FORMFACTOR INC
Form 10-Q/A
July 20, 2004

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q/A
Amendment No. 1

(Mark one)

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

For the quarterly period ended March 27, 2004

or

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

For the transition period from to

Commission file number: 000-50307

FormFactor, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**13-3711155**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

2140 Research Drive, Livermore, California 94550

(Address of principal executive offices, including zip code)

(925) 294-4300

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

The number of shares of the registrant s common stock, par value $0.001 per share, outstanding as of April 30, 2004 was 37,466,484 shares.

FORMFACTOR, INC.

Explanatory Note

The Registrant is filing this Amendment No. 1 to its Quarterly Report on Form 10-Q for the period ended March 27, 2004 to amend and restate its Form 10-Q for the same period that it initially filed with the Securities and Exchange Commission on May 11, 2004. This Amendment No. 1 restates the Registrant s financial results for three months ended March 29, 2003 and March 27, 2004 to reflect a change in the amortization schedule of deferred stock-based compensation recorded in connection with its June 2003 initial public offering.

In connection with this adjustment, the Registrant reclassified a portion of the stock-based compensation expenses from operating expenses to cost of revenues and has revised its provision for income taxes accordingly. The aggregate amount of deferred stock-based compensation initially recorded remains unchanged.

The adjustment to the amortization schedule relates to pre-IPO refresh stock option grants issued in 2001 and 2002. These option grants were designed to add an additional year on to the vesting period of the employees existing option grant. This provides employees with consistent option compensation following full vesting of their original option grants, which generally occurs four years after grant. In connection with its IPO, the Registrant recorded $8.3 million of deferred stock based-compensation for these refresh grants to be amortized over their future one year vesting period. During the second quarter of 2004, the Registrant s independent auditors indicated that deferred stock based compensation relating to these refresh grants should have been amortized from the date of grant through the vesting period rather than during the vesting period. At the recommendation of its audit committee, the Registrant disclosed the matter to the SEC, Office of the Chief Accountant, to report and confirm that the amortization should begin from the grant date. The adjustment will result in higher stock-based compensation expense for the years fiscal 2001 through fiscal 2004, and lower stock-based compensation expense for fiscal 2005 through fiscal 2007 related to these refresh grants.

The restatement has no impact on the Company s net cash flows from operating activities or on the Registrant s cash and cash equivalents in the consolidated statements of cash flows for the periods restated.

Please see Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations and Note 11 to the Notes to Consolidated Financial Statements contained in this Amendment No. 1 for further information regarding the revisions to the Registrant s financial results.

This Amendment No. 1 amends and restates the following items of the initial filing of the Registrant s Form 10-Q: (i) Part I, Item 1 Unaudited Condensed Consolidated Financial Statements, (ii) Part I, Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations, (iii) Part I, Item 4 - Controls and Procedures, and (iv) Part II, Item 6 Exhibits and Reports on Form 8-K.

All information in the Registrant s Quarterly Report on Form 10-Q for the three months ended March 27, 2004, as amended by this Amendment No. 1, speaks as of the date of the original filing of the Registrant s Form 10-Q for such period and does not reflect any subsequent information or events, except as expressly noted in this Amendment No. 1 and except for Exhibits 31.01, 31.02 and 32.01. References to Annual Report and Form 10-K in this Amendment No. 1 refer to the Registrant s Annual Report on Form 10-K for the fiscal year ended December 27, 2003, as amended. References to Amendment No. 1, Quarterly Report and Form 10-Q in this Amendment No. 1, refer to the Registrant s quarterly report on Form 10-Q for the three months ended March 27, 2004, as amended.

All information contained in this Amendment No. 1 is subject to updating and supplementing as provided in the Registrant s reports filed with the Securities and Exchange Commission subsequent to the date of the filing of the

Registrant s Quarterly Report on Form 10-Q for the three months ended March 27, 2004, as amended.

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FORM 10-Q FOR THE QUARTERLY PERIOD ENDED MARCH 27, 2004

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PART I. FINANCIAL INFORMATION

Item 1. *Unaudited Condensed Consolidated Financial Statements*

FORMFACTOR, INC.

CONDENSED CONSOLIDATED INCOME STATEMENTS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended	
	March 29, 2003	March 27, 2004
	(As restated)	(As restated)
Revenues	$18,669	$37,118
Cost of revenues	9,800	18,026
Stock-based compensation	138	155
Gross margin	8,731	18,937
Operating expenses:		
Research and development(1)	3,525	4,349
Selling, general and administrative(1)	4,013	5,874
Stock-based compensation	636	552
Total operating expenses	8,174	10,775
Operating income	557	8,162
Interest income	162	533
Interest expense	(14)	
Other expense	(19)	(395)
	129	138
Income before income taxes	686	8,300
Provision for income taxes	(263)	(3,197)
Net income	$ 423	$ 5,103
Net income per share:		
Basic	$ 0.09	$ 0.14
Diluted	$ 0.01	$ 0.13
Weighted-average number of shares used in per share calculations:		
Basic	4,539	37,083
Diluted	29,070	40,231

(1) Amounts exclude stock-based compensation expense, as follows:		
Research and development	220	164
Selling, general and administrative	416	388
Total	$ 636	$ 552

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

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FORMFACTOR, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)
(Unaudited)

	December 27, 2003	March 27, 2004
	(As restated)	(As restated)
ASSETS		
Current assets:		
Cash and cash equivalents	$116,305	$ 99,232
Marketable securities	62,965	82,520
Accounts receivable, net of allowance for doubtful accounts of $103 in 2003 and 2004	19,698	26,375
Inventories, net	8,025	8,744
Deferred tax assets	2,825	2,773
Prepaid expenses and other current assets	2,744	2,756
Total current assets	212,562	222,400
Restricted cash	2,550	2,550
Property and equipment, net	20,495	27,374
Deferred tax assets	1,202	1,202
Other assets	356	349
Total assets	$237,165	$253,875
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 10,579	$ 15,334
Accrued liabilities	10,134	8,794
Deferred revenue and customer advances	1,005	1,278
Total current liabilities	21,718	25,406
Deferred revenue and customer advances	433	374
Total liabilities	22,151	25,780
Stockholders equity:		
Common stock, $0.001 par value	37	38
Additional paid-in capital	226,592	232,892
Notes receivable from stockholders	(661)	
Deferred stock-based compensation, net	(7,902)	(6,958)
Accumulated other comprehensive income (loss)	(4)	68
Retained earnings (accumulated deficit)	(3,048)	2,055
Total stockholders equity	215,014	228,095
Total liabilities and stockholders equity	$237,165	$253,875

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

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FORMFACTOR, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)
(Unaudited)

	Three Months Ended	
	March 29, 2003	**March 27, 2004**
	(As restated)	**(As restated)**
Cash flows from operating activities:		
Net income	$ 423	$ 5,103
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	1,281	1,380
Stock-based compensation expense	774	707
Deferred tax assets		52
Tax benefit from employee stock option plans		2,524
Interest income from stockholders notes receivable	(58)	
Provision for doubtful accounts	(50)	
Provision for excess and obsolete inventories	1,102	656
Loss on disposal of property and equipment	10	
Changes in assets and liabilities:		
Accounts receivable	1,731	(6,678)
Inventories	(1,901)	(1,376)
Prepaid and other current assets	(356)	(3)
Accounts payable	(1,641)	(1,951)
Accrued liabilities	(2,504)	(1,366)
Deferred revenues	(157)	213
Net cash used in operating activities	(1,346)	(739)
Cash flows from investing activities:		
Acquisition of property and equipment	(960)	(1,560)
Purchase of marketable securities	(2,810)	(31,060)
Proceeds from maturities of marketable securities	6,030	11,597
Restricted cash	2,835	
Other assets	10	
Net cash provided by (used in) investing activities	5,105	(21,023)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net	67	4,013
Repayment of notes receivable from stockholders	10	661
Repayment of notes payable	(125)	
Net cash provided by (used in) financing activities	(48)	4,674
Effect of exchange rate changes on cash and cash equivalents	12	15
Net increase (decrease) in cash and cash equivalents	3,723	(17,073)
Cash and cash equivalents, beginning of the period	26,786	116,305
Cash and cash equivalents, end of the period	$30,509	$ 99,232

Supplemental disclosure of significant non-cash investing activities:		
Purchases of property and equipment through accounts payable and accrued liabilities	$	$ 6,700

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

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FORMFACTOR, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
Three Months Ended March 27, 2004

Note 1 Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of FormFactor, Inc. and its subsidiaries (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission. Accordingly, the interim financial statements do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three months ended March 27, 2004 are not necessarily indicative of the results that may be expected for the year ending December 25, 2004, or for any other period. The balance sheet at December 27, 2003 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. These financial statements and notes should be read with the financial statements and notes thereto for the year ended December 27, 2003 included in the Company s annual report on Form 10-K/A for the year ended December 27, 2003 filed with the Securities and Exchange Commission.

Note 2 Significant Accounting Policies

The Company s significant accounting policies are disclosed in the Company s annual report on Form 10-K/A for the year ended December 27, 2003 filed with the Securities and Exchange Commission. The Company s significant accounting policies have not materially changed during the three months ended March 27, 2004.

Note 3 Inventories

Inventories are stated at the lower of cost (principally standard cost which approximates actual cost on a first-in, first-out basis) or market value. Reserves for potentially excess and obsolete inventory are made based on inventory levels and future sales forecasts.

Inventories, net of reserves, consisted of the following (in thousands):

	December 27, 2003	March 27, 2004
Raw materials	$3,128	$3,915
Work-in-progress	4,628	4,829
Finished goods	269	
	$8,025	$8,744

Note 4 Warranty

The Company offers warranties on certain products and records a liability for the estimated future costs associated with customer claims, which is based upon historical experience and the Company s estimate of the level of future costs. Warranty costs are reflected in the income statement as a cost of revenues. A

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FORMFACTOR, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

reconciliation of the changes in the Company s warranty liability for the three months ended March 27, 2004 follows (in thousands):

	Three Months Ended	
	March 29, 2003	March 27, 2004
Beginning balance	$ 679	$ 446
Reserve for warranties issued during the period	197	196
Settlements made during the period	(340)	(196)
Ending balance	$ 536	$ 446

Management believes that the accrual balance at March 27, 2004 is adequate to cover estimated future costs associated with warranty claims.

Note 5 Stock-Based Compensation

The Company uses the intrinsic value method of Accounting Principles Board Opinion No. 25 (APB No. 25), Accounting for Stock Issued to Employees, in accounting for its employee stock options, and presents disclosure of the pro forma information required under SFAS No. 123 (SFAS No. 123), Accounting for Stock-Based Compensation as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure. The Company uses the Black-Scholes option pricing model to compute its pro forma option expense.

