ULTRA CLEAN HOLDINGS INC
Form 10-Q
August 02, 2013
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended June 28, 2013

or

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

For the transition period from to

Commission file number 000-50646

Ultra Clean Holdings, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**61-1430858**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
26462 Corporate Avenue, Hayward, California	**94545**
(Address of principal executive offices)	**(Zip Code)**

(510) 576-4400

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

Number of shares outstanding of the issuer s common stock as of July 26, 2013: 28,454,048

Table of Contents

ULTRA CLEAN HOLDINGS, INC.

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited; in thousands, except share amounts)

	June 28, 2013	December 28, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$ 71,333	$ 54,311
Accounts receivable, net of allowance of $5 and $8, respectively	47,070	50,074
Inventory	48,672	53,965
Prepaid expenses and other	6,838	6,769
Total current assets	173,913	165,119
Equipment and leasehold improvements, net	8,494	9,282
Goodwill	55,918	56,662
Purchased intangibles, net	24,761	27,702
Other non-current assets	6,244	7,164
Total assets	$ 269,330	$ 265,929
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Bank borrowings	$ 48,706	$ 48,706
Accounts payable	30,069	23,485
Accrued compensation and related benefits	5,048	4,611
Deferred rent, current portion	567	16
Other current liabilities	2,267	2,418
Total current liabilities	86,657	79,236
Long-term debt, net of current portion	19,677	26,934
Deferred rent and other liabilities	2,947	2,979
Total liabilities	109,281	109,149
Commitments and contingencies (See Note 8)		
Stockholders equity:		
Preferred stock $0.001 par value, 10,000,000 authorized; none outstanding		
Common stock $0.001 par value, 90,000,000 authorized; 28,434,650 and 27,910,851 shares issued and outstanding, in 2013 and 2012, respectively	144,444	143,180
Common shares held in treasury, at cost, 601,944 shares in 2013 and 2012	(3,337)	(3,337)
Retained earnings	18,942	16,937
Total stockholders equity	160,049	156,780

Total liabilities and stockholders equity	$ 269,330	$ 265,929

(See accompanying notes to condensed consolidated financial statements)

Table of Contents

ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited; in thousands, except per share data)

	Three months ended		Six months ended	
	June 28, 2013	June 29, 2012	June 28, 2013	June 29, 2012
Sales	$ 110,107	$ 101,949	$ 210,571	$ 212,514
Cost of goods sold	94,004	87,695	180,645	182,600
Gross profit	16,103	14,254	29,926	29,914
Operating expenses:				
Research and development	1,489	1,288	2,746	2,694
Sales and marketing	2,465	1,666	4,784	3,410
General and administrative	8,522	6,838	18,148	13,081
Total operating expenses	12,476	9,792	25,678	19,185
Income from operations	3,627	4,462	4,248	10,729
Interest and other income (expense), net	(730)	(14)	(1,687)	(119)
Income before provision for income taxes	2,897	4,448	2,561	10,610
Income tax provision	581	1,658	556	3,160
Net income	$ 2,316	$ 2,790	$ 2,005	$ 7,450
Net income per share:				
Basic	$ 0.08	$ 0.12	$ 0.07	$ 0.32
Diluted	$ 0.08	$ 0.12	$ 0.07	$ 0.31
Shares used in computing net income per share:				
Basic	28,370	23,292	28,172	23,289
Diluted	28,757	23,710	28,750	23,893

(See accompanying notes to condensed consolidated financial statements)

Table of Contents

ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited; in thousands)

	Six months ended June 28, 2013	Six months ended June 29, 2012
Cash flows from operating activities:		
Net income	$ 2,005	$ 7,450
Adjustments to reconcile net income to net cash provided operating activities:		
Depreciation	1,539	1,463
Amortization of intangibles	2,940	
Excess tax benefit from stock-based compensation	(101)	(30)
Amortization of debt issuance costs	243	
Stock-based compensation	2,320	2,649
Changes in assets and liabilities:		
Accounts receivable, net of allowance	3,004	(891)
Inventory	6,138	11,022
Prepaid expenses and other	(69)	(469)
Deferred income taxes net and other non-current assets	920	6
Accounts payable	6,543	(3,777)
Accrued compensation and related benefits	437	1,121
Other liabilities	(435)	1,775
Net cash provided by operating activities	25,484	20,319
Cash flows used in investing activities:		
Purchases of equipment and leasehold improvements	(710)	(216)
Net cash used in investing activities	(710)	(216)
Cash flows used in financing activities:		
Proceeds from revolving credit facility	28,000	19,482
Principal payments on revolving credit facility, term debt and capital lease obligations	(35,501)	(40,543)
Excess tax benefit from stock-based compensation	101	30
Employees taxes paid upon vesting of restricted stock units	(506)	(268)
Proceeds from issuance of common stock	154	178
Net cash used in financing activities	(7,752)	(21,121)
Net increase (decrease) in cash	17,022	(1,018)
Cash and cash equivalents at beginning of period	54,311	52,155
Cash and cash equivalents at end of period	$ 71,333	$ 51,137
Supplemental items:		
Cash paid during the period:		
Income taxes paid	$ 657	$ 1,716
Income tax refunds	$ (22)	$ (649)
Interest	$ 1,147	$ 167

Non-cash activities:				
Restricted stock issued	$	2,624	$	2,674
Fixed asset purchases in accounts payable	$	54	$	45

(See accompanying notes to condensed consolidated financial statements)

5

ULTRA CLEAN HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Organization and Significant Accounting Policies

Organization Ultra Clean Holdings, Inc. (the Company) is a leading developer and supplier of critical subsystems, primarily for the semiconductor capital equipment industry. The Company also leverages the specialized skill sets required to support semiconductor capital equipment to serve the technologically similar markets in the flat panel, medical, energy and research industries, collectively referred to as Other Addressed Industries . The Company develops, designs, prototypes, engineers, manufactures and tests subsystems which are highly specialized and tailored to specific steps in the semiconductor manufacturing process as well as the manufacturing processes in Other Addressed Industries. Revenue is derived from the sale of gas delivery systems and other critical subsystems including chemical mechanical planarization (CMP) subsystems, chemical delivery modules, top-plate assemblies, frame assemblies, process modules and other high level assemblies.

The Company s customers are primarily original equipment manufacturers (OEMs) in industries it supports, providing customers complete subsystem solutions that combine the Company s expertise in design, test, component characterization and highly flexible manufacturing operations with quality control and financial stability. This combination helps the Company to drive down total manufacturing costs, reduce design-to-delivery cycle times and maintain high quality standards for the Company s customers. The Company believes these characteristics, as well as the Company s standing as a leading supplier of gas delivery systems and other critical subsystems, place the Company in a strong position to benefit from the demand for subsystem outsourcing.

Basis of Presentation The unaudited condensed consolidated financial statements included in this quarterly report on Form 10-Q include the accounts of the Company and its wholly-owned subsidiaries and have been prepared in accordance with generally accepted accounting principles in the United States of America (GAAP). This financial information reflects all adjustments which are, in the opinion of the Company, normal, recurring and necessary to present fairly the statements of financial position, results of operations and cash flows for the dates and periods presented. Certain information and footnote disclosures normally included in our annual financial statements, prepared in accordance with GAAP, have been condensed or omitted. The Company s December 28, 2012, balance sheet data was derived from audited financial statements as of that date.

In July 2012, the Company completed its acquisition of American Integration Technologies LLC (AIT). Beginning in the third quarter of fiscal 2012, the acquired business is included in the Company s consolidated results of operations.

Principles of Consolidation The Company s condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and all intercompany accounts and transactions have been eliminated in consolidation.

Foreign Currency Translation The Company has reviewed its non-U.S. subsidiaries (of which all of its non-U.S. asset base resides in Asia) that operate in a local currency environment to determine their functional currency by examining how and in what currency each subsidiary generates cash through billings and cash receipts and how and in what currency the subsidiary expends cash through payment of its vendors and payment of its workforce. Also, these subsidiaries individual assets and liabilities that are primarily denominated in the local foreign currency are examined for their impact on the Company s cash flows. All have been determined to have the U.S. dollar as its functional currency. Foreign currency transaction gains and losses are recorded in other income (expense), net.

Use of Accounting Estimates The presentation of condensed financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company bases its estimates and judgments on historical experience and on various other assumptions that it believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Actual amounts may differ from those estimates.

Certain Significant Risks and Uncertainties The Company operates in a dynamic industry and, accordingly, can be affected by a variety of factors. For example, any of the following areas could have a negative effect on the Company in terms of its future financial position, results of operations or cash flows: the general state of the U.S. and world economies, the highly cyclical nature of the industries the Company serves; the loss of any of a small number of customers; ability to obtain additional financing; inability to meet certain debt covenants; failure to successfully integrate completed acquisitions; ineffectiveness in pursuing acquisition opportunities; regulatory changes; fundamental changes in the technology underlying semiconductor, flat panel, solar and medical device manufacturing processes or manufacturing equipment; the hiring, training and retention of key employees; successful and timely completion of product design efforts; and new product design introductions by competitors.

Concentration of Credit Risk Financial instruments which subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and accounts receivable. The Company sells its products primarily to semiconductor capital equipment manufacturers in the United States. The Company performs credit evaluations of its customers financial condition and generally requires no collateral.

Significant sales to customers The Company had significant sales to three customers, each of which accounted for 10% or more of sales for the six months ended June 28, 2013. The Company had significant sales to two customers, each of which accounted for 10% or more of sales for the six months ended June 29, 2012. Sales to each of these customers as a percentage of total sales were as follows:

	Six months ended	
	June 28, 2013	**June 29, 2012**
Applied Materials, Inc.	33.2%	44.5%
Lam Research Corporation (1)	31.0%	37.7%
ASM International (2)	14.8%	
Total	79.1%	82.2%

(1) In June 2012, Lam Research Corporation completed the acquisition of Novellus Systems, Inc., one of the Company s customers. The sales percentages for Lam Research Corporation for the six months ended June 29, 2012, have been updated to reflect the inclusion of sales to Novellus Systems, Inc., for comparison purposes.

(2) Sales to ASM International are the result of the Company s acquisition of AIT during the third quarter of 2012, and, therefore, there were no sales to ASM International during the same period of the prior year.

Three customers accounts receivable balances- Applied Materials, Inc., Lam Research Corporation and ASM International- were individually greater than 10% of accounts receivable as of June 28, 2013, and, in the aggregate, represented approximately 78% of accounts receivable. Three customers accounts receivable balances- Applied Materials, Inc., Lam Research Corporation and ASM International- were individually greater than 10% of accounts receivable as of December 28, 2012 and, in the aggregate, represented approximately 84% of accounts receivable.

Fair Value of Financial Instruments-The Company s financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and bank borrowings. The carrying value of cash and cash equivalents, accounts receivable and accounts payable approximates their fair value because of their short-term nature.

The accounting guidance for fair value measurements prioritizes the inputs used in measuring fair value in the following hierarchy:

Level I Quoted prices in active markets for identical assets or liabilities,

Level 2 Observable inputs other than the Level I prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of assets or liabilities,

Level 3 Unobservable inputs in which there is little or no market data, and that are significant to the fair value of the assets or liabilities.

The Company s only financial asset measured at fair value on a recurring basis is an overnight sweep account invested in money market funds which are presented as cash and cash equivalents with a carrying value and fair value of $31.9 million at June 28, 2013, based on Level 2 inputs. The Company s only financial liability measured at fair value is our credit facility. Specifically, our long term debt was based on level 2 inputs and fair value was determined using quoted prices for similar liabilities in inactive markets and our outstanding borrowings under our revolving credit facility were based on level 2 inputs and fair value was determined using inputs other than quoted prices that are observable, specifically, discounted cash flows of expected payments at current borrowing rates. Our carrying value approximates fair value for our long term debt and revolving credit facility.

Fiscal Year The Company uses a 52-53 week fiscal year ending on the Friday nearest December 31. All references to quarters refer to fiscal quarters and all references to years refer to fiscal years.

Income Taxes The Company utilizes the asset and liability method of accounting for income taxes, under which deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the basis differences reverse. A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets will not be realized.

Income tax positions must meet a more-likely-than-not recognition threshold to be recognized. Income tax positions that previously failed to meet the more-likely-than-not threshold are recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met. The Company recognizes potential accrued interest and penalties related to unrecognized tax benefits within the consolidated statements of income as income tax expense.

The determination of the Company s tax provision is subject to judgments and estimates. The carrying value of the Company s net deferred tax assets, which is made up primarily of tax deductions, assumes it will be able to generate sufficient future income to fully realize these deductions. In determining whether the realization of these deferred tax assets may be impaired, the Company makes judgments with respect to whether it is likely to generate sufficient future taxable income to realize these assets. The Company has a valuation allowance on the deferred tax assets of one of its China subsidiaries in the amount of $851,000 as of June 28, 2013 and December 28, 2012.

The calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of complex tax laws. Resolution of these uncertainties in a manner inconsistent with the Company s expectations could have a material impact on its results of operations and financial position. Management believes that it has adequately provided for any adjustments that may result from these examinations, however, the outcome of tax audits cannot be predicted with certainty.

Product Warranty The Company provides a warranty on its products for a period of up to two years and provides for warranty costs at the time of sale based on historical activity. The determination of such provisions requires the Company to make estimates of product return rates and expected costs to repair or replace the products under warranty. If actual return rates and/or repair and replacement costs differ significantly from these estimates, adjustments to cost of sales may be required in future periods. Components of the reserve for warranty costs consisted of the following (in thousands):

	Six months ended	
	June 28, 2013	**June 29, 2012**
Beginning balance	$ 152	$ 350
Change in reserve	30	58
Warranty claims	(77)	(83)
Ending balance	$ 105	$ 325

Revenue Recognition Product revenue is generally recorded upon shipment. In arrangements which specify title transfer upon delivery, revenue is not recognized until the product is delivered. The Company recognizes revenue when persuasive evidence of an arrangement exists, shipment has occurred, price is fixed or determinable and collectability is reasonably assured. If the Company has not substantially completed a product or fulfilled the terms of a sales agreement at the time of shipment, revenue recognition is deferred until fulfillment. The Company s standard arrangement for its customers includes a signed purchase order or contract, no right of return of delivered products and no customer acceptance provisions.

The Company assesses collectability based on the credit worthiness of the customer and past transaction history. The Company performs on-going credit evaluations of customers and generally does not require collateral from customers.

Research and Development Costs Research and development costs are expensed as incurred.

