016 |
|--------------------------------------|--|---|--|--|
| Cash equivalents: | | | | |
| Money market funds | \$ 10,114 | \$ | \$ | \$ 10,114 |
| Long-term investments: | | | | |
| Failed Auction Security | | | 2,508 | 2,508 |
| Liabilities: | | | | |
| Contingent consideration obligations | | | (253) | (253) |

As of June 30, 2017, there was insufficient observable auction rate security market information available to determine the fair value of the Failed Auction Security using Level 1 or Level 2 inputs. As such, the Company's investment in the

Failed Auction Security was deemed to require valuation using Level 3 inputs. Management, after consulting with advisors, valued the Failed Auction Security using analyses and pricing models similar to those used by market participants (i.e., buyers, sellers, and the broker-dealers responsible for execution of the Dutch auction pricing mechanism by which each issue's interest rate was set). Management utilized a probability weighted discounted cash flow (DCF) model to determine the estimated fair value of this security as of June 30, 2017. The major assumptions used in preparing the DCF model included: estimates for the amount and timing of future interest and principal payments based on default probability assumptions used to measure the credit loss of 2.0%; the rate of return required by investors to own this type of security in the current environment, which management estimates to be 5.0% above the risk free rate of return; and an estimated timeframe of three to five years for successful auctions for this type of security to occur. In making these assumptions, management considered relevant factors including: the formula applicable to the security defining the interest rate paid to investors in the event of a failed auction (the Penalty Rate); forward projections of the interest rate benchmarks specified in such formulas; the likely timing of principal repayments; the probability of full repayment considering the guarantees by the U.S. Department of Education of the underlying student loans, guarantees by other third parties, and additional credit enhancements provided through other means; and publicly available pricing data for recently issued student loan asset-backed securities not subject to auctions. In developing its estimate of the rate of return required by investors to own

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Notes to Condensed Consolidated Financial Statements

June 30, 2017

(unaudited)

the security, management compared the Penalty Rate of the Failed Auction Security with yields of actively traded long-term bonds with similar characteristics and, reflecting the limited liquidity for auction rate securities and the discounts to par value seen in recent tender offers by issuers and arm's length market transactions between informed buyers and sellers, estimated the implied yield (i.e., the discount to par value) necessary to complete a sale of the Failed Auction Security. Management has calculated an increase or decrease in the liquidity risk premium of 5.0% referenced above of 1.0% (i.e., 100 basis points) as used in the model, would decrease or increase, respectively, the fair value of the Failed Auction Security by approximately \$100,000.

The significant unobservable inputs used in the fair value measurement of the Failed Auction Security are the cumulative probability of earning the maximum rate until maturity, the cumulative probability of principal return prior to maturity, the cumulative probability of default, the liquidity risk premium, and the recovery rate in default. Significant increases (decreases) in any of those inputs in isolation would result in changes in fair value measurement. Significant increases (decreases) in the cumulative probability of earning the maximum rate until maturity, the cumulative probability of principal return prior to maturity, and the recovery rate in default would result in a higher (lower) fair value measurement, while increases (decreases) in the cumulative probability of default and the liquidity risk premium would result in a lower (higher) fair value measurement.

Generally, the interrelationships are such that a change in the assumption used for the cumulative probability of principal return prior to maturity is accompanied by a directionally similar change in the assumption used for the cumulative probability of earning the maximum rate until maturity and a directionally opposite change in the assumptions used for the cumulative probability of default and the liquidity risk premium. The recovery rate in default is somewhat independent and based upon the security's specific underlying assets and published recovery rate indices.

Quantitative information about Level 3 fair value measurements as of June 30, 2017 is as follows (dollars in thousands):

| | Fair Value | Valuation Technique | Unobservable Input | Weighted Average |
|----------------------------|------------|-------------------------|--|---------------------|
| Failed Auction Security | \$ 2,565 | Discounted cash flow | Cumulative probability of earning the maximum rate until maturity | 0.04% |
| | | | Cumulative probability of principal return prior to maturity | 94.37% |
| | | | Cumulative probability of default | 5.58% |
| | | | Liquidity risk premium | 5.00% |

Recovery rate in default

40.00%

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Notes to Condensed Consolidated Financial Statements

June 30, 2017

(unaudited)

The change in the estimated fair value calculated for the investment valued on a recurring basis utilizing Level 3 inputs (i.e., the Failed Auction Security) for the six months ended June 30, 2017 was as follows (in thousands):

| | |
|--|----------|
| Balance at the beginning of the period | \$ 2,508 |
| Credit gain on available-for-sale securities included in Other income (expense), net | 6 |
| Gain included in Other comprehensive income (loss) | 51 |
| Balance at the end of the period | \$ 2,565 |

The Company has classified its contingent consideration obligations as Level 3 because the fair value for these liabilities was determined using unobservable inputs. The liabilities were based on estimated sales of legacy products over the period of royalty payments at the royalty rate, discounted using the Company's estimated cost of capital.

The change in the estimated fair value calculated for the liabilities valued on a recurring basis utilizing Level 3 inputs (i.e., the Contingent consideration obligations) for the six months ended June 30, 2017 was as follows (in thousands):

| | |
|--|--------|
| Balance at the beginning of the period | \$ 253 |
| Payments | (111) |
| Balance at the end of the period | \$ 142 |

There were no transfers between Level 1 and Level 2 of the fair value hierarchy during the six months ended June 30, 2017.

4. Stock-Based Compensation

The Company uses the Black-Scholes option pricing model to calculate the fair value of stock option awards as of their grant date. Stock-based compensation expense, net for the three and six months ended June 30 was as follows (in thousands):

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| | Three Months Ended | | Six Months Ended | |
|-------------------------------------|--------------------|--------|------------------|--------|
| | June 30, | | June 30, | |
| | 2017 | 2016 | 2017 | 2016 |
| Cost of revenues | \$ 38 | \$ 54 | \$ 72 | \$ 106 |
| Selling, general and administrative | 215 | 237 | 395 | 475 |
| Research and development | 34 | 49 | 74 | 88 |
| Total stock-based compensation | \$ 287 | \$ 340 | \$ 541 | \$ 669 |

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Notes to Condensed Consolidated Financial Statements

June 30, 2017

(unaudited)

5. Net Loss per Share

The following table sets forth the computation of basic and diluted net loss per share for the three and six months ended June 30 (in thousands, except per share amounts):

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|-----------|------------------|------------|
| | June 30, | | June | |
| | 2017 | 2016 | 2017 | 2016 |
| Numerator: | | | | |
| Net loss attributable to Vicor Corporation | \$ (459) | \$ (544) | \$ (1,433) | \$ (5,895) |
| Denominator: | | | | |
| Denominator for basic net loss per share-weighted average shares (1) | 39,172 | 38,801 | 39,121 | 38,798 |
| Effect of dilutive securities: | | | | |
| Employee stock options (2) | | | | |
| Denominator for diluted net loss per share adjusted weighted-average shares and assumed conversions | 39,172 | 38,801 | 39,121 | 38,798 |
| Basic net loss per share | \$ (0.01) | \$ (0.01) | \$ (0.04) | \$ (0.15) |
| Diluted net loss per share | \$ (0.01) | \$ (0.01) | \$ (0.04) | \$ (0.15) |

- (1) Denominator represents weighted average number of shares of Common Stock and Class B Common Stock outstanding.
- (2) Options to purchase 1,510,728 and 1,889,038 shares of Common Stock for the three and six months ended June 30, 2017 and 2016, respectively, were not included in the calculation of net loss per share as the effect would have been antidilutive.

6. Inventories

Inventories are valued at the lower of cost (determined using the first-in, first-out method) or net realizable value. Fixed production overhead is allocated to the inventory cost per unit based on the normal capacity of the production facilities. Abnormal production costs, including fixed cost variances from normal production capacity, if any, are charged to cost of revenues in the period incurred. All shipping and handling costs incurred in connection with the

sale of products are included in cost of revenues.

