ADVANCED PHOTONIX INC
Form 10-K/A
November 14, 2006

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U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
FORM 10-K/A

(Mark One)

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

For the fiscal year ended March 27, 2005

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 1-11056

ADVANCED PHOTONIX, INC. ®

(Exact name of registrant as specified in its charter)

Delaware	33-0325826
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1240 Avenida Acaso, Camarillo, CA 93012
(Address of principal executive offices) (Zip Code)
(805) 987-0146
(Registrant s telephone number, including area code)
SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:
None
SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:
Common Stock, $.001 Par Value
Class A Common Stock

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in any definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Total revenues for registrant s fiscal year ended March 27, 2005 were $14,802,761.

As of September 26, 2004, the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $24,000,000.

As of June 17, 2005 there were 16,087,631 shares of Class A Common Stock and 31,691 shares of Class B Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement for the Annual Meeting for 2005 are incorporated by reference in Part III.

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EXPLANATORY NOTE

In accordance with Emerging Issues Task Force Issue 98-5, Accounting for Convertible Securities with a Beneficial Conversion Features or Contingently Adjustable Conversion Ratios (EITF 98-5), the Company recognized an imbedded beneficial conversion feature present in the Convertible Note. The Company allocated a portion of the proceeds equal to the intrinsic value of that feature to additional paid-in capital. The Company recognized and measured an aggregate of $3,165,000 of the proceeds, which is equal to the intrinsic value of the embedded beneficial conversion feature, to additional paid-in capital and a discount against the Convertible Notes.

In connection with the placement of the Convertible Notes in October 2004, September 2005 and March 2006, the Company issued detachable warrants granting the holders the right to acquire 1,446,398 shares of the Company s common stock at $1.78 per share. The warrants expire five years from the date of registration. In accordance with Emerging Issues Task Force Issue 00-27, Application of Issue No. 98-5 to Certain Convertible Instruments (EITF -0027), the Company recognized the value attributable to the warrants in the amount of $1,881,000 to additional paid-in capital and a discount against the Convertible Notes. The Company valued the warrants in accordance with EITF 00-27 using the Black-Scholes pricing model and the following assumptions: contractual terms of 5 years, an average risk free interest rate of 4.9%, a dividend yield of 0%, and volatility of 72%, 52% and 52%, respectively.

The debt discount attributed to the beneficial conversion feature and value of the warrants issued is amortized over the Convertible Note s maturity period (three year) as interest expense. In Q2 & Q3 of FY 2006, $3,475,000 and $1,000,000, respectively of the Convertible Notes were converted to the Company s common stock, and accordingly, that portion of the un-amortized debt discount was charged to interest expense. Additionally, in FY 2006, the un-amortized debt discount of $331,000 on the warrants associated with the convertible notes was charged to interest expense.

The Company recorded non-cash interest expense in the amount of $176,000 during the year ended March 27, 2005 in connection with the Convertible Notes.

The changes to the Balance Sheet and Statement of Operations as of and for the year ended March 27, 2005 are as follows:

Balance Sheet	**As Reported**	**Restated**
Long-term debt, less current portion	4,859,000	3,832,000
Total long-term debt	4,861,000	3,834,000
Additional paid-in capital	27,995,000	29,198,000
Accumulated deficit	(12,731,000)	(12,907,000)
Total shareholders equity	15,277,000	16,304,000

Consolidated Statement of Operations	**As Reported**	**Restated**
Interest expense, warrant fair value		176,000
Total other Income (expense)	(146,000)	(322,000)
Net Income (Loss)	5,254,000	5,078,000
Basic earnings (loss) per share	$ 0.39	$ 0.38
Diluted earnings (loss) per share	$ 0.34	$ 0.33

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PART I

Item 1. Business

General

Advanced Photonix, Inc. ® (the Company), was incorporated under the laws of the State of Delaware in June 1988. The Company is engaged in the development and manufacture of custom optoelectronic solutions, serving a variety of global Original Equipment Manufacturer (OEM) markets. While the Company specializes in silicon-based custom photodiode assemblies, its product families range from custom light detection assemblies, including its patented Avalanche Photodiode technology, to light emitting diode (LED) assemblies. The Company supports the customer from the initial concept and design phase of the product, through to full-scale production and test. The Company has two manufacturing and wafer fabricating facilities; one in Camarillo, CA and one in Dodgeville, WI.