Had compensation cost for the Company s stock option grants to employees been determined based on the fair values of the stock option at the date of grant consistent with the provisions of SFAS No. 123, the Company s net income would have been changed to the pro-forma amounts as follows:

	Three Months Ended	
	March 29, 2003	March 27, 2004
	(As restated)	(As restated)
	(In thousands, except per share amounts)	
Net income, as reported	$ 423	$5,103
Add: Stock-based employee compensation expense included in reported net income, net of tax	478	435
Deduct: Total stock-based employee compensation expense determined under minimum and fair value based methods for all awards, net of tax	(286)	(843)
Pro forma net income	$ 615	$4,695
Net income per share		
Basic:		
As reported	$0.09	$ 0.14
Pro forma	$0.14	$ 0.13

Diluted:		
As reported	$ 0.01	$ 0.13
Pro forma	$ 0.02	$ 0.12

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FORMFACTOR, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

The Company has adopted the disclosure only provisions of SFAS No. 123. Prior to the Company s initial public offering in June 2003, the Company calculated the fair value of each option on the date of grant using the minimum value method as prescribed by SFAS No. 123. Since June 12, 2003, the Company includes an expected volatility factor of 67% in addition to the factors prescribed in the following table in determining the fair value of all options granted. Therefore, the pro forma net income and pro forma net income per share may not be representative for future periods. The weighted-average assumptions used are as follows:

	Stock Options Three Months Ended		ESPP Three Months Ended
	March 29, 2003	March 27, 2004	March 27, 2004
Dividend yield			
Risk-free interest rate	3.03%	2.86%	0.89%
Expected life (in years)	5	5	0.5
Expected volatility		67%	67%

The weighted-average per share grant date fair value of options granted during the three months ended March 29, 2003 and March 27, 2004 was $0.90 and $11.44, respectively. The weighted-average per share estimated fair value of purchase rights granted under the 2002 Employee Stock Purchase Plan was $6.63 for the three months ended March 27, 2004.

Note 6 Net Income per Share

Basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted net income per share is computed giving effect to all potential dilutive common stock, including options, warrants, common stock subject to repurchase and redeemable convertible preferred stock.

A reconciliation of the numerator and denominator used in the calculation of basic and diluted net income per share follows:

	Three Months Ended	
	March 29, 2003	March 27, 2004
	(As restated)	(As restated)
	(In thousands)	
Numerator:		
Net income	$ 423	$ 5,103
Denominator:		
Weighted-average common stock outstanding	4,722	37,232
Less:		
Weighted-average shares subject to repurchase	(183)	(149)
Weighted-average shares used in computing basic net income per share	4,539	37,083
Dilutive potential common shares used in computing diluted net income per share	24,531	3,148

Total weighted-average number of shares used in computing diluted net income per share	29,070	40,231

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FORMFACTOR, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

The following outstanding options to purchase common stock and warrants were excluded from the computation of diluted net income per share as they had an antidilutive effect:

	March 29, 2003	March 27, 2004
	(In thousands)	
Options to purchase common stock	258	1,092
Warrants	46	

Note 7 Commitments and Contingencies

Legal Proceedings

From time to time, the Company may be subject to legal proceedings and claims in the ordinary course of business. As of the date of filing this quarterly report, the Company was not involved in any material legal proceedings, other than as set forth below.

On February 24, 2004, the Company filed in the Seoul Southern District Court, located in Seoul, South Korea, two separate complaints against Phicom Corporation, a Korean corporation, alleging infringement of a total of four Korean patents issued to the Company. One Complaint alleges that Phicom is infringing the Company s Korean Patent Nos. 252,457, entitled Method of Fabricating Interconnections Using Cantilever Elements and Sacrificial Substrates, and 324,064, entitled Contact Tip Structures for Microelectronic Interconnection Elements and Methods of Making Same. The other Complaint alleges Phicom is infringing the Company s Korean Patent Nos. 278,342, entitled Method of Altering the Orientation of Probe Elements in a Probe Card Assembly, and 399,210, entitled Probe Card Assembly. Both of the Complaints seek injunctive relief. The court actions are a part of the Company s ongoing efforts to protect the intellectual property embodied in its proprietary technology, including its MicroSpring interconnect technology. The Company has been advised that in March 2004, Phicom filed in the Korean Intellectual Property Office invalidity actions challenging the validity of each of the Company s four patents at issue. The Company could incur material expenses in these litigations.

Indemnification Obligations

The Company from time to time in the ordinary course of its business enters into contractual arrangements with third parties that include indemnification obligations. Under these contractual arrangements, the Company has agreed to defend, indemnify and hold the third party harmless from and against certain losses. These arrangements may limit the time within which an indemnification claim can be made, the type of the claim and the total amount that the Company can be required to pay in connection with the indemnification obligation. In addition, the Company has entered into indemnification agreements with its directors and officers, and the Company s bylaws contain indemnification obligations in favor of the Company s directors, officers and agents. It is not possible to determine or reasonably estimate the maximum potential amount of future payments under these indemnification obligations due to the varying terms of such obligations, the history of prior indemnification claims and the unique facts and circumstances involved in each particular contractual arrangement and in each potential future claim for indemnification. The Company has not had any requests for indemnification under these arrangements. The Company has not recorded any liabilities for these indemnification arrangements on the Company s condensed consolidated balance sheet as of March 27, 2004.

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FORMFACTOR, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

Note 8 Stockholders Equity

Comprehensive Income (Loss)

Comprehensive income (loss) includes foreign currency translation adjustments and unrealized gains (losses) on marketable securities, the impact of which has been excluded from net income and reflected as components of equity.

Components of accumulated other comprehensive income were as follows:

	Three Months Ended	
	March 29, 2003	March 27, 2004
	(As restated)	(As restated)
	(in thousands)	
Net income	$423	$5,103
Change in unrealized gain on marketable securities	47	92
Foreign currency translation adjustments	(51)	(20)
Comprehensive income	$419	$5,175

Components of accumulated comprehensive income (loss) were as follows:

	December 27, 2003	March 27, 2004
	(in thousands)	
Unrealized gain on marketable securities	$ 47	$139
Cumulative translation adjustments	(51)	(71)
Accumulated other comprehensive income (loss)	$ (4)	$ 68

Note 9 Derivative Financial Instruments

The Company purchases forward exchange contracts to hedge certain existing foreign currency denominated accounts receivable. These hedges do not qualify for hedge accounting treatment per the provisions of Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities. The Company recognizes gains or losses from the fluctuation in foreign exchange rates and the valuation of these hedge contracts in other expense. The Company does not use derivative financial instruments for trading or speculative purposes.

As of March 27, 2004, the Company had six forward exchange contracts outstanding, allowing the Company to sell 1.4 billion Yen for $12.7 million with contract rates ranging from 106.21 Yen to 112.06 Yen per U.S. dollar. These contracts are due between April and July 2004.

Note 10 Recent Accounting Pronouncements

In December 2003, the FASB issued a revised FASB Interpretation No. 46 (FIN 46R), Consolidation of Variable Interest Entities, an interpretation of ARB No. 51. The FASB published the revision to clarify and amend some of the original provisions of FIN 46, which was issued in January 2003, and to exempt certain entities from its requirements. A variable interest entity (VIE) refers to an entity subject to consolidation according to the provisions of this Interpretation. FIN 46R applies to entities whose equity investment at risk is insufficient to finance that entity s activities without receiving additional subordinated financial support provided by any parties, including equity holders, or where the equity investors (if any) do not have a controlling financial interest. FIN 46R provides that if an entity is the primary beneficiary of a VIE, the assets, liabilities, and results of operations of the VIE should be consolidated in the entity s financial statements. In addition, FIN 46R requires that both the primary beneficiary and all other enterprises with a significant variable interest in a VIE provide additional disclosures. The provisions of FIN 46R are effective for the Company s fiscal 2004 first quarter. The adoption of FIN46R did not have a material impact on the Company s financial position or on its results of operations.

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Note 11 Restatement of Financial Statements:

On July 20, 2004, the Company announced that it would restate its financial results for fiscal years 2001, 2002, 2003 and the three months ended March 27, 2004 to reflect an adjustment to the amortization schedule of deferred stock-based compensation recorded in connection with its June 2003 initial public offering. In connection with this adjustment, the Company reclassified a portion of the stock-based compensation expense from operating expenses to cost of revenues and has revised its provision for income taxes accordingly. The aggregate amount of deferred stock-based compensation initially recorded remains unchanged.

The adjustment to the amortization schedule relates to pre-IPO refresh stock option grants issued in 2001 and 2002. These option grants were designed to add an additional year on to the vesting period of the employees existing option grant. This provides employees with consistent option compensation following full vesting of their original option grants, which generally occurs four years after grant. In connection with its IPO, the Company recorded $8.3 million of deferred stock-based compensation for these refresh grants to be amortized over their future one year vesting period. During the second quarter of 2004, the Company s independent auditors indicated that deferred stock based compensation relating to these refresh grants should have been amortized from the date of grant through the vesting period rather than during the vesting period. At the recommendation of its audit committee, the Company disclosed the matter to the SEC, Office of the Chief Accountant, to report and confirm that the amortization should begin from the grant date. The adjustment will result in higher stock based compensation expense for the years fiscal 2001 through fiscal 2004, and lower stock-based compensation expense in fiscal 2005 through fiscal 2007 related to these refresh grants.

The periods affected by the restatement include fiscal years ended December 29, 2001, December 28, 2002, December 27, 2003 and the three months ended March 27, 2004.

The restatement has no impact on the Company s net cash flows from operating activities or on the Company s cash and cash equivalents in the consolidated statements of cash flows for the periods restated.

	Quarter Ended March 27, 2004	
	(As originally reported)	(As restated)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 99,232	$ 99,232
Marketable securities	82,520	82,520
Accounts receivable, net of allowance for doubtful accounts of $253 in 2002 and $103 in 2003	26,375	26,375
Inventories, net	8,744	8,744
Deferred tax assets	2,523	2,773
Prepaid expenses and other current assets	2,756	2,756
Total current assets	222,150	222,400
Restricted cash	2,550	2,550
Property and equipment, net	27,374	27,374
Deferred tax assets	398	1,202
Other assets	349	349

Total assets	$ 252,821	$ 253,875
LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND STOCKHOLDERS EQUITY		
Current liabilities:		
Bank line of credit	$	$
Notes payable, current portion		
Accounts payable	15,334	15,334
Accrued liabilities	9,032	8,794
Deferred revenue and customer advances	1,278	1,278
Total current liabilities	25,644	25,406
Notes payable, less current portion		
Deferred revenue and customer advances	374	374
Total liabilities	26,018	25,780
Redeemable convertible preferred stock, $0.001 par value: Authorized: 23,126,983 shares for 2002 and none in 2003 Issued and outstanding: 23,002,626 shares in 2002 and none in 2003 (Liquidation preferences: $66,263 at December 28, 2002 and none at December 27, 2003)		
Redeemable convertible preferred stock warrants		
Stockholders equity (deficit):		
Preferred stock, $0.001 par value: Authorized: 10,000,000 shares Issued and outstanding: none in 2002 and 2003		
Common stock, $0.001 par value: Authorized: 250,000,000 shares		
Issued and outstanding: 4,680,118 shares in 2002 and 36,808,906 shares in 2003	38	38
Additional paid-in capital	232,950	232,892
Deferred stock-based compensation, net	(10,623)	(6,958)
Accumulated other comprehensive loss	68	68
Accumulated deficit	4,370	2,055
Total stockholders equity	226,803	228,095
Total liabilities, redeemable convertible preferred stock and stockholders equity	$ 252,821	$ 253,875

Three Months Ended

	March 27, 2004 (As originally reported)	March 27, 2004 (As restated)
Revenues	$ 37,118	$ 37,118
Cost of revenues	18,026	18,026
Stock-based compensation		155
Gross margin	19,092	18,937
Operating expenses:		
Research and development	4,349	4,349
Selling, general and administrative	5,874	5,874
Stock-based compensation	409	552
Total operating expenses	10,632	10,775
Operating income	8,460	8,162
Interest income	533	533
Interest expense		
Other income (expense), net	(395)	(395)
	138	138
Income before income taxes	8,598	8,300
Provision for income taxes	(3,422)	(3,197)
Net income	$ 5,176	$ 5,103
Net income per share:		
Basic	$ 0.14	$ 0.14
Diluted	$ 0.13	$ 0.13
Weighted-average number of shares used in per share calculations:		
Basic	37,083	37,083

Diluted	40,042	40,231

	Three Months Ended	
	March 28, 2003	**March 28, 2003**
	(As originally reported)	**(As restated)**
Revenues	$ 18,669	$ 18,669
Cost of revenues	9,800	9,800
Stock-based compensation		138
Gross Margin	8,869	8,731
Operating expenses:		
Research and development	3,525	3,525
Selling, general and administrative	4,013	4,013
Stock-based compensation	333	636
Total operating expenses	7,871	8,174
Operating income	998	557
Interest income	162	162
Interest expense	(14)	(14)
Other income (expense), net	(19)	(19)
	129	129
Income before income taxes	1,127	686
Provision for income taxes	(428)	(263)
Net income	$ 699	$ 423
Net income per share:		
Basic	$ 0.15	$ 0.09
Diluted	$ 0.02	$ 0.01

Weighted-average number of shares used in per share calculations:		
Basic	4,539	4,539
Diluted	29,266	29,070

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

Cautionary Statement Regarding Forward-Looking Statements

This quarterly report on Form 10-Q/A contains forward-looking statements within the meaning of the Securities Exchange Act of 1934 and the Securities Act of 1933, which are subject to risks, uncertainties and assumptions that are difficult to predict. The forward-looking statements include statements concerning, among other things, our business strategy, including anticipated trends and developments in and management plans for our business and the markets in which we operate, financial results, operating results, revenues, gross margin, operating expenses, products, projected costs and capital expenditures, research and development programs, sales and marketing initiatives, and competition. In some cases, you can identify these statements by forward-looking words such as may, might, will, could, should, expect, plan, anticip believe, estimate, predict, intend and continue, the negative or plural of these words and other comparable terminology.

The forward-looking statements are only predictions based on our current expectations and our projections about future events. All forward-looking statements included in this quarterly report are based upon information available to us as of the filing date of this quarterly report. You should not place undue reliance on these forward-looking statements. We undertake no obligation to update any of these statements for any reason. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from those expressed or implied by these statements. These factors include the matters discussed in the section titled Risks That May Affect Future Results and elsewhere in this quarterly report. You should carefully consider the numerous risks and uncertainties described under Risks That May Affect Future Results.

The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and the accompanying notes contained in this quarterly report. Unless expressly stated or the context otherwise requires, the terms we, our, us and FormFactor refer to FormFactor, Inc. and its subsidiaries. The following discussion and analysis of our financial condition and results of operations have been revised to reflect the adjustments related to amortization of deferred stock-based compensation described in Note 11 of the Notes to Consolidated Financial Statements included in this Form 10-Q/A. Other than the revisions described in the preceding sentence, the following discussion and analysis, including the risk factors discussed under Risks That May Affect Future Results, do not reflect any information or events subsequent to March 27, 2004.

Overview

We design, develop, manufacture, sell and support precision, high performance advanced semiconductor wafer probe cards. Semiconductor manufacturers use our wafer probe cards to perform wafer probe test on the whole semiconductor wafer in the front end of the semiconductor manufacturing process. After the fabrication of a semiconductor wafer, the chips on the wafer are subject to wafer probe test. During wafer probe test, a wafer probe card is mounted in a prober, which is in turn connected to a semiconductor tester, and the wafer probe card is used as an interface to electrically connect with and test individual chips on a wafer. At the core of our product offering is our proprietary technology including our MicroSpring interconnect technology and proprietary design process. Our MicroSpring interconnect technology includes a resilient contact element manufactured at our production facilities in Livermore, California. To date, we have derived our revenues primarily from the sale of wafer probe cards incorporating our MicroSpring interconnect technology.

We work closely with our customers to design, develop and manufacture custom wafer probe cards. Each wafer probe card is a custom product that is specific to the chip and wafer designs of the customer. As a result, our revenue growth is driven by the number of new semiconductor designs, technology transitions and increased semiconductor production volumes.

Revenues. Wafer probe card sales comprise substantially all of our revenues. Increases in revenues have resulted from increased demand for our existing products, the introduction of new, more complex products and the penetration of new markets. Revenues from our customers are subject to both quarterly and annual fluctuations due to a number of issues, including design cycles, technology adoption rates and cyclicality of the different end markets into which our customers products are sold. We expect that revenues from the sale of wafer probe cards will continue to account for substantially all of our revenues for the foreseeable future.

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Cost of Revenues. Cost of revenues consists primarily of manufacturing materials, payroll and manufacturing-related overhead. In addition, cost of revenues also includes costs related to the start up of our new manufacturing facility. Our manufacturing operations rely upon a limited number of suppliers to provide key components and materials for our products, some of which are sole source. We order materials and supplies based on backlog and non-binding forecasted customer orders. Tooling and setup costs related to changing manufacturing lots at our suppliers are also included in the cost of revenues. We expense all warranty costs and inventory reserves or write-offs as cost of revenues. We design, manufacture and sell a custom product into a market that has been subject to cyclicality and significant demand fluctuations. Wafer probe cards are complex products, custom to a specific chip design and have to be delivered on lead-times shorter than most manufacturers cycle times. It is therefore common to start production and to acquire production materials ahead of the receipt of an actual purchase order. Wafer probe cards are manufactured in low volumes, therefore, material purchases are often subject to minimum purchase order quantities in excess of our actual demand. Inventory valuation adjustments for these factors are considered a normal component of cost of revenues.

Research and Development. Research and development expenses include expenses related to product development, engineering and material costs. All research and development costs are expensed as incurred. We plan to invest a significant amount in research and development activities to develop new technologies for current and new markets and new applications in the future.

Selling, General and Administrative. Selling, general and administrative expenses include expenses related to sales, marketing, and administrative personnel, internal and outside sales representatives commissions, market research and consulting, and other marketing, sales and administrative activities. We expect that selling expenses will increase as revenues increase, and we expect that general and administrative expenses will increase in absolute dollars to support future revenue growth, as well as from the additional costs of being a publicly traded company.

Stock-Based Compensation. In connection with the grant of stock options to employees in fiscal 2001 and fiscal 2002, and in fiscal 2003 through our initial public offering in June 2003, we recorded an aggregate of $14.3 million in deferred stock-based compensation. These options are considered compensatory because the fair value of our stock determined for financial reporting purposes is greater than the fair value determined on the date of the grant. As of March 27, 2004, we had an aggregate of $7.0 million of deferred stock-based compensation remaining to be amortized. This deferred stock-based compensation balance will be amortized as follows: $2.3 million during the remainder of fiscal 2004; $2.6 million during fiscal 2005; $1.5 million during fiscal 2006; and $591,000 during fiscal 2007. We are amortizing the deferred stock-based compensation on a straight line basis over the vesting period of the related options, which is generally four years. For options granted to employees to date, the amount of stock-based compensation amortization to be recognized in future periods could decrease if options for which deferred but unvested compensation has been recorded are forfeited.

Use of Estimates. Our discussion and analysis of our financial condition and results of operations are based upon our unaudited condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to uncollectible receivables, inventories, marketable securities, intangible assets, income taxes, warranty obligations, excess component and order cancellation costs, and contingencies and litigation. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

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Results of Operations

The following table sets forth our operating results as a percentage of revenues for the periods indicated:

	Three Months Ended	
	March 29, 2003	March 27, 2004
	(As restated)	(As restated)
Revenues	100.0%	100.0%
Cost of revenues	52.5	48.6
Stock-based compensation	0.7	0.4
Gross margin	46.8	51.0
Operating expenses:		
Research and development	18.9	11.7
Selling, general and administrative	21.5	15.8
Stock-based compensation	3.4	1.5
Total operating expenses	43.8	29.0
Operating income	3.0	22.0
Interest income	0.9	1.4
Interest expense	(0.1)	
Other expense	(0.1)	(1.1)
	0.7	0.3
Income before income taxes	3.7	22.3
Provision for income taxes	(1.4)	(8.6)
Net income	2.3%	13.7%

Three Months Ended March 27, 2004 and March 29, 2003

Revenues. Revenues for the three months ended March 27, 2004 were $37.1 million compared with $18.7 million for the three months ended March 29, 2003, an increase of $18.4 million, or 98.8%. The $18.4 million increase was due primarily to an increase of $17.9 million in revenues from DRAM manufacturers, an increase of $1.0 million from manufacturers of flash memory devices and an increase of $155,000 in other revenues, offset in part by a reduction of $600,000 in revenues generated from sales to flip chip logic manufacturers.

The majority of revenues for the three months ended March 27, 2004 was generated by sales of wafer probe cards to manufacturers of DRAM devices. Sales of wafer probe cards to test DRAM devices accounted for $28.8 million, or 77.5% of revenues, for the quarter ended March 27, 2004 compared to $10.9 million, or 58.5% of revenues, for the quarter ended March 29, 2003.

Revenues generated from sales to flash memory device manufacturers increased from $3.2 million for the quarter ended March 29, 2003 to $4.2 million for the quarter ended March 27, 2004. The increase was driven by continued bit growth and production ramp in the flash market as well as the continuous trend to higher parallelism wafer probe test of flash memory devices.

Revenues from manufacturers of flip chip logic devices decreased to $3.9 million for the three months ended March 27, 2004 from $4.5 million for the three months ended March 29, 2003. The decrease was primarily driven by the substantial completion of tooling cycles for some current production designs. The significant customer concentration for these products will continue to drive quarter to quarter cyclicality

from these tooling cycles.

Revenues by geographic region for the three months ended March 27, 2004 as a percentage of revenues were 40.4% in North America, 7.5% in Europe, 39.3% in Japan and 12.8% in Asia Pacific. Revenues by geographic region for the three months ended March 29, 2003 as a percentage of revenues were 52.4% in

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North America, 8.5% in Europe, 24.1% in Asia Pacific and 15.0% in Japan. For the three months ended March 27, 2004, revenues for all geographic regions increased due to strong demand for our wafer probe cards.

The following customers accounted for more than 10% of our revenues for the three months ended March 29, 2003 or March 27, 2004:

	Three Months Ended	
	March 29, 2003	March 27, 2004
Elpida	*%	34.3%
Intel Corporation	38.0	15.0
Micron Technologies Inc.	*	13.2
Spirox Corporation	18.7	12.0
Infineon Technologies AG	10.0	*

* Less than 10% of revenues.