Net Income (loss) per Share Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of shares outstanding for the period. Diluted net income (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding and common equivalent shares from dilutive stock options and restricted stock using the treasury stock method, except when such shares are anti-dilutive (see Note 7 to Condensed Consolidated Financial Statements).

Comprehensive Income (Loss) The Company reports by major components and as a single total, the change in its net assets during the period from non-owner sources. Comprehensive income (loss) for all periods presented was the same as net income (loss).

Segments The Financial Accounting Standards Board s (FASB) guidance regarding disclosure about segments in an enterprise and related information establishes standards for the reporting by public business enterprises of information about reportable segments, products and services, geographic areas, and major customers. The method for determining what information to report is based on the manner in which management organizes the reportable segments within the Company for making operational decisions and assessments of financial performance. The Company s chief operating decision-maker is considered to be the Chief Executive Officer. The Company operates in one reporting segment.

Business Combinations The Company recognizes assets acquired (including goodwill and identifiable intangible assets) and liabilities assumed at fair value on the acquisition date. Subsequent changes to the fair value of such assets acquired and liabilities assumed are recognized in earnings, after the expiration of the measurement period, a period not to exceed 12 months from the acquisition date. Acquisition-related expenses and acquisition-related restructuring costs are recognized in earnings in the period in which they are incurred.

Stock-Based Compensation Expense

The Company maintains stock-based compensation plans which allow for the issuance of equity-based awards to executives and certain employees. These equity-based awards include stock options, restricted stock awards and restricted stock units which can be either time-based or performance-based. The Company also maintains an employee stock purchase plan that provides for the issuance of shares to all eligible employees of the Company at a discounted price.

Stock-based compensation expense includes compensation costs related to estimated fair values of stock options and awards granted. The estimated fair value of the Company s equity-based awards, net of expected forfeitures, is amortized over the awards vesting period on a straight-line basis over a weighted average period of four years for stock options (three years for restricted stock units and one year for restricted stock awards) and will be adjusted for subsequent changes in estimated forfeitures and future option grants.

The Company applies the fair value recognition provisions based on the FASB s guidance regarding *stock-based compensation*. The exercise price of each stock option equals the market price of the Company s stock on the date of grant. The estimated fair value of the Company s equity-based awards, less expected forfeitures, is amortized over the awards vesting periods on a straight-line basis over the applicable vesting period and will be adjusted for subsequent changes in estimated forfeitures and future option grants. Most options are scheduled to vest over four years and expire no later than ten years from the grant date. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. The determination of the fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company s stock price as well as assumptions regarding a number of complex and subjective variables. These variables include the expected term of the awards; the Company s expected stock price volatility over the term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate and expected dividends. The Company estimates the expected term of share-based awards granted based on the Company s historical option term experience. The Company estimates the volatility of its common stock based upon the Company s historical stock price volatility over the length of the expected term of the options. The Company bases the risk-free interest rate that it uses in the option valuation model on U.S. Treasury zero-coupon issues with remaining maturities similar to the expected term of the options. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore uses an expected dividend yield of zero in the option valuation model. The Company is required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures and records share-based compensation expense only for those awards that are expected to vest. The Company also considers, each quarter, whether there have been any significant changes in facts and circumstances that would affect its forfeiture rate.

Stock Options

The following table summarizes information with respect to options granted, exercised and canceled in the six months ended June 28, 2013 and outstanding at June 28, 2013:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at December 28, 2012	1,514,113	$ 6.98	4.0	$ 1,444,653
Granted				
Exercised	(66,243)	$ 1.19		
Canceled	(8,673)	$ 8.74		
Outstanding at June 28, 2013	1,439,197	$ 7.23	3.4	$ 1,793,435
Vested and expected to vest at June 28, 2013	1,439,146	$ 7.23	3.4	$ 1,793,378
Vested and exercisable at June 28, 2013	1,434,216	$ 7.24	3.4	$ 1,784,377

8

There were no options granted by the Company during either of the six month periods ended June 28, 2013 and June 29, 2012.

The total unamortized expense of the Company s unvested options, net of forfeitures, as of June 28, 2013, was less than $0.1 million.

Employee Stock Purchase Plan

The Company also maintains an employee stock purchase plan (ESPP) that provides for the issuance of shares to all eligible employees of the Company at a discounted price. Under the ESPP, substantially all employees may purchase the Company s common stock through payroll deductions at a price equal to 95 percent of the fair market value of the Company s stock at the end of each applicable purchase period.

Restricted Stock Units and Restricted Stock Awards

The Company grants Restricted Stock Units (RSU s) to employees and Restricted Stock Awards (RSA) to non-employee directors as part of the Company s long term equity compensation plan.

Restricted Stock Units RSU s are granted to employees with a per share or unit purchase price of zero dollars and either have time based or performance based vesting. RSU s typically vest over three years, subject to the employee s continued service with the Company. For purposes of determining compensation expense related to these RSU s, the fair value is determined based on the closing market price of the Company s common stock on the date of RSU grant. The expected cost of the grant is reflected over the service period, and is reduced for estimated forfeitures. The Company granted 193,200 RSU s during the quarter ended March 29, 2013, with a weighted average fair value of $5.39 per share and the Company granted 548,900 RSU s (including 110,375 performance stock units) during the quarter ended March 30, 2012, with a weighted average fair value of $8.21 per share. The Company granted 408,000 RSU s (including 152,750 performance stock units) during the quarter ended June 28, 2013, with a weighted average fair value of $6.06 per share and granted 4,450 RSU s during the quarter ended June 29, 2012, with a weighted average fair value of $6.41 per share. During the six months ended June 28, 2013, 82,949 vested shares were withheld to satisfy withholding tax obligations, resulting in the net issuance of 139,258 shares. As of June 28, 2013, approximately $6.0 million of stock-based compensation cost, net of forfeitures, related to RSU s remains to be amortized, of which substantially all is expected to be recognized over an estimated period of less than three years. As of June 28, 2013, a total of 1,230,550 RSU s remain outstanding with an aggregate intrinsic value of $7.4 million and a weighted average remaining contractual term of 1.3 years.

Restricted Stock Awards The total unamortized expense of the Company s unvested restricted stock awards as of June 28, 2013, was less than $0.2 million.

The following table summarizes the Company s restricted stock unit and restricted stock award activity for the six months June 28, 2013:

	Number of Shares
Unvested restricted stock units and restricted stock awards at December 28, 2012	1,312,706
Granted	631,200
Vested	(527,705)
Forfeited	(154,717)
Unvested restricted stock units and restricted stock awards at June 28, 2013	1,261,484

Table of Contents

The following table shows the Company s stock-based compensation expense included in the condensed consolidated statements of operations (in thousands):

	Three months ended		Six months ended	
	June 28, 2013	June 29, 2012	June 28, 2013	June 29, 2012
Cost of sales(1)	$ 308	$ 422	$ 725	$ 815
Research and development	59	86	147	165
Sales and marketing	96	112	228	206
General and administrative	537	777	1,220	1,463
Total stock-based compensation expense	1,000	1,397	2,320	2,649
Income tax benefit	(201)	(279)	(504)	(585)
Total stock-based compensation expense, net of income tax benefit	$ 799	$ 1,118	$ 1,816	$ 2,064

(1) As of June 28, 2013 and June 29, 2012, there were no stock-based compensation expenses capitalized in inventory.

2. Balance Sheet Information (in thousands)

Inventory consisted of the following (in thousands):

	June 28, 2013	December 28, 2012
Raw materials	$ 39,002	$ 47,825
Work in process	12,977	9,994
Finished goods	3,466	2,349
	55,445	60,168
Reserve for excess and obsolete	(6,773)	(6,203)
Total	$ 48,672	$ 53,965

Equipment and leasehold improvements, net, consisted of the following (in thousands):

	June 28, 2013	December 28, 2012
Computer equipment and software	$ 8,479	$ 8,148
Furniture and fixtures	1,608	1,682
Machinery and equipment	8,567	8,597
Leasehold improvements	10,536	10,092
	29,190	28,519
Accumulated depreciation	(20,696)	(19,237)
Total	$ 8,494	$ 9,282

3. Acquisition

On July 3, 2012, the Company completed the acquisition of American Integration Technologies LLC (AIT), a supplier of critical subsystems to the semiconductor capital equipment, medical, energy, industrial and aerospace industries, for approximately $75.3 million in cash and 4.5 million shares of newly issued common stock valued at $29.6 million for a total purchase price of $104.9 million. The acquisition serves to increase the Company s competitive position and market share, as it resulted in an expansion and diversification of the Company s customer base and product and service portfolio. By acquiring AIT s complementary product and service portfolio and well established customers, the Company is able to immediately go to market with a more complete and integrated solution. The Company financed the cash portion of the merger, and repaid existing indebtedness, by borrowing a total of $79.8 million under a senior secured credit facility, of which $40.0 million represents borrowings under a term loan and $39.8 million represents borrowings under a revolving credit facility. See further discussion of the borrowing arrangements in Note 5.

Table of Contents

The Company allocated the purchase price of AIT to tangible assets, liabilities and identifiable intangible assets acquired, based on their estimated fair values. Accounts receivable, net of allowance for doubtful accounts and other current assets and liabilities were stated at their historical carrying values, which approximate fair value given the short-term nature of these assets and liabilities. The fair value of the inventory was derived from model-based valuations for which all significant inputs and value drivers are observable directly or indirectly (Level 2 inputs). The fair value of fixed assets was determined using market data for similar assets. The fair value of the non-financial assets, summarized below, were derived from significant unobservable inputs (Level 3 inputs) determined by management based on market analysis, income analysis and discounted cash flow model. The fair value of purchased identifiable intangible assets was determined using the Company s discounted cash flow models from income projections prepared by management, using weighted average cost of capital plus a 1.4% premium.

The excess of purchase price over the aggregate fair values was recorded as goodwill. Although goodwill is not amortized for financial accounting purposes, it is amortized for tax purposes over fifteen years. The Company determined the fair values assigned to identifiable intangible assets acquired based on its consideration of a number of inputs, including an independent third party analysis that was based upon estimates and assumptions provided by the Company. These estimates and assumptions were determined through established and generally accepted valuation techniques. In determining the fair value of the identifiable intangible assets, the Company considered, among other factors, the best use of acquired assets, analyses of historical financial performance and estimates of future performance of AIT s products. The fair values of identifiable intangible assets were calculated considering market participant expectations and using an income approach. The rates utilized to discount estimated net cash flows to their present values were based on a weighted average cost of capital of 12.5% and a long term growth rate of 4%. This discount rate was determined after consideration of the rate of return on debt capital and equity that typical investors would require from an investment in companies similar in size and operating in similar markets as AIT. The estimated fair value of the tangible and intangible assets acquired was allocated at AIT s acquisition date. During the three months ended June 28, 2013, the Company completed the purchase price allocation for the AIT acquisition. The purchase price for the acquisition is allocated as follows (in thousands):

Fair Market Values	
Cash and cash equivalents	$ 380
Accounts receivable, net	16,959
Inventories	23,618
Other current assets	381
Property and equipment, net	1,880
Goodwill	55,918
Purchased intangible assets	22,500
Total assets acquired	121,636
Accounts payable and accrued expenses	(13,807)
Other liabilities	(2,939)
Total liabilities assumed	(16,746)
Purchase price allocated	$ 104,890

Table of Contents

Details of purchased intangible assets with finite lives were as follows as of June 28, 2013 (in thousands):

	Useful Life (in years)	Purchased Intangible Assets
Customer relationships	7	$ 19,000
Trade-name	6	1,900
Intellectual Property/Know-How	7	1,600
Total purchased intangible assets		22,500
Accumulated amortization December 28, 2012		(3,786)
Carrying amount December 28, 2012		18,714
Amortization for the six months ended June 28, 2013		(2,940)
Carrying amount June 28, 2013		$ 15,774

An accelerated method of amortization is used for the Customer Relationships intangible asset based on the expected pattern of future benefits. For the Tradename and Intellectual Property Know-how intangible assets a straight-line amortization method is used.

The following unaudited pro forma consolidated results of operations assume the acquisition was completed as of the beginning of the fiscal reporting periods presented. The unaudited pro forma consolidated results of operations for the three and six months ended June 29, 2012 combine the results of Ultra Clean and AIT, as follows (in thousands, except for per share amounts):

	Three Months Ended June 29, 2012	Six Months Ended June 29, 2012
	(In thousands, except per share amounts)	
Net sales	$ 148,325	$ 290,135
Net income	$ 5,665	$ 9,083
Basic earnings per share	$ 0.20	$ 0.33
Diluted earnings per share	$ 0.20	$ 0.32

The unaudited pro forma results above include adjustments related to the purchase price allocation and financing of the acquisition, primarily to increase amortization for the identifiable intangible assets, to increase interest expense for the additional debt incurred to complete the acquisition, to reflect the related income tax effect and to adjust weighted shares issued as part of the acquisition. The pro forma results for the six months ended June 29, 2012 include acquisition costs of $2.4 million which are not expected to occur in future quarters. The unaudited pro forma condensed combined financial information has been prepared by management for illustrative purposes only and are not necessarily indicative of the consolidated financial position or results of income in future periods or the results that actually would have been realized had Ultra Clean and AIT been a combined company during the specified periods. The unaudited pro forma condensed combined financial information does not reflect any operating efficiencies and/or cost savings that we may achieve with respect to the combined companies, or any liabilities that may result from integration activities.

Table of Contents

Goodwill associated with the acquisition is primarily attributable to the expected synergies and other benefits that the Company believes will result from combining the operations of the Company and AIT. The acquisition serves to increase the Company s competitive position and market share, as it resulted in an expansion and diversification of the Company s customer base and product and service portfolio. By acquiring AIT s complementary product and service portfolio and well established customers, the Company was able to immediately go to market with a more complete and integrated solution.

4. Goodwill and Purchased Intangible Assets

The Company s methodology for allocating the purchase price relating to purchase acquisitions is determined through established and generally accepted valuation techniques. Goodwill is measured as the excess of the cost of the acquisition over the sum of the amounts assigned to tangible and identifiable intangible assets acquired less liabilities assumed. Goodwill and purchased intangible assets with indefinite useful lives are not amortized, but are reviewed for impairment at least annually and whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. The process of evaluating the potential impairment of goodwill and intangible assets requires significant judgment. The Company regularly monitors current business conditions and other factors including, but not limited to, adverse industry or economic trends and lower projections of profitability that may impact future operating results.