Products & Technologies

The Company designs and manufactures silicon-based optoelectronic components and assemblies for a global OEM customer base. The core technology used in the majority of the Company s products is silicon-based photodiodes. Photodiodes sense light of varying wavelengths and intensity and convert that light into electrical signals. The Company manufactures photodiodes of varying complexity, from basic PIN (positive-intrinsic-negative) photodiodes to the more sophisticated avalanche photodiode (APD). The APD is a specialized silicon photodiode capable of detecting very low light levels due to an internal gain phenomenon known as avalanching. All devices are designed by the Company s experienced engineering staff, and fabricated in two state-of-the-art clean rooms. The Company s basic products and technologies include the following:

- Silicon PIN photodetectors spectrally enhanced, both single and multi-element
- Silicon high resistivity p-type detectors
- Silicon APDs discrete, with and without thermoelectric coolers, and with integrated modules
- Photodetector hybrids, which include signal amplification circuitry within the detector package
- Custom LED assemblies and LED displays
- FILTRODE® patented technology integrating optical filters directly on photodiode chips

Markets

These products serve customers in a variety of global markets, typically North America, Asia, Europe and Australia. The target markets and applications served by the Company are as follows:

Military & Aerospace:

- Missile guidance
- Laser range finders
- Laser training systems
- Heads-up displays
- Satellite positioning

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Industrial & Commercial:

- Optical encoders
- Laboratory instrumentation
- Baggage/Cargo scanners
- Bar code scanners
- Laser positioning systems

Medical:

- Blood analysis, including pulse oximetry and glucometry
- Bacteriology
- Medical imaging

Automotive:

- Laser detection
- Adaptive cruise control
- Automatic power windows
- Drive-by-wire

Communications:

- VCSEL monitor
- Pump laser monitor
- Wireless communication

One of the key competitive advantages held by the Company is its ability to supply detector assemblies for high reliability (Hi-Rel) applications, including military and commercial aerospace. Hi-Rel devices are designed, manufactured and tested to function in severe environmental conditions. The Company has many years of experience in supplying Hi-Rel devices that demand modern wafer fabrication techniques, a dedicated assembly area, and a sophisticated test lab. These assembly and test capabilities meet several military approvals, including MIL-PRF-19500, MIL-STD-883 and MIL-STD-750. Hi-Rel products manufactured by the Company include:

- Multi-element hybrid assemblies used on the U.S. Navy s Rolling Airframe Missile (RAM) developed by Raytheon
- Narrow and wide field-of-view detectors used in Tube-launched Optically-tracked Wire-guided (TOW) missile tracking systems
- LED arrays for use in thermal image displays in military night vision applications
- Quadrant photodetectors used in the autocollimator for airborne navigation/FLIR (Forward Looking Infrared) pods and smart bombs
- Opto assemblies for biological and blood analysis
- Assemblies used in automotive distance control systems

Recent Developments

In March 2005, the Company formed a new subsidiary, Michigan Acquisition Sub, LLC (Newco), a Delaware limited liability company, for purposes of entering into an Agreement and Plan of Merger with Picotronix, Inc. (doing business as and referred to herein as Picometrix), a Michigan corporation, whereby Picometrix merged with and into Newco, with Newco being the surviving entity. The merger was completed in May 2005. The merger consideration was determined through arm s-length negotiations

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between the parties. (See Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations and Item 8. Notes to the Consolidated Financial Statements for more information on the transaction.)

Raw Materials

The principal raw materials used by the Company in the manufacture of its semiconductor components and sensor assemblies are silicon wafers, chemicals and gases used in processing wafers, gold wire, lead frames, and a variety of packages and substrates, including metal, printed circuit board, flex circuits, ceramic and plastic packages. All of these raw materials can be obtained from several suppliers. From time to time, particularly during periods of increased industry-wide demand, silicon wafers and other materials have been in short supply. However, the Company has not been materially affected by such shortages. As is typical in the industry, the Company allows for a significant lead-time (2 months or greater) between order and delivery of raw materials.

Research and Development

Since its inception in June 1988, the Company has incurred material research and development expenses, with the intent of commercializing these investments into profitable new standard and custom product offerings. During the fiscal years ended in 2005, 2004, and 2003, research and development expenses amounted to $146,000, $280,000, and $511,000 respectively. The Company expects that continued research and development funding will be required for new projects as well as the continuing development of new derivatives of the Company s current product line, and for the commercialization of these products. The Company has in the past, and will continue to pursue customer funded, as well as internally funded, research and development projects when they are in support of the Company s development objectives.

During the last fiscal year, the Company shifted its primary research and development focus from overall APD development to those projects which have strong existing markets and can be transitioned to full commercialization in a relatively short period of time. As we begin the new fiscal year, the following research and development projects are currently underway:

- APD performance enhancements designed specifically for certain military and medical imaging applications
- Silicon PIN photodiodes, which are being developed to meet unique customer requirements, such as higher speeds, lower electrical noise, and unique multi-element geometries.
- Additional applications leveraging the Company s patented Filtrode family, integrating a variety of filters onto a detector chip
- Position Sensitive Devices the Company is broadening its offering of these devices with improved performance for industrial sensing markets

Environmental Regulations

The photonics industry, as well as the semiconductor industry in general, is subject to governmental regulations for the protection of the environment, including those relating to air and water quality, solid and hazardous waste handling, and the promotion of occupational safety. Various federal, state and local laws and regulations require that the Company maintain certain environmental permits. The Company believes that it

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has obtained all necessary environmental permits required to conduct its manufacturing processes. Changes in the aforementioned laws and regulations or the enactment of new laws, regulations or policies could require increases in operating costs and additional capital expenditures and could possibly entail delays or interruptions of operations.

Backlog and Customers

The Company s sales are made primarily pursuant to standard purchase orders for delivery of products. However, by industry practice, orders may be canceled or modified at any time. When a customer cancels an order, they are responsible for all finished goods, all costs, direct and indirect, incurred by the Company, as well as a reasonable allowance for anticipated profits. No assurance can be given that the Company will receive these amounts after cancellation. The current backlog contains only those orders for which the Company has received a confirmed purchase order and also includes contracts which have scheduled shipping dates beyond the upcoming fiscal year. As such, the current backlog represents only a portion of expected annual revenues for fiscal year 2006. The Company had approximately $8.2 million in total backlog at the end of fiscal years 2005 and 2004.

Customers normally purchase the Company s products and incorporate them into products that they in turn sell in their own markets on an ongoing basis. As a result, the Company s sales are dependent upon the success of its customers products and its future performance is dependent upon its success in finding new customers and receiving new orders from existing customers.

Marketing

The Company markets its products in the United States and Canada through its own technical sales engineers and through independent sales representatives. International sales, including Europe, the Middle East and Pacific Rim, are conducted through foreign distributors (see Note 1 to the Financial Statements). The Company s products are primarily sold as components or assemblies to original equipment manufacturers (OEM s). The Company markets its products and capabilities through industry specific channels, both on the internet and in print through trade journals.

Competition

The Company competes with a range of companies for the custom optoelectronic and silicon photodetector requirements of customers in its target markets. The Company believes that its principal competitors for sales of custom devices are small to medium size companies. Because the Company specializes in custom devices requiring a high degree of engineering expertise to meet the requirements of specific applications, it generally does not compete to any significant degree with other large United States, European or Pacific Rim manufacturers of standard off the shelf optoelectronic components or silicon photodetectors.

Proprietary Technology

The Company utilizes proprietary design rules and processing steps in the development and fabrication of its PIN photodiodes and avalanche photodiodes. In addition, the Company owns the following patents:

US PATENT NO.	DESCRIPTION	DATE ISSUED
6,111,299	Active Large Area Avalanche Photodiode Array	August 2000
6,005,276	Solid State Photodetector with Light Responsive Rear Face	December 1999
5,801,430	Solid State Photodetector with Light Responsive Rear Face	September 1998
5,757,057	Large Area Avalanche Array	May 1998
5,477,075	Solid State Photodetector with Light Responsive Rear Face	December 1995
5,311,044	Avalanche Photomultiplier Tube	May 1994
5,146,296	Devices for Detecting and/or Imaging Single Photoelectron	September 1992
5.057,892	Light Responsive Avalanche Diode	October 1991
5,021,854	Silicon Avalanche Photodiode Array	June 1991
4,782,382	High Quantum Efficiency Photodiode Devices	November 1988 (by predecessor co.)
4,717,946	Thin Line Junction Photodiode	January 1988 (by predecessor co.)

There can be no assurance that any issued patents will provide the Company with significant competitive advantages, or that challenges will not be instituted against the validity or enforceability of any patent owned by the Company, or, if instituted, that such challenges will not be successful. The cost of litigation to uphold the validity and to prevent the infringement of a patent could be substantial. Furthermore, there can be no assurance that the Company s APD technology will not infringe on patents or rights owned by others, licenses to which might not be available to the Company. Based on limited patent searches, contacts with others knowledgeable in the field of APD technology, and a review of the published materials, the Company believes that its competitors hold no patents, licenses or other rights to the APD technology which would preclude the Company from pursuing its intended operations.

In some cases, the Company may rely on trade secrets to protect its innovations. There can be no assurance that trade secrets will be established, that secrecy obligations will be honored or that others will not independently develop similar or superior technology. To the extent that consultants, key employees or other third parties apply technological information independently developed by them or by others to Company projects, disputes might arise as to the proprietary rights to such information which may not be resolved in favor of the Company.

Employees

At June 17, 2005 (and subsequent to the merger with Picometrix) the Company had 156 employees, comprised of 148 full time employees (including 4 officers) and 9 part time employees. Included are 19 engineering and development personnel, 11 sales and marketing personnel, 111 operations personnel, and 15 general and administrative personnel (including 4 officers). The Company may, from time to time, engage personnel to perform consulting services and to perform research and development under third party funding. In certain cases, the cost of such personnel may be included in the direct cost of the contract rather than in payroll expense.

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Item 2. Properties

The Company leases all of its executive offices, research, marketing and manufacturing facilities. At March 27, 2005, those leases consisted of primarily 45,000 square feet in two facilities. The facility located at 1240 Avenida Acaso in Camarillo, California is leased through February 2009. A second manufacturing facility is located at 305 County YZ, Dodgeville, Wisconsin, and is leased through November 2007. For a portion of the year, the Company also held a lease on the prior Photonic Detectors, Inc. facility in Simi Valley, California which was terminated effective April 30, 2005. The Company believes that its existing facilities are adequate to meet its needs for the foreseeable future.

Item 3. Legal Proceedings

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Company s Class A Common Stock is traded on the American Stock Exchange (AMEX) under the symbol API . At June 17, 2005, the Company had 106 holders of record for the Class A Common Stock (including shares held in street name), representing approximately 6,000 beneficial owners of the Class A Common Stock. On the same date, there were 6 holders of record of the Class B Common Stock (none of which were held in street name).

The following table sets forth high and low closing prices by quarter for fiscal years 2005 and 2004.

Quarterly Stock Market Data

	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter	
	2005	2004	2005	2004	2005	2004	2005	2004
Common Stock[1]								
High	3.21	1.05	2.57	1.89	1.85	2.51	2.17	2.45
Low	2.02	.87	1.65	.88	1.57	1.37	1.64	1.66

[1] Price ranges on the American Stock Exchange

The Company has never paid any cash dividends on its capital stock. The Company intends to retain earnings, if any, for use in its business and does not anticipate that any funds will be available for the payment of cash dividends on its outstanding shares in the foreseeable future. The holders of Common Stock will not be entitled to receive dividends in any year until the holders of the Class A Redeemable Convertible Preferred

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Stock receive an annual non-cumulative dividend preference of $.072 per share. To date, a total of 740,000 shares of Class A Redeemable Convertible Preferred Stock have been converted into 222,000 shares of Class A Common Stock, leaving outstanding 40,000 shares of Class A Redeemable Convertible Preferred Stock. The aggregate non-cumulative annual dividend preference of such Class A Redeemable Convertible Preferred Stock is $2,880. There is no public market for the Company s Class A Redeemable Convertible Preferred Stock or Class B Common Stock; however, such stock is convertible into Class A Common Stock at the option of the holder and upon transfer by the holder of the Class A Redeemable Convertible Preferred Stock.

Item 6. Selected Financial Data

The selected financial data for each of the five years presented below is derived from our audited consolidated financial statements and should be read in conjunction with the consolidated financial statements, the notes to the consolidated financial statements, and Management s Discussion and Analysis of Financial Condition and Results of Operations , all of which are contained in this report on Form 10-K.

(in thousands, except per share data)

	2005 restated	**2004**	**2003**	**2002**	**2001**
Net Sales	$14,803	$12,401	$ 9,147	$ 6,931	$ 6,806
Gross Profit	$ 4,732	$ 4,297	$ 2,699	$ 2,761	$ 2,544
as a percentage of Sales	32%	35%	30%	40%	37%
Net Income (Loss) from Continuing Operations	$ 5,078	$ 794	$ (803)	$ (284)	$ 212
Earnings (Loss) Per Common Share - Basic	$ 0.38	$ 0.06	$ (0.06)	$ (0.02)	$ 0.02
Earnings (Loss Per Common Share - Diluted	$ 0.33	$ 0.06	$ (0.06)	$ (0.02)	$ 0.02
Weighted Average Common Shares Outstanding	13,461	13,400	12,356	12,209	12,204
Total Assets	$23,355	$12,574	$11,552	$ 9,255	$ 9,476
Current Liabilities	$ 3,185	$ 2,858	$ 2,640	$ 612	$ 523
Long Term Liabilities	$ 3,834	$ 11	$ 22	$	$
Class A Redeemable Convertible Preferred Stock	$ 32	$ 32	$ 32	$ 32	$ 32
Shareholders Equity	$16,304	$ 9,673	$ 8,858	$ 8,611	$ 8,921
Working Capital	$11,261	$ 5,802	$ 4,811	$ 7,461	$ 7,953
Dividends declared on Capital Stock	$	$	$	$	$

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Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operation

Application of Critical Accounting Policies

Application of our accounting policies requires management to make certain judgments and estimates about the amounts reflected in the financial statements. Management uses historical experience and all available information to make these estimates and judgