FORMFACTOR INC
Form 10-Q
July 29, 2015

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

Form 10-Q

(Mark one)

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

For the quarterly period ended June 27, 2015

Or

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

For the transition period from to

Commission file number: 000-50307

FormFactor, Inc.
(Exact name of registrant as specified in its charter)

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

7005 Southfront Road, Livermore, California 94551
(Address of principal executive offices, including zip code)

(925) 290-4000
(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 ý No o

Indicate by check mark whether the registrant 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 the 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 ý No o

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

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

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

As of July 28, 2015, 58,068,157 shares of the registrant’s common stock, par value $0.001 per share, were outstanding.

FORMFACTOR, INC.

FORM 10-Q FOR THE QUARTERLY PERIOD ENDED JUNE 27, 2015

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

FORMFACTOR, INC.

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

	Three Months Ended		Six Months Ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Revenues	$73,885	$67,352	$144,714	$123,311
Cost of revenues	50,582	47,328	98,621	90,962
Gross profit	23,303	20,024	46,093	32,349
Operating expenses:				
Research and development	11,217	11,074	22,302	20,821
Selling, general and administrative	11,381	13,191	23,265	25,445
Restructuring charges, net	—	59	503	2,056
Impairment of long-lived assets	8	—	8	743
Total operating expenses	22,606	24,324	46,078	49,065
Operating income (loss)	697	(4,300)	15	(16,716)
Interest income, net	65	79	149	158
Other income (expense), net	100	(156)	1,602	(222)
Income (loss) before income taxes	862	(4,377)	1,766	(16,780)
Provision (benefit) for income taxes	24	(51)	145	257
Net income (loss)	$838	$(4,326)	$1,621	$(17,037)
Net income (loss) per share:				
Basic	$0.01	$(0.08)	$0.03	$(0.31)
Diluted	$0.01	$(0.08)	$0.03	$(0.31)
Weighted-average number of shares used in per share calculations:				
Basic	58,109	55,812	57,532	55,431
Diluted	59,094	55,812	58,874	55,431

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

FORMFACTOR, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)
(Unaudited)

	Three Months Ended		Six Months Ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Net income (loss)	$ 838	$ (4,326)	$ 1,621	$ (17,037)
Other comprehensive (loss) income, net of tax:				
Foreign currency translation adjustments	(302)	297	(248)	438
Unrealized gains on available-for-sale marketable securities	1	22	11	24
Other comprehensive (loss) income, net of tax	(301)	319	(237)	462
Comprehensive income (loss)	$ 537	$ (4,007)	$ 1,384	$ (16,575)

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

FORMFACTOR, INC.

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

	June 27, 2015	December 27, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 137,088	$ 113,940
Marketable securities	41,668	49,897
Accounts receivable, net	43,979	45,152
Inventories, net	24,247	25,548
Deferred tax assets	2,030	2,036
Refundable income taxes	—	782
Prepaid expenses and other current assets	7,602	6,919
Total current assets	256,614	244,274
Restricted cash	435	435
Property, plant and equipment, net	24,485	25,498
Goodwill	30,731	30,731
Intangibles, net	32,187	38,689
Deferred tax assets	3,437	3,466
Other assets	864	1,150
Total assets	$ 348,753	$ 344,243
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 21,449	$ 20,274
Accrued liabilities	19,660	21,217
Income taxes payable	180	68
Deferred revenue	5,766	6,303
Total current liabilities	47,055	47,862
Long-term income taxes payable	902	1,094
Deferred tax liabilities	2,208	2,208
Deferred rent and other liabilities	3,580	3,643
Total liabilities	53,745	54,807
Commitments and contingencies (Note 16)		
Stockholders' equity:		
Preferred stock, $0.001 par value:		
10,000,000 shares authorized; no shares issued and outstanding at June 27, 2015 and December 27, 2014, respectively	—	—
Common stock, $0.001 par value:		
250,000,000 shares authorized; 58,368,157 and 56,518,428 shares issued and outstanding at June 27, 2015 and December 27, 2014, respectively	58	57
Additional paid-in capital	715,863	711,676
Accumulated other comprehensive loss	(1,998)	(1,761)
Accumulated deficit	(418,915)	(420,536)
Total stockholders' equity	295,008	289,436
Total liabilities and stockholders' equity	$ 348,753	$ 344,243