During the quarter ended June 28, 2013, the Company concluded there were no triggering events which would require an impairment analysis of the carrying amount of goodwill, primarily due to operating cash flows during the period. During the six months ended June 28, 2013, the Company reduced the goodwill balance by $0.7 million due to the change in the provisional measurement of acquired inventory and sales and use tax balances. The change was not material to the presented financial statements, therefore the comparative information was not revised.

Details of goodwill from inception of the Company through June 28, 2013 are as follows (in thousands):

	Gross Amount	Accumulated Impairment	Net Carrying Amount
Six months ended June 28, 2013			
Goodwill (1)	$ 89,961	$ (34,043)	$ 55,918
Year ended December 28, 2012			
Goodwill (1)	$ 90,705	$ (34,043)	$ 56,662

(1) Represents aggregate goodwill recorded for the UCT acquisition in 2002, the Sieger Engineering LLC acquisition in 2006 and the AIT acquisition in 2012.

Details of goodwill and other intangible assets were as follows (in thousands):

	June 28, 2013			December 28, 2012		
	Goodwill	Intangible Assets	Total	Goodwill	Intangible Assets	Total
Carrying amount	$ 55,918	$ 24,761	$ 80,679	$ 56,662	$ 27,702	$ 84,364

Purchased Intangible Assets

Intangible assets are generally recorded in connection with a business acquisition. The value assigned to the intangible assets purchased as part of the acquisition of AIT was based on estimates and judgments regarding expectations for the success and life cycle of intellectual property/know-how acquired, tradename recognition and developed customer relationships. The Company evaluates the useful lives of its intangible assets each reporting period to determine whether events and circumstances require revising the remaining period of amortization. In addition, the Company reviews intangible assets for impairment when events or changes in circumstances indicate their carrying value may not be recoverable. Management considers such indicators as significant differences in actual product acceptance from the estimates, changes in the competitive and economic environment, technological advances, and changes in cost structure.

Details of purchased intangible assets as of June 28, 2013, are as follows (in thousands):

	As of December 28, 2012 Purchased Intangible Assets	As of December 28, 2012 Accumulated Amortization	As of December 28, 2012 Carrying Value	Six Months June 28, 2013 Amortization	As of June 28, 2013 Carrying Value	Useful Life (in years)
Customer relationships	$ 19,000	$ (3,449)	$ 15,551	$ (2,594)	$ 12,957	7
Tradename (AIT)	1,900	(223)	1,677	$ (231)	$ 1,446	6
Intellectual property/know-how	1,600	(114)	1,486	$ (115)	$ 1,371	7
Tradename (UCT)	8,987		8,987		$ 8,987	*
Total	$ 31,487	$ (3,786)	$ 27,701	$ (2,940)	$ 24,761	

* The UCT tradename was determined to have an indefinite life and is therefore not amortized.

The Company amortizes its customer relationships intangible asset using an accelerated method over the estimated economic life of the asset, or 7 years. The Company amortizes its trade-name and intellectual property/know-how intangible assets on a straight-line basis ranging from six to seven years. Amortization expense was approximately $3.0 million for the six months ended June 28, 2013. The Company had no amortization in the same quarter and six-month period of the previous year.

As of June 28, 2013, future estimated amortization expense is expected to be as follows (in thousands):

	Amortization Expense
2013 (remaining in year)	$ 3,052
2014	4,884
2015	2,813
2016	2,293
2017	1,386
2018	848
2019	498
Total	$ 15,774

In addition to the AIT tradename intangible of $1.9 million, which the Company concluded has a definite life of six years, the Company is also carrying a UCT trade-name intangible asset of $9.0 million as a result of a previous acquisition. The Company concluded that the UCT trade-name intangible asset life is indefinite and is therefore not amortized. During the quarter ended June 28, 2013, the Company concluded there were no triggering events which would require an impairment analysis of the carrying amount of UCT trade-name, primarily due to operating cash flows during the period.

5. Borrowing Arrangements

On July 3, 2012, in connection with the Company s acquisition of AIT and the refinancing of its prior credit facility, the Company entered into a credit agreement (the Credit Agreement) by and among the Company, certain of its subsidiaries, Silicon Valley Bank, U.S. Bank National Association and HSBC Bank (collectively, the Lenders). The Credit Agreement provides for a term loan in an aggregate principal amount of $40.0 million (the Term Loan) and a revolving credit facility in an aggregate principal amount of $40.0 million (the Revolving Credit Facility), a letter of credit facility in the aggregate availability amount of $15.0 million (as a sublimit of such Revolving Credit Facility) (the L/C Facility) and a swingline sub-facility in the aggregate availability amount of $4.0 million (as a sublimit of the Revolving Credit Facility) (together with the Term Loan, the Revolving Credit Facility and the L/C Facility, the Credit Facility). On July 3, 2012, the Company borrowed an aggregate of $40.0 million under the Term Loan and approximately $39.8 million under the Revolving Credit Facility. The borrowed funds were used at the closing of the Company s acquisition of AIT to finance the acquisition and repay the outstanding balance of $3.7 million to Silicon Valley Bank as lender under the Company s prior credit facility. The prior credit facility was terminated in connection with this transaction.

The Credit Facility must be repaid in consecutive quarterly installments of $2.5 million, with the first payment made on September 30, 2012, and with the balance of the then-outstanding principal amount due at the final maturity, which is July 3, 2016. The Revolving Credit Facility is available for the four-year period beginning on July 3, 2012. The Credit Agreement includes customary representations, warranties, covenants and events of default. The Company and certain of its subsidiaries have agreed to secure all of their obligations under the Credit Agreement by granting a first priority lien in substantially all of their respective personal property assets of these entities (subject to certain exceptions and limitations).

At the Company s option, borrowings under the Term Loan and Revolving Credit Facility (subject to certain limitations) bear interest at either a base rate or at the London Interbank Offered Rate (LIBOR) (with the LIBOR being adjusted for certain Eurocurrency reserve requirements, if any, as described in the Credit Agreement), plus, in each case, an applicable margin based on our consolidated leverage ratio. All loans described above made on July 3, 2012 were initially base rate loans, carrying interest of 3.75%. The Company expects, however, that the effective interest rate will be higher due to the incurrence of certain loan-related costs of approximately $1.9 million that will be treated as deferred interest and amortized over the life of the loan.

The Credit Agreement requires the Company to maintain certain financial covenants including a minimum consolidated fixed charge coverage ratio, a maximum consolidated leverage ratio and minimum domestic cash balances. On February 15, 2013, the Company and the Lenders amended the Credit Agreement in order to modify the financial covenants contained in the Credit Agreement, effective January 30, 2013. The Credit Agreement, as amended, requires the Company to comply with the following financial covenants:

- a minimum consolidated fixed charge coverage ratio (as defined in the Credit Agreement, as amended), measured over the preceding four fiscal quarters, beginning as of the end of the third quarter of fiscal 2014, of 1.10 to 1.00, increasing to 1.25 to 1.00 as of the end of each fiscal quarter beginning with the first quarter of fiscal 2015 and thereafter;

- a maximum consolidated leverage ratio (as defined in the Credit Agreement, as amended) measured over the receding four fiscal quarters, beginning, as of the end of the third quarter of fiscal 2014, of 4.00 to 1.00, stepping down to 3.75 to 1.00 as of the end of the fourth quarter of fiscal 2014 and thereafter to and including the third quarter of 2015, and 3.25 to 1.00 as of the end of each fiscal quarter beginning with the fourth quarter of 2015 and thereafter;

- minimum domestic cash of $15.0 million as of the last day of any fiscal quarter and $10.0 million as of the last day of any other fiscal month from January 25, 2013 and thereafter;

- a minimum consolidated quick ratio (as defined in the Credit Agreement, as amended) of 1.10 to 1.00 as of the end of each fiscal month from January 25, 2013 and thereafter;

- minimum consolidated adjusted EBITDA (as defined in the Credit Agreement, as amended), measured over the preceding two quarters, of $3.5 million as of the end of the fourth quarter of 2012, $2.5 million as of the end of the first quarter of 2013, $3.0 million as of the end of the second quarter of 2013, $4.0 million as of the end of the third quarter of 2013, $6.0 million as of the end of the fourth quarter of 2013, $7.0 million as of the end of the first quarter of 2014 and $8.0 million as of the end of the second quarter of 2014 and each quarter thereafter.

For the quarter ended June 28, 2013, the Company was in compliance with all covenants.

The Credit Agreement contains provisions requiring the following mandatory prepayments (subject to certain exceptions and limitations): (i) prepayments equal to 50% of the net cash proceeds from the issuance of capital stock by the Company s primary operating subsidiary (or any of its subsidiaries); (ii) prepayments equal to 100% of the net cash proceeds from the incurrence of any indebtedness by the Company s primary operating subsidiary over $250,000; (iii) prepayments equal to the net cash proceeds from certain asset sales or insurance or condemnation recoveries; and (iv) annual prepayments in an amount equal to (a) 33% of excess cash flow (as defined in the Credit Agreement, as amended) if the aggregate outstanding principal amount of the Term Loan equals or exceeds $20.0 million and (b) 25% of excess cash flow if the aggregate outstanding principal amount of the Term Loan equals or exceeds $10.0 million but is less than $20.0 million.

The Credit Agreement also restricts the Company from declaring or paying any cash dividends.

As of June 28, 2013, the Company s term loan and revolver balances were $28.6 million and $39.8 million, respectively, which are net of unamortized debt issuance costs of $1.5 million for a total debt balance of $68.4 million. The Company analyzed the Credit Agreement and determined that the outstanding balance of revolver debt should be classified as short-term due to acceleration clauses in the agreement.

6. Income Tax

The Company s income tax provision and related effective tax rate for the three and six month periods ended June 28, 2013 was $581,000 and 20.1% and $556,000 and 21.7%, respectively, compared to $1,658,000 and 37.3% and $3,160,000 and 29.8%, respectively for the same periods a year ago. The change in respective rates reflects, primarily, changes in the geographic mix of worldwide earnings and financial results for the three and six month periods ended June 28, 2013 compared to the same period in 2012.

Undistributed earnings of the Company s foreign subsidiaries at June 28, 2013, are considered to be indefinitely reinvested and no provision for U.S. income taxes has been provided thereon. Upon distribution of those earnings in the form of dividends or otherwise, the Company would be subject to U.S. income taxes. It is not practicable to determine the income tax liability that might be incurred if these earnings were to be distributed.

The following table summarizes the activity related to the Company s uncertain tax positions (in thousands):

	Six months ended	
	June, 28, 2013	June 29, 2012
Balance as of the beginning of period	$ 109	$ 132
Increases (decreases) related to prior year tax positions	(22)	22
Balance as of the end of period	$ 87	$ 154

The Company s gross liability for unrecognized tax benefits as of June 28, 2013 and June 29, 2012, was $87,000 and $154,000, respectively. Increases or decreases to interest and penalties on uncertain tax positions are included in income tax provision (benefit) in the Condensed Consolidated Statements of Operations. Interest related to uncertain tax positions was $2,000 for each of the six months ended June 28, 2013 and June 29, 2012, respectively. Although it is possible some of the unrecognized tax benefits could be settled within the next twelve months, the Company cannot reasonably estimate the outcome at this time.

The determination of the Company s tax provision is subject to judgments and estimates. The carrying value of our net deferred tax assets, which is made up primarily of tax deductions, assumes we will be able to generate sufficient future income to fully realize these deductions. In determining whether the realization of these deferred tax assets may be impaired, we make judgments with respect to whether we are likely to generate sufficient future taxable income to realize these assets. In addition, the calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of complex tax laws. Resolution of these uncertainties in a manner inconsistent with the Company s expectations could have a material impact on its results of operations and financial position.

As of June 28, 2013, the Company maintained a full valuation allowance on one of its China subsidiaries in the amount of $851,000 as the Company believes it is more likely than not that the deferred tax asset will not be realized. In order to reverse a valuation allowance, accounting principles generally accepted in the United States of America suggests that the Company review the cumulative income/loss in recent years as well as determine the Company s ability to generate sufficient future taxable income to realize the Company s net deferred tax assets.

The Company files income tax returns in the U.S. federal jurisdiction, various states and foreign jurisdictions. The Company s 2010 through 2012 federal income tax returns are open to audit through the statute of limitations by the Internal Revenue Service. The Company s 2008 through 2012 state income tax returns are open to audit by the California Franchise Tax Board. The Company is also subject to examination in various other jurisdictions for various periods. The Company is currently experiencing a tax holiday related to its Singapore subsidiary that will expire for tax years beginning January 2015. The Company s Singapore subsidiary recorded a net profit, considered insignificant by the Company, for the quarter ended June 28, 2013.

7. Net Income Per Share

Basic net income per share excludes dilution and is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted net income per share reflects the potential dilution that would occur if outstanding securities or other contracts to issue common stock were exercised or converted into common stock.

Table of Contents

The following is a reconciliation of the numerators and denominators used in computing basic and diluted net income per share (in thousands, except per share data):

	Three months ended		Six months ended	
	June 28, 2013	June 29, 2012	June 28, 2013	June 29, 2012
Numerator:				
Net income	$ 2,316	$ 2,790	$ 2,005	$ 7,450
Denominator:				
Shares used in computation basic:				
Weighted average common shares outstanding	28,370	23,292	28,172	23,289
Shares used in computation diluted:				
Shares used in computing basic net income per share	28,370	23,292	28,172	23,289
Dilutive effect of common shares outstanding subject to repurchase	140	101	256	239
Dilutive effect of options outstanding	247	317	322	365
Weighted average shares used in computing diluted net income per share	28,757	23,710	28,750	23,893
Net income per share basic	$ 0.08	$ 0.12	$ 0.07	$ 0.32
Net income per share diluted	$ 0.08	$ 0.12	$ 0.07	$ 0.31

The Company had securities outstanding which could potentially dilute basic earnings per share in the future, but the incremental shares from the assumed exercise of these securities were excluded in the computation of diluted net income (loss) per share, as their effect would have been anti-dilutive. Such outstanding securities consisted of 1,015,906 stock options for the quarter ended June 28, 2013 and 618,156 stock options outstanding for the quarter ended June 29, 2012 and 1,018,040 and 547,473 stock options for the six months ended June 28, 2013 and June 29, 2012, respectively.

8. Commitments and Contingencies

The Company had commitments to purchase inventory totaling approximately $43.8 million at June 28, 2013.

The Company leases properties domestically in Hayward, California; Austin, Texas, Pflugerville, Texas; Chandler, Arizona; and South San Francisco, California and internationally in China, Singapore and the Philippines. The Company leases certain of its facilities under non-cancelable leases, which expire on various dates through 2022.

As of June 28, 2013, future minimum payments under these operating leases were as follows (in thousands):

Fiscal year	
2013 (remaining in year)	$ 2,367
2014	3,819
2015	3,247
2016	2,658
2017	2,125
Thereafter	8,571
Total minimum lease payments	$ 22,787

From time to time, the Company is subject to various legal proceedings and claims, either asserted or unasserted, that arise in the ordinary course of business. Although the outcome of the various legal proceedings and claims cannot be predicted with certainty, the Company has not had a history of outcomes to date that have been material to the statement of operations and does not believe that any of these proceedings or other claims will have a material adverse effect on its consolidated financial condition or results of operations.

Table of Contents

9. Segment Information

The Company operates in one reportable segment and is engaged in the development, manufacture and supply of critical subsystems for the semiconductor capital equipment, flat panel, medical, energy and research industries. Multiple operating segments were aggregated into one reportable segment as the nature of the Company s products and production processes, as well as type of customers and distribution methods, is consistent among all the Company s products. In addition, all operating segments have similar economic characteristics. The Company s foreign operations are conducted primarily through its wholly-owned subsidiary in China. The Company s principal markets include North America, Asia and, to a lesser degree, Europe. Sales by geographic area represent sales to unaffiliated customers.

All information on sales by geographic area is based upon the location to which the products were shipped. The following table sets forth revenue by geographic area (in thousands):

	Three months ended		Six months ended	
	June 28, 2013	June 29, 2012	June 28, 2013	June 29, 2012
United States	$ 84,875	$ 73,291	$ 168,088	$ 155,279
China	9,681	7,176	14,433	14,906
Singapore	11,987	20,810	22,492	40,237
Other	3,564	672	5,558	2,092
	$ 110,107	$ 101,949	$ 210,571	$ 212,514

At June 28, 2013 and June 29, 2012, approximately $3.8 million and $4.4 million, respectively, of the Company s net long-lived assets were located in Asia, and the remaining balances were located in the United States.

10. Correction of Previously Reported Quarterly Financial Statements

As described in the Annual Report on Form 10-K for the year ended December 28, 2012, the Company has made certain corrections to amounts previously reported for the quarter ended June 29, 2012. The Company has concluded that, due to the nature of the affected expenses, these corrections were not material to the interim financial statements for the three and six month periods ended June 29, 2012. The Company has included such corrections to its 2012 interim financial statements for the period ended June 29, 2012 included within this report on Form 10-Q as of and for the quarter ended June 28, 2013.

	Three months ended June 29, 2012 as reported	Corrections to the three months ended June 29, 2012	Three months ended June 29, 2012 as corrected	Six months ended June 29, 2012 as reported	Corrections to the six months ended June 29, 2012	Six months ended June 29, 2012 as corrected
			(In thousands, except per share data)			
Sales	$ 101,949		$ 101,949	$ 212,514		$ 212,514
Gross profit	$ 14,254		$ 14,254	$ 29,914		$ 29,914
Operating expenses	$ 9,338	$ 454(a)	$ 9,792	$ 18,731	$ 454(a)	$ 19,185
Income from operations	$ 4,916	$ (454)	$ 4,462	$ 11,183	$ (454)	$ 10,729
Income tax provision	$ 979	$ 679(b)(c)	$ 1,658	$ 2,481	$ 679(b)(c)	$ 3,160
Net income (loss)	$ 3,923	$ (1,133)	$ 2,790	$ 8,583	$ (1,133)	$ 7,450
Earnings per share basic	$ 0.17	$ (0.05)	$ 0.12	$ 0.37	$ (0.05)	$ 0.32
Earnings per share diluted	$ 0.17	$ (0.05)	$ 0.12	$ 0.37	$ (0.06)	$ 0.31

The corrections relate to:

a) $454,000 of costs associated with the acquisition of AIT that were capitalized at June 29, 2012 and expensed in the quarter ended September 29, 2012, which should have been expensed in the quarter ended June 29, 2012;

b) foreign tax payments of $770,000 that were recorded as a reduction of other current liabilities as of June 29, 2012, and expensed in the quarter ended December 28, 2012, but should have been expensed in the quarter ended June 29, 2012.

c) the tax effect of item a) above.

Similarly, as described in the Annual Report on Form 10-K for the year ended December 28, 2012, the balances for the period ended September 29, 2012 will be corrected to reflect the corrections noted above in the 10-Q for the fiscal quarter ended September 27, 2013.

ITEM 2. Management s Discussion And Analysis of Financial Condition And Results Of Operations

You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q and in our consolidated financial statements included in our Annual Report on Form 10-K filed with the SEC on March 13, 2013. This Quarterly Report on Form 10-Q contains forward-looking statements that involve substantial risks and uncertainties. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, including, but not limited to, statements regarding our expectations, beliefs, intentions, strategies, future operations, future financial position, future revenue, projected expenses, gross margins and the plans and objectives of management. In some cases, you can identify forward-looking statements by terms such as anticipate, believe, estimate, expect, intend, may, might, plan, project, will, would, should, could, can, predict, potential, continue, or the negative of these terms, and similar expressions intended to identify forward-looking statements. However, not all forward-looking statements contain these identifying words. These forward-looking statements reflect our current views about future events and involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievement to be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled Risk Factors included in this Quarterly Report on Form 10-Q, in our Annual Report on Form 10-K filed with the SEC on March 13, 2013and in our Quarterly Report on Form 10-Q filed with the SEC on May 3, 2013. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We are a leading developer and supplier of critical subsystems, primarily for the semiconductor capital equipment industry. We also leverage the specialized skill sets required to support semiconductor capital equipment to serve the technologically similar markets in the flat panel, medical, energy and research industries, collectively referred to as Other Addressed Industries . We develop, design, prototype, engineer, manufacture and test subsystems which are highly specialized and tailored to specific steps in the semiconductor manufacturing process as well as the manufacturing process in Other Addressed Industries. Our revenue is derived primarily from the sale of gas delivery systems and other critical subsystems including chemical mechanical planarization (CMP) subsystems, chemical delivery modules, top-plate assemblies, frame assemblies, process modules and other high level assemblies.

On July 3, 2012, we completed the acquisition of American Integration Technologies LLC (AIT), a supplier of critical subsystems to the semiconductor capital equipment, medical, energy, industrial and aerospace industries, for approximately $75.3 million in cash and 4.5 million shares of our newly issued common stock valued at $29.6 million for a total purchase price of $104.9 million. We financed the cash portion of the merger, and repaid our pre-existing indebtedness, by borrowing a total of $79.8 million under a senior secured credit facility, of which $40.0 million represented borrowings under a term loan and $39.8 million represented borrowings under a revolving credit facility.

Financial Highlights

Sales for the three months ended June 28, 2013, were $110.1 million, an increase of $8.2 million, or 8.0%, from the comparable quarter of 2012. Gross profit for the three months ended June 28, 2013 increased $1.8 million, to $16.1 million, or 14.6% of sales, from $14.3 million, or 14.0% of sales, for the three months ended June 29, 2012. Total operating expenses for the three months ended June 28, 2013, were $12.5 million, or 11.3% of sales, compared to $9.8 million, or 9.6% of sales, for the three months ended June 29, 2012. We earned net income of $2.3 million for the three months ended June 28, 2013, compared to net income of $2.8 million for the three months ended June 29, 2012.

Sales for the six months ended June 28, 2013, were $210.6 million, a decrease of $1.9 million, or 0.9%, from the comparable period of 2012. Gross profit for the six months ended June 28, 2013 was relatively the same at $29.9 million or 14.2% of sales, compared to $29.9 million, or 14.1% of sales, during the comparable period of 2012. Total operating expenses for the six months ended June 28, 2013, were $25.7 million, or 12.2% of sales, compared to $19.2 million, or 9.0% of sales, for the six months ended June 29, 2012. We earned net income of $2.0 million for the six months ended June 28, 2013 as compared to $7.5 million for the six months ended June 29, 2012.

We had significant sales to three customers, each of which accounted for 10% or more of sales for the six months ended June 28, 2013. For a further discussion, see Note 1. Organization Basis of Presentation and Significant Accounting Policies -*Significant Sales to Customers* in Notes to Condensed Consolidated Financial Statements above.

Table of Contents

Effective as of the end of the first quarter of 2012, we agreed to terminate our arrangement with FEI Corporation, whereby FEI would take back the manufacturing process they had been outsourcing to us since 2008. As part of an arrangement, we agreed to assist FEI during the transition period through our third quarter of fiscal 2012 and, as a result, recorded revenue totaling $2.1 million related to these efforts during that timeframe, offset by associated costs.

We announced in the third quarter of fiscal 2012 that one of our larger semiconductor equipment customers has decided to in-source a portion of their gas panel business. While this decision did not have a material impact on our sales in fiscal 2012, it could have a negative quarterly impact of 7% to 9% on total sales by the end of fiscal 2013.

Results of Operations

For the periods indicated, the following table sets forth certain costs and expenses and other income items as a percentage of sales. The table and subsequent discussion should be read in conjunction with our condensed consolidated financial statements and notes thereto included elsewhere in our quarterly report.

	Three months ended		**Six months ended**	
	June 28, 2013	**June 29, 2012**	**June 28, 2013**	**June 29, 2012**
Sales	100%	100.0%	100%	100.0%
Cost of goods sold	85.4%	86.0%	85.8%	85.9%
Gross profit	14.6%	14.0%	14.2%	14.1%
Operating expenses:				
Research and development	1.4%	1.3%	1.3%	1.3%
Sales and marketing	2.2%	1.6%	2.3%	1.6%
General and administrative	7.7%	6.7%	8.6%	6.2%
Total operating expenses	11.3%	9.6%	12.2%	9.1%
Income from operations	3.3%	4.4%	2.0%	5.0%
Interest and other income (expense), net	(0.7)%	(0.0)%	(0.8)%	(0.0)%
Income before provision for income taxes	2.6%	4.4%	1.2%	5.0%
Income tax provision	0.5%	1.7%	0.2%	1.5%
Net income	2.1%	2.7%	1.0%	3.5%

Sales

Sales for the three months ended June 28, 2013, increased $8.2 million, or 8.0%, to $110.1 million from $101.9 million in the comparable period of 2012. Sales for the six months ended June 28, 2013 decreased $1.9 million, or 0.9%, to $210.6 million from $212.5 million in the comparable period of 2012. The increase in sales during the three month period ended June 28, 2013 was due primarily to our acquisition of AIT in July 2012, which resulted in the inclusion of sales of $34.4 million from AIT in the three month period ended June 28, 2013 for which there was no corresponding sales included in our consolidated results for 2012. The decrease in sales for the six months ended June 28, 2013 reflects primarily a decrease in semiconductor revenues resulting from a downturn in the semiconductor industry which began during the third quarter of fiscal 2011, as well as the continued softness in the energy industry, partially offset by the inclusion of sales of $62.6 million due to the inclusion of AIT s sales from January through June 2013. Sales for the six months ended June 29, 2012, also included sales to FEI of $2.1 million for which no corresponding amount is included in the results for 2013. We expect overall sales to be flat in the third quarter of fiscal 2013 compared to the second quarter of fiscal 2012.

Table of Contents

Gross Profit

Cost of goods sold consists primarily of purchased materials, labor and overhead, including depreciation related to certain capital assets associated with the design and manufacture of products sold. Gross profit for the three months ended June 28, 2013, increased $1.8 million to $16.1 million, or 14.6% of sales, from $14.3 million, or 14.0% of sales, for the same period in 2012. Our gross margin for the three months ended June 29, 2013, increased from the comparable period in 2012 due primarily to the change in sales mix between the two comparable quarters. Gross profit for the six months ended June 28, 2013, increased less than $0.1 million to $29.9 million, or 14.2% of sales, from $29.9 million, or 14.1% of sales, for the same period in 2012. Our gross margin for the six months ended June 28, 2013, increased from the comparable period in 2012 due primarily to a change in sales mix and lower material and direct labor costs as a percentage of gross revenues. We expect our gross profit to be flat in the third quarter of 2013 when compared to the quarter ended June 28, 2013.

Research and Development Expense

Research and development expense consists primarily of activities related to new component testing and evaluation, test equipment and fixture development, product design, and other product development activities. Research and development expense for the three months ended June 28, 2013, increased $0.2 million, or 15.6%, to $1.5 million, or 1.4% of sales, compared to $1.3 million, or 1.3% of sales in the comparable period in 2012. Research and development expense for the six months ended June 28, 2013 increased less than $0.1 million, or 1.9%, to $2.7 million, or 1.3% of sales, compared to $2.7 million, or 1.3% of sales in the comparable period in 2012. The change in research and development expenses during both the three and six month periods was due primarily to the timing of reassignment of existing resources to research and development activities.

Sales and Marketing Expense

Sales and marketing expense consists primarily of salaries and commissions paid to our sales and service employees and salaries paid to our configuration engineers who work with the sales and service employees to help determine the components and configuration requirements for new products and other costs related to the sales of our products. Sales and marketing expense for the three months ended June 28, 2013, increased $0.8 million to $2.5 million, or 2.2% of sales, compared to $1.7 million, or 1.6% of sales, in the comparable period of 2012. Sales and marketing expenses for the six months ended June 28, 2013, increased $1.4 million to $4.8 million, or 2.3% of sales, compared to $3.4 million, or 1.6% of sales in the comparable period of 2012. The increase in expense was primarily due to the inclusion of sales costs for AIT after our acquisition of AIT offset by decreased payroll and related benefit costs due to reduced fully employed and temporary headcount.

General and Administrative Expense

Our general and administrative expense has historically consisted primarily of salaries and overhead associated with our administrative staff and professional fees. General and administrative expense increased approximately $1.7 million, or 24.6% for the three months ended June 28, 2013, to $8.5 million, or 7.7% of sales, compared with $6.8 million, or 6.7% of sales in the comparable period of 2012. General and administrative expense increased approximately $5.1 million, or 39% for the six months ended June 28, 2013, to $18.1 million, or 8.6% of sales, compared with $13.1 million, or 6.2% of sales, in the comparable period of 2012. The increase when comparing the three and six months ended June 28, 2013, with the comparable periods in 2012 is primarily due to the amortization of finite-lived intangibles associated with the AIT acquisition of approximately $1.5 million per quarter and additional general and administrative expenses as a result of the acquisition of AIT.

Interest and Other Income (Expense), net

Interest and other income (expense), net, for the three months ended June 28, 2013, was $(0.7) million compared to less than $(0.1) million in the comparable period of 2012. Interest and other income (expense), net, for the six months ended June 28, 2013, was $(1.7) million compared to $(0.1) million in the comparable period of 2012. The change in both periods was primarily due to an increase in interest expense as a result of the increase in outstanding debt in the third quarter of 2012 resulting from the acquisition of AIT.

Income Tax Provision

Our effective tax rate for the three months ended June 28, 2013, and June 29, 2012, was 20.1% and 37.3%, respectively. Our effective tax rate for the six months ended June 28, 2013, and June 29, 2012, was 21.7% and 29.8%, respectively. The change in respective rates reflects, primarily, a change in the geographic distribution of our world-wide earnings to foreign jurisdictions with lower tax rates or tax holidays offset by certain discrete tax items in the first and second quarters of 2013.

Liquidity and Capital Resources

We have required capital principally to fund our acquisitions and working capital needs, satisfy our debt obligations, maintain our equipment and purchase new capital equipment. As of June 28, 2013, we had cash of $71.3 million compared to $54.3 million as of December 28, 2012. Our cash and cash equivalents, as well as cash generated from operations, was our principal source of liquidity as of June 28, 2013.

For the six months ended June 28, 2013, we generated cash from operating activities of $25.5 million compared to $20.3 million for the comparable period of 2012. Operating cash flows generated in the six months ended June 28, 2013 were impacted by non-cash activity, including depreciation, amortization of intangibles and debt issuance costs in the aggregate, of $4.6 million and stock-based compensation of $2.3 million; decreases in accounts receivable and inventory of $3.0 million and $6.1 million, respectively; and an increase in accounts payable of $6.5 million, accrued compensation and related benefits of $0.4 million and a decrease in other liabilities of $0.4 million. Our cash flows from operations in any given period are largely driven by the timing of sales, the collection of accounts receivable and the payment of accounts payable.

Net cash used in investing activities for the six months ended June 28, 2013, was $0.7 million for capital expenditures. These investments are driven by the timing of our capital expenditures budget.

Net cash used in financing activities for the six months ended June 28, 2013 was $(7.8) million compared to $(21.1) million for the comparable period of 2012. For the six months ended June 28, 2013, our cash used in financing activities was due primarily to payments of $7.5 million on the term loan under our current credit facility and $0.5 million associated with employees taxes paid upon vesting of restricted stock units, offset by an excess tax benefit from stock compensation of $0.1 million. See Borrowing Arrangements below for information about our current borrowing arrangements which we entered into in connection with our acquisition of AIT on July 3, 2012.

We anticipate that our existing cash balance and operating cash flow will be sufficient to service our indebtedness and meet our working capital requirements and technology development projects for at least the next twelve months. The adequacy of these resources to meet our liquidity needs beyond that period will depend on our operating results, the state of the worldwide economy, our ability to meet our financial covenants with our credit facility, the cyclical expansion or contraction of the semiconductor capital equipment industry and the other industries we serve and capital expenditures required to meet possible increased demand for our products.

In order to expand our business or acquire additional complementary businesses or technologies, we may need to raise additional funds through equity or debt financings. If required, additional financing may not be available on terms that are favorable to us, if at all. If we raise additional funds through the issuance of equity or convertible debt securities, our stockholders equity interest will be diluted and these securities might have rights, preferences and privileges senior to those of our current stockholders. We may also require the consent of our senior lenders to raise additional funds through equity or debt financings. No assurance can be given that additional financing will be available or that, if available, such financing can be obtained on terms favorable to our stockholders and us.

In addition, the undistributed earnings of our foreign subsidiaries at June 28, 2013, are considered to be indefinitely reinvested and unavailable for distribution in the form of dividends or otherwise. Accordingly, no provisions for U.S. income taxes have been provided thereon. We anticipate that we have adequate liquidity and capital resources and would not need to repatriate earnings. As of June 28, 2013, we have approximately $41.6 million cash in our foreign subsidiaries.

Borrowing Arrangements

On July 3, 2012, in connection with our acquisition of AIT and the refinancing of our prior credit facility, we entered into a credit agreement (the Credit Agreement) by and among the Company, certain of our subsidiaries, Silicon Valley Bank, U.S. Bank National Association and HSBC Bank (collectively, the Lenders). The Credit Agreement provides for a term loan in an aggregate principal amount of $40.0 million (the Term Loan) and a revolving credit facility in an aggregate principal amount of $40.0 million (the Revolving Credit Facility), a letter of credit facility in the aggregate availability amount of $15.0 million (as a sublimit of such Revolving Credit Facility) (the L/C Facility) and a swingline sub-facility in the aggregate availability amount of $4.0 million (as a sublimit of the Revolving Credit Facility) (together with the Term Loan, the Revolving Credit Facility and the L/C Facility, the Credit Facility). On July 3, 2012, we borrowed an aggregate of $40.0 million under the Term Loan and approximately $39.8 million under the Revolving Credit Facility. The borrowed funds were used at the closing of our acquisition of AIT to finance the acquisition and repay the outstanding term loan balance of $3.7 million to Silicon Valley Bank under our prior credit facility. The prior credit facility was terminated in connection with this transaction.

The Credit Facility must be repaid in consecutive quarterly installments of $2.5 million, with the first payment made on September 30, 2012, and with the balance of the then-outstanding principal amount due at the final maturity, which is July 3, 2016. The Revolving Credit Facility is available for the four-year period beginning on July 3, 2012. The Credit Agreement includes customary representations, warranties, covenants and events of default. The Company and certain of our subsidiaries have agreed to secure all of our obligations under the Credit Agreement by granting a first priority lien in substantially all of our respective personal property assets (subject to certain exceptions and limitations).

At our option, borrowings under the Term Loan and Revolving Credit Facility (subject to certain limitations) bear interest at either a base rate or at the London Interbank Offered Rate (LIBOR) (with the LIBOR being adjusted for certain Eurocurrency reserve requirements, if any, as described in the Credit Agreement), plus, in each case, an applicable margin based on our consolidated leverage ratio. All loans described above made on July 3, 2012 were initially base rate loans, carrying interest of 3.75%. We expect, however, that the effective interest rate will be higher due to the incurrence of certain loan-related costs of approximately $1.9 million that will be treated as deferred interest and amortized over the life of the loan.

Table of Contents

The Credit Agreement requires us to maintain certain financial covenants including a minimum consolidated fixed charge coverage ratio, a maximum consolidated leverage ratio and minimum domestic cash balances. For the measurement periods ending in November and December of 2012, we were not in compliance with such covenants. On February 15, 2013, the Company and the Lenders amended the Credit Agreement in order for the lenders to waive such non-compliance and to modify the financial covenants contained in the Credit Agreement, effective January 30, 2013. The Credit Agreement, as amended, requires us to comply with the following financial covenants:

- a minimum consolidated fixed charge coverage ratio (as defined in the Credit Agreement, as amended), measured over the preceding four fiscal quarters, beginning as of the end of the third quarter of fiscal 2014, of 1.10 to 1.00, stepping up to 1.25 to 1.00 as of the end of each fiscal quarter beginning with the first quarter of fiscal 2015 and thereafter;

- a maximum consolidated leverage ratio (as defined in the Credit Agreement, as amended) measured over the preceding four fiscal quarters, beginning, as of the end of the third quarter of fiscal 2014, of 4.00 to 1.00, stepping down to 3.75 to 1.00 as of the end of the fourth quarter of fiscal 2014 and thereafter to and including the third quarter of 2015, and 3.25 to 1.00 as of the end of each fiscal quarter beginning with the fourth quarter of 2015 and thereafter;

- minimum domestic cash of $15.0 million as of the last day of any fiscal quarter and $10.0 million as of the last day of any other fiscal month from January 25, 2013 and thereafter;

- a minimum consolidated quick ratio (as defined in the Credit Agreement, as amended) of 1.10 to 1.00 as of the end of each fiscal month from January 25, 2013 and thereafter;

- minimum consolidated adjusted EBITDA (as defined in the Credit Agreement, as amended), measured over the preceding two quarters, of $3.5 million as of the end of the fourth quarter of 2012, $2.5 million as of the end of the first quarter of 2013, $3.0 million as of the end of the second quarter of 2013, $4.0 million as of the end of the third quarter of 2013, $6.0 million as of the end of the fourth quarter of 2013, $7.0 million as of the end of the first quarter of 2014 and $8.0 million as of the end of the second quarter of 2014 and each quarter thereafter.

For the quarter ended June 28, 2013, we were in compliance with all covenants.

The Credit Agreement contains provisions requiring the following mandatory prepayments (subject to certain exceptions and limitations): (i) prepayments equal to 50% of the net cash proceeds from the issuance of capital stock by our primary operating subsidiary (or any of its subsidiaries); (ii) prepayments equal to 100% of the net cash proceeds from the incurrence of any indebtedness by the Company s primary operating subsidiary over $250,000; (iii) prepayments equal to the net cash proceeds from certain asset sales or insurance or condemnation recoveries; and (iv) annual prepayments in an amount equal to (a) 33% of excess cash flow (as defined in the Credit Agreement, as amended) if the aggregate outstanding principal amount of the Term Loan equals or exceeds $20.0 million and (b) 25% of excess cash flow if the aggregate outstanding principal amount of the Term Loan equals or exceeds $10.0 million but is less than $20.0 million.

The Credit Agreement also restricts us from declaring or paying any cash dividends.

As of June 28, 2013, our term loan and revolver balances were $28.6 million and $39.8 million, respectively, which are net of unamortized debt issuance costs of $1.5 million for a total debt balance of $68.4 million. We have analyzed the Credit Agreement and determined that the outstanding balance of revolver debt should be classified as short-term due to acceleration clauses in the agreement.

Capital Expenditures

Capital expenditures were approximately $0.5 million in the six months ended June 28, 2013. The Company s anticipated capital expenditures for the remainder of 2013 are anticipated to be financed through cash from operations.

Off-Balance Sheet Arrangements

During the periods presented, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Table of Contents

Contractual Obligations

Other than operating leases for certain equipment and real estate and purchase order commitments primarily for inventory, we have no off-balance sheet transactions, unconditional purchase obligations or similar instruments and, other than the arrangements described under Borrowing Arrangements above, are not a guarantor of any other entities debt or other financial obligations. The following table summarizes our future minimum lease payments, principal payments under debt obligations and our purchase obligations for the purchase of inventory as of June 28, 2013, (in thousands):

	2013	2014	2015	2016	2017	2018 and Thereafter	Total
Capital leases	$ 5	$ 7	$	$	$	$	$ 12
Operating leases (1)	2,367	3,819	3,247	2,658	2,125	8,571	22,787
Borrowing arrangements (2)	44,844	10,000	10,000	5,000			69,844
PO commitments	43,816						43,816
Total	$ 91,032	$ 13,826	$ 13,247	$ 7,658	$ 2,125	$ 8,571	$ 136,459

(1) Operating lease expense reflects (a) the lease for our headquarters facility in Hayward, California that was modified in the fourth quarter of 2012 such that the lease now expires in 2022; (b) the leases for manufacturing facilities in South San Francisco that expire in 2013 (c) the leases for manufacturing facilities in China, Singapore and the Philippines that expire in 2013 thru 2016; (d) the leases for manufacturing facilities in Austin and Pflugerville, Texas that expire thru 2016 and; (d) the leases for manufacturing facilities in Chandler, Arizona that expire in 2017. We have options to renew certain of the leases in South San Francisco, Hayward and Austin which we expect to exercise.

(2) Amounts reflect our Credit Facility, under which we borrowed $40.0 million under the term loan and approximately $39.8 million under the revolving credit facility on July 3, 2012. The term loan must be repaid in consecutive quarterly installments of $2.5 million and with the balance of the outstanding principal amount of the term loan due at the final maturity, which is July 3, 2016. The revolving credit facility is available for the four-year period beginning on July 3, 2012. See Note 5. Borrowing Arrangements in Notes to Condensed Consolidated Financial Statements above.

Critical Accounting Policies, Significant Judgments and Estimates

Our condensed consolidated financial statements have been prepared in accordance with GAAP, which requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses and related disclosure at the date of our financial statements. Estimates and judgments are reviewed on an on-going basis, including those related to sales, inventories, intangible assets, stock compensation and income taxes. The estimates and judgments are based on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis of the judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. We consider certain accounting policies related to the purchase accounting, revenue recognition, inventory valuation, accounting for income taxes, valuation of intangible assets and goodwill and equity incentives to employees to be critical policies due to the estimates and judgments involved in each. Our significant accounting policies and critical estimates are disclosed in our 2012 Annual Report on Form 10-K as filed with the SEC on March 13, 2013. No material changes to our significant accounting policies and critical estimates have occurred subsequent to December 28, 2012.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk represents the risk of changes in value of financial instruments caused by fluctuations in interest rates and foreign exchange rates.

Foreign Exchange Rates

Currently, a significant majority of our sales and arrangements with third-party suppliers provide for pricing and payment in US dollars, and, therefore, are not subject to material exchange rate fluctuations. Therefore, we do not expect foreign currency exchange rate fluctuations to have a material effect on our results of operations. However, increases in the value of the U.S. dollar relative to other currencies would make our products more expensive relative to competing products priced in such other currencies, which could negatively impact our ability to compete. Conversely, decreases in the value of the U.S. dollar relative to other currencies could result in our foreign suppliers raising their prices in order to continue doing business with us.

Chinese authorities recently relaxed controls of China s currency, the Renminbi, and allowed the currency to strengthen against other world currencies, including the U.S. dollar. We continue to monitor any potential impact of the appreciation of the Renminbi on our operations in China as well as globally. Changes in the value of the Renminbi did not have a material impact on our results of operations for any period presented.in this Form 10-Q.

Interest Rates

Our interest rate risk relates primarily to our debt which totals $68.4 million (net of debt issuance costs) as of June 28, 2013, and carries interest rates pegged to either the PRIME rate or LIBOR. An immediate increase in interest rates of 100 basis points would increase our interest expense by approximately $0.2 million per quarter. This would be partially offset by increased interest income on our invested cash. Conversely, an immediate decline of 100 basis points in interest rates would decrease our interest expense by approximately $0.2 million per quarter. This would be partially offset by decreased interest income on our invested cash.

ITEM 4. Controls and Procedures

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934 (the Exchange Act), management, including our Chief Executive Officer and Chief Financial Officer, conducted an evaluation as of the end of the period covered by this report, of the effectiveness of our disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e). Based upon our evaluation, we concluded that our disclosure controls and procedures were effective as of June 28, 2013.