Gross Margin. Gross margin as a percentage of revenues was 51.0% for the three months ended March 27, 2004 compared with 46.8% for the three months ended March 29, 2003. The increase in gross margin percentage was primarily due to increased revenues and product mix. During the quarter we incurred $340,000 of non-recurring expenses related to the bring up of our new manufacturing facility. Stock-based compensation reduced the gross margin by $155,000, or 0.4% of revenues in the three months ended March 27, 2004 compared to $138,000, or 0.7% of revenues in the three months ended March 29, 2003.

Research and Development. Research and development expenses increased to $4.3 million, or 11.7% of revenues, for the three months ended March 27, 2004 compared to $3.5 million, or 18.9% of revenues, for the three months ended March 29, 2003. The increase in absolute dollars was mainly due to increased personnel costs. Through the three month period ended March 27, 2004, we continued the development of our next generation parallelism product, fine pitch memory and logic products, advanced MicroSpring interconnect technology and new process technologies.

Selling, General and Administrative. Selling, general and administrative expenses were $5.9 million for the three months ended March 27, 2004, or 15.8% of revenues, compared to $4.0 million, or 21.5% of revenues, for the three months ended March 29, 2003. The increase in absolute dollars was mainly due to increased personnel related expenses and sales commissions driven by the increase in bookings and revenues and costs associated with being a public company.

Interest and Other Income (Expense), Net. Interest and other expense, for the three months ended March 27, 2004 was $138,000 compared with $129,000 for the three months ended March 29, 2003. We generated greater interest income in the first quarter of 2004 resulting from a larger cash, cash equivalents and marketable securities balance throughout the quarter as a result of our initial public offering and follow-on public offering in 2003, partially offset by foreign currency losses from the valuation of our outstanding foreign currency forward exchange contracts.

Provision for Income Taxes. Provision for income taxes was $3.2 million for the three months ended March 27, 2004 compared with $263,000 for the three months ended March 29, 2003. The $3.2 million provision for the first quarter of 2004 reflected an effective tax rate of 38.5% compared with an effective tax rate of 38.3% for the first quarter of 2003. The increase in the effective tax rate was primarily driven by the expiration of the current legislation for research and development credits.

Critical Accounting Policies and Estimates

For a description of the critical accounting policies that affect our more significant judgments and estimates used in the preparation of our condensed consolidated financial statements, refer to our annual report on Form 10-K filed with the Securities and Exchange Commission. There have been no changes to our critical accounting policies since March 27, 2004.

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Liquidity and Capital Resources

As of March 27, 2004, we had $184.3 million in cash, cash equivalents, marketable securities and restricted cash, compared with $181.8 million as of December 27, 2003.

Net cash used in operating activities was $739,000 for the three months ended March 27, 2004 compared with $1.3 million for the three months ended March 29, 2003. Net cash used in operating activities for the three months ended March 27, 2004 resulted primarily from an increase in accounts receivable partially offset by an increase in net income.

Accounts receivable increased by $6.7 million for the three months ended March 27, 2004 due to an increase in worldwide sales and specifically due to an increase in sales in Japan, where we typically experience longer payment terms. For the three months ended March 27, 2004, net inventories increased by $719,000 due to an increase in raw materials and work-in-process to support revenue growth. Accrued liabilities decreased by $1.1 million for the three month period ended March 27, 2004 due primarily to the payout of accrued employee incentive compensation.

Net cash used in investing activities was $21.0 million for the three months ended March 27, 2004, compared to net cash provided by investing activities of $5.1 million for the three months ended March 29, 2003. Net cash provided by or used in investing activities resulted primarily from the net purchase of marketable securities or maturity of marketable securities in each of these periods. Capital expenditures were $1.6 million for the three months ended March 27, 2004 and $960,000 for the three months ended March 29, 2003. The increase in capital expenditures was due primarily to our investment in our new manufacturing facility. For the three months ended March 27, 2004 we purchased $6.7 million of property and equipment through accrued liabilities.

Net cash provided by financing activities was $4.7 million for the three months ended March 27, 2004, compared with net cash used in financing activities of $48,000 for the three months ended March 29, 2003. Net cash provided by financing activities for the first quarter of 2004 was primarily due to the issuance of common stock upon exercises of stock options. Net cash used in financing activities for the first quarter of 2003 was primarily due to the repayment of notes payables, offset in part by the issuance of common stock.

In May 2001, we signed a ten-year lease for an additional 119,000 square feet of manufacturing, research and development and office space. The total rent obligation over the term of the lease is $21.8 million and is accounted for as an operating lease. We expect to invest approximately $25.0 million in leasehold improvements for our new headquarters and manufacturing facility through the third quarter of 2004. Of this amount, approximately $18.0 million relates to the design and construction of a new manufacturing facility, while the remaining amount relates to the build out and infrastructure of research and development and office space.

The following table describes our commitments to settle contractual obligations in cash as of March 27, 2004.

	Payments Due by Fiscal Year				
	2004	2005-2006	2007-2008	After 2008	Total
			(In thousands)		
Operating leases	$2,564	$5,056	$5,232	$11,160	$24,012

We believe that cash generated from operations, together with the liquidity provided by our existing cash, cash equivalents and marketable securities will be sufficient to meet our anticipated cash needs for at least the next 12 months. Our future capital requirements will depend on many factors, including our rate of revenue growth, the timing and extent of spending to support product development efforts, the expansion of sales and marketing activities, the timing and introductions of new products and enhancements to existing products, the costs to ensure access to adequate manufacturing capacity, including the build out of our new manufacturing facility, and the continuing market acceptance of our products.

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Off-Balance Sheet Arrangements

As part of our ongoing business, we do not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, or SPEs, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of March 27, 2004, we are not involved in any unconsolidated SPE transactions.

Recent Accounting Pronouncements

In December 2003, the FASB issued a revised FASB Interpretation No. 46, or FIN 46R, Consolidation of Variable Interest Entities, an interpretation of ARB No. 51. The FASB published the revision to clarify and amend some of the original provisions of FIN 46, which was issued in January 2003, and to exempt certain entities from its requirements. A variable interest entity, or VIE, refers to an entity subject to consolidation according to the provisions of this Interpretation. FIN 46R applies to entities whose equity investment at risk is insufficient to finance that entity s activities without receiving additional subordinated financial support provided by any parties, including equity holders, or where the equity investors (if any) do not have a controlling financial interest. FIN 46R provides that if an entity is the primary beneficiary of a VIE, the assets, liabilities, and results of operations of the VIE should be consolidated in the entity s financial statements. In addition, FIN 46R requires that both the primary beneficiary and all other enterprises with a significant variable interest in a VIE provide additional disclosures. The provisions of FIN 46R are effective for our fiscal 2004 first quarter. The adoption of FIN46R did not have a material impact on our financial position or on our results of operations.

Risks That May Affect Future Results

You should carefully consider the following risk factors, as well as the other information in this quarterly report on Form 10-Q, in evaluating FormFactor and our business. If any of the following risks actually occur, our business, financial condition and results of operations would suffer. In this case, the trading price of our common stock would likely decline and you might lose all or part of your investment in our common stock. The risks described below are not the only ones we face. Additional risks that we currently do not know about or that we currently believe to be immaterial may also impair our business operations.

Our operating results are likely to fluctuate, which could cause us to miss expectations about these results and cause the trading price of our common stock to decline.

Our operating results are likely to fluctuate. Some of the important factors that could cause our revenues and operating results to fluctuate from period-to-period include:

customer demand for our products;

our ability to deliver reliable, cost-effective products in a timely manner;

the reduction, rescheduling or cancellation of orders by our customers;

the timing and success of new product introductions and new technologies by our competitors and us;

our product and customer sales mix and geographical sales mix;

changes in the level of our operating expenses needed to support our anticipated growth;

a reduction in the price or the profitability of our products;

changes in our production capacity or the availability or the cost of components and materials;

our ability to transition efficiently and effectively to our new production facility;

our ability to bring new products into volume production efficiently;

the timing of and return on our investments in research and development;

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our ability to collect accounts receivable;

seasonality, principally due to our customers purchasing cycles; and

market conditions in our industry, the semiconductor industry and the economy as a whole.

The occurrence of one or more of these factors might cause our operating results to vary widely. As a result, we believe that you should not rely on period-to-period comparisons of our financial results as an indication of our future performance. If our revenues or operating results fall below the expectations of market analysts or investors, the market price of our common stock could decline substantially.

Cyclicality in the semiconductor industry historically has affected our sales and might do so in the future, and as a result we could experience reduced revenues or operating results.

The semiconductor industry has historically been cyclical and is characterized by wide fluctuations in product supply and demand. From time to time, this industry has experienced significant downturns, often in connection with, or in anticipation of, maturing product and technology cycles, excess inventories and declines in general economic conditions. This cyclicality could cause our operating results to decline dramatically from one period to the next. For example, our revenues in the three months ended March 29, 2003 declined by 15.7% compared to our revenues in the three months ended December 28, 2002. Our business depends heavily upon the development of new semiconductors and semiconductor designs, the volume of production by semiconductor manufacturers and the overall financial strength of our customers, which, in turn, depend upon the current and anticipated market demand for semiconductors and products, such as personal computers, that use semiconductors. If we are unable to adjust our levels of manufacturing and human resources or manage our costs and deliveries from suppliers in response to lower spending by semiconductor manufacturers, our gross margin might decline and cause us to experience decreased operating results or operating losses.

If we do not keep pace with technological developments in the semiconductor industry, our products might not be competitive and our revenues and operating results could suffer.

We must continue to invest in research and development to improve our competitive position and to meet the needs of our customers. Our future growth depends, in significant part, upon our ability to work effectively with and anticipate the testing needs of our customers, and on our ability to develop and support new products and product enhancements to meet these needs on a timely and cost-effective basis. Our customers testing needs are becoming more challenging as the semiconductor industry continues to experience rapid technological change driven by the demand for complex circuits that are shrinking in size and at the same time are increasing in speed and functionality and becoming less expensive to produce. Examples of recent trends driving demand for technological research and development include semiconductor manufacturers transitions to 110 nanometer and 90 nanometer technology nodes, to 512 megabit density devices and to Double Data Rate II, or DDR II, architecture devices. Our customers expect that they will be able to integrate our wafer probe cards into any manufacturing process as soon as it is deployed. Therefore, to meet these expectations and remain competitive, we must continually design, develop and introduce on a timely basis new products and product enhancements with improved features. Successful product design, development and introduction on a timely basis require that we:

design innovative and performance-enhancing features that differentiate our products from those of our competitors;

transition our products to new manufacturing technologies;

identify emerging technological trends in our target markets;

maintain effective marketing strategies;

respond effectively to technological changes or product announcements by others; and

adjust to changing market conditions quickly and cost-effectively.

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We must devote significant research and development resources to keep up with the rapidly evolving technologies used in semiconductor manufacturing processes. Not only do we need the technical expertise to implement the changes necessary to keep our technologies current, but we must also rely heavily on the judgment of our management to anticipate future market trends. If we are unable to timely predict industry changes, or if we are unable to modify our products on a timely basis, we might lose customers or market share. In addition, we might not be able to recover our research and development expenditures, which could harm our operating results.

If semiconductor memory device manufacturers delay, cancel and/or postpone the conversion to 300 mm wafers, our growth could be impeded.

The growth of our business for the foreseeable future depends in large part upon sales of our wafer probe cards to manufacturers of dynamic random access memory, or DRAM, and flash memory devices. The recent downturn in the semiconductor industry caused various chip manufacturers to readdress their respective strategies for converting existing 200 mm wafer fabrication facilities to 300 mm wafer fabrication, or for building new 300 mm wafer fabrication facilities. We believe that the decision to convert to a 300 mm wafer fabrication facility is made by each manufacturer based upon both internal and external factors, which could include considerations such as:

current and projected chip prices;

projected price erosion for the manufacturer s particular chips;

supply and demand issues;

overall manufacturing capability within the manufacturer s target market(s);

the availability of funds to the manufacturer;

the technology roadmap of the manufacturer; and

the price and availability of equipment needed within the 300 mm facility.

One or more of these internal and external factors, as well as other factors, including factors that a manufacturer may choose to not publicly disclose, can impact the decision to maintain a 300 mm conversion schedule, to delay the conversion schedule for a period of time, or to cancel the conversion. It is also possible that the conversion to 300 mm wafers will occur on different schedules for DRAM chip manufacturers and flash memory chip manufacturers. We have invested significant resources to develop technology that addresses the market for 300 mm wafers. If manufacturers of memory devices delay or discontinue the transition to 300 mm wafers, or make the transition more slowly than we currently expect, our growth and profitability could be impeded. In addition, any delay in large-scale adoption of manufacturing based upon 300 mm wafers would provide time for other companies to develop and market products that compete with ours, which could harm our competitive position.

We are subject to general economic and market conditions.

Our business is subject to the effects of general economic conditions in the United States and worldwide, and to market conditions in the semiconductor industry in particular. For example, in fiscal 2001, our operating results were adversely affected by unfavorable global economic conditions and reduced capital spending by semiconductor manufacturers. These adverse conditions resulted in a decrease in the demand for semiconductors and products using semiconductors, and in a sharp reduction in the development of new semiconductors and semiconductor designs. As a result, we experienced a decrease in the demand for our wafer probe cards. If such conditions occur again or other events occur that adversely impact general economic and market conditions, we could experience material negative effects on our business.

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We depend upon the sale of our wafer probe cards for substantially all of our revenues, and a downturn in demand for our products could have a more disproportionate impact on our revenues than if we derived revenues from a more diversified product offering.

Historically, we have derived substantially all of our revenues from the sale of our wafer probe cards. We anticipate that sales of our wafer probe cards will represent a substantial majority of our revenues for the foreseeable future. Our business depends in large part upon continued demand in current markets for, and adoption in new markets of, current and future generations of our wafer probe cards. Large-scale market adoption depends upon our ability to increase customer awareness of the benefits of our wafer probe cards and to prove their reliability, ability to increase yields and cost effectiveness. We may be unable to sell our wafer probe cards to certain potential customers unless those customers change their device test strategies, change their wafer probe card and capital equipment buying strategies, or change or upgrade their existing test equipment. We might not be able to sustain or increase our revenues from sales of our wafer probe cards, particularly if conditions in the semiconductor market deteriorate or if the market enters into another downturn in the future. Any decrease in revenues from sales of our wafer probe cards could harm our business more than it would if we offered a more diversified line of products.

If demand for our products in the memory device and flip chip logic markets declines or fails to grow as we anticipate, our revenues could decline.

We derive substantially all of our revenues from wafer probe cards that we sell to manufacturers of DRAM memory and flash memory devices and manufacturers of microprocessor, chipset and other logic devices. In the microprocessor, chipset and other logic device markets, our products are primarily used for devices employing flip chip packaging, which devices are commonly referred to as flip chip logic devices. In the three months ended March 27, 2004, sales to manufacturers of DRAM devices accounted for 77.5% of our revenues, sales to manufacturers of flip chip logic devices accounted for 10.5% of our revenues, and sales to manufacturers of flash memory devices accounted for 11.3% of our revenues. For fiscal 2003, sales to manufacturers of DRAM devices accounted for 61.3% of our revenues, sales to manufacturers of flip chip logic devices accounted for 19.1% of our revenues, and sales to manufacturers of flash memory devices accounted for 18.4% of our revenues. Our success depends in part upon the continued acceptance of our products within these markets and our ability to continue to develop and introduce new products on a timely basis for these markets. For example, the market might not accept an increasingly high parallelism wafer test solution.

A substantial portion of these semiconductor devices is sold to manufacturers of personal computers and computer-related products. The personal computer market has historically been characterized by significant fluctuations in demand and continuous efforts to reduce costs, which in turn have affected the demand for and price of DRAM devices and microprocessors. The personal computer market might not grow in the future at historical rates or at all and design activity in the personal computer market might decrease, which could negatively affect our revenues and operating results.

The markets in which we participate are intensely competitive, and if we do not compete effectively, our operating results could be harmed.

The wafer probe card market is highly competitive. With the introduction of new technologies and market entrants, we expect competition to intensify in the future. In the past, increased competition has resulted in price reductions, reduced gross margins or loss of market share, and could do so in the future. Competitors might introduce new competitive products for the same markets that our products currently serve. These products may have better performance, lower prices and broader acceptance than our products. In addition, for products such as wafer probe cards, semiconductor manufacturers typically qualify more than one source, to avoid dependence on a single source of supply. As a result, our customers will likely purchase products from our competitors. Current and potential competitors include Advantest Corporation, AMST Co., Ltd., Cascade Microtech, Inc., ESJ Corporation, Feinmetall GmbH, Japan Electronic Materials Corporation, Kulicke and Soffa Industries, Inc., Micronics Japan Co., Ltd., MicroProbe, Inc., NanoNexus Inc., Phicom Corporation, SCS Hightech, Inc., Tokyo Cathode Laboratory Co., Ltd. and Wentworth Laboratories, Inc.,

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among others. Many of our current and potential competitors have greater name recognition, larger customer bases, more established customer relationships or greater financial, technical, manufacturing, marketing and other resources than we do. As a result, they might be able to respond more quickly to new or emerging technologies and changes in customer requirements, devote greater resources to the development, promotion, sale and support of their products, and reduce prices to increase market share. Some of our competitors also supply other types of test equipment, or offer both advanced wafer probe cards and needle probe cards. Those competitors that offer both advanced wafer probe cards and needle probe cards might have strong, existing relationships with our customers or with potential customers. Because we do not offer a needle probe card or other conventional technology wafer probe card for less advanced applications, it may be difficult for us to introduce our advanced wafer probe cards to these customers and potential customers for certain wafer test applications. It is possible that existing or new competitors, including test equipment manufacturers, may offer new technologies that reduce the value of our wafer probe cards.

We derive a substantial portion of our revenues from a small number of customers, and our revenues could decline significantly if any major customer cancels, reduces or delays a purchase of our products.

A relatively small number of customers accounts for a significant portion of our revenues in any particular period. In the three months ended March 27, 2004, four customers accounted for 74.5% of our revenues. In fiscal 2003, four customers accounted for 66.2% of our revenues. Our ten largest customers accounted for 96.4% of our revenues in the three months ended March 27, 2004, and 93.5% of our revenues in fiscal 2003. We anticipate that sales of our products to a relatively small number of customers will continue to account for a significant portion of our revenues. The cancellation or deferral of even a small number of purchases of our products could cause our revenues to decline in any particular quarter. A number of factors could cause customers to cancel or defer orders, including manufacturing delays, interruptions to our customers operations due to fire, natural disasters or other events or a downturn in the semiconductor industry. Our agreements with our customers do not contain minimum purchase commitments, and our customers could cease purchasing our products with short or no notice to us or fail to pay all or part of an invoice. In some situations, our customers might be able to cancel orders without a significant penalty. In addition, the continuing trend toward consolidation in the semiconductor industry, particularly among manufacturers of DRAMs, could reduce our customer base and lead to lost or delayed sales and reduced demand for our wafer probe cards. Industry consolidation also could result in pricing pressures as larger DRAM manufacturers could have sufficient bargaining power to demand reduced prices and favorable nonstandard terms. Additionally, certain customers may not want to rely entirely or substantially on a single wafer probe card supplier and, as a result, such customers could reduce their purchases of our wafer probe cards.

If our relationships with our customers and companies that manufacture semiconductor test equipment deteriorate, our product development activities could be harmed.

The success of our product development efforts depends upon our ability to anticipate market trends and to collaborate closely with our customers and with companies that manufacture semiconductor test equipment. Our relationships with these customers and companies provide us with access to valuable information regarding manufacturing and process technology trends in the semiconductor industry, which enables us to better plan our product development activities. These relationships also provide us with opportunities to understand the performance and functionality requirements of our customers, which improve our ability to customize our products to fulfill their needs. Our relationships with test equipment companies are important to us because test equipment companies can design our wafer probe cards into their equipment and provide us with the insight into their product plans that allows us to offer wafer probe cards for use with their products when they are introduced to the market. Our relationships with our customers and test equipment companies could deteriorate if they:

become concerned about our ability to protect their intellectual property;

develop their own solutions to address the need for testing improvement;

regard us as a competitor;

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establish relationships with others in our industry; or

attempt to restrict our ability to enter into relationships with their competitors.

Many of our customers and the test equipment companies we work with are large companies. The consequences of a deterioration in our relationship with any of these companies could be exacerbated due to the significant influence these companies can exert in our markets. If our current relationships with our customers and test equipment companies deteriorate, or if we are unable to develop similar collaborative relationships with important customers and test equipment companies in the future, our long-term ability to produce commercially successful products could be impaired.

Because we generally do not have a sufficient backlog of unfilled orders to meet our quarterly revenue targets, revenues in any quarter are substantially dependent upon customer orders received and fulfilled in that quarter.

Our revenues are difficult to forecast because we generally do not have a sufficient backlog of unfilled orders to meet our quarterly revenue targets at the beginning of a quarter. Rather, a majority of our revenues in any quarter depends upon customer orders for our wafer probe cards that we receive and fulfill in that quarter. Because our expense levels are based in part on our expectations as to future revenues and to a large extent are fixed in the short term, we might be unable to adjust spending in time to compensate for any unexpected shortfall in revenues. Accordingly, any significant shortfall of revenues in relation to our expectations could hurt our operating results.

We rely upon a distributor for a substantial portion of our revenues, and a disruption in our relationship with our distributor could have a negative impact on our revenues.

We rely on Spirox Corporation, our distributor in Taiwan, Singapore and China, for a substantial portion of our revenues. Sales to Spirox accounted for 12.0% of our revenues in the three months ended March 27, 2004 and 13.4% of our revenues in fiscal 2003. Spirox also provides customer support. A reduction in the sales or service efforts or financial viability of our distributor, or deterioration in, or termination of, our relationship with our distributor could harm our revenues, our operating results and our ability to support our customers in the distributor s territory. In addition, establishing alternative sales channels in the region could consume substantial time and resources, decrease our revenues and increase our expenses.

If our relationships with our independent sales representatives change, our business could be harmed.

We currently rely on independent sales representatives to assist us in the sale of our products in various geographic regions. If we make the business decision to terminate or modify our relationships with one or more of our independent sales representatives, or if an independent sales representative decides to disengage from us, and we do not effectively and efficiently manage such a change, we could lose sales to existing customers and fail to obtain new customers.