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

FORMFACTOR, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended	
	June 27, 2015	June 28, 2014
Cash flows from operating activities:		
Net income (loss)	$1,621	$(17,037)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation and amortization	11,908	16,185
Amortization of discount on investments	—	168
Stock-based compensation expense	5,415	6,089
Deferred income tax provision (benefit)	7	(46)
(Benefit) provision for doubtful accounts receivable	(11)	1
Provision for excess and obsolete inventories	2,964	3,830
Loss on disposal and write-off of long-lived assets	—	2
Impairment of long-lived assets	8	743
Non-cash restructuring	500	600
Foreign currency transaction losses (gains)	681	(178)
Changes in assets and liabilities:		
Accounts receivable	1,077	(11,633)
Inventories	(1,663)	(5,170)
Prepaid expenses and other current assets	(817)	(436)
Refundable income taxes	782	—
Other assets	259	—
Accounts payable	1,051	2,400
Accrued liabilities	(1,640)	3,500
Income tax payable	(81)	140
Deferred rent and other liabilities	148	112
Deferred revenues	(539)	209
Net cash provided by (used in) operating activities	21,670	(521)
Cash flows from investing activities:		
Acquisition of property, plant and equipment	(4,245)	(2,994)
Proceeds from sale of subsidiary	35	54
Purchases of marketable securities	(23,761)	(31,693)
Proceeds from maturities of marketable securities	32,000	44,275
Net cash provided by investing activities	4,029	9,642
Cash flows from financing activities:		
Proceeds from issuances of common stock	1,803	1,426
Purchase and retirement of common stock	(3,508)	—
Payments made on capital leases	—	(271)
Net cash (used in) provided by financing activities	(1,705)	1,155
Effect of exchange rate changes on cash and cash equivalents	(846)	387
Net increase in cash and cash equivalents	23,148	10,663
Cash and cash equivalents, beginning of period	113,940	59,196
Cash and cash equivalents, end of period	$137,088	$69,859
Supplemental cash flow disclosures:		

Changes in accounts payable and accrued liabilities related to property, plant and equipment purchases	$42	$(394)
Income and property taxes (refunded) paid, net	$(819)	$123

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

FORMFACTOR, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 — Basis of Presentation and Summary of Significant Accounting Policies

Basis of presentation. The accompanying unaudited condensed consolidated interim financial statements of FormFactor, Inc. and our subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X of the U.S. Securities and Exchange Commission (the "SEC"). Our interim financial statements do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary to fairly present our financial position, results of operations and cash flows have been included. Operating results for the three and six months ended June 27, 2015 are not necessarily indicative of the results that may be expected for the year ending December 26, 2015, or for any other period. The balance sheet at December 27, 2014 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements. The condensed consolidated financial statements include our accounts as well as those of our wholly-owned subsidiaries after elimination of all inter-company balances and transactions.

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in our condensed consolidated financial statements and accompanying notes. Actual results could differ from those estimates, and may result in material effects on our consolidated operating results and financial position.

These financial statements and notes should be read with the consolidated financial statements and notes for the year ended December 27, 2014 included in our Annual Report on Form 10-K filed with the SEC on March 6, 2015.

Fiscal year. We operate on a 52/53 week fiscal year, whereby the fiscal year ends on the last Saturday of December. Fiscal 2015 and 2014 each contain 52 weeks and the three and six months ended June 27, 2015 and June 28, 2014 each contained 13 and 26 weeks, respectively. Fiscal 2015 will end on December 26, 2015.

Critical Accounting Policies. Our critical accounting policies have not changed during the three and six months ended June 27, 2015 from those disclosed in our Annual Report on Form 10-K for the year ended December 27, 2014.

Note 2 — Concentration of Credit and Other Risks

Financial instruments that potentially subject us to concentrations of credit risk consist primarily of cash equivalents, marketable securities and trade receivables. Our cash equivalents and marketable securities are held in safekeeping by large, credit worthy financial institutions. We invest our excess cash primarily in U.S. banks, government and agency bonds, money market funds and corporate obligations. We have established guidelines relative to credit ratings, diversification and maturities that seek to maintain safety and liquidity. Deposits in these banks may exceed the amounts of insurance provided on such deposits. To date, we have not experienced any losses on our deposits of cash and cash equivalents.
We market and sell our products to a narrow base of customers and generally do not require collateral. The following customers accounted for more than 10% of our revenues for the periods indicated:

	Three Months Ended	Six Months Ended

	June 27, 2015		June 28, 2014		June 27, 2015		June 28, 2014	
Micron	17.8	%	12.2	%	14.3	%	13.5	%
Intel	17.1		19.5		17.8		18.0	
Samsung	13.1		*		13.4		*	
SK hynix	13.0		21.4		15.2		19.5	
	61.0	%	53.1	%	60.7	%	51.0	%

* Less than 10% of revenues.

At June 27, 2015, two customers accounted for 18% and 15% of gross accounts receivable. At December 27, 2014, two customers accounted for approximately 26% and 18% of gross accounts receivable. No other customers accounted for more than 10% of gross accounts receivable at either of these fiscal period ends. We operate in the intensely competitive semiconductor industry, including the Dynamic Random Access Memory, or DRAM, Flash memory, and System-on-Chip, or SoC markets, which have been characterized by price erosion, rapid technological change, short product life, cyclical market patterns and heightened foreign and domestic competition. Significant technological changes in the industry could adversely affect our operating results.

Certain components for our wafer probe card products that meet our requirements are available only from a limited number of suppliers. The rapid rate of technological change and the necessity of developing and manufacturing products with short life cycles may intensify our reliance on such suppliers. The inability to obtain components as required, or to develop alternative sources, if and as required in the future, could result in delays or reductions in product shipments, which in turn could have a material adverse effect on our business, financial condition, results of operations or cash flows.

Note 3 — Goodwill and Intangible Assets

Goodwill recorded from the acquisition of MicroProbe on October 16, 2012 was $30.7 million as of June 27, 2015 and remained unchanged from the amounts recorded as of December 27, 2014. The Company has not recorded any historical goodwill impairments as of June 27, 2015.

The changes in intangible assets during the six months ended June 27, 2015 and the net book value of intangible assets as of June 27, 2015 and December 27, 2014 were as follows (in thousands):

	Intangible Assets, Gross Amount			Accumulated Amortization			Intangible Assets, Net		Weighted Average Useful Life
Other Intangible Assets (1)	December 27, 2014	Additions/Disposals	June 27, 2015	December 27, 2014	Expense, net	June 27, 2015	December 27, 2014	June 27, 2015	June 27, 2015
Existing developed technologies	$51,248	$ 2,400	$53,648	$35,045	$5,176	$40,221	$16,203	$13,427	2.1
Trade name	4,388	—	4,388	970	218	1,188	3,418	3,200	7.3
Customer relationships	17,000	—	17,000	4,832	1,108	5,940	12,168	11,060	5.3
Total finite-lived intangible assets	72,636	2,400	75,036	40,847	6,502	47,349	31,789	27,687	
In-process research and development	6,900	(2,400)	4,500	—	—	—	6,900	4,500	
Total intangible assets	$79,536	$ —	$79,536	$40,847	$6,502	$47,349	$38,689	$32,187	

(1) Excludes fully amortized intangible assets

During the six months ended June 27, 2015, a purchased in-process research and development ("IPR&D") project with a carrying value of $2.4 million was completed and reclassified as a finite-lived intangible asset, and is currently being amortized over its estimated useful life.

The remaining IPR&D asset is classified as an indefinite lived intangible asset that is not currently subject to amortization but is reviewed for impairment annually or whenever events or changes in circumstances indicate that the carrying value of such asset may not be recoverable. The IPR&D asset will be subject to amortization upon completion of its respective research project and at the start of commercialization. The fair value assigned to the IPR&D asset was determined using the income approach based on estimates and judgments regarding risks inherent in the development process, including the likelihood of achieving technological success and market acceptance. If the IPR&D project is abandoned, the acquired technology attributable to the project will be expensed in the Condensed Consolidated Statements of Operations.

For the three and six months ended June 27, 2015, amortization expense of $2.6 million and $0.7 million, and $5.2 million and $1.3 million, respectively, was included in cost of revenues and selling, general and administrative expenses, respectively. For the three and six months ended June 28, 2014, amortization expense of $4.4 million and $0.7 million, and $8.8 million and $1.4 million, respectively, was included in cost of revenues and selling, general and administrative expenses, respectively.

Based on the carrying values of the finite-lived intangible assets recorded as of June 27, 2015 and assuming no subsequent additions to or impairment of the underlying assets, the remaining estimated annual amortization expense is expected to be as follows (in thousands):

Fiscal Year	Amount
2015	$6,635
2016	9,511
2017	3,314
2018	2,949
2019	2,447
and thereafter	2,831
Total	$27,687

Note 4 — Restructuring Charges

Restructuring charges include costs related to employee termination benefits, cost of long-lived assets abandoned or impaired, as well as contract termination costs. Restructuring charges are reflected separately as "Restructuring charges, net" in the Condensed Consolidated Statements of Operations. A summary of the actions we have taken during the three and six months ended June 27, 2015 and June 28, 2014, the purposes of which were to improve operating efficiency, streamline and simplify our operations and reduce our operating costs, are discussed below.

2015 Restructuring Activities

There were no restructuring activities during the three months ended June 27, 2015. During the three months ended March 28, 2015, we recorded stock-based compensation expense of approximately $0.5 million relating to the modification of certain equity-based awards of a full-time employee who was notified of his termination during the fourth quarter of fiscal 2014. The severance terms relating to the modification of his equity-based awards were finalized during the first quarter of fiscal 2015.