The Company provides reserves for inventories estimated to be excess, obsolete or unmarketable. The Company's estimation process for assessing net realizable value is based upon its known backlog, projected future demand, historical consumption and expected market conditions. If the Company's estimated demand and/or market expectation were to change or if product sales were to decline, the Company's estimation process may cause larger inventory reserves to be recorded, resulting in larger charges to cost of revenues.

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Notes to Condensed Consolidated Financial Statements

June 30, 2017

(unaudited)

Inventories were as follows (in thousands):

| | June 30, 2017 | December 31, 2016 |
|-----------------|---------------|-------------------|
| Raw materials | \$ 21,538 | \$ 18,648 |
| Work-in-process | 3,431 | 3,361 |
| Finished goods | 5,545 | 5,127 |
| Net balance | \$ 30,514 | \$ 27,136 |

7. Product Warranties

The Company generally offers a two-year warranty for all of its products, though it is party to a limited number of supply agreements with certain customers contractually committing the Company to warranty and indemnification requirements exceeding those to which the Company has been exposed in the past. Effective January 1, 2017, the Company extended the warranty period to three years for certain military grade products sold after that date. The Company provides for the estimated cost of product warranties at the time product revenue is recognized. Factors influencing the Company's warranty reserves include the number of units sold, historical and anticipated rates of warranty returns, and the cost per return. The Company periodically assesses the adequacy of warranty reserves and adjusts the amounts as necessary. Warranty obligations are included in Accrued expenses in the accompanying Condensed Consolidated Balance Sheets.

Product warranty activity for the three and six months ended June 30 was as follows (in thousands):

| | Three Months Ended | | Six Months | |
|---|--------------------|--------|------------|--------|
| | June 30, | | Ended | |
| | 2017 | 2016 | 2017 | 2016 |
| Balance at the beginning of the period | \$ 185 | \$ 587 | \$ 214 | \$ 584 |
| Accruals for warranties for products sold in the period | 91 | 107 | 195 | 229 |
| Fulfillment of warranty obligations | (24) | (198) | (97) | (267) |
| Revisions of estimated obligations | (8) | | (68) | (50) |
| Balance at the end of the period | \$ 244 | \$ 496 | \$ 244 | \$ 496 |

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Notes to Condensed Consolidated Financial Statements

June 30, 2017

(unaudited)

8. Income Taxes

The tax provision is based on the estimated annual effective tax rate for the year, which includes estimated federal, state and foreign income taxes on the Company's projected pre-tax income (loss).

The provision for income taxes and the effective income tax rates for the three and six months ended June 30 were as follows (dollars in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|----------------------------|--------------------------------|-------|------------------------------|-------|
| | 2017 | 2016 | 2017 | 2016 |
| Provision for income taxes | \$ 267 | \$ 13 | \$ 168 | \$ 35 |
| Effective income tax rate | 150.0% | 2.4% | 13.6% | 0.6% |

The provisions for income taxes in each 2017 and 2016 period were primarily due to estimated foreign income taxes and for estimated state taxes in jurisdictions in which the Company does not have net operating loss carryforwards. No tax benefit could be recognized for the majority of the Company's losses during the periods due to a full valuation allowance against all net domestic deferred tax assets. The provision and effective income tax rate were higher in the second quarter of 2017 as the Company had previously recorded a tax benefit in the first quarter of 2017. In addition, in connection with the Company's acquisition of 100% ownership of certain operating assets and cash of the Company's consolidated subsidiary, Converpower Corporation, the related deferred tax liability for unremitted earnings of \$55,000 was reversed and recorded as a discrete benefit in the first quarter of 2016.

As described in Note 11- Impact of Recently Issued Accounting Standards, the Company adopted new guidance for employee share-based payment accounting during the first quarter of 2017. The new guidance, among other considerations, requires excess tax benefits and tax deficiencies related to employee share-based compensation to now be recorded in earnings when the awards vest or are settled, rather than in shareholders' equity under previous guidance. In addition, it eliminates the requirement that excess tax benefits be realized with the taxing authority before they can be recognized. In connection with the adoption of this new guidance, the Company recorded a cumulative-effect adjustment as of January 1, 2017 to increase gross deferred tax assets and the related valuation allowance against deferred tax assets by \$3,485,000. This amount was allocated and added to deferred tax assets for research and development tax credit carryforwards, net operating loss carryforwards and the alternative minimum tax credit carryforward but, as noted above, was fully offset by a corresponding increase in the valuation allowance against deferred tax assets, resulting in no net effect on the Company's condensed consolidated financial statements.

As of June 30, 2017, the Company continues to maintain a valuation allowance of approximately \$32,746,000 against all domestic net deferred tax assets and the majority of foreign net deferred tax assets, for which realization cannot be

considered more likely than not at this time.

In May 2017, the Company received notice from the Internal Revenue Service that its federal corporate tax return for tax year 2015 had been selected for examination. The examination is in the preliminary stages.

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9. Commitments and Contingencies

At June 30, 2017, the Company had approximately \$5,526,000 of capital expenditure commitments.

On January 28, 2011, SynQor, Inc. (SynQor) filed a complaint for patent infringement against Ericsson, Inc. (Ericsson), Cisco Systems, Inc. (Cisco) and the Company in the U.S. District Court for the Eastern District of Texas (the Texas Action). Ericsson and Cisco subsequently settled with SynQor and are no longer parties to the Texas Action. With respect to the Company, SynQor s complaint in the Texas Action alleged that the Company s products, including but not limited to unregulated bus converters used in intermediate bus architecture power supply systems, infringe SynQor s U.S. patent numbers 7,072,190, 7,272,021, and 7,564,702 (the 190 patent , the 021 patent and the 702 patent , respectively). SynQor s complaint sought an injunction against further infringement and an award of unspecified compensatory and enhanced damages, interest, costs and attorney fees. On September 20, 2011, SynQor filed an amended complaint in the Texas Action that further alleged that the Company s products, including, but not limited to, unregulated bus converters used in intermediate bus architecture power supply systems, infringe SynQor s U.S. patent number 8,023,290 (the 290 patent). The Company responded to SynQor s amended complaint in the Texas Action by denying its products infringe any of the SynQor patents, and asserting that the SynQor patents are invalid. The Company has further alleged that the SynQor 290 patent is unenforceable due to inequitable conduct by SynQor or its agents during the examination of the 290 patent at the United States Patent and Trademark Office (USPTO). The Company has also asserted counterclaims seeking damages against SynQor for deceptive trade practices and tortious interference with prospective economic advantage arising from SynQor s attempted enforcement of its patents against the Company.

The Company has initiated administrative review proceedings at the USPTO challenging the validity of certain claims of the SynQor patents asserted in the Texas Action, including all claims that were asserted against the Company by SynQor. Regarding the 190 patent, the Patent Trial and Appeal Board (PTAB) of the USPTO issued a decision upholding the validity of the 190 patent claims. That decision was appealed by the Company to the United States Court of Appeals for the Federal Circuit (the Federal Circuit), which issued a decision on March 13, 2015 reversing the PTAB, determining that certain claims were invalid, and remanding the matter to the PTAB for further proceedings. On May 2, 2016, the PTAB issued a decision determining that all but one of the remaining claims of the 190 patent were invalid and remanding the remaining claim to a patent examiner for further examination. On June 22, 2017, the examiner issued an determination under 37 C.F.R. § 41.77(d), finding that the remaining claim of the 190 patent was unpatentable. That decision is expected to be further reviewed by the PTAB pursuant to 37 C.F.R. § 41.77(f).

On May 2, 2016, the PTAB also issued decisions finding all challenged claims of SynQor s 021 patent invalid and upholding the validity of all challenged claims of SynQor s 702 and 290 patents. The Company filed an appeal with the Federal Circuit from the PTAB s decision upholding the validity of the challenged claims of the 702 and 290 patents. SynQor has filed an appeal with the Federal Circuit from the PTAB s decision that the challenged claims of

the '021 patent are invalid. Oral arguments in all three appeals were heard on May 2, 2017. Decisions in these appeals are expected later in 2017. On May 23, 2016, the Texas Court issued an order staying the Texas Action until the completion of all of the administrative review proceedings concerning the asserted SynQor patents, including any appeals from such proceedings to the Federal Circuit.

The Company continues to believe none of its products, including its unregulated bus converters, infringe any valid claim of the asserted SynQor patents, either alone or when used in an intermediate bus architecture implementation. The Company believes SynQor's claims lack merit and, therefore, continues to vigorously defend itself against SynQor's patent infringement allegations. The Company does not believe a loss is probable for this matter. If a loss were to be incurred, however, the Company cannot estimate the amount of possible loss or range of possible loss at this time.

In addition to the SynQor matter, the Company is involved in certain other litigation and claims incidental to the conduct of its business. While the outcome of lawsuits and claims against the Company cannot be predicted with certainty, management does not expect any current litigation or claims will have a material adverse impact on the Company's financial position or results of operations.

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10. Segment Information

The Company has organized its business segments according to its key product lines. The Brick Business Unit segment (BBU) designs, develops, manufactures and markets the Company's modular DC-DC converters and configurable products, and also includes the entities comprising Vicor Custom Power and the BBU operations of Vicor Japan Company, Ltd. (VJCL). The VI Chip segment includes VI Chip Corporation, which designs, develops, manufactures and markets many of the Company's advanced power component products. The VI Chip segment also includes the VI Chip business conducted through VJCL. The Picor segment includes Picor Corporation, which designs, develops, manufactures and markets integrated circuits and related products for use in a variety of power management and power system applications. The Picor segment develops these products for use in the Company's BBU and VI Chip modules, to be sold as complements to the Company's BBU and VI Chip products, or for sale to third parties for separate (i.e., stand-alone) applications.

The Company's chief operating decision maker evaluates performance and allocates resources based on segment revenues and segment operating income (loss). The operating income (loss) for each segment includes selling, general and administrative and research and development expenses directly attributable to the segment. Certain of the Company's indirect overhead costs, which include corporate selling, general and administrative expenses, are allocated among the segments based upon an estimate of costs associated with each segment. Assets allocated to each segment are based upon specific identification of such assets, which include accounts receivable, inventories, fixed assets and certain other assets. The Corporate segment consists of those operations and assets shared by all segments. The costs of certain centralized executive and administrative functions are recorded in this segment, as are certain shared assets, most notably cash and cash equivalents, deferred tax assets, long-term investments, the Company's facilities in Massachusetts, real estate and other assets. The Company's accounting policies and method of presentation for segments are consistent with that used throughout the Condensed Consolidated Financial Statements.

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The following table provides segment financial data for the three months ended June 30 (in thousands):

| | BBU | VI Chip | Picor | Corporate | Eliminations (1) | Total |
|-------------------------------|-----------|-----------|----------|-----------|---------------------|-----------|
| 2017: | | | | | | |
| Net revenues | \$ 39,077 | \$ 15,168 | \$ 6,335 | \$ | \$ (2,871) | \$ 57,709 |
| Income (loss) from operations | 2,535 | (3,889) | 1,098 | (282) | | (538) |
| Total assets | 219,195 | 27,621 | 11,287 | 67,764 | (162,252) | 163,615 |
| Depreciation and amortization | 1,000 | 659 | 190 | 340 | | 2,189 |
| 2016: | | | | | | |
| Net revenues | \$ 40,576 | \$ 10,418 | \$ 4,321 | \$ | \$ (2,374) | \$ 52,941 |
| Income (loss) from operations | 4,235 | (4,508) | (133) | (195) | | (601) |
| Total assets | 190,135 | 19,583 | 6,111 | 71,513 | (133,193) | 154,149 |
| Depreciation and amortization | 1,149 | 545 | 135 | 287 | | 2,116 |

The following table provides segment financial data for the six months ended June 30 (in thousands):

| | BBU | VI Chip | Picor | Corporate | Eliminations (1) | Total |
|-------------------------------|-----------|-----------|-----------|-----------|---------------------|------------|
| 2017: | | | | | | |
| Net revenues | \$ 76,612 | \$ 28,090 | \$ 13,193 | \$ | \$ (5,724) | \$ 112,171 |
| Income (loss) from operations | 3,955 | (7,809) | 2,466 | (528) | | (1,916) |
| Total assets | 219,195 | 27,621 | 11,287 | 67,764 | (162,252) | 163,615 |
| Depreciation and amortization | 1,973 | 1,288 | 370 | 715 | | 4,346 |
| 2016: | | | | | | |
| Net revenues | \$ 77,445 | \$ 18,165 | \$ 7,276 | \$ | \$ (3,918) | \$ 98,968 |
| Income (loss) from operations | 5,741 | (10,216) | (1,137) | (418) | | (6,030) |
| Total assets | 190,135 | 19,583 | 6,111 | 71,513 | (133,193) | 154,149 |
| Depreciation and amortization | 2,268 | 1,129 | 262 | 652 | | 4,311 |

- (1) The elimination for net revenues is principally related to inter-segment sales by Picor to BBU and VI Chip and for inter-segment sales by VI Chip to BBU. The elimination for total assets is principally related to inter-segment accounts receivable due to BBU for the funding of VI Chip and Picor operations.

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11. Impact of Recently Issued Accounting Standards

In May 2017, the Financial Accounting Standards Board (FASB) issued guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718, *Compensation – Stock Compensation*. The new guidance is effective for annual and interim periods beginning after December 15, 2017, with early adoption permitted. The Company has not yet determined the impact this new guidance will have on its consolidated financial statements and related disclosures.

In August 2016, the FASB issued guidance to clarify how certain cash receipts and cash payments should be presented in the statement of cash flows. These include debt prepayment, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, distributions received from equity method investees and beneficial interests in securitization transactions. The new guidance is effective for interim and annual reporting periods beginning after December 15, 2017, with early adoption permitted. The Company does not expect the adoption of the new guidance will have a material impact on its consolidated financial statements and related disclosures.

In June 2016, the FASB issued new guidance which will require measurement and recognition of expected credit losses on certain types of financial instruments. It also modifies the impairment model for available-for-sale debt securities and provides for a simplified accounting model for purchased financial assets with credit deterioration since their origination. The new guidance is effective for interim and annual reporting periods beginning after December 15, 2019, with early adoption permitted. It is required to be applied on a modified-retrospective approach with certain elements being adopted prospectively. The Company has not yet determined the impact this new guidance will have on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued new guidance for employee share-based payment accounting, which makes several modifications to existing guidance related to the accounting for forfeitures, employer tax withholding on share-based compensation and the financial statement presentation of excess tax benefits or deficiencies. This new guidance also clarifies the statement of cash flows presentation for certain components of share-based awards. In terms of the accounting for forfeitures, the new guidance allows an option for them to either be estimated, as currently required, or recognized when they occur. The Company will continue to estimate forfeitures. The Company adopted the new standard on January 1, 2017. (See Note 8 – Income Taxes for additional details on the impact of the adoption).