If semiconductor manufacturers do not migrate elements of final test to wafer probe test, market acceptance of other applications of our technology could be delayed.

We intend to work with our customers to migrate elements of final test from the device level to the wafer level. This migration will involve a change in semiconductor test strategies from concentrating final test at the individual device level to increasing the amount of test at the wafer level. Semiconductor manufacturers typically take time to qualify new strategies that affect their testing operations. As a result, general acceptance of wafer-level final test might not occur in the near term or at all. In addition, semiconductor manufacturers might not accept and use wafer-level final test in a way that uses our technology. If the migration of elements of final test to wafer probe test does not grow as we anticipate, or if semiconductor manufacturers do not adopt our technology for their wafer probe test requirements, market acceptance of other applications for our technology could be delayed.

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Changes in test strategies, equipment and processes could cause us to lose revenues.

The demand for wafer probe cards depends in large part upon the number of semiconductor designs and the overall semiconductor unit volume. The time it takes to test a wafer depends upon the number of devices being tested, the complexity of these devices, the test software program and the test equipment itself. As test programs become increasingly effective and test throughput increases, the number of wafer probe cards required to test a given volume of devices declines. Therefore, advances in the test process could cause us to lose sales.

If semiconductor manufacturers implement chip designs that include increased built-in self-test capabilities, or similar functions or methodologies that increase test throughput, it could negatively impact our sales or the migration of elements of final test to the wafer level. Additionally, if new chip designs or types of chips are implemented that require less, or even no, test using wafer probe cards, our revenues could be impacted. Further, if new chip designs are implemented which we are unable to test, or which we are unable to test efficiently and provide our customers with an acceptably low overall cost of test, our revenues could be negatively impacted.

We incur significant research and development expenses in conjunction with the introduction of new product platforms. Because our customers use our water probe cards with test equipment manufactured by third parties, if we time one of our product introductions to the introduction of a new test equipment platform manufactured by a third party, any delay or disruption of the introduction of the new test equipment platforms would negatively affect our growth.

We manufacture all of our products at a single facility, and any disruption in the operations of that facility could adversely impact our business and operating results.

Our processes for manufacturing our wafer probe cards require sophisticated and costly equipment and a specially designed facility, including a semiconductor clean room. We manufacture all of our wafer probe cards at one facility located in Livermore, California. Any disruption in the operation of that facility, whether due to technical or labor difficulties, destruction or damage from fire or earthquake, infrastructure failures such as power or water shortage or any other reason, could interrupt our manufacturing operations, impair critical systems, disrupt communications with our customers and suppliers and cause us to write off inventory and to lose sales. In addition, if the recent energy crises in California that resulted in disruptions in power supply and increases in utility costs were to recur, we might experience power interruptions and shortages, which could disrupt our manufacturing operations. This could subject us to loss of revenues as well as significantly higher costs of energy. Further, current and potential customers might not purchase our products if they perceive our lack of an alternate manufacturing facility to be a risk to their continuing source of supply.

If we do not transition effectively to our new operations and manufacturing site, our manufacturing capacity will be negatively impacted.

We plan to move our manufacturing operations into a new facility in Livermore in 2004. The costs of starting up our new manufacturing facility, including capital costs such as equipment and fixed costs such as rent, will be substantial. We might not be able to shift from our current production facility to the new production facility efficiently or effectively. The transition will require us to have both our existing and new manufacturing facilities operational for several quarters, including into 2005. This will cause us to incur significant costs due to redundancy of infrastructure and the need to employ operations teams at both sites. Furthermore, the qualification of the new manufacturing facility will require us to use materials and build product and product components that will not be sold to our customers, causing higher than normal material spending. The transition might also lead to manufacturing interruptions, which could mean delayed deliveries or lost sales. Some or all of our customers could require a full qualification of our new facility. Any qualification process could take longer than we anticipate. Any difficulties with the transition or with bringing the new manufacturing facility to full capacity and volume production could increase our costs, disrupt our production process and cause delays in product delivery and lost sales, which would harm our operating results.

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If we are unable to manufacture our products efficiently, our operating results could suffer.

We must continuously modify our manufacturing processes in an effort to improve yields and product performance, lower our costs and reduce the time it takes us to design and produce our products. We will incur significant start-up costs associated with implementing new manufacturing technologies, methods and processes and purchasing new equipment, which could negatively impact our gross margin. We could experience manufacturing delays and inefficiencies as we refine new manufacturing technologies, methods and processes, implement them in volume production and qualify them with customers, which could cause our operating results to decline. The risk of encountering delays or difficulties increases as we manufacture more complex products. In addition, if demand for our products increases, we will need to expand our operations to manufacture sufficient quantities of products without increasing our production times or our unit costs. As a result of such expansion, we could be required to purchase new equipment, upgrade existing equipment, develop and implement new manufacturing processes and hire additional technical personnel. Further, new or expanded manufacturing facilities could be subject to qualification by our customers. In the past, we have experienced difficulties in expanding our operations to manufacture our products in volume on time and at acceptable cost. Any difficulties in expanding our manufacturing operations could cause product delivery delays and lost sales. If demand for our products decreases, we could have excess manufacturing capacity. The fixed costs associated with excess manufacturing capacity could cause our operating results to decline. If we are unable to achieve further manufacturing efficiencies and cost reductions, particularly if we are experiencing pricing pressures in the marketplace, our operating results could suffer.

If we are unable to continue to reduce the time it takes for us to design and produce a wafer probe card, our growth could be impeded.

Our customers continuously seek to reduce the time it takes them to introduce new products to market. The cyclicality of the semiconductor industry, coupled with changing demands for semiconductor devices, requires our customers to be flexible and highly adaptable to changes in the volume and mix of products they must produce. Each of those changes requires a new design and each new design requires a new wafer probe card. For some existing semiconductor devices, the manufacturers volume and mix of product requirements are such that we are unable to design, manufacture and ship products to meet such manufacturers relatively short cycle time requirements. If we are unable to reduce the time it takes for us to design, manufacture and ship our products in response to the needs of our customers, our competitive position could be harmed. If we are unable to meet a customer s schedule for wafer probe cards for a particular design, our customer might purchase wafer probe cards from a competitor and we might lose sales.

We obtain some of the components and materials we use in our products from a single or sole source or a limited group of suppliers, and the partial or complete loss of one of these suppliers could cause production delays and a substantial loss of revenues.

We obtain some of the components and materials used in our products, such as printed circuit board assemblies, plating materials and ceramic substrates, from a single or sole source or a limited group of suppliers. Alternative sources are not currently available for sole source components and materials. Because we rely on purchase orders rather than long-term contracts with the majority of our suppliers, we cannot predict with certainty our ability to obtain components and materials in the longer term. A sole or limited source supplier could increase prices, which could lead to a decline in our gross margin. Our dependence upon sole or limited source suppliers exposes us to several other risks, including a potential inability to obtain an adequate supply of materials, late deliveries and poor component quality. Disruption or termination of the supply of components or materials could delay shipments of our products, damage our customer relationships and reduce our revenues. For example, if we are unable to obtain an adequate supply of a component or material, we might have to use a substitute component or material, which could require us to make changes in our manufacturing process. From time to time in the past, we have experienced difficulties in receiving shipments from one or more of our suppliers, especially during periods of high demand for our products. If we cannot obtain an adequate supply of the components and materials we require, or do not receive them in a timely manner, we might be required to identify new suppliers. We might not be able to identify new suppliers

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on a timely basis or at all. Our customers and we would also need to qualify any new suppliers. The lead-time required to identify and qualify new suppliers could affect our ability to timely ship our products and cause our operating results to suffer. Further, a sole or limited source supplier could require us to enter into non-cancelable purchase commitments or pay in advance to ensure our source of supply. In an industry downturn, commitments of this type could result in charges for excess inventory of parts. If we are unable to predict our component and materials needs accurately, or if our supply is disrupted, we might miss market opportunities by not being able to meet the demand for our products.

Wafer probe cards that do not meet specifications or that contain defects could damage our reputation, decrease market acceptance of our technology, cause us to lose customers and revenues, and result in liability to us.

The complexity and ongoing development of our wafer probe card manufacturing process, combined with increases in wafer probe card production volumes, have in the past and could in the future lead to design or manufacturing problems. For example, the presence of contaminants in our plating baths has caused a decrease in our manufacturing yields or has resulted in unanticipated stress-related failures when our wafer probe cards are being used in the manufacturing test environment. Manufacturing design errors such as the miswiring of a wafer probe card or the incorrect placement of probe contact elements have caused us to repeat manufacturing design steps. In addition to these examples, problems might result from a number of factors, including design defects, materials failures, contamination in the manufacturing environment, impurities in the materials used, unknown sensitivities to process conditions, such as temperature and humidity, and equipment failures. As a result, our products have in the past contained and might in the future contain undetected errors or defects. Any errors or defects could:

cause lower than anticipated yields and lengthening of delivery schedules;

cause delays in product shipments;

cause delays in new product introductions;

cause us to incur warranty expenses;

result in increased costs and diversion of development resources;

cause us to incur increased charges due to unusable inventory;

require design modifications; or

decrease market acceptance or customer satisfaction with these products.

The occurrence of any one or more of these events could hurt our operating results.

In addition, if any of our products fails to meet specifications or has reliability, quality or compatibility problems, our reputation could be damaged significantly and customers might be reluctant to buy our products, which could result in a decline in revenues, an increase in product returns or warranty costs and the loss of existing customers or the failure to attract new customers. Our customers use our products with test equipment and software in their manufacturing facilities. Our products must be compatible with the customers equipment and software to form an integrated system. If the system does not function properly, we could be required to provide field application engineers to locate the problem, which can take time and resources. If the problem relates to our wafer probe cards, we might have to invest significant capital, manufacturing capacity and other resources to correct it. Our current or potential customers also might seek to recover from us any losses resulting from defects or failures in our products. Liability claims could require us to spend significant time and money in litigation or to pay significant damages.

If we fail to forecast demand for our products accurately, we could incur inventory losses.

Each semiconductor chip design requires a custom wafer probe card. Because our products are design-specific, demand for our products is difficult to forecast. Due to our customers short delivery time requirements, we often design, and at times produce, our products in anticipation of demand for our products

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rather than in response to an order. Due to the uncertainty inherent in forecasts, we are and expect to continue to be subject to inventory risk. If we do not obtain orders as we anticipate, we could have excess inventory for a specific customer design that we would not be able to sell to any other customer, which would likely result in inventory write-offs.

If we fail to effectively manage our regional service centers, our business might be harmed.

In 2002, we opened a regional repair and service center in Seoul, South Korea, and in 2003, we opened a regional repair and service center in Dresden, Germany. These regional service centers are part of our strategy to, among other things, provide our customers with more efficient service and repair of our wafer probe cards. If we are unable to effectively manage our regional service centers, or if the work undertaken in the regional service centers is not equivalent to the level and quality provided by repairs and services performed by our North American repair and service operations, which are part of our manufacturing facility in Livermore, California, we could incur higher wafer probe card repair and service costs, which could harm our operating results.

If we do not effectively manage changes in our business, these changes could place a significant strain on our management and operations and, as a result, our business might not succeed.