2014 Restructuring Activities

On January 27, 2014, we announced a global organizational restructuring and cost reduction plan. As part of the plan, we eliminated 52 full-time employees. In addition, we reduced our temporary workforce by 9 positions. We recorded $2.0 million of restructuring charges during the first quarter of fiscal 2014, which was comprised of $1.4 million in severance and related benefits and $0.6 million in impairment charges for certain equipment that would no longer be utilized. During the three months ended June 28, 2014, we eliminated an additional 2 full-time employees and recorded $59 thousand in severance charges. The activities comprising these restructuring activities and the related cash payments were completed and paid by June 28, 2014.

The activities in the restructuring accrual for the six months ended June 27, 2015 were as follows (in thousands):

	Employee Severance and Benefits	Stock-based Compensation	Total
Accrual at December 27, 2014	$584	$—	$584
Restructuring charges	—	500	500
Cash Payments	(569)	—	(569)
Adjustment to restructuring charges	3	—	3
Non-cash settlement	—	(500)	(500)

Accrual at June 27, 2015	$ 18	$ —	$ 18

The activities in the restructuring accrual for the three months ended June 28, 2014 were as follows (in thousands):

	Employee Severance and Benefits	Property and Equipment Impairment	Total
Accrual at December 28, 2013	$ 138	$ —	$ 138
Restructuring charges	1,456	600	2,056
Cash payments	(1,592)	—	(1,592)
Asset impairments	—	(600)	(600)
Non-cash settlements	(2)	—	(2)
Accrual at June 28, 2014	$ —	$ —	$ —

Note 5 — Fair Value
Assets Measured at Fair Value on a Recurring Basis

We measure and report certain assets and liabilities at fair value on a recurring basis, including money market funds, U.S. Treasury securities, agency securities and foreign currency derivatives (see Note 17 to the Condensed Consolidated Financial Statements - Derivative Financial Instruments, for a discussion of fair value of foreign currency derivatives).

Assets measured at fair value on a recurring basis as of June 27, 2015 was as follows (in thousands):

	Level 1	Level 2	Total
Assets:			
Cash equivalents			
Money market funds	$ 82,627	$ —	$ 82,627
Marketable securities			
U.S. Treasuries	—	27,414	27,414
Agency securities (Federal)	—	14,254	14,254
Total	$ 82,627	$ 41,668	$ 124,295

Assets measured at fair value on a recurring basis as of December 27, 2014 was as follows (in thousands):

	Level 1	Level 2	Total
Assets:			
Cash equivalents			
Money market funds	$ 65,303	$ —	$ 65,303
Marketable securities			
U.S. Treasuries	—	42,395	42,395
Agency securities (Federal)	—	7,502	7,502
Total	$ 65,303	$ 49,897	$ 115,200

The Level 1 assets consist of our money market fund deposits. The Level 2 assets consist of our available-for-sale investment portfolio, which are valued utilizing a market approach. Our investments are priced by pricing vendors who provided observable inputs for their pricing without applying significant judgment. Broker pricing is used mainly when a quoted price is not available, the investment is not priced by our pricing vendors or when a broker price is more reflective of fair values in the market in which the investment trades. Our broker-priced investments are labeled as Level 2 investments because fair values of these investments are based on similar assets without applying significant judgments. In addition, all of our investments have a sufficient level of trading volume to demonstrate that the fair values used are appropriate for these investments.

We did not have any transfers of assets measured at fair value on a recurring basis to or from Level 1 and Level 2 during each of the three and six months ended June 27, 2015 and June 28, 2014.

Assets Measured at Fair Value on a Non-Recurring Basis

We measure and report goodwill and intangible assets at fair value on a non-recurring basis if we determine these assets to be impaired. Refer to Note 3 to the Condensed Consolidated Financial Statements-Goodwill and Intangible Assets, for further details. There were no assets measured at fair value on a nonrecurring basis during the three and six months ended June 27, 2015 and June 28, 2014.

Note 6 — Marketable Securities

We classify our marketable securities as available-for-sale. All marketable securities represent the investment of funds available for current operations, notwithstanding their contractual maturities. Such marketable securities are recorded at fair value and unrealized gains and losses are recorded in accumulated other comprehensive income until realized.

Marketable securities at June 27, 2015 consisted of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasuries	$27,393	$21	$—	$27,414
Agency securities (Federal)	14,255	—	(1)	14,254
	$41,648	$21	$(1)	$41,668

Marketable securities at December 27, 2014 consisted of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasuries	$42,386	$13	$(4)	$42,395
Agency securities (Federal)	7,502	—	—	7,502
	$49,888	$13	$(4)	$49,897

The marketable securities with gross unrealized losses have been in a loss position for less than twelve months as of June 27, 2015 and December 27, 2014, respectively.