In February 2016, the FASB issued new guidance for lease accounting, which will require lessees to recognize leases on the balance sheet and disclose key information about leasing arrangements. The new guidance establishes a right-of-use model (ROU) that will require a lessee to recognize a ROU asset and a lease liability on the balance sheet for all leases with a term longer than twelve months. Leases will be classified as finance or operating, with classification affecting the pattern and classification of expense recognition in the income statement. For lessors, the

guidance modifies the classification criteria and accounting for sales-type and direct financing leases. The new standard is effective for interim and annual periods beginning after December 15, 2018, with early adoption permitted. The Company plans to adopt the new guidance effective January 1, 2019. The new standard must be adopted using a modified retrospective transition which includes certain practical expedients. The majority of the Company's leases are for certain of its office and manufacturing space. The Company has not yet determined the impact this new guidance will have on its consolidated financial statements and related disclosures.

In May 2014, the FASB issued new guidance for revenue recognition, which will require an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The new guidance, which includes several amendments, will replace most existing revenue recognition guidance in U.S. Generally Accepted Accounting Principles when it becomes effective which will be, for the Company, on January 1, 2018. The new standard permits the use of either the retrospective or cumulative effect transition method. The Company has established an implementation team to assess the potential impact of the new standard which includes identifying appropriate changes to the business processes, systems and controls to support revenue recognition and disclosure requirements under the new standard. While the implementation team is still in the process of completing its evaluation of the new standard, it has reached preliminary conclusions on substantially all key accounting assessments, and currently believes the most significant impact will be related to the timing of recognition of sales to its stocking distributors. The Company currently defers revenue and the related cost of sales on shipments to stocking distributors until the distributors resell the products to their customers. Upon adoption of the new guidance, the Company will no

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longer be permitted to defer revenue until sale by the stocking distributor to the end customer, but rather, will be required to estimate the effects of returns and allowances provided to stocking distributors and record revenue at the time of sale to the stocking distributor. The Company currently plans to utilize the retrospective transition method for adoption of the standard. Upon adoption under that method, the Company will recognize the cumulative effect of adopting this guidance as an adjustment to the balance of retained earnings as of January 1, 2016. The implementation team is continuing to evaluate the method of adoption and the future impact the new guidance will have on its consolidated financial statements and related disclosures and expects to complete its initial assessment of those financial statement impacts by the third quarter of 2017. The other principal remaining implementation items include completing the identification and documentation of key transition controls and, later, the identification and documentation of any new or revised key ongoing process controls. The implementation team expects to complete those tasks by the end of the fourth quarter of 2017. The implementation team has reported its findings and status to the Audit Committee on a regular basis over the last year.

Other new pronouncements issued but not effective until after June 30, 2017 are not expected to have a material impact on the Company's consolidated financial statements.

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

Except for statements of historical fact contained herein, statements in this report constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The words believes, expects, anticipates, intends, estimates, plans, assumes, may, will, would, should, continue, prospective, project, and other similar words or expressions are used to identify forward-looking statements. Forward-looking statements include, without limitation, statements regarding the transition of the Company's business strategically and organizationally from serving a large number of relatively low volume customers across diversified markets and geographies to serving a small number of relatively large volume customers, typically concentrated in computing and communications; the level of customer orders overall and, in particular, from large customers and the delivery lead times associated therewith; the financial and operational impact of customer changes to shipping schedules; the derivation of a portion of the Company's sales in each quarter from orders booked in the same quarter; the Company's ongoing development of power conversion architectures, switching topologies, packaging technologies, and products; the Company's plans to invest in expanded manufacturing capacity and the timing and location thereof; the Company's continued success depending in part on its ability to attract and retain qualified personnel; the Company's belief that cash generated from operations and the total of its cash and cash equivalents will be sufficient to fund operations for the foreseeable future; the Company's belief that it has limited exposure to currency risks; the Company's intentions regarding the declaration and payment of cash dividends; the Company's intentions regarding protecting its rights under its patents; and the Company's expectation that no current litigation or claims will have a material adverse impact on its financial position or results of operations. These statements are based upon the Company's current expectations and estimates as to the prospective events and circumstances which may or may not be within the Company's control and as to which there can be no assurance. Actual results could differ materially from those expressed or implied by forward-looking statements as a result of various factors, including the Company's ability to: grow its revenues, establish and maintain profitability, develop and market new products and technologies cost effectively, and on a timely basis leverage the Company's new technologies in standard products to promote market acceptance of the Company's new approach to power system architecture; leverage design wins into increased product sales; continue to meet requirements of key customers and prospects; enter into licensing agreements increasing the Company's market opportunity and accelerating market penetration; realize significant royalties under such licensing agreements; achieve sustainable bookings rates for the Company's products across served markets and geographies; improve manufacturing and operating efficiencies; successfully enforce the Company's intellectual property rights; successfully defend outstanding litigation; hire and retain key personnel; and maintain an effective system of internal controls over financial reporting. These and other factors that may influence actual results are described in the risk factors set forth in the Company's Annual Report on Form 10-K for the year ended December 31, 2016, under Part I, Item 1 Business, under Part I, Item 1A Risk Factors, under Part I, Item 3 Legal Proceedings, and under Part II, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations. The risk factors contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2016 may not be exhaustive. Therefore, the information contained therein should be read together with other reports and documents that the Company files with the Securities and Exchange Commission from

time to time, including Forms 10-Q, 8-K and 10-K, which may supplement, modify, supersede or update those risk factors. Except as required by law, the Company does not undertake any obligation to update any forward-looking statements as a result of future events or developments.

Overview

We design, develop, manufacture, and market modular power components and power systems for converting, regulating, and controlling electric current. We also license certain rights to our technology in return for recurring royalties. The principal customers for our power converters and systems are large original equipment manufacturers (OEMs) and their contract manufacturers, and smaller, lower volume users. We serve a broad range of market segments and geographies worldwide.

We have organized our business segments according to our key product lines. Reflecting our history and direction, we broadly categorize our products as either legacy or advanced , generally based on design, performance, and form factor considerations, as well as the range of applications for which the products are appropriate.

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The BBU segment designs, develops, manufactures and markets our legacy lines of DC-DC converters and configurable products, as well as complementary components providing AC line rectification, input filtering, power factor correction, and transient protection. The BBU segment also includes the BBU business conducted through VJCL and our Vicor Custom Power subsidiaries. The BBU has customers concentrated in aerospace and aviation, defense electronics, industrial automation and equipment, medical diagnostics, rail transportation, and test and measurement instrumentation.

The VI Chip segment consists of our subsidiary, VI Chip Corporation, which designs, develops, manufactures, and markets many of our advanced power component products. The VI Chip segment also includes VI Chip business conducted in Japan through VJCL. VI Chip generally targets large, high volume customers concentrated in the datacenter and supercomputer segments of the computing market, although we also target applications in aerospace and aviation, defense electronics, electric and hybrid vehicles, instrumentation and test equipment, and networking equipment.

The Picor segment consists of our subsidiary, Picor Corporation, which designs, develops, and markets integrated circuits and related solid-state products for use in a variety of power management and power system applications. Picor is a fabless manufacturer, as its products are manufactured, assembled, packaged, and tested by third parties. Picor develops products for use in our BBU and VI Chip modules, to be sold as complements to our BBU and VI Chip products, or for sale to third parties for separate (i.e., stand-alone) applications, often integrated with VI Chip products to represent a customer solution, particularly in the datacenter and supercomputer segments of the computing market.

Our consolidated results for the second quarter of 2017 showed sequential improvement, with higher revenue and a reduced net loss, yet our operating performance continues to reflect the general weakness of demand for our legacy products, which are used in industries and geographies that continue to experience macroeconomic uncertainty. Customer interest in our expanding portfolio of recently-introduced advanced products continues to increase, as evidenced by the second quarter's higher bookings and sequentially higher quarter-end backlog, both reflecting market uptake of our new products, notably our 48 volt to point-of-load solutions for datacenters and supercomputers.