Our ability to grow successfully requires an effective planning and management process. We plan to increase the scope of our operations and the size of our direct sales force domestically and internationally. For example, we have leased a new facility in Livermore, California and plan to move our corporate headquarters and manufacturing operations into this facility in 2004. Our growth could place a significant strain on our management systems, infrastructure and other resources. To manage our growth effectively, we must invest the necessary capital and continue to improve and expand our systems and infrastructure in a timely and efficient manner. Those resources might not be available when we need them, which would limit our growth. Our officers have limited experience in managing large or rapidly growing businesses. In addition, the majority of our management has no experience in managing a public company or communicating with securities analysts and public company investors. Our controls, systems and procedures might not be adequate to support a growing public company. If our management fails to respond effectively to changes in our business, our business might not succeed.

If we fail to attract, integrate and retain qualified personnel, our business might be harmed.

Our future success depends largely upon the continued service of our key management, technical, and sales and marketing personnel, and on our continued ability to hire, integrate and retain qualified individuals, particularly engineers and sales and marketing personnel in order to increase market awareness of our products and to increase revenues. For example, in the future, we might need technical personnel experienced in competencies that we do not currently have or require. Competition for qualified individuals may be intense, and we might not be successful in retaining our employees or attracting new personnel. The loss of any key employee, the inability to successfully integrate replacement personnel, the failure of any key employee to perform in his or her current position or our inability to attract and retain skilled employees as needed could impair our ability to meet customer and technological demands. All of our key personnel in the United States are employees at-will. We have no employment contracts with any of our personnel in the United States.

We may make acquisitions, which could put a strain on our resources, cause ownership dilution to our stockholders and adversely affect our financial results.

While we have made no acquisitions of businesses, products or technologies in the past, we may make acquisitions of complementary businesses, products or technologies in the future. Integrating newly acquired businesses, products or technologies into our company could put a strain on our resources, could be expensive and time consuming, and might not be successful. Future acquisitions could divert our management s attention from other business concerns and expose our business to unforeseen liabilities or risks associated with entering new markets. In addition, we might lose key employees while integrating new organizations. Consequently, we might not be successful in integrating any acquired businesses, products or technologies, and

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might not achieve anticipated revenues and cost benefits. In addition, future acquisitions could result in customer dissatisfaction, performance problems with an acquired company, potentially dilutive issuances of equity securities or the incurrence of debt, contingent liabilities, possible impairment charges related to goodwill or other intangible assets or other unanticipated events or circumstances, any of which could harm our business.

As part of our sales process, we could incur substantial sales and engineering expenses that do not result in revenues, which would harm our operating results.

Our customers generally expend significant efforts evaluating and qualifying our products prior to placing an order. The time that our customers require to evaluate and qualify our wafer probe cards is typically between three and 12 months and sometimes longer. While our customers are evaluating our products, we might incur substantial sales, marketing, and research and development expenses. For example, we typically expend significant resources educating our prospective customers regarding the uses and benefits of our wafer probe cards and developing wafer probe cards customized to the potential customer s needs, for which we might not be reimbursed. Although we commit substantial resources to our sales efforts, we might never receive any revenues from a customer. For example, many semiconductor designs never reach production, including designs for which we have expended design effort and expense. In addition, prospective customers might decide not to use our wafer probe cards. The length of time that it takes for the evaluation process and for us to make a sale depends upon many factors including:

the efforts of our sales force and our distributor and independent sales representatives;

the complexity of the customer s fabrication processes;

the internal technical capabilities of the customer; and

the customer s budgetary constraints and, in particular, the customer s ability to devote resources to the evaluation process.

In addition, product purchases are frequently subject to delays, particularly with respect to large customers for which our products may represent a small percentage of their overall purchases. As a result, our sales cycles are unpredictable. If we incur substantial sales and engineering expenses without generating revenues, our operating results could be harmed.

From time to time, we might be subject to claims of infringement of other parties proprietary rights, or to claims that our intellectual property rights are invalid or unenforceable, which could result in significant expense and loss of intellectual property rights.

In the future, we might receive claims that we are infringing intellectual property rights of others, or claims that our patents or other intellectual property rights are invalid or unenforceable. We have received in the past, and may receive in the future, communications from third parties inquiring about our interest in licensing certain of their intellectual property or more generally identifying intellectual property that may be of interest to us. For example, we received such a communication from Microelectronics and Computer Technology Corporation in October 2001, with a follow-up letter in January 2002, inquiring about our interest in acquiring a license to certain of their patents and technology, and from IBM Corporation in February 2002, with a follow-up letter in August 2003, inquiring about our interest and need to acquire a license to IBM patents and technology related to high density integrated probes. We have not engaged in a dialog with Microelectronics and Computer Technology Corporation. We have engaged in a dialog with IBM regarding our companies respective intellectual property portfolios and technologies, and anticipate that this dialog will continue. In August 2002, subsequent to our initiating correspondence with Japan Electronic Materials Corporation regarding the scope of our intellectual property rights and the potential applicability of those rights to certain of its wafer probe cards, Japan Electronic Materials Corporation offered that precedent technologies exist as to one of our foreign patents that we had identified, and also referenced a U.S. patent in which it stated we might take interest. For the inquiries we have received to date, we do not believe we infringe any of the identified patents and technology. The semiconductor industry is characterized by uncertain and

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conflicting intellectual property claims and vigorous protection and pursuit of these rights. The resolution of any claims of this nature, with or without merit, could be time consuming, result in costly litigation or cause product shipment delays. In the event of an adverse ruling, we might be required to pay substantial damages, cease the use or sale of infringing products, spend significant resources to develop non-infringing technology, discontinue the use of certain technology or enter into license agreements. License agreements, if required, might not be available on terms acceptable to us or at all. The loss of access to any of our intellectual property or the ability to use any of our technology could harm our business.

If we fail to protect our proprietary rights, our competitors might gain access to our technology, which could adversely affect our ability to compete successfully in our markets and harm our operating results.

If we fail to protect our proprietary rights adequately, our competitors might gain access to our technology. Unauthorized parties might attempt to copy aspects of our products or to obtain and use information that we regard as proprietary. Others might independently develop similar or competing technologies or methods or design around our patents. In addition, the laws of many foreign countries in which we or our customers do business do not protect our intellectual property rights to the same extent as the laws of the United States. As a result, our competitors might offer similar products and we might not be able to compete successfully. We also cannot assure that:

- our means of protecting our proprietary rights will be adequate;
- patents will be issued from our currently pending or future applications;
- our existing patents or any new patents will be sufficient in scope or strength to provide any meaningful protection or commercial advantage to us;
- any patent, trademark or other intellectual property right that we own will not be invalidated, circumvented or challenged in the United States or foreign countries; or
- others will not misappropriate our proprietary technologies or independently develop similar technology, duplicate our products or design around any patent or other intellectual property rights that we own.

We might be required to spend significant resources to monitor and protect our intellectual property rights. We presently believe that it is likely that one or more of our competitors are using methodologies or have implemented structures into certain of their products that are covered by one or more of our intellectual property rights. On February 24, 2004, we filed in the Seoul Southern District Court, located in Seoul, South Korea, two separate complaints against Phicom Corporation, a Korean corporation, alleging infringement of a total of four Korean patents issued to FormFactor. One Complaint alleges that Phicom is infringing our Korean Patent Nos. 252,457, entitled Method of Fabricating Interconnections Using Cantilever Elements and Sacrificial Substrates, and 324,064, entitled Contact Tip Structures for Microelectronic Interconnection Elements and Methods of Making Same. The other Complaint alleges Phicom is infringing our Korean Patent Nos. 278,342, entitled Method of Altering the Orientation of Probe Elements in a Probe Card Assembly, and 399,210, entitled Probe Card Assembly. Both of the Complaints seek injunctive relief. The court actions are a part of our ongoing efforts to protect the intellectual property embodied in our proprietary technology, including our MicroSpring interconnect technology. We have been advised that in March 2004, Phicom filed in the Korean Intellectual Property Office invalidity actions challenging the validity of each of our four patents at issue. We could incur material expenses in these litigations. We may initiate other claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. If we threaten or initiate litigation, we may be subject to claims by third parties against which we must defend. Any litigation, whether or not it is resolved in our favor, could result in significant expense to us and divert the efforts of our technical and management personnel. In addition, many of our customer contracts contain provisions that require us to indemnify our customers for third party intellectual property infringement claims, which would increase the cost to us of an adverse ruling in such a claim. An adverse determination could also prevent us from licensing our technologies and methods to others.

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Our failure to comply with environmental laws and regulations could subject us to significant fines and liabilities, and new laws and regulations or changes in regulatory interpretation or enforcement could make compliance more difficult and costly.

We are subject to various and frequently changing U.S. federal, state and local, and foreign governmental laws and regulations relating to the protection of the environment, including those governing the discharge of pollutants into the air and water, the management and disposal of hazardous substances and wastes, the cleanup of contaminated sites and the maintenance of a safe workplace. We could incur substantial costs, including cleanup costs, civil or criminal fines or sanctions and third-party claims for property damage or personal injury, as a result of violations of or liabilities under environmental laws and regulations or non-compliance with the environmental permits required at our facilities.

For instance, in May 2003, we received a Notice of Violation from the Bay Area Air Quality Management District, or BAAQMD, regarding our record keeping relating to our usage of wipe cleaning solvent. We introduced corrective action to prevent any continued or recurrent record keeping violation, and we resolved the Notice of Violation with a monetary payment which was not significant. By way of further example, in December 2003, we received an Inspection Report from the Department of Toxic Substances Control, or DTSC, in connection with an inspection conducted in August 2003 of the Company s facilities. The DTSC Report reflects certain violations that had not been previously addressed by us in correspondence with the DTSC. We promptly took appropriate steps to address all of the violations noted, believe that all such violations were addressed, and sent correspondence to the DTSC confirming such corrective steps. At the present time it is not clear whether any monetary penalty will be imposed by the DTSC for the violations, and if so, the relative significance of the penalty. In January 2004, we received a Notice of Violation from the BAAQMD for Failure to Meet Permit Condition during a routine inspection of our facilities conducted by an Inspector with the Compliance & Enforcement Division of the BAAQMD. The January BAAQMD Notice reflects that we recently exceeded permissible usage limits on its solvent bench operations. The limit was exceeded only recently, in November 2003. We have identified appropriate corrective action and are also continuing our efforts to get the permit modified to reflect the current usage requirements. Notwithstanding our contemplated corrective action, the January BAAQMD Notice remains unresolved and we may be subject to a penalty based upon the unresolved January BAAQMD Notice. In view of the May BAAQMD Notice discussed above and the fact that a payment was associated with the resolution thereof, we presently believe that it is likely the January BAAQMD Notice will result in the imposition of a monetary penalty. At the present time it is not clear whether any monetary payment would be significant. In February 2004, a contractor at our manufacturing facility discharged certain diesel fuel mixed with water into a storm drain. We notified the appropriate agencies, assisted in their investigation and in the activities of a third party to assist with the cleanup activities. We have not yet been notified as to whether any financial penalties will be imposed based upon the incident and, if imposed, whether such penalties would be significant. It is possible that in the future, we may receive environmental violation notices, and that final resolution of the violations identified by these notices could harm our operating results.