When evaluating the investments for other-than-temporary impairment, we review factors such as the length of time and extent to which fair value has been below the amortized cost basis, review of current market liquidity, interest rate risk, the financial condition of the issuer, as well as credit rating downgrades. We believe that the unrealized losses are not other-than-temporary. We do not have a foreseeable need to liquidate the portfolio and anticipate recovering the full cost of the securities either as market conditions improve or as the securities mature.

Contractual maturities of marketable securities as of June 27, 2015 were as follows (in thousands):

	Amortized Cost	Fair Value
Due in one year or less	$41,648	$41,668
Due after one year to five years	—	—

	$41,648	$41,668

There were no realized gains and losses on sales and maturities of marketable securities during the three and six months ended June 27, 2015 and June 28, 2014, respectively.

Note 7 — Allowance for Doubtful Accounts

A reconciliation of the changes in our allowance for doubtful accounts receivable for the six months ended June 27, 2015 and June 28, 2014, respectively, is as follows (in thousands):

	June 27, 2015	June 28, 2014
Balance at beginning of period	$266	$265
Additions	—	5
Reductions	(11)	(4)
Balance at end of period	$255	$266

Note 8 — Inventories

Inventories consisted of the following (in thousands):

	June 27, 2015	December 27, 2014
Raw materials	$9,701	$10,646
Work-in-progress	12,927	12,813
Finished goods	1,619	2,089
	$24,247	$25,548

Note 9 — Warranty

A reconciliation of the changes in our warranty liability for the six months ended June 27, 2015 and June 28, 2014, respectively, is as follows (in thousands):

	June 27, 2015	June 28, 2014
Balance at beginning of period	$1,592	$691
Accruals	828	1,260
Settlements	(1,338)	(1,066)
Balance at the end of period	$1,082	$885

Note 10 — Long-lived Assets

Impairment of long-lived assets

During the six months ended June 27, 2015, long-lived asset impairment charges recorded were insignificant. During the six months ended June 28, 2014, we recorded $0.7 million of impairments related to manufacturing assets we no longer utilized. These charges were included in "Impairment of long-lived assets" in the Condensed Consolidated Statements of Operations in their respective periods.

Long-lived Assets

Property, plant and equipment consisted of the following (in thousands):

	June 27, 2015	December 27, 2014
Machinery and equipment	$ 148,780	$ 145,995
Computer equipment and software	28,898	28,953
Furniture and fixtures	5,401	5,402
Leasehold improvements	66,759	66,821
Sub total	249,838	247,171
Less: accumulated depreciation and amortization	(228,786)	(224,135)
Net long-lived assets	21,052	23,036
Construction-in-progress	3,433	2,462
Total	$ 24,485	$ 25,498

Assets held for sale

There were no assets held for sale as of June 27, 2015. During the six months ended June 28, 2014, we reclassified $0.6 million of building and $0.5 million of machinery and equipment from "Property, plant and equipment, net" to "Prepaid expenses and other current assets" in our balance sheet as these assets were identified as held for sale as of June 28, 2014. The sale of the building closed during the third quarter of fiscal 2014 and we recorded a gain of $0.2 million on the sale during the third quarter of fiscal 2014.

Refer to Note 3 to the Condensed Consolidated Financial Statements - Goodwill and Intangible Assets for further details relating to our intangible long-lived assets.

Note 11 — Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss includes foreign currency translation adjustments and unrealized losses on available-for-sale securities, net of tax, the impact of which has been excluded from earnings and reflected as components of stockholders' equity as shown below (in thousands):

	June 27, 2015	December 27, 2014
Unrealized loss on marketable securities, net of tax of $428 at June 27, 2015 and December 27, 2014, respectively	$ (408)	$ (419)
Cumulative translation adjustments	(1,590)	(1,342)
Accumulated other comprehensive loss	$ (1,998)	$ (1,761)

Note 12 — Stockholders’ Equity

Common Stock Repurchase Program

On April 16, 2015, our Board of Directors authorized a program to repurchase up to $25.0 million of outstanding common stock. Under the authorized stock repurchase program, we may repurchase shares from time to time on the open market. The pace of repurchase activity will depend on levels of cash generation, current stock price and other factors. The stock repurchase program was announced on April 16, 2015 and expires on April 15, 2016. The program may be modified or discontinued at any time. During the three months ended June 27, 2015, under this repurchase authorization, we repurchased 400,362 shares of common stock for approximately $3.5 million.

Repurchased shares are retired upon the settlement of the related trade transactions. Our policy related to repurchases of our common stock is to charge the excess of cost over par value to additional paid-in capital. All repurchases were made in compliance with Rule 10b-18 under the Securities Exchange Act of 1934, as amended.

Restricted Stock Units

Restricted stock unit (RSU) activity under our equity incentive plan during the six months ended June 27, 2015 is set forth below:

	Units	Weighted Average Grant Date Fair Value
Restricted stock units at December 27, 2014	3,250,046	$ 6.07
Awards granted	1,478,750	8.70
Awards vested	(1,922,779)	6.04
Awards canceled	(138,619)	6.18
Restricted stock units at June 27, 2015	2,667,398	$ 7.54

On May 28, 2015, we issued 195,000 RSUs to seven senior executives of our company that will vest based on certain market performance criteria. The performance criteria are based on a metric called our Total Shareholder Return (TSR) for the period from April 1, 2015 to March 31, 2017 relative to the TSR of the companies identified as being part of the S&P Semiconductor Select Industry Index (FormFactor peer companies), as of April 1, 2015. The total stock-based compensation cost of approximately $1.5 million will be recognized ratably over the requisite service period.

On May 5, 2014, we issued 350,000 RSUs to seven senior executives of our company that will vest based on certain market performance criteria. The performance criteria are based on our TSR for the period from April 1, 2014 to March 31, 2016 relative to the TSR of the companies identified as being part of the S&P Semiconductor Select Industry Index (FormFactor peer companies), as of April 1, 2014. The total stock-based compensation cost of approximately $1.8 million will be recognized ratably over the requisite service period.

On May 6, 2013, we issued 355,000 RSUs to seven senior executives and one non-executive of our company that would vest based on certain market performance criteria. The performance criteria were based on our TSR for the period from April 1, 2013 to March 31, 2015 relative to the TSR of the companies identified as being part of the S&P Semiconductor Select Industry Index (FormFactor peer companies), as of April 1, 2013. On April 8, 2015, upon the review of the market performance criteria, our Compensation Committee certified a total earn out of 443,750 RSUs which immediately vested as of this date.

The total fair value of RSUs vested during the three and six months ended June 27, 2015 and June 28, 2014 was $10.0 million and $17.5 million, and $4.3 million and $7.1 million, respectively.

Stock Options

During the three months ended June 27, 2015, we did not grant any stock options. During the three months ended March 28, 2015, we granted 450,000 stock options to our Chief Executive Officer with a grant-date fair value of approximately $1.7 million which will be recognized as stock compensation expense ratably over the service period. The following weighted average assumptions were used in the estimated grant-date fair value calculations using the Black-Scholes option pricing model:

Stock Options:		
Dividend yield	—	%
Expected volatility	47.5	%
Risk-free interest rate	1.57	%

Expected term (in years)	5.52

During the six months ended June 28, 2014, we did not grant any stock options.

Note 13 — Stock-Based Compensation

We account for all stock-based compensation to employees and directors, including grants of RSUs and stock options, as stock-based compensation costs based on the fair value measured as of the date of grant. These costs are recognized as an expense in the Condensed Consolidated Statements of Operations over the requisite service period.

The table below shows stock-based compensation charges included in the Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended		Six Months Ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Stock-based compensation included in:				
Cost of revenues	$602	$661	$1,185	$1,155
Research and development	726	937	1,571	1,561
Selling, general and administrative	1,178	1,921	2,659	3,373
Total stock-based compensation	2,506	3,519	5,415	6,089
Tax effect of stock-based compensation	—	—	—	—
Total stock-based compensation, net of tax	$2,506	$3,519	$5,415	$6,089

During the six months ended June 27, 2015, we recorded stock-based compensation expense of approximately $0.5 million relating to a full-time employee who was impacted by our restructuring activities. Hence, we classified this stock-based compensation expense as a restructuring expense and the table above therefore does not include this expense. Refer to Note 4 to the Condensed Consolidated Financial Statements - Restructuring Charges for further details.

Employee Stock Purchase Plan

Under our 2012 Employee Stock Purchase Plan ("ESPP"), the offering periods are 12 months commencing on February 1 of each calendar year and ending on January 31 of the subsequent calendar year, and a six month fixed offering period commencing on August 1 of each calendar year and ending on January 31 of the subsequent calendar year. The 12 month offering period consists of two six month purchase periods and the six month offering period consists of one six month purchase period. The price of the common stock purchased is 85% of the lesser of the fair market value of the common stock on the first day of the applicable offering period or the last day of each purchase period.

During the three months ended June 27, 2015 and June 28, 2014, we did not issue any ESPP shares. During the six months ended June 27, 2015 and June 28, 2014, we issued 302,705 and 320,919 ESPP shares, respectively.

The following weighted-average assumptions were used in estimating the fair value of employees' purchase rights under our approved employee stock purchase plans:

	Three Months Ended		Six Months Ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
ESPP:				
Dividend yield	— %	— %	— %	— %
Expected volatility	54.7 %	42.5 %	51.7 %	40.9 %
Risk-free interest rate	0.07 %	0.07 %	0.08 %	0.11 %

Expected term (in years)	0.50	0.50	1.00	1.00

Unrecognized Compensation Costs

At June 27, 2015, the unrecognized stock-based compensation, adjusted for estimated forfeitures, was as follows (in thousands):

	Unrecognized Expense	Average Expected Recognition Period in years
Stock options	$ 1,547	3.61
Restricted stock units	15,363	2.18
Employee stock purchase plan	80	0.10
Total unrecognized stock-based compensation expense	$ 16,990	

Note 14 — Net Income (Loss) per Share

Basic net income (loss) per share for the three and six months ended June 27, 2015 and June 28, 2014 was computed by dividing net income (loss) by the weighted-average number of common shares outstanding for the period. Diluted net income per share for the three and six months ended June 27, 2015 was computed by dividing net income by the diluted weighted-average number of shares outstanding during that period. Diluted net loss per share for the three and six months ended June 28, 2014 was computed by dividing net loss by the weighted-average number of common shares outstanding for the period as the inclusion of any common stock equivalents would have been anti-dilutive.

A reconciliation of the numerator and denominator used in the calculation of basic and diluted net income (loss) per share is as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Numerator:				
Net income (loss) used in computing basic and diluted net loss per share	$ 838	$ (4,326)	$ 1,621	$ (17,037)
Denominator:				
Weighted-average shares used in computing basic net income (loss) per share	58,109	55,812	57,532	55,431
Add potentially dilutive securities	985	—	1,342	—
Weighted-average shares used in computing basic and diluted net income (loss) per share	59,094	55,812	58,874	55,431

The following table sets forth the weighted-average number of all potentially dilutive securities excluded from the computation in the table above because their effect would have been anti-dilutive (in thousands):

	Three Months Ended		Six Months Ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Options to purchase common stock	1,948	2,981	2,059	3,133
Restricted stock units	—	—	197	3
Employee stock purchase plan	—	26	—	16
Total potentially dilutive securities	1,948	3,007	2,256	3,152

Note 15 — Income Taxes

We recorded an income tax provision of $24 thousand and $0.1 million, for the three and six months ended June 27, 2015, respectively. We recorded an income tax benefit of $51 thousand and a provision of $0.3 million for the three and six months ended June 28, 2014, respectively. Income tax provisions reflect the tax provision on our operations in the foreign and U.S jurisdictions offsetting by tax benefit from lapsing of statute of limitations in foreign jurisdictions. We continue to maintain a valuation allowance for our U.S. Federal and State deferred tax assets.

Note 16 — Commitments and Contingencies

Contractual and purchase obligations

We lease facilities under non-cancellable operating leases with various expiration dates through 2021. The facilities generally require us to pay property taxes, insurance and maintenance costs. Further, several lease agreements contain rent escalation clauses or rent holidays. For purposes of recognizing minimum rental expenses on a straight-line basis over the terms of the leases, we use the date of initial possession to begin amortization. We have the option to extend or renew most of our leases, which may increase the future minimum lease commitments. Purchase obligations are primarily for purchases of inventory and manufacturing related service contracts. Purchase obligations are defined as agreements that are enforceable and legally binding and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Timing of payments and actual amounts paid may be different depending on the time of receipt of goods or services or changes to agreed-upon amounts for some obligations.

Our lease and purchase obligations have not materially changed as of June 27, 2015 from those disclosed in our Annual Report on Form 10-K for the year ended December 27, 2014.

Environmental Matters

We are subject to U.S. Federal, State and local, and foreign governmental laws and regulations relating to the protection of the environment, including those governing the discharge of pollutants into the air and water, the management and disposal of hazardous substances and wastes, the clean-up of contaminated sites and the maintenance of a safe workplace. We believe that we comply in all material respects with the environmental laws and regulations that apply to us, including those of the California Department of Toxic Substances Control, the Bay Area Air Quality Management District, the City of Livermore Water Resources Division, County of Santa Clara Department of Environmental Health, County of San Diego Hazardous Materials Division and Encino Water District, and the California Division of Occupational Safety and Health. We did not receive any notices of violations of environmental laws and regulations during the six months ended June 27, 2015, or in our fiscal 2014. We do not believe that any loss from environmental remediation liabilities would have a material impact on our financial condition.