While second quarter bookings and revenues were encouraging, improved global demand for our legacy brick converters, configurable products, and associated components remains at volumes lower than historical trend, which we attribute to the ongoing macroeconomic concerns influencing customer confidence across the industries and geographies we serve. Our legacy products commonly are used in high-value capital goods and sizeable infrastructure projects, the end demand for which has been unpredictable, reflecting low-growth economies and budgetary uncertainty.

Although the number of identified opportunities for our new products continues to expand, as evidenced by booking patterns, the sales cycles associated with these products have proven longer than we anticipated, in part due to the same macroeconomic trends and industry-specific conditions influencing bookings and sales of our legacy product

lines. In many mature markets, existing and potential customers remain risk-averse and have slowed or curtailed their own new product development. We believe such caution has limited their near-term interest in our new products, although we are experiencing increasing interest in our new products as replacements for legacy power modules, whether our own or those of competitors, when customers are refreshing or upgrading existing designs.

In more robust markets, such as those we are targeting with our new products, existing and potential customers are actively pursuing their own growth strategies, developing products with higher performance enabled by our new products and the modular component approach of our Factorized Power Architecture. As such, we increasingly are asked by existing and potential customers to collaborate on the development of new or highly modified implementations of our new products. While such collaborations are attractive opportunities to enhance customer relationships and gain competitive advantage, they also are resource and time intensive. Additionally, when we have successfully designed-in our new product solutions, we may encounter delays and uncertainty associated with scheduling production of such solutions.

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We believe the following considerations may influence our performance over the second half of 2017:

Operational Considerations

We operate a highly automated electronics manufacturing facility in Andover, Massachusetts, and our profitability is closely aligned with production unit volumes. We have invested significantly in state-of-the-art systems, equipment, and robotics, which allow us to generate relatively higher profitability when operating at or near factory capacity, even with a high mix of products produced. However, periods of low volume production and/or brief, low volume production runs contribute to lower profitability, largely due to lower absorption of relatively high manufacturing overhead costs associated with our manufacturing model. While direct labor and associated variable costs correlate with volume, manufacturing overhead costs are inflexible and, therefore, problematic during periods of low volume or brief production runs. We have invested in the production capacity to meet our internal volume projections, and believe these projections are reasonable. However, if sustained, uniform, high volume production levels are not achieved, our product-level profitability likely will not reach the levels necessary to cover our fixed spending, consisting of manufacturing overhead costs and operating costs.

Our ability to achieve sustained, high volume production levels is tied to our ability to forecast manufacturing requirements of a range of inputs, notably raw material inventories. Because we utilize a number of components and other materials of proprietary design, our ability to sustain targeted production schedules and meet customer delivery requirements has been vulnerable to delays or shortages of such inventories. Over the last two years, we have made progress in reducing potential vulnerabilities to stock-outs, vendor shortages, and similar supply chain disruptions. We also have reorganized our supply chain management effort, strengthened with new hires. We have implemented safety-stock programs for certain critical components and materials and have established second-source supply relationships in order to reduce these vulnerabilities. However, our product-level profitability and overall performance could be negatively influenced by an unplanned shortage of a particular component or material.

We expect our operating expenses, notably in engineering and sales, to remain relatively high, as percentages of revenue, for the foreseeable future. If revenue reaches our forecasted levels, these percentages are expected to decline, although we do not expect such expenses to decline on an absolute basis. We have expanded and focused our engineering and sales organizations to pursue the promising opportunities afforded by our new, innovative products, and we believe our current level of spending is necessary to achieve our strategic goals. However, many of these opportunities are in early phases of development, and

near-term revenue growth may not be sufficient to reduce the percentages of revenue represented by our operating expenses to forecast levels or levels comparable to our high volume competitors.

Market and Macroeconomic Considerations

Customer adoption of certain new products has been delayed by unanticipated influences beyond our control. For example, our leadership position in the transition of datacenter computing to 48 volt to point-of-load solutions using our Factorized Power Architecture was the basis for our expectation of an earlier, higher-volume uptake of such solutions and our decisions to focus our resources on such customers and opportunities. However, delays in the transition of processor generations and associated supply chain disruption caused repeated delays in customer purchase orders well into 2016. Based on current customer activity, an expanding customer list, and an expanding backlog, we believe the 48 volt to point-of-load opportunity has entered an accelerated, second phase of development, with a broadening of interest and the entry of new vendors. As such, we face a more complex competitive landscape, with additional challenges. We continue to believe our new products will be adopted in volume by multiple, leading customers. However, we cannot control the actions by, or the timing of, our customers, their contract manufacturers, or the significant vendors also participating in the market. Many of these vendors possess resources far greater than Vicor and have operational and financial flexibility we do not.

We anticipate aggregate demand for certain mature markets to grow, at best, only at the rate of the overall economy (i.e., in the United States, for example, at the rate of growth of gross domestic product) for the foreseeable future. Given our long-standing customer relationships and the status of our legacy products in long-lived customer applications, we anticipate maintaining our share of these mature markets. In 2016, we completed two years of restructuring initiatives to reduce our

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exposure to certain problematic market segments, notably the custom systems portion of the defense electronics market, and have experienced improved resource allocation, operating efficiencies, and asset utilization. We also have substantially restructured our distribution channels, notably across Europe, with the goal of improving our breadth of presence across important geographies and targeted market segments. Other initiatives to improve the performance of the BBU continue today. However, we do not expect the performance of the BBU and its legacy products to significantly improve until macroeconomic conditions improve in industries and geographies served by the BBU.

Financial Highlights:

Net revenues increased 9.0% to \$57,709,000 for the second quarter of 2017, from \$52,941,000 for the second quarter of 2016, primarily due to an overall 13.1% increase in bookings in the second quarter of 2017, compared to the second quarter of 2016, with significant increases from the VI Chip and Picor segments.

Net revenues for the six months ended June 30, 2017 increased by 13.3% to \$112,171,000 from \$98,968,000 for the six months ended June 30, 2016, primarily due to an overall 15.5% increase in bookings for the six months ended June 30, 2017, compared to the six months ended June 30, 2016, with significant increases from the VI Chip and Picor segments.

Export sales, as a percentage of total revenues, represented approximately 65.4% in the second quarter of 2017 and 60.5% in the second quarter of 2016. Export sales, as a percentage of total revenues, for the six months ended June 30, 2017 and 2016 were approximately 64.4% and 59.8%, respectively.

Gross margin increased to \$25,930,000 for the second quarter of 2017, from \$24,471,000 for the second quarter of 2016, primarily due to the increase in net revenues. Gross margin, as a percentage of net revenues, despite the increase in net revenues, decreased to 44.9% for the second quarter of 2017 from 46.2% for the second quarter of 2016, primarily due to a less favorable product mix.

Gross margin increased to \$49,582,000 for the six months ended June 30, 2017 from \$43,787,000 for the six months ended June 30, 2016, primarily due to the increase in net revenues. Gross margin, as a percentage of revenues, despite the increase in net revenues, remained flat at 44.2% for the six months ended June 30, 2017 compared to the six months ended June 30, 2016, primarily due to a less favorable product mix.

Backlog, representing the total of orders for products received for which shipment is scheduled within the next 12 months, was approximately \$53,157,000 at the end of the second quarter of 2017, as compared to \$51,732,000 at the end of the first quarter of 2017.

Operating expenses for the second quarter of 2017 increased \$1,396,000, or 5.6%, to \$26,468,000 from \$25,072,000 for the second quarter of 2016, primarily due to an increase in research and development expense of \$1,175,000.

Operating expenses for the six months ended June 30, 2017 increased \$1,681,000, or 3.4%, to \$51,498,000 from \$49,817,000 for the six months ended June 30, 2016, primarily due to an increase in research and development expense of \$1,453,000.