As required by Rule 13a-15(d), management, including our Chief Executive Officer and Chief Financial Officer, also conducted an evaluation of our internal control over financial reporting to determine whether any changes occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on our evaluation, we concluded that there has been no such change during the fiscal quarter covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. We completed the acquisition of AIT in July 2012 and are currently evaluating the internal controls at AIT. We intend to include this acquired entity into our assessment of the effectiveness of internal control over financial reporting in our fiscal 2013 annual management report, following the first anniversary of the acquisition.

Any system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system will be met. In addition, the design of any control system is based in part upon certain assumptions about the likelihood of future events.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

From time to time, we are subject to various legal proceedings and claims, either asserted or unasserted, that arise in the ordinary course of business. Although the outcome of the various legal proceedings and claims cannot be predicted with certainty, we have not had a history of outcomes to date that have been material to our statement of operations and do not believe that any of these proceedings or other claims will have a material effect on our consolidated financial condition or results of operations.

ITEM 1A. Risk Factors

The highly volatile nature of the industries we serve could harm our operating results.

Our business and operating results depend in significant part upon capital expenditures by manufacturers in the semiconductor capital equipment, flat panel, medical, energy and research industries, which in turn depend upon the current and anticipated market demand for such products. Historically, the industries we serve (in particular the semiconductor industry) have been highly cyclical, with recurring periods of over-supply of products that have had a severe negative effect on the demand for capital equipment used to manufacture such products. We have experienced and anticipate that we will continue to experience significant fluctuations in customer orders for our products through such cycles, including a continued decline in demand within the semiconductor capital equipment industry through the end of fiscal 2013. Slowdowns in the industries we serve have had, and future slowdowns may also have, a material adverse effect on our operating results. During periods of decreasing demand for our products, we must be able to appropriately align our cost structure with prevailing market conditions, effectively manage our supply chain and motivate and retain employees. During periods of increased demand, we must increase manufacturing capacity and inventory to meet customer demands, effectively manage our supply chain and attract, retain and motivate a sufficient number of employees. If we are not able to timely and appropriately adapt to the changes in our business environment, our results of operations will be harmed. Also, the cyclical and volatile nature of the industries we serve make future revenues, results of operations and net cash flows difficult to estimate.

We rely on a small number of customers for a significant portion of our sales, and any impairment of our relationships with these customers would adversely affect our business.

A relatively small number of OEM customers have historically accounted for a significant portion of our sales, and we expect this trend to continue. As a group, three customers accounted for 80%, 68% and 72% of our sales for fiscal years 2012, 2011 and 2010, respectively, and we expect that our sales will continue to be concentrated among a small number of customers. Because of the small number of OEMs in the markets we serve, most of which are already our customers, it would be difficult to replace lost revenue resulting from the loss of, or the reduction, cancellation or delay in purchase orders by, any one of these customers. Our customer contracts generally do not require customers to place any orders. Consolidation among our customers, or a decision by any one or more of our customers to outsource all or most manufacturing and assembly work to a single equipment manufacturer, may further concentrate our business in a limited number of customers and expose us to increased risks relating to dependence on an even smaller number of customers. For example, two of our largest semiconductor customers, Novellus Systems, Inc. and Lam Research Corporation, announced in June 2012 that they had completed a transaction pursuant to which they consolidated their businesses. Also, in November 2011, Applied Materials, Inc. completed the acquisition of Varian Semiconductor Equipment Associates, Inc., one of our customers. In addition, we have in the past lost business from customers who have taken the manufacturing of our products in-house. For example, we terminated our manufacturing services to FEI Company at the beginning of our second quarter of fiscal 2012. In addition, we announced in the third quarter of fiscal 2012 that one of our larger semiconductor equipment customers has decided to in-source a portion of their gas panel business. While this decision did not have a material impact on our revenue in fiscal 2012, it could have a negative quarterly impact of 7% to 9% on total revenue by the end of fiscal 2013. If we are unable to replace revenue from customers who determine to take subsystem assembly in-house, or if additional customers determine to in-source subsystem assembly, such events could have a material adverse impact on our financial position and results of operation.

In addition, by virtue of our largest customers size and the significant portion of revenue that our combined company derives from them, they are able to exert significant influence and pricing pressure in the negotiation of our commercial agreements and the conduct of our business with them. If we are unable to retain and expand our business with these customers on favorable terms, our business and operating results will be adversely affected.

We have had to qualify, and are required to maintain our status, as a supplier for each of our customers. This is a lengthy process that involves the inspection and approval by a customer of our engineering, documentation, manufacturing and quality control procedures before that customer will place volume orders. Our ability to lessen the adverse effect of any loss of, or reduction in sales to, an existing customer through the rapid addition of one or more new customers is minimal because of these qualification requirements. Consequently, our business, operating results and financial condition would be adversely affected by the loss of, or any reduction in orders by, any of our significant customers.

We are exposed to risks associated with weakness in the global economy.

We rely to a significant extent on OEM customers, whose business, in turn, depends largely on consumer spending and capital expenditures by businesses. Continuing difficulties in the financial markets and uncertainty regarding the global economy continue to pose challenges to our business. Economic uncertainty and related factors, including unemployment, the European debt crisis, inflation and fuel prices, exacerbate negative trends in business and consumer spending and may cause certain of our customers to push out, cancel, or refrain from placing orders for products or services, which may reduce sales. Difficulties in obtaining capital, uncertain market conditions, or reduced profitability may also cause some customers to scale back operations, exit businesses, merge with other manufacturers, or file for bankruptcy protection and potentially cease operations, leading to customers reduced research and development funding and/or capital expenditures and, in turn, lower orders from our customers and/or additional slow moving or obsolete inventory or bad debt expense for us. These conditions may also similarly affect key suppliers, which could impair their ability to deliver parts and result in delays for our products or require us to either procure products from high-cost suppliers, or if no additional suppliers exist, to reconfigure the design and manufacture of our products, and we may be unable to fulfill some customer orders. While past downturns in our business have been followed by periods of growth, this correlation may not occur in the future.

Table of Contents

We have significant existing indebtedness; the restrictive covenants under our credit agreement or other limitations on financing may limit our ability to expand or pursue our business strategy or make capital expenditures; if we are forced to prepay some or all of our indebtedness our financial position would be severely and adversely affected.

We have significant outstanding indebtedness. On July 3, 2012, we refinanced our prior credit facility and entered into our current credit agreement with Silicon Valley Bank, U.S. Bank National Association and HSBC Bank.

The current credit agreement provides for a new term loan in an aggregate principal amount of $40.0 million and a revolving credit facility in an aggregate principal amount of $40.0 million. On July 3, 2012, we borrowed $40.0 million under the term loan and $39.8 million under the revolving credit facility to finance our acquisition of AIT and repay Silicon Valley Bank as lender under our prior credit facility. As of June 28, 2013, the long-term portion of our outstanding indebtedness, net of debt issuance costs, under our credit facility was $19.7 million, and the short-term portion was $48.7 million.

Our credit agreement contains certain covenants that restrict our ability to take certain actions, including our ability to:

- incur additional debt, including guarantees, or create liens;
- pay dividends and make distributions in respect of our capital stock;
- repurchase capital stock;
- make investments or other restricted payments;
- engage in transactions with stockholders and affiliates;
- sell or otherwise dispose of assets;
- make payments on subordinated indebtedness; and
- engage in certain mergers and acquisitions, new lines of business or make other fundamental changes.

Our credit agreement also requires us to maintain certain financial and other covenants. We cannot assure you that we will be able to maintain compliance with such financial or other covenants. For example, for the measurement periods ending in November and December of 2012, the Company was not in compliance with the minimum consolidated fixed charge coverage ratio, the maximum consolidated leverage ratio or the minimum domestic cash balance covenants under the credit agreement. On February 15, 2013, the Company and its lenders amended the credit agreement in order for the lenders to waive such non-compliance and to modify the financial covenants contained in the credit agreement, effective January 30, 2013. We cannot assure you, however, that we will be able to meet the financial or other covenants under our amended credit agreement in subsequent periods. Our failure to comply with these covenants could result in an event of default which, if not cured or waived, could result in the acceleration of all of our indebtedness, which would adversely affect our financial health. We cannot assure you that we would have sufficient funds to repay all the outstanding amounts, and any acceleration of amounts due under our credit agreement would have a material adverse effect on us. If we are unable to meet our debt obligations, we could be forced to restructure or refinance such obligations, seek additional equity financing or sell assets, which we may not be able to do on satisfactory terms or at all.

In addition, the credit agreement has certain mandatory prepayment provisions, including annual prepayments of excess cash flow above certain thresholds. As long as our indebtedness remains outstanding, the restrictive covenants and mandatory prepayment provisions could impair our ability to expand or pursue our business strategies or obtain additional funding.

Our dependence on our suppliers may prevent us from delivering an acceptable product on a timely basis.

We rely on both single-source and sole-source suppliers, some of whom are relatively small, for many of the components we use in our products. In addition, our customers often specify components of particular suppliers that we must incorporate into our products. Our suppliers are under no obligation to provide us with components. As a result, the loss of or failure to perform by any of these providers could adversely affect our business and operating results. In addition, the manufacturing of certain components and subsystems is an extremely complex process. Therefore, if a supplier were unable to provide the volume of components we require on a timely basis and at acceptable prices and quality, we would have to identify and qualify replacements from alternative sources of supply. However, the process of qualifying new suppliers for complex components is also lengthy and could delay our production, which would adversely affect our business, operating results and financial condition.

Table of Contents

Disruption in supply resulting from natural disasters, such as the recent earthquakes, tsunami and related events in Japan, may result in certain of our suppliers being unable to deliver sufficient quantities of components or raw materials at all or in a timely manner. If we, or our vendors, are unable to procure sufficient quantities of components or raw materials from suppliers, it could influence decisions by our customers to delay or cancel orders and decisions by our vendors to fulfill our purchase orders and, consequently, have a material adverse effect on our results of operations.

We may also experience difficulty in obtaining sufficient supplies of components and raw materials in times of significant growth in our business. For example, we have in the past experienced shortages in supplies of various components, such as mass flow controllers, valves and regulators, and certain prefabricated parts, such as sheet metal enclosures, used in the manufacture of our products. In addition, one of our competitors manufactures mass flow controllers that may be specified by one or more of our customers. If we are unable to obtain these particular mass flow controllers from our competitor or convince a customer to select alternative mass flow controllers, we may be unable to meet that customer s requirements, which could result in a loss of market share.

We may not be able to respond quickly enough to increases in demand for our products.

Demand shifts in the industries we serve are rapid and difficult to predict, and we may not be able to respond quickly enough to an increase in demand. Our ability to increase sales of our products depends, in part, upon our ability to:

- mobilize our supply chain in order to maintain component and raw material supply;
- optimize the use of our design, engineering and manufacturing capacity in a timely manner;
- deliver our products to our customers in a timely fashion;
- expand, if necessary, our manufacturing capacity; and
- maintain our product quality as we increase production.

If we are unable to respond to rapid increases in demand for our products on a timely basis or to manage any corresponding expansion of our manufacturing capacity effectively, our customers could increase their purchases from our competitors, which would adversely affect our business.

We may not be able to fund our future capital requirements or strategic acquisitions from our operations, and financing from other sources may not be available on favorable terms or at all.

We made capital expenditures of approximately $0.6 million in fiscal 2012 and $4.0 million in fiscal 2011 related to our manufacturing facilities in the United States, China and Singapore. Capital expenditures only include AIT s capital expenditures from its acquisition date of July 3, 2012. In addition, we paid approximately $75.3 million in cash and issued 4.5 million shares of our common stock valued at $29.6 million for a total purchase price of $104.9 million in connection with our acquisition of AIT. The cash portion of the merger consideration was financed through the credit facility described above. The amount of our future capital requirements or strategic acquisitions will depend on many factors, including:

- the cost required to ensure access to adequate manufacturing capacity;
- the timing and extent of spending to support product development efforts;

the timing of introductions of new products and enhancements to existing products;

the cost required to complete AIT s enterprise resource planning implementation and to migrate AIT and its subsidiaries to our enterprise resource planning system;

changing manufacturing capabilities to meet new customer requirements;

market acceptance of our products; and

our ability to identify appropriate acquisition opportunities and successfully negotiate the terms of such acquisitions.

We had $71.3 million in cash and cash equivalents and no borrowings available under our revolving credit facility for future borrowings as of June 28, 2013. In addition, as of June 28, 2013, $41.6 million of our cash and cash equivalents was held by our foreign subsidiaries. If these funds are needed for our operations or to fund capital expenditures or other strategic acquisitions in the U.S., we would be required to accrue and pay U.S. taxes to repatriate these funds.

Table of Contents

Given our significant existing leverage, lack of additional availability under our current revolving line of credit and the potential tax effects of repatriating foreign cash, we may need to raise additional funds through public or private equity or debt financing if our current domestic cash and cash flow from operations are insufficient to fund our future activities. We may not be able to obtain additional debt financing when and if necessary in a timely manner. Access to capital markets has, in the past, been unavailable to companies such as ours and there can be no assurance that we would be able to complete an equity or other financing with terms satisfactory to us or at all. In addition, equity financings could be dilutive to holders of our common stock, and debt financings would likely involve additional covenants that restrict our business operations. Any potential strategic acquisition or significant capital expenditure may also require the consent of our existing lenders. If we cannot raise funds on acceptable terms, if and when needed, we may not be able to develop or enhance our products, take advantage of future opportunities, including potential acquisitions, grow our business or respond to competitive pressures or unanticipated requirements, any of which could adversely affect our business, operating results and financial condition.

Our quarterly revenue and operating results fluctuate significantly from period to period, and this may cause volatility in our common stock price.

Our quarterly revenue and operating results have fluctuated significantly in the past, and we expect them to continue to fluctuate in the future for a variety of reasons which may include:

- demand for and market acceptance of our products as a result of the cyclical nature of the industries we serve or otherwise, often resulting in reduced sales during industry downturns and increased sales during periods of industry recovery;
- overall economic conditions;
- changes in the timing and size of orders by our customers;
- strategic decisions by our customers to terminate their outsourcing relationship with us;
- strategic consolidation by our customers;
- cancellations and postponements of previously placed orders;
- pricing pressure from either our competitors or our customers, resulting in the reduction of our product prices;
- disruptions or delays in the manufacturing of our products or in the supply of components or raw materials that are incorporated into or used to manufacture our products, thereby causing us to delay the shipment of products;
- decreased margins for several or more quarters following the introduction of new products, especially as we introduce new subsystems;
- delays in ramp-up in production, low yields or other problems experienced at our manufacturing facilities in China;
- changes in design-to-delivery cycle times;

- inability to reduce our costs quickly in step with reductions in our prices or in response to decreased demand for our products;

- changes in our mix of products sold;

- write-offs of excess or obsolete inventory;

- one-time expenses or charges associated with failed acquisition negotiations or completed acquisitions;

- announcements by our competitors of new products, services or technological innovations, which may, among other things, render our products less competitive; and

- geographic mix of worldwide earnings.

As a result of the foregoing, we believe that quarter-to-quarter comparisons of our revenue and operating results may not be meaningful and that these comparisons may not be an accurate indicator of our future performance. Changes in the timing or terms of a small number of transactions could disproportionately affect our operating results in any particular quarter. Moreover, our operating results in one or more future quarters may fail to meet our guidance or the expectations of securities analysts or investors. If this occurs, we would expect to experience an immediate and significant decline in the trading price of our common stock.

We have established, and as markets will allow, intend to expand our operations in Asia, which exposes us to risks associated with operating in a foreign country.

Depending on market conditions, we intend to expand our operations in Asia, principally in China and Singapore. In addition, through our acquisition of AIT, we acquired a manufacturing facility in Cebu, Philippines. The carrying amount of our fixed assets in Asia was $3.8 million as of June 28, 2013.

We are exposed to political, economic, legal and other risks associated with operating in Asia, including:

- foreign currency exchange fluctuations;
- political, civil and economic instability;
- tariffs and other barriers;
- timing and availability of export licenses;
- disruptions to our and our customers operations due to the outbreak of diseases, such as SARS and avian flu;
- disruptions in operations due to China s developing domestic infrastructure, including transportation and energy;
- difficulties in developing relationships with local suppliers;
- difficulties in attracting new international customers;
- difficulties in accounts receivable collections;
- difficulties in staffing and managing distant international subsidiary and branch operations;
- the burden of complying with foreign and international laws and treaties;
- legal systems potentially subject to undue influence or corruption;
- difficulty in transferring funds to other geographic locations; and
- potentially adverse tax consequences, including restrictions on the repatriation of earnings.

Our operations in Asia also subject us to U.S. laws governing the export of equipment. These laws are complex and require us to obtain clearances for the export to Asia of certain equipment. We may fail to comply with these laws and regulations, which could require us to cease use of certain equipment and expose us to fines or penalties.

Over the past several years the Chinese government has pursued economic reform policies, including the encouragement of private economic activity and greater economic decentralization. The Chinese government may not continue these policies or may significantly alter them to our detriment from time to time without notice. Changes in laws and regulations or their interpretation, the imposition of confiscatory taxation policies, new restrictions on currency conversion or limitations on sources of supply could materially and adversely affect our Chinese operations, which could result in the partial or total loss of our investment in that country and materially and adversely affect our future operating results.

Table of Contents

We are subject to order and shipment uncertainties and any significant reductions, cancellations or delays in customer orders could cause our revenue to decline and our operating results to suffer.

Our revenue is difficult to forecast because we generally do not have a material backlog of unfilled orders and because of the short time frame within which we are often required to design, produce and deliver products to our customers. Most of our revenue in any quarter depends on customer orders for our products that we receive and fulfill in the same quarter. We do not have long-term purchase orders or contracts that contain minimum purchase commitments from our customers. Instead, we receive non-binding forecasts of the future volume of orders from our customers. Occasionally, we order and build component inventory in advance of the receipt of actual customer orders. Customers may cancel order forecasts, change production quantities from forecasted volumes or delay production for reasons beyond our control. Furthermore, reductions, cancellations or delays in customer order forecasts usually occur without penalty to or compensation from, the customer. Reductions, cancellations or delays in forecasted orders could cause us to hold inventory longer than anticipated, which could reduce our gross profit, restrict our ability to fund our operations and cause us to incur unanticipated reductions or delays in revenue. If we do not obtain orders as we anticipate, we could have excess component inventory for a specific product that we would not be able to sell to another customer, likely resulting in inventory write-offs, which could have a material adverse effect on our business, financial condition and operating results. In addition, because many of our costs are fixed in the short term, we could experience deterioration in our gross profit when our production volumes decline.

The manufacturing of our products is highly complex, and if we are not able to manage our manufacturing and procurement process effectively, our business and operating results will suffer.

The manufacturing of our products is a highly complex process that involves the integration of multiple components and requires effective management of our supply chain while meeting our customers design-to-delivery cycle time requirements. Through the course of the manufacturing process, our customers may modify design and system configurations in response to changes in their own customers requirements. In order to rapidly respond to these modifications and deliver our products to our customers in a timely manner, we must effectively manage our manufacturing and procurement process. If we fail to manage this process effectively, we risk losing customers and damaging our reputation. We may also be subject to liability under our agreements with our customers if we or our suppliers fail to re-configure manufacturing processes or components in response to these modifications, which may lead to product defect claims by our customers. In addition, if we acquire inventory in excess of demand or that does not meet customer specifications, we could incur excess or obsolete inventory charges. These risks are even greater during the current extended period of macroeconomic uncertainty and as we continue to expand our business beyond gas delivery systems into new subsystems. In the current economic environment, certain of our suppliers may be forced out of business, which could require us to either procure products from higher-cost suppliers or, if no additional suppliers exist, reconfigure the design and manufacture of our products. This could limit our growth and have a material adverse effect on our business, financial condition and operating results.

OEMs may not continue to outsource critical subsystems, which would adversely impact our operating results.

The success of our business depends on OEMs continuing to outsource the manufacturing of critical subsystems. Most of the largest OEMs have already outsourced production of a significant portion of their critical subsystems. If OEMs do not continue to outsource critical subsystems for their capital equipment, our revenue would be significantly reduced, which would have a material

Table of Contents

adverse effect on our business, financial condition and operating results. In addition, if we are unable to obtain additional business from OEMs, even if they continue to outsource their production of critical subsystems, our business, financial condition and operating results could be adversely affected.

If our new products are not accepted by OEMs or if we are unable to obtain historical margins on our new products, our operating results would be adversely impacted.

We design, develop and market critical subsystems to OEMs. The introduction of new products is inherently risky because it is difficult to foresee the adoption of new standards, coordinate our technical personnel and strategic relationships and win acceptance of new products by OEMs. We may not be able to recoup design and development expenditures if our new products are not accepted by OEMs. Newly introduced products typically carry lower gross margins than existing products for several or more quarters following their introduction. If any of our new subsystems are not successful in the market, or if we are unable to obtain gross margins on new products that are similar to the gross margins we have historically achieved, our business, operating results and financial condition could be adversely affected.

The success of our merger with AIT will depend, among other things, on successfully maintaining or improving relationships with AIT s pre-existing customers and motivating and retaining AIT s employees, and any failure to integrate successfully the businesses of Ultra Clean and AIT will adversely affect the combined company s future results.

Our acquisition of AIT in the third quarter of fiscal 2012 was a significant acquisition to us and the largest acquisition in our history. The success of our merger with AIT will depend, in large part, on the ability of the combined company to realize the anticipated benefits of the transaction, including combined capabilities and resources, new customers and, to a lesser extent, annual net operating synergies. To realize these anticipated benefits, the combined company must successfully integrate the businesses of Ultra Clean and AIT. Our efforts to fully integrate two companies that have previously operated independently may result in significant challenges, and we may be unable to accomplish the integration smoothly or successfully. The failure to integrate successfully and to manage successfully the challenges presented by the integration process may result in the combined company s failure to achieve some or all of the anticipated benefits of the merger. In particular, like us, AIT s revenue is concentrated in a small number of customers who do not have long-term purchase orders or contracts that contain minimum purchase commitments. AIT s customers may react negatively to the combined business and reduce or cease doing business with the combined company in favor of our competitors or taking our business in-house. The failure to maintain important customer relationships could have a material adverse effect on the business, financial condition or results of operations of the combined company. The integration also requires combining personnel with varied business backgrounds and combining businesses with different corporate cultures and objectives. AIT has its own unique business culture and business processes that may be disrupted in the process of integrating the businesses of the combined company. These disruptions could result in employee dissatisfaction and attrition, operational inefficiencies or increased operating costs and have a material adverse impact on the combined company s results of operation and financial condition.

Other potential difficulties that may be encountered in the integration process include the following:

- Complexities associated with managing the larger, more complex, combined business, including integrating supply and distribution channels, computer and accounting systems, and other aspects of operations;

- Ensuring AIT and the combined company are in compliance with public company obligations within required periods, including the corporate governance and other requirements of the Sarbanes-Oxley Act of 2002, to which AIT was not previously subject as a privately held company;

- Integrating capabilities from the two companies while maintaining focus on providing consistent, high quality products;

- Incorporating different financial and reporting controls, processes, systems and technologies into our existing business environment.

Potential unknown liabilities and unforeseen expenses, delays or regulatory conditions associated with the merger for which we do not have recourse under the merger agreement; and

Performance shortfalls at one or both of the companies as a result of the diversion of management s attention caused by integrating the companies operations.

32

Table of Contents

We may incur substantial costs associated with these activities and we may suffer other material adverse effects from our integration efforts, including write-downs, impairment charges or unforeseen liabilities which could negatively affect our operating results or financial position or could otherwise harm our business. We cannot assure you that the combined company will be successful or will realize expected operating efficiencies, revenue and earnings accretion and other benefits currently anticipated to result from the merger. The dedication of management resources to such integration may also detract attention from the day-to-day business, and we may need to hire additional management personnel to manage our acquisitions successfully, resulting in increased operating costs.

We may not be able to integrate efficiently the operations of other businesses acquired in the future, which would adversely affect the combined company s future results.

We have made, and may in the future make, acquisitions of, or significant investments in, businesses that offer complementary products, services, technologies or market access. For example, we acquired Sieger Engineering, Inc. in June 2006 and AIT in July 2012. Management also evaluates other potential strategic transactions regularly with its advisors and our board of directors in the ordinary course of business. If we identify an appropriate acquisition candidate, we may not be successful in negotiating the terms of the acquisition, financing the acquisition, or effectively integrating the acquired business, product or technology into our existing business and operations. Our due diligence may fail to identify all of the problems, liabilities or other shortcomings or challenges of an acquired business, product or technology, including issues related to intellectual property, product quality or product architecture, regulatory compliance practices, revenue recognition or other accounting practices or employee or customer issues.

Additionally, in connection with any acquisitions we are able to complete, we would likely face challenges in integrating the acquired business that are similar to those we may face in integrating AIT s operations that are discussed in the preceding risk factor. These challenges may result in substantial costs, the failure to achieve expected synergies or other anticipated benefits and other effects which could adversely affect our results of operations in a material way. The dedication of management resources to such integration or divestitures may divert attention from our day-to-day business, and we may need to hire additional management personnel to manage our acquisitions successfully.

Moreover, our recent acquisition of AIT could compound the challenges of integrating complementary products, services and technologies in the future. As discussed above, our integration with AIT is not complete, and the integration could divert a significant amount of management resources, resulting in less employee time and resources available to focus on negotiating and integrating new acquisitions.

If we finance future acquisitions by issuing convertible debt or equity securities, our existing stockholders may be diluted, which could affect the market price of our stock. Even if an acquisition or other investment is not completed, we may incur significant management time and effort and financial cost in evaluating such acquisition or investment, which has in the past had, and could in the future have, an adverse effect on our results of operations. Furthermore, due to the limited liquidity in the credit market and our existing leverage, the financing of any such acquisition may be difficult to obtain, and the terms of such financing may not be favorable.

If we were required to write down all or part of our goodwill, our net income and net worth could be materially adversely affected.

We had $55.9 million of goodwill recorded on our consolidated balance sheet as of June 28, 2013. Goodwill represents the excess of cost over the fair market value of net tangible and finite lived, identifiable intangible assets acquired in business combinations. If our market capitalization drops significantly below the amount of net equity recorded on our balance sheet, it could indicate a decline in our value and would require us to further evaluate whether our goodwill has been impaired. During the fourth quarter of each year, we perform an annual review of our goodwill to determine if it has become impaired, in which case we would write down the impaired portion of our goodwill. We also evaluate goodwill for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If we were required to write down all or a significant part of our goodwill, our operating results and net worth could be materially adversely affected.

Our business is largely dependent on the know-how of our employees, and we generally do not have a protected intellectual property position.

Our business is largely dependent upon our design, engineering, manufacturing and testing know-how. We rely on a combination of trade secrets and contractual confidentiality provisions and, to a much lesser extent, patents, copyrights and trademarks to protect our proprietary rights. Accordingly, our intellectual property position is more vulnerable than it would be if it were protected by patents. If we fail to protect our proprietary rights successfully, our competitive position could suffer, which could harm our operating results. We may be required to spend significant resources to monitor and protect our proprietary rights, and, in the event we do not detect infringement of our proprietary rights, we may lose our competitive position in the market if any such infringement occurs. In addition, competitors may design around our technology or develop competing technologies and know-how.

Third parties have claimed and may in the future claim we are infringing their intellectual property, which could subject us to litigation or licensing expenses, and we may be prevented from selling our products if any such claims prove successful.

We have in the past and may in the future receive claims that our products, processes or technologies infringe the patents or other proprietary rights of third

Table of Contents

parties. In addition, we may be unaware of intellectual property rights of others that may be applicable to our products. Any litigation regarding our patents or other intellectual property could be costly and time-consuming and divert our management and key personnel from our business operations, any of which could have a material adverse effect on our business and results of operations. The complexity of the technology involved in our products and the uncertainty of intellectual property litigation increase these risks. Claims of intellectual property infringement may also require us to enter into costly license agreements. However, we may not be able to obtain licenses on terms acceptable to us, or at all. We also may be subject to significant damages or injunctions against the development, manufacture and sale of certain of our products if any such claims prove successful.

If we do not keep pace with developments in the industries we serve and with technological innovation generally, our products may not be competitive.

Rapid technological innovation in the markets we serve requires us to anticipate and respond quickly to evolving customer requirements and could render our current product offerings and technology obsolete. Technological innovations are inherently complex. We must devote resources to technology development in order to keep pace with such rapidly evolving technologies. We believe that our future success will depend upon our ability to design, engineer and manufacture products that meet the changing needs of our customers. This requires that we successfully anticipate and respond to technological changes in design, engineering and manufacturing processes in a cost-effective and timely manner. If we are unable to integrate new technical specifications into competitive product designs, develop the technical capabilities necessary to manufacture new products or make necessary modifications or enhancements to existing products, our business prospects could be harmed.

The timely development of new or enhanced products is a complex and uncertain process which requires that we:

- design innovative and performance-enhancing features that differentiate our products from those of our competitors;
- identify emerging technological trends in the industries we serve, including new standards for our products;
- accurately identify and design new products to meet market needs;
- collaborate with OEMs to design and develop products on a timely and cost-effective basis;
- ramp-up production of new products, especially new subsystems, in a timely manner and with acceptable yields;
- successfully manage development production cycles; and
- respond effectively to technological changes or product announcements by others.

The industries in which we participate are highly competitive and rapidly evolving, and if we are unable to compete effectively, our operating results will be harmed.

Although we have not faced competition in the past from the largest subsystem and component manufacturers in the industries we serve, these suppliers could compete with us in the future. Increased competition has in the past resulted, and could in the future result, in price reductions, reduced gross margins or loss of market share, any of which would harm our operating results. We are subject to significant pricing pressure as we attempt to maintain and increase market share with our existing customers. Competitors may introduce new products for the markets currently served by our products. These products may have better performance, lower prices and achieve broader market acceptance than our products. Further, OEMs typically own the design rights to their products and may provide these designs to other subsystem manufacturers. If our competitors obtain proprietary rights to these designs such that we are unable to obtain the designs necessary to manufacture products for our OEM customers, our business, financial condition and operating results could be adversely affected.

Our competitors may have greater financial, technical, manufacturing and marketing resources than we do. As a result, they may 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. Moreover, there may be merger and acquisition activity among our competitors and potential competitors that may provide our competitors and potential competitors an advantage over us by enabling them to expand their product offerings and service capabilities to meet a broader range of customer needs. Further, if one of our customers develops or acquires the internal capability to develop and produce critical subsystems that we produce, the loss of that customer could have a material adverse effect on our business, financial condition and operating results. The introduction of new technologies and new market entrants may also increase competitive pressures.

We must achieve design wins to retain our existing customers and to obtain new customers.

New capital equipment typically has a lifespan of several years, and OEMs frequently specify which systems, subsystems, components and instruments are to be used in their equipment. Once a specific system, subsystem, component or instrument is incorporated into a piece of capital equipment, it will likely continue to be incorporated into that piece of equipment for at least several months before the OEM would be in a position to switch to the product of another supplier.

Accordingly, it is important that our products are designed into the new capital equipment of OEMs, which we refer to as a design win, in order to retain our competitive position with existing customers and to obtain new customers.

We incur technology development and sales expenses with no assurance that our products will ultimately be designed into an OEM s capital equipment. Further, developing new customer relationships, as well as increasing our market share at existing customers, requires a substantial investment of our sales, engineering and management resources without any assurance from prospective customers that they will place significant orders. We believe that OEMs often select their suppliers and place orders based on long-term relationships. Accordingly, we may have difficulty achieving design wins from OEMs that are not currently our customers. Our operating results and potential growth could be adversely affected if we fail to achieve design wins with leading OEMs.

Defects in our products could damage our reputation, decrease market acceptance of our products, cause the unintended release of hazardous materials and result in potentially costly litigation.

A number of factors, including design flaws, material and component failures, contamination in the manufacturing environment, impurities in the materials used and unknown sensitivities to process conditions, such as temperature and humidity, as well as equipment failures, may cause our products to contain undetected errors or defects. Problems with our products may:

- cause delays in product introductions and shipments;
- result in increased costs and diversion of development resources;
- cause us to incur increased charges due to unusable inventory;
- require design modifications;
- result in liability for the unintended release of hazardous materials;
- create claims for rework, replacement and/or damages under our contracts with customers;
- decrease market acceptance of, or customer satisfaction with, our products, which could result in decreased sales and product returns; or
- result in lower yields for semiconductor manufacturers.

If any of our products contain defects or have reliability, quality or compatibility problems, our reputation might be damaged and customers might be reluctant to buy our products. We may also face a higher rate of product defects as we increase our production levels. Product defects could result in the loss of existing customers or impair our ability to attract new customers. In addition, we may not find defects or failures in our products until after they are installed in a manufacturer s fabrication facility. We may have to invest significant capital and other resources to correct these problems. Our current or potential customers also might seek to recover from us any losses resulting from defects or failures in our products. Hazardous materials flow through and are controlled by our products and an unintended release of these materials could result in serious injury or death. Liability claims could require us to spend significant time and money in litigation or pay significant damages.

The technology labor market is very competitive, and our business will suffer if we are unable to hire and retain key personnel.

Our future success depends in part on the continued service of our key executive officers, as well as our research, engineering, sales, manufacturing and administrative personnel, most of whom are not subject to employment or non-competition agreements. In addition, competition for qualified personnel in the technology industry is intense, and we operate in geographic locations in which labor markets are particularly competitive.

Our business is particularly dependent on expertise which only a very limited number of engineers possess. The loss of any of our key employees and officers, including our Chief Executive Officer, our President and Chief Operating Officer, our Chief Financial Officer, any of our Senior Vice Presidents or any of the senior managers of AIT, or the failure to attract and retain new qualified employees, could adversely affect our business, operating results and financial condition.

The challenges of employee retention may also increase during the integration process with AIT because of the necessity of combining personnel with varied business backgrounds and combining different corporate cultures and objectives. The process of integrating operations and making such adjustments could cause an interruption of, or loss of momentum in, the activities of one or more of our businesses and the loss of key personnel. Employee uncertainty, lack of focus or turnover during the integration process may also disrupt our businesses.

If we fail to maintain an effective system of internal controls, we might not be able to report our financial results accurately or prevent fraud; in that case, our stockholders could lose confidence in our financial reporting, which would harm our business and could negatively impact the price of our stock.

Effective internal controls are necessary for us to provide reliable financial reports and prevent fraud. In addition, Section 404 of the Sarbanes-Oxley Act of 2002 requires us and our independent registered public accounting firm to evaluate and report on our internal control over financial reporting. The process of designing, implementing, maintaining and updating our internal controls and complying with Section 404 is expensive and time consuming, and requires significant attention from management and company resources. For example, we are in the process of integrating AIT into our internal control framework, and we and our independent registered public accounting firm will be required to evaluate and report on AIT s internal controls beginning as of the fiscal year ending December 27, 2013. We anticipate that integrating AIT will require substantial resources, and we cannot assure you that we will be able to successfully or effectively implement and maintain adequate controls over our financial processes at AIT. Even though we have concluded, and our independent registered public accounting firm has concurred, that our internal control over financial reporting provides reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles as of December 28, 2012, because of its inherent limitations, internal control over financial reporting may not prevent or detect fraud or misstatements, and our internal control may not be effective as of future periods. Failure to maintain existing or implement new or improved controls, or difficulties encountered in their implementation, could harm our results of operations or cause us to fail to meet our reporting obligations. If we or our independent registered public accounting firm discover a material weakness, the disclosure of that fact, even if quickly remedied, could reduce the market s confidence in our financial statements and harm our stock price.

Fluctuations in currency exchange rates may adversely affect our financial condition and results of operations.

Our international sales are denominated primarily, though not entirely, in U.S. dollars. Many of the costs and expenses associated with our Chinese subsidiaries and Singapore subsidiary are paid in Chinese Renminbi and Singapore dollars, respectively, and we expect our exposure to Chinese Renminbi and Singapore dollars to increase as we increase production in those facilities. In addition, purchases of some of our components are denominated in Japanese Yen and Euros. Changes in exchange rates among other currencies in which our revenue or costs are denominated and the U.S. dollar may affect our revenue, cost of sales and operating margins. While fluctuations in the value of our revenue, cost of sales and operating margins as measured in U.S. dollars have not materially affected our results of operations historically, we do not currently hedge our foreign exchange exposure, and exchange rate fluctuations could have an adverse effect on our financial condition and results of operations in the future.

Table of Contents

If environmental contamination were to occur in one of our manufacturing facilities, we could be subject to substantial liabilities.

We use substances regulated under various foreign, domestic, federal, state and local environmental laws in our manufacturing facilities. In addition, we may not be aware of all environmental laws or regulations that could subject us to liability in the U.S. or internationally. Our failure or inability to comply with existing or future environmental laws could result in significant remediation liabilities, the imposition of fines or the suspension or termination of the production of our products, and thus a material adverse impact on our business.

If our facilities were to experience catastrophic loss due to natural disasters, our operations would be seriously harmed.

Our facilities could be subject to a catastrophic loss caused by natural disasters, including fires and earthquakes. We have facilities in areas with above average seismic activity, such as our manufacturing facility in South San Francisco, California and our manufacturing and headquarters facilities in Hayward, California. If any of our facilities were to experience a catastrophic loss, it could disrupt our operations, delay production and shipments, reduce revenue and result in large expenses to repair or replace the facility. In addition, we have in the past experienced, and may in the future experience, extended power outages at our facilities. We do not carry insurance policies that cover potential losses caused by earthquakes or other natural disasters or power loss.

Changes in tax rates or tax assets and liabilities could affect results of operations.

As a global company, we are subject to taxation in the United States and various other countries. Significant judgment is required to determine and estimate worldwide tax liabilities. Our future annual and quarterly tax rates could be affected by numerous factors, including changes in the: (1) applicable tax laws; (2) amount and composition of pre-tax income in countries with differing tax rates; or (3) valuation of our deferred tax assets and liabilities.

In addition, we are subject to regular examination by the Internal Revenue Service and other tax authorities, and from time to time we initiate amendments to previously filed tax returns. We regularly assess the likelihood of favorable or unfavorable outcomes resulting from these examinations and amendments to determine the adequacy of our provision for income taxes, which requires estimates and judgments. Although we believe our tax estimates are reasonable, there can be no assurance that the tax authorities will agree with such estimates. We may have to engage in litigation to achieve the results reflected in the estimates, which may be time-consuming and expensive. There can be no assurance that we will be successful or that any final determination will not be materially different from the treatment reflected in our historical income tax provisions and accruals, which could materially and adversely affect our financial condition and results of operations.

Table of Contents

The market for our stock is subject to significant fluctuation.

The size of our public market capitalization is relatively small, and the average volume of our shares that are traded is relatively low. The market price of our common stock could be subject to significant fluctuations. Among the factors that could affect our stock price are:

- quarterly variations in our operating results;
- our ability to successfully introduce new products and manage new product transitions;
- changes in revenue or earnings estimates or publication of research reports by analysts;
- speculation in the press or investment community;
- strategic actions by us or our competitors, such as acquisitions or restructurings;
- announcements relating to any of our key customers, significant suppliers or the semiconductor manufacturing and capital equipment industry generally;
- general market conditions;
- the effects of war and terrorist attacks; and
- domestic and international economic factors unrelated to our performance.

The stock markets in general, and the markets for technology stocks in particular, have experienced extreme volatility that has often been unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the trading price of our common stock.

A sale of a substantial number of shares of our common stock by the former owner of AIT may cause the price of our common stock to decline.

Sales of a substantial number of shares of our common stock in the public market could harm the market price of our common stock. We issued 4.5 million shares of our common stock in connection with our acquisition of AIT, representing approximately 16% of our total common shares outstanding immediately following the completion of the merger. We entered into a lock-up and standstill agreement with AIT s former owner, AIT Holding Company, LLC, and certain of its affiliates which prohibited any sales of the shares until January 3, 2013. After January 3, 2013, the holders are permitted to sell up to 25% of the shares in any given 90-day period over the subsequent twelve months, after which twelve month period there are no further contractual transfer restrictions on the shares, and the shares can be freely sold by their holders, subject to compliance with state and federal securities laws. As the lock-up restrictions expire, the shares issued in connection with the merger will thus become available for resale in the public market, and such sales could significantly decrease the market price of our common stock.

If securities or industry analysts do not publish research or reports about our business, or if they issue an adverse opinion regarding our stock, our stock price and trading volume could decline.

The trading market for our common stock is influenced by the research and reports that industry or securities analysts publish about us or our business. If any of the analysts who cover us issue an adverse opinion regarding our stock, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

We do not currently intend to pay dividends on our common stock and, consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.

We do not intend to declare and pay dividends on our capital stock for the foreseeable future. We currently intend to invest our future earnings, if any, to fund our growth. Additionally, the terms of the credit agreement we entered into in July 2012 restricts our ability to pay dividends. Therefore, you are not likely to receive any dividends on your common stock for the foreseeable future.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not Applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

(a) Exhibits

The following exhibits are filed with this current Report on Form 10-Q for the quarter ended June 28, 2013:

4.1(1)	Amendment No. 1 to Registration Right Agreement dated June 13, 2013 between Ultra Clean Holdings, Inc. and AIT Holding Company LLC
10.1(2)	Ultra Clean Holdings, Inc. Amended and Restated Stock incentive Plan (Amended as of May 22, 2013)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer and the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Calculation Linkbase Document
101.DEF	XBRL Taxonomy Definition Linkbase Document
101.LAB	XBRL Taxonomy Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Incorporated by reference to Exhibit 4.5 to Amendment No. 3 to Registration Statement on Form S-1 on Form S-3 (File No. 333-184941) filed with the SEC on June 13, 2013.

(2) Incorporated by reference to Exhibit 10.1 of the Company s Current Report on Form 8-K filed with the SEC on May 24, 2013

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ULTRA CLEAN HOLDINGS, INC.
(Registrant)

Date: August 2, 2013

By:	/s/ CLARENCE L. GRANGER
Name:	**Clarence L. Granger**
Title:	**Chairman and Chief Executive Officer**
	(Principal Executive Officer and duly authorized signatory)

Date: August 2, 2013

By:	/s/ KEVIN C. EICHLER
Name:	**Kevin C. Eichler**
Title:	**Chief Financial Officer**
	(Principal Financial Officer and duly authorized signatory)

Exhibit Index

Exhibit Number	Description
4.1(1)	Amendment No. 1 to Registration Right Agreement dated June 13, 2013 between Ultra Clean Holdings, Inc. and AIT Holding Company LLC
10.1(2)	Ultra Clean Holdings, Inc. Amended and Restated Stock incentive Plan (Amended as of May 22, 2013)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer and the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Calculation Linkbase Document
101.DEF	XBRL Taxonomy Definition Linkbase Document
101.LAB	XBRL Taxonomy Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Incorporated by reference to Exhibit 4.5 to Amendment No. 3 to Registration Statement on Form S-1 on Form S-3 (File No. 333-184941) filed with the SEC on June 13, 2013.

(2) Incorporated by reference to Exhibit 10.1 of the Company s Current Report on Form 8-K filed with the SEC on May 24, 2013