These laws, regulations and permits also could require the installation of costly pollution control equipment or operational changes to limit pollution emissions or decrease the likelihood of accidental releases of hazardous substances. In addition, new laws and regulations, stricter enforcement of existing laws and regulations, the discovery of previously unknown contamination at our or others sites or the imposition of new cleanup requirements could require us to curtail our operations, restrict our future expansion, subject us to liability and cause us to incur future costs that would have a negative effect on our operating results and cash flow.

Because we conduct some of our business internationally, we are subject to operational, economic, financial and political risks abroad.

Sales of our products to customers outside the United States have accounted for an important part of our revenues. Our international sales as a percentage of our revenues were 59.6% for the three months ended March 27, 2004. In the future, we expect international sales, particularly into Europe, Japan, South Korea and Taiwan, to continue to account for a significant percentage of our revenues. Accordingly, we will be subject to

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risks and challenges that we would not otherwise face if we conducted our business only in the United States. These risks and challenges include:

- compliance with a wide variety of foreign laws and regulations;
- legal uncertainties regarding taxes, tariffs, quotas, export controls, export licenses and other trade barriers;
- political and economic instability in, or foreign conflicts that involve or affect, the countries of our customers;
- difficulties in collecting accounts receivable and longer accounts receivable payment cycles;
- difficulties in staffing and managing personnel, distributors and representatives;
- reduced protection for intellectual property rights in some countries;
- currency exchange rate fluctuations, which could affect the value of our assets denominated in local currency, as well as the price of our products relative to locally produced products;
- seasonal fluctuations in purchasing patterns in other countries; and
- fluctuations in freight rates and transportation disruptions.

Any of these factors could harm our existing international operations and business or impair our ability to continue expanding into international markets.

We might require additional capital to support business growth, and such capital might not be available.

We intend to continue to make investments to support business growth and may require additional funds to respond to business challenges, which include the need to develop new products or enhance existing products, enhance our operating infrastructure and acquire complementary businesses and technologies. Accordingly, we may need to engage in equity or debt financing to secure additional funds. Equity and debt financing, however, might not be available when needed or, if available, might not be available on terms satisfactory to us. If we are unable to obtain adequate financing or financing on terms satisfactory to us, our ability to continue to support our business growth and to respond to business challenges could be significantly limited.

Our reported financial results may be adversely affected by changes in accounting principles generally accepted in the United States.

We prepare our financial statements in conformity with accounting principles generally accepted in the United States. These accounting principles are subject to interpretation by the Financial Accounting Standards Board, the American Institute of Certified Public Accountants, the Securities and Exchange Commission and various bodies formed to interpret and create appropriate accounting principles. A change in these principles or interpretations could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of a change.

Recently enacted and proposed changes in securities laws and regulations are likely to increase our costs.

The Sarbanes-Oxley Act of 2002 that became law in July 2002, as well as new rules and regulations subsequently implemented by the Securities and Exchange Commission, have required changes to some of our corporate governance practices. The Act also requires the Securities and Exchange Commission to promulgate additional new rules on a variety of subjects. In addition to final rules and rule proposals already made by the Securities and Exchange Commission, Nasdaq has adopted revisions to its requirements for companies, such as us, that are Nasdaq-listed. We expect these new rules and regulations to increase our legal and financial compliance costs, and to make some activities more difficult, time consuming and/or costly and to make it more difficult and more expensive for us to obtain director and officer liability insurance. These new rules and

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regulations could also make it more difficult for us to attract and retain qualified members of our board of directors, particularly to serve on our audit committee, and qualified executive officers.

Unanticipated changes in our tax rates or exposure to additional income tax liabilities could affect our profitability.

We are subject to income taxes in both the United States and various foreign jurisdictions, and our domestic and international tax liabilities are subject to the allocation of expenses in different jurisdictions. Our effective tax rate could be adversely affected by changes in the mix of earnings in countries with different statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes in tax laws including pending tax law changes, such as the benefit from export sales and the research and development credit by material audit assessments. In particular, the carrying value of deferred tax assets, which are predominantly in the United States, is dependent on our ability to generate future taxable income in the United States. In addition, the amount of income taxes we pay could be subject to ongoing audits in various jurisdictions and a material assessment by a governing tax authority could affect our profitability.

The trading price of our common stock is likely to be volatile, and you might not be able to sell your shares at or above the price that you paid for them.

The trading prices of the securities of technology companies have been highly volatile. Accordingly, the trading price of our common stock is likely to be subject to wide fluctuations. Further, our securities have a limited trading history. Factors affecting the trading price of our common stock include:

variations in our operating results;

announcements of technological innovations, new products or product enhancements, strategic alliances or significant agreements by us or by our competitors;

recruitment or departure of key personnel;

the gain or loss of significant orders or customers;

changes in the estimates of our operating results or changes in recommendations by any securities analysts that elect to follow our common stock;

sales or perceived sales of substantial amounts of our common stock held by existing stockholders, including our directors and executive officers;

market conditions in our industry, the industries of our customers and the economy as a whole; and

sales or perceived sales of substantial amounts of common stock held by each stockholder.

In addition, if the market for technology stocks or the stock market in general experiences continued or greater loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, operating results or financial condition. The trading price of our common stock also might decline in reaction to events that affect other companies in our industry even if these events do not directly affect us.

If securities analysts do not publish research or reports about our business, our stock price could decline.

The trading market for our common stock will rely in part on the research and reports that industry or financial analysts publish about us or our business. We do not control these analysts. If one or more of the analysts who cover us downgrade our stock, our stock price would likely decline rapidly. If one or more of these analysts cease coverage of our company, we could lose visibility in the market, which in turn could cause our stock price to decline.

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The concentration of our capital stock ownership with insiders will likely limit your ability to influence corporate matters.

Our executive officers, directors, current 5% or greater stockholders and entities affiliated with any of them together beneficially own a large percentage of our outstanding common stock. As a result, these stockholders, acting together, have substantial influence over all matters that require approval by our stockholders, including the election of directors and approval of significant corporate transactions. As a result, corporate actions might be taken even if other stockholders, including you, oppose them. This concentration of ownership might also have the effect of delaying or preventing a change of control of our company that other stockholders may view as beneficial.

Our management has broad discretion over the use of our cash, cash equivalents and marketable securities and might not apply these current assets in ways that enhance our results of operations.

Our management has broad discretion to use our cash, cash equivalents and marketable securities, which include net proceeds from our initial public offering and follow-on public offering, and you will be relying on the judgment of our management regarding the application of these assets. We intend to use a portion of the net proceeds from our initial public offering for leasehold improvements at our new corporate headquarters and manufacturing facility. Although we expect our management to use the remaining assets for general corporate purposes, including working capital and for potential strategic investments or acquisitions, we have not allocated these assets for specific purposes. Our management might not be able to yield a significant return, if any, on any investment of these assets. Our management might not use efficiently our cash, cash equivalents and marketable securities or in a manner that enhances our operating results.

Provisions of our certificate of incorporation and bylaws or Delaware law might discourage, delay or prevent a change of control of our company or changes in our management and, therefore, depress the trading price of our common stock.

Delaware corporate law and our certificate of incorporation and bylaws contain provisions that could discourage, delay or prevent a change in control of our company or changes in our management that the stockholders of our company may deem advantageous. These provisions:

establish a classified board of directors so that not all members of our board are elected at one time;

provide that directors may only be removed for cause and only with the approval of 66 2/3% of our stockholders;

require super-majority voting to amend some provisions in our certificate of incorporation and bylaws;

authorize the issuance of blank check preferred stock that our board could issue to increase the number of outstanding shares and to discourage a takeover attempt;

limit the ability of our stockholders to call special meetings of stockholders;

prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;

provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and

establish advance notice requirements for nominations for election to our board or for proposing matters that can be acted upon by stockholders at stockholder meetings.

In addition, Section 203 of the Delaware General Corporation Law may discourage, delay or prevent a change in control of our company.

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Item 4. ***Controls and Procedures***

Disclosure Controls and Procedures

As required by Rule 13a-15(b) of the Securities Exchange Act of 1934, FormFactor management, including the Chief Executive Officer and Chief Financial Officer, conducted an evaluation as of the end of the period covered by this quarterly report on Form 10-Q, of the effectiveness of FormFactor s disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that as of March 27, 2004, FormFactor s disclosure controls and procedures were effective for ensuring that information required to be disclosed in the reports that FormFactor files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms. Pursuant to the Public Company Accounting Oversight Board s Auditing Standard No. 2, *An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements,* effective June 17, 2004, a restatement is by definition a significant deficiency in a company s internal control over financial reporting. This Amendment No. 1 to FormFactor s Quarterly Report on Form 10-Q restates its financial results for the three months ended March 27, 2004 to reflect a change in the amortization schedule of deferred stock-based compensation recorded in connection with its June 2003 public offering and to reflect a portion of the stock-based compensation amortization in cost of revenues.

Internal Control Over Financial Reporting

As required by Rule 13a-15(d) of the Securities Exchange Act of 1934, FormFactor management, including the Chief Executive Officer and Chief Financial Officer, also conducted an evaluation of FormFactor s internal control over financial reporting as defined in Exchange Act Rule 13a-15(f) to determine whether any changes in FormFactor s internal control over financial reporting occurred during the first quarter of 2004 that materially affected, or are reasonably likely to materially affect, FormFactor s internal control over financial reporting. Based on that evaluation, there has been no such change during the first quarter of fiscal 2004.

Limitation on Effectiveness of Controls

It should be noted that any system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system are met. The design of any control system is based, in part, upon the benefits of the control system relative to its costs. Control systems can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management

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override of the control. In addition, over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of these and other inherent limitations of control systems, there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

PART II. OTHER INFORMATION

Item 6. ***Exhibits and Reports on Form 8-K***

(a) *Exhibits*

The following exhibits are filed herewith:

Exhibit Number	Exhibit Description	Incorporated by Reference			Filed Herewith
		Form	Date	Number	
31.01	Certification of Chief Executive Officer pursuant to 15 U.S.C. Section 7241, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				X
31.02	Certification of Chief Financial Officer pursuant to 15 U.S.C. Section 7241, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				X
32.01*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				X

* This exhibit shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in any filings.

(b) *Reports on Form 8-K*

Date of Report	Item(s)	Description
January 20, 2004	7, 12	FormFactor announced financial results for the fourth quarter ended December 27, 2003 and fiscal year 2003.
January 29, 2004	5	FormFactor announced the date of its 2004 Annual Meeting of Stockholders and the deadline for submitting stockholder proposals.
February 24, 2004	5	FormFactor announced the filing in the Seoul Southern District Court, Seoul, South Korea, of two separate complaints against Phicom Corporation that allege infringement of a total of four Korean patents issued to FormFactor.
March 3, 2004	5	FormFactor announced that on March 2, 2004, several executive officers and other persons established Rule 10b5-1 plans under the Securities Exchange Act of 1934 to provide for pre-determined sales of a portion of their FormFactor common stock.

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SIGNATURE

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.

FORMFACTOR, INC.

By: /s/ JENS MEYERHOFF

Jens Meyerhoff
Chief Operating Officer and
Chief Financial Officer
(Principal Financial Officer and
Duly Authorized Officer)

July 20, 2004

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