We reported a net loss for the second quarter of 2017 of \$(459,000), as compared to net loss of \$(544,000) for the second quarter of 2016, and a net loss per share of \$(0.01) for the second quarter of 2017, as compared to net loss per share of \$(0.01) for second quarter of 2016.

We reported a net loss for the six months ended June 30, 2017, of \$(1,433,000), or \$(0.04) per share, compared to \$(5,895,000), or \$(0.15) per share, for the six months ended June 30, 2016.

For the six months ended June 30, 2017, depreciation and amortization totaled \$4,346,000, and capital additions totaled \$5,631,000, compared to \$4,311,000 and \$4,646,000, respectively, for the six months ended June 30, 2016.

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Inventories increased by approximately \$3,378,000, or 12.4%, to \$30,514,000 at June 30, 2017, compared to \$27,136,000 at December 31, 2016. This increase was primarily associated with increases in VI Chip and Picor inventories of \$2,574,000 and \$1,252,000, respectively, to meet increased bookings for the two segments, partially offset by a decrease in BBU inventories of \$448,000.

Critical Accounting Policies and Estimates

Please refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2016 for a summary of the Company's critical accounting policies and estimates.

Three months ended June 30, 2017, compared to three months ended June 30, 2016

Consolidated net revenues for the second quarter of 2017 were \$57,709,000, an increase of \$4,768,000, or 9.0%, as compared to \$52,941,000 for the second quarter of 2016, and an increase of \$3,247,000, or 6.0%, on a sequential basis from \$54,462,000 for the first quarter of 2017.

Net revenues, by segment, for the second quarter of 2017 and the second quarter of 2016 were as follows (dollars in thousands):

| | 2017 | 2016 | Increase (decrease) | |
|---------|-----------|-----------|---------------------|--------|
| | | | \$ | % |
| BBU | \$ 39,077 | \$ 40,576 | \$ (1,499) | (3.7)% |
| VI Chip | 14,527 | 10,080 | 4,447 | 44.1% |
| Picor | 4,105 | 2,285 | 1,820 | 79.6% |
| Total | \$ 57,709 | \$ 52,941 | \$ 4,768 | 9.0% |

The increase in consolidated net revenues for the second quarter of 2017 from the second quarter of 2016 was primarily due to an overall 13.1% increase in bookings in the second quarter of 2017, compared to the second quarter of 2016. VI Chip and Picor bookings increased by 48.2% and 127.3%, respectively, while BBU bookings remained flat. The decrease in BBU revenues was primarily attributable to decreases in BBU module and configurable product revenues of approximately \$2,378,000, partially offset by an increase in Vicor Custom Power revenues of \$963,000. Increases in revenues recorded by VI Chip and Picor for the second quarter of 2017 were associated largely with fulfillment of increased orders for our 48 volt to point-of-load solutions. Customer bookings and scheduling patterns continue to be unpredictable, particularly for the VI Chip and Picor segments.

Gross margin for the second quarter of 2017 increased \$1,459,000, or 6.0%, to \$25,930,000, from \$24,471,000 for the second quarter of 2016 primarily due to the increase in net revenues. Despite the increase in net revenues, gross margin as a percentage of net revenue decreased to 44.9% for the second quarter of 2017 compared to 46.2% for the second quarter of 2016, primarily due to a less favorable product mix.

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Selling, general, and administrative expenses were \$14,536,000 for the second quarter of 2017, an increase of \$221,000, or 1.5%, from \$14,315,000 for the second quarter of 2016. Selling, general, and administrative expenses as a percentage of net revenues decreased to 25.2% for the second quarter of 2017 from 27.0% for the second quarter of 2016, primarily due to the increase in net revenues.

The components of the \$221,000 increase in selling, general and administrative expenses for the second quarter of 2017 from the second quarter of 2016 were as follows (dollars in thousands):

| | Increase (decrease) | |
|---------------------------------|---------------------|------------|
| Advertising expenses | \$ 102 | 16.9%(1) |
| Compensation | 94 | 1.1%(2) |
| Travel expenses | 62 | 7.7%(3) |
| Freight expenses | 49 | 89.0% |
| Audit, tax, and accounting fees | 42 | 14.3% |
| Legal fees | (49) | (10.5)% |
| Depreciation and amortization | (71) | (10.1)%(4) |
| Telephone expenses | (90) | (32.4)%(5) |
| Other, net | 82 | 3.6% |
| | \$ 221 | 1.5% |

- (1) Increase primarily attributed to increases in sales support expenses, direct mailings, and advertising in trade publications.
- (2) Increase primarily attributable to annual compensation adjustments in May 2017, partially offset by decreases in fringe benefit expenses.
- (3) Increase primarily attributable to increased travel by the Company's sales and marketing personnel.
- (4) Decrease attributable to certain BBU segment fixed assets becoming fully depreciated during 2016.
- (5) Decrease attributable to reduced service provider costs.

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Research and development expenses were \$11,932,000 for the second quarter of 2017, an increase of \$1,175,000, or 10.9%, compared to \$10,757,000 for the second quarter of 2016, primarily due to the increase in project and pre-production materials. As a percentage of net revenues, research and development expenses increased to 20.7% for the second quarter of 2017 from 20.3% for the second quarter of 2016.

The components of the \$1,175,000 increase in research and development expenses were as follows (dollars in thousands):

| | Increase (decrease) | |
|--------------------------------------|---------------------|-------------|
| Project and pre-production materials | \$ 1,155 | 80.9%(1) |
| Compensation | 306 | 4.1%(2) |
| Facilities expenses | 101 | 21.5%(3) |
| Deferred costs | (417) | (370.4)%(4) |
| Other, net | 30 | 2.0% |
| | \$ 1,175 | 10.9% |

- (1) Increase primarily attributable to increases in spending for new product development by the VI Chip segment.
- (2) Increase primarily attributable to annual compensation adjustments in May 2017.
- (3) Increase primarily attributable to an increase in utilities and building maintenance expenses.
- (4) Decrease primarily attributable to an increase in deferred costs capitalized for certain non-recurring engineering projects for which the related revenues have been deferred.

The significant components of Other income (expense), net for the three months ended June 30, and the changes between the periods were as follows (in thousands):

| | 2017 | 2016 | Increase |
|---|--------|-------|----------|
| Rental income | \$ 198 | \$ 66 | \$ 132 |
| Foreign currency gains (losses), net | 110 | (7) | 117 |
| Interest income | 23 | 12 | 11 |
| Gain on disposals of equipment | 21 | (6) | 27 |
| Credit gains on available-for-sale securities | 3 | 3 | |
| Other, net | 5 | (4) | 9 |

| | | |
|--------|-------|--------|
| \$ 360 | \$ 64 | \$ 296 |
|--------|-------|--------|

During the second quarter of 2016, we began recognizing rental income under a new leasing agreement with a third party for the former Westcor facility. Our exposure to market risk fluctuations in foreign currency exchange rates relate primarily to the operations of VJCL, for which the functional currency is the Japanese Yen. The functional currency of all other subsidiaries in Europe and Asia is the U.S. Dollar. While our Vicor B.V. operation also potentially exposes us to exchange rate risk, as that subsidiary's sales are denominated in Euros and Pounds Sterling, any periodic gains or losses associated with exchange rate fluctuations are small, given the small U.S. Dollar value of shipments we make to Vicor B.V.

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Loss before income taxes was \$(178,000) for the second quarter of 2017, as compared to loss before taxes of \$(537,000) for the second quarter of 2016.

The provision for income taxes and the effective income tax rates for the second quarter of 2017 and the second quarter of 2016 were as follows (dollars in thousands):

| | 2017 | 2016 |
|----------------------------|--------|-------|
| Provision for income taxes | \$ 267 | \$ 13 |
| Effective income tax rate | 150.0% | 2.4% |

The provisions for income taxes in each 2017 and 2016 period were primarily due to estimated foreign income taxes and for estimated state taxes in jurisdictions in which we do not have net operating loss carryforwards. No tax benefit could be recognized for the majority of our losses during the periods due to a full valuation allowance against all net domestic deferred tax assets. The provision and effective income tax rate were higher in the second quarter of 2017 as we had previously recorded a tax benefit in the first quarter of 2017.

Net loss per share attributable to Vicor Corporation was \$(0.01) for the second quarter of 2017 and \$(0.01) for the second quarter of 2016.

Six months ended June 30, 2017, compared to six months ended June 30, 2016

Consolidated net revenues for the six months ended June 30, 2017 were \$112,171,000, an increase of \$13,203,000, or 13.3%, from \$98,968,000 for the six months ended June 30, 2016.

Net revenues, by segment, for the six months ended June 30, 2017 and the six months ended June 30, 2016 were as follows (dollars in thousands):

| | 2017 | 2016 | Increase (decrease) | |
|---------|------------|-----------|---------------------|--------|
| | | | \$ | % |
| BBU | \$ 76,612 | \$ 77,445 | \$ (833) | (1.1)% |
| VI Chip | 26,951 | 17,420 | 9,531 | 54.7% |
| Picor | 8,608 | 4,103 | 4,505 | 109.8% |
| Total | \$ 112,171 | \$ 98,968 | \$ 13,203 | 13.3% |

The overall increase in consolidated net revenues for the six months ended June 30, 2017 from the six months ended June 30, 2016 was primarily due to an overall 15.5% increase in bookings for the six months ended June 30, 2017, compared to the six months ended June 30, 2016. VI Chip and Picor bookings increased by 77.7% and 85.4%, respectively, while BBU bookings decreased 2.5%. The decrease in BBU revenues was primarily attributable to decreases in BBU module and configurable product revenues of approximately \$2,426,000, partially offset by an increase in Vicor Custom Power revenues of \$1,543,000. Increases in revenues recorded by VI Chip and Picor for the six months ended June 30, 2017 were associated largely with fulfillment of increased orders for our 48 volt to point-of-load solutions. Customer bookings and scheduling patterns continue to be unpredictable, particularly for the VI Chip and Picor segments.

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Gross margin for the six months ended June 30, 2017 increased \$5,795,000, or 13.2%, to \$49,582,000 from \$43,787,000 for the six months ended June 30, 2016, primarily due to the increase in net revenues. Despite the increase in net revenues, gross margin as a percentage of net revenues remained flat at 44.2% for the six month period ended June 30, 2017 compared to the six month period ended June 30, 2016, primarily due to a less favorable product mix.

Selling, general and administrative expenses were \$28,559,000 for the six months ended June 30, 2017, an increase of \$228,000, or 0.8%, compared to \$28,331,000 for the six months ended June 30, 2016. Selling, general and administrative expenses as a percentage of net revenues decreased to 25.5% for the six month period ended June 30, 2017 from 28.6% for the six month period ended June 30, 2016, primarily due to the increase in net revenues.

The components of the \$228,000 increase in selling, general and administrative expenses for the six months ended June 30, 2017 from the six months ended June 30, 2016 were as follows (dollars in thousands):

| | Increase (decrease) | |
|---------------------------------|---------------------|-------------|
| Compensation | \$ 395 | 2.3%(1) |
| Advertising expenses | 332 | 31.3%(2) |
| Stockholder reporting | 58 | 46.6% |
| Audit, tax, and accounting fees | (55) | (6.3)% |
| Outside services | (73) | (7.4)% |
| Commissions expense | (80) | (4.3)% |
| Telephone expense | (101) | (18.6)%(3) |
| Depreciation and amortization | (133) | (9.5)%(4) |
| Legal fees | (166) | (17.9)%(5) |
| Other, net | 51 | 1.6% |
| | \$ 228 | 0.8% |

- (1) Increase primarily attributable to annual compensation adjustments in May 2017.
- (2) Increase primarily attributed to increases in sales support expenses, direct mailings, and advertising in trade publications.
- (3) Decrease attributable to reduced service provider costs.
- (4) Decrease attributable to certain BBU segment fixed assets becoming fully depreciated during 2016.
- (5)

Decrease attributable to reduced activity associated with the patent infringement claims filed against the Company during the first quarter of 2011 by SynQor. See Note 9 to the Condensed Consolidated Financial Statements.

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Research and development expenses were \$22,939,000 for the six months ended June 30, 2017, an increase of \$1,453,000, or 6.8%, from \$21,486,000 for the six months ended June 30, 2016, primarily due to the increase in project and pre-production materials. As a percentage of net revenues, research and development expenses decreased to 20.5% for the six month period ended June 30, 2017 from 21.7% for the six month period ended June 30, 2016, primarily due to the increase in net revenues for the six months ended June 30, 2017 compared to the six months ended June 30, 2016.

The components of the \$1,453,000 increase in research and development expenses for the six months ended June 30, 2017 from the six months ended June 30, 2016 were as follows (dollars in thousands):

| | Increase (decrease) | |
|--------------------------------------|---------------------|-------------|
| Project and pre-production materials | \$ 1,324 | 47.4%(1) |
| Compensation | 891 | 6.0%(2) |
| Facilities expenses | 191 | 19.8%(3) |
| Outside services | (119) | (30.5%)(4) |
| Depreciation and amortization | (140) | (12.4%)(5) |
| Deferred costs | (679) | (560.6%)(6) |
| Other, net | (15) | (1.0)% |
| | \$ 1,453 | 6.8% |

- (1) Increase primarily attributable to increases in spending for new product development by the VI Chip segment.
- (2) Increase primarily attributable to annual compensation adjustments in May 2017.
- (3) Increase primarily attributable to an increase in utilities and building maintenance expenses.
- (4) Decrease primarily attributable to decreased use of outside contractors associated with the development of certain VI Chip products.
- (5) Decrease attributable to certain BBU segment fixed assets becoming fully depreciated during 2016.
- (6) Decrease primarily attributable to an increase in deferred costs capitalized for certain non-recurring engineering projects for which the related revenues have been deferred.

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The significant components of Other income (expense), net for the six months ended June 30, 2017 and the six months ended June 30, 2016 and the changes from period to period were as follows (in thousands):

| | 2017 | 2016 | Increase (decrease) |
|---|--------|--------|------------------------|
| Rental income | \$ 396 | \$ 66 | \$ 330 |
| Foreign currency gains, net | 204 | 48 | 156 |
| Interest income | 47 | 26 | 21 |
| Gain (loss) on disposals of equipment | 23 | (4) | 27 |
| Credit gains on available-for-sale securities | 6 | 7 | (1) |
| Other, net | 9 | (4) | 13 |
| | \$ 685 | \$ 139 | \$ 546 |

During the second quarter of 2016, we began recognizing rental income under a new leasing agreement with a third party for the former Westcor facility. Our exposure to market risk fluctuations in foreign currency exchange rates relate primarily to the operations of VJCL, for which the functional currency is the Japanese Yen. The functional currency of all other subsidiaries in Europe and Asia is the U.S. Dollar. While our Vicor B.V. operation also potentially exposes us to exchange rate risk, as that subsidiary's sales are denominated in Euros and Pounds Sterling, any periodic gains or losses associated with exchange rate fluctuations are small, given the small U.S. Dollar value of shipments we make to Vicor B.V.

Loss before income taxes was \$(1,231,000) for the six months ended June 30, 2017, as compared to loss before taxes \$(5,891,000) for the six months ended June 30, 2016.

The provision for income taxes and the effective income tax rates for the six months ended June 30, 2017 and the six months ended June 30, 2016 were as follows (dollars in thousands):

| | 2017 | 2016 |
|----------------------------|--------|-------|
| Provision for income taxes | \$ 168 | \$ 35 |
| Effective income tax rate | 13.6% | 0.6% |

The provisions for income taxes in each 2017 and 2016 period were primarily due to estimated foreign income taxes and for estimated state taxes in jurisdictions in which we do not have net operating loss carryforwards. No tax benefit could be recognized for the majority of our losses during the periods due to a full valuation allowance against all net

domestic deferred tax assets. In addition, in connection with our acquisition of 100% ownership of certain operating assets and cash of our consolidated subsidiary, Converpower Corporation, the related deferred tax liability for unremitted earnings of \$55,000 was reversed and recorded as a discrete benefit in the first quarter of 2016.

As described in Note 11- Impact of Recently Issued Accounting Standards, we adopted new guidance for employee share-based payment accounting during the first quarter of 2017. The new guidance, among other considerations, requires excess tax benefits and tax deficiencies related to employee share-based compensation to now be recorded in earnings when the awards vest or are settled, rather than in shareholders' equity under previous guidance. In addition, it eliminates the requirement that excess tax benefits be realized with the taxing authority before they can be recognized. In connection with the adoption of this new guidance, we recorded a cumulative-effect adjustment as of January 1, 2017 to increase gross deferred tax assets and the related valuation allowance against deferred tax assets by \$3,485,000. This amount was allocated and added to deferred tax assets for research and development tax credit carryforwards, net operating loss carryforwards and the alternative minimum tax credit carryforward but, as noted above, was fully offset by a corresponding increase in the valuation allowance against deferred tax assets, resulting in no net effect on our condensed consolidated financial statements.

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Net loss per share attributable to Vicor Corporation was \$(0.04) for the six months ended June 30, 2017, compared to net loss per share of \$(0.15) for the six months ended June 30, 2016.

Liquidity and Capital Resources

As of June 30, 2017, we had \$51,425,000 in cash and cash equivalents. The ratio of total current assets to total current liabilities was 3.9:1 as of June 30, 2017 and 5.0:1 as of December 31, 2016. Working capital, defined as total current assets less total current liabilities, decreased \$413,000 to \$89,132,000 as of June 30, 2017 from \$89,545,000 as of December 31, 2016.

The changes in working capital from December 31, 2016 to June 30, 2017 were as follows (in thousands):

| | Increase (decrease) |
|-----------------------------------|------------------------|
| Cash and cash equivalents | \$ (4,745) |
| Accounts receivable | 8,876 |
| Inventories, net | 3,378 |
| Other current assets | 617 |
| Accounts payable | (2,954) |
| Accrued compensation and benefits | (960) |
| Accrued expenses | (296) |
| Income taxes payable | 6 |
| Deferred revenue | (4,335) |
| | \$ (413) |

The primary uses of cash for the six months ended June 30, 2017 was for operating activities of \$703,000 and the purchase of equipment of \$5,631,000. The primary sources of cash for the six months ended June 30, 2017 was from proceeds from the issuance of Common Stock associated with the exercise of options for the purchase of shares of our Common Stock of \$1,769,000.

In November 2000, our Board of Directors authorized the repurchase of up to \$30,000,000 of our Common Stock (the November 2000 Plan). The November 2000 Plan authorizes us to make such repurchases from time to time in the open market or through privately negotiated transactions. The timing and amounts of Common Stock repurchases are at the discretion of management based on its view of economic and financial market conditions. We did not repurchase shares of Common Stock under the November 2000 Plan during the six months ended June 30, 2017. As of

June 30, 2017, we had approximately \$8,541,000 remaining under the November 2000 Plan.

Our primary liquidity needs are for making continuing investments in manufacturing equipment. We believe cash generated from operations and the total of our cash and cash equivalents will be sufficient to fund planned operations and capital equipment purchases for the foreseeable future. We had approximately \$5,526,000 of capital expenditure commitments, principally for manufacturing equipment, as of June 30, 2017.

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Item 3 Quantitative and Qualitative Disclosures About Market Risk

We are exposed to a variety of market risks, including changes in interest rates affecting the return on our cash and cash equivalents and fluctuations in foreign currency exchange rates. As our cash and cash equivalents consist principally of cash accounts and money market securities, which are short-term in nature, we believe our exposure to market risk on interest rate fluctuations for these investments is not significant. As of June 30, 2017, our long-term investment portfolio, recorded on our Condensed Consolidated Balance Sheet as Long-term investments, net, consisted of a single auction rate security with a par value of \$3,000,000, purchased through and held in custody by a broker-dealer affiliate of Bank of America, N.A., that has experienced failed auctions (the Failed Auction Security) since February 2008. While the Failed Auction Security is Aaa/AA+ rated by major credit rating agencies, collateralized by student loans and guaranteed by the U.S. Department of Education under the Federal Family Education Loan Program, continued failure to sell at its periodic auction dates (i.e., reset dates) could negatively impact the carrying value of the investment, in turn leading to impairment charges in future periods. Periodic changes in the fair value of the Failed Auction Security attributable to credit loss (i.e., risk of the issuer's default) are recorded through earnings as a component of Other income (expense), net, with the remainder of any periodic change in fair value not related to credit loss (i.e., temporary mark-to-market carrying value adjustments) recorded in Accumulated other comprehensive (loss) income, a component of Stockholders' Equity. Should we conclude a decline in the fair value of the Failed Auction Security is other than temporary, such losses would be recorded through earnings as a component of Other income (expense), net. We do not believe there was an other-than-temporary decline in value in this security as of June 30, 2017.

Our exposure to market risk for fluctuations in foreign currency exchange rates relates primarily to the operations of VJCL, for which the functional currency is the Japanese Yen, and changes in the relative value of the Yen to the U.S. Dollar. As the functional currency of all other subsidiaries in Europe and other subsidiaries in Asia is the U.S. Dollar, we believe risk to fluctuations in foreign currency exchange rates is not significant, as these operations do not incur material foreign exchange exposures.

Item 4 Controls and Procedures

(a) Disclosure regarding controls and procedures.

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the Exchange Act), management, with the participation of our Chief Executive Officer (CEO) (who is our principal executive officer) and Chief Financial Officer (CFO) (who is our principal financial officer), conducted an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the last fiscal quarter (i.e., June 30, 2017). The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure information required to be disclosed by a company in the reports it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow

timely decisions regarding required disclosure. Management recognizes any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of June 30, 2017, our CEO and CFO concluded, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

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

future conditions. Projections of any control's effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

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June 30, 2017

(b) Changes in internal control over financial reporting.

There was no change in our internal control over financial reporting that occurred during the fiscal quarter ended June 30, 2017, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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Part II Other Information

June 30, 2017

Item 1 Legal Proceedings

See Note 9. Commitments and Contingencies in the Notes to Condensed Consolidated Financial Statements in Part I, Item 1 Financial Statements.

Item 1A Risk Factors

There have been no material changes in the risk factors described in Part I, Item 1A Risk Factors of the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

Item 6 Exhibits

| Exhibit Number | Description |
|----------------|--|
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Exchange Act. |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Exchange Act. |
| 32.1 | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101 | The following material from the Company's Quarterly Report on Form 10-Q, for the quarter ended June 30, 2017, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets; (ii) the Condensed Consolidated Statements of Operations; (iii) the Condensed Consolidated Statements of Comprehensive Income (Loss); (iv) the Condensed Consolidated Statements of Cash Flows; and (v) the Notes to Condensed Consolidated Financial Statements. |

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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.

VICOR CORPORATION

Date: July 31, 2017

By: /s/ Patrizio Vinciarelli
Patrizio Vinciarelli
Chairman of the Board, President and
Chief Executive Officer
(Principal Executive Officer)

Date: July 31, 2017

By: /s/ James A. Simms
James A. Simms
Vice President, Chief Financial Officer
(Principal Financial Officer)