While we believe that we are in compliance in all material respects with the environmental laws and regulations that apply to us, in the future, we may receive environmental violation notices, and if received, final resolution of the violations identified by these notices could harm our operations, which may adversely impact our operating results and cash flows. New laws and regulations, amended enforcement practices around existing laws and regulations, the discovery of previously unknown contamination at our or others' sites or the imposition of new cleanup requirements could also harm our operations, thereby adversely impacting our operating results and cash flows.

Consulting

I

Temporary consultants were used to replace normal employee attrition.

Commission

I

Commissionable sales increased against sales with no commissions.

Capital Resources and Liquidity

The Company’s sources and (uses) of cash for the nine months ended September 30, 2012 and 2011 are shown below:

	2012	2011
Cash provided by (used by) operations	303,834	(2,077,108)
Construction of plant in Taber, AB	-	(675,313)
Purchases of equipment	(93,007)	(65,503)
Short term line of credit	225,000	1,500,000
Repayment of loans	(94,164)	(96,464)
Purchase of common stock	-	(1,030,349)
Changes in exchange rates	2,876	(1,677)

In February 2011 the Company purchased 792,576 shares of its common stock from unrelated third parties. The shares were acquired in privately negotiated transactions for a total purchase price of $1,030,349. None of the share were acquired in open market transactions.

In 2007, the Company began construction of a plant in Taber Alberta. The plant is being used to manufacture aspartic acid which is the major component of TPAs. Presently the Company buys most of its aspartic acid from China, where the base raw material is oil and supplements from the Taber facility. The Company's plant in Taber uses sugar as the base raw material. Although the Company expects that it will still import some aspartic acid from China, using aspartic acid manufactured by its plant from sugar will reduce its raw material costs, reduce price fluctuations generated by oil prices and reduce shipping costs.

The Company has sufficient cash resources to meets its future commitments and cash flow requirements for the coming year. As of September 30, 2012 working capital was $3,562,822 (2011 - $3,620,125) and the Company has no substantial commitments that require significant outlays of cash over the coming fiscal year other than repayment of the long-term loans.

The Company is committed to minimum rental payments for property and premises aggregating approximately $246,804 over the term of three leases, the last expiring on July 31, 2014.

Commitments in each of the next three years are approximately as follows:

2012	42,021
2013	156,247
2014	48,536

Other than as disclosed as above, the Company does not anticipate any capital requirements for the twelve months ended December 31, 2012.

Other than as disclosed in this report, the Company does not know of any trends, demands, commitments, events or uncertainties that will result in, or that are reasonably likely to result in, the Company’s liquidity increasing or decreasing in any material way.

Other than as disclosed in this report, the Company does not know of any significant changes in its expected sources and uses of cash.

The Company does not have any commitments or arrangements from any person to provide the Company with any sources of equity capital.

See Note 2 to the financial statements included as part of this report for a description of the Company’s significant accounting policies and recent accounting pronouncements.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the direction and with the participation of our management, including our Principal Executive and Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of September 30, 2012. We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our periodic reports with the Securities and Exchange Commission is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and regulations, and that such information is accumulated and communicated to our management, including our principal executive and financial officer, as appropriate, to allow timely decisions regarding required disclosure. Our disclosure controls and procedures are designed to provide a reasonable level of assurance of reaching desired disclosure control objectives. Based on the evaluation, our Principal Executive and Financial Officer concluded that these disclosure controls and procedures are effective as of September 30, 2012.

Changes in Internal Control over Financial Reporting

Our management, with the participation of our Principal Executive and Financial Officer, evaluated whether any change in our internal control over financial reporting occurred during the three months ended September 30, 2012. Based on that evaluation, it was concluded that there has been no change in our internal control over financial reporting during the three months ended September 30, 2012 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II

ITEM 6. EXHIBITS.

Number	Description
3.1	Amended and Restated Certificate of Incorporation of the registrant. (1)
3.2	Bylaws of the registrant. (1)
31.1	Certification of Principal Executive Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of Principal Financial Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification of Principal Executive and Financial Officer Pursuant to 18 U.S.C. §1350 and §906 of the Sarbanes-Oxley Act of 2002.*

* Filed with this report.

(1) Incorporated by reference to the registrant's Registration Statement on Form 10-SB (SEC File. No. 000-29649) filed February 22, 2000.

SIGNATURES

In accordance with the requirements of Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

	Flexible Solutions International, Inc.	
Date: November 14, 2012	By:	/s/ Daniel B. O’Brien
	Name:	Daniel B. O’Brien
	Title:	President and Principal Executive Officer
	By:	/s/ Daniel B. O’Brien
	Name:	Daniel B. O’Brien
	Title:	Principal Financial and Accounting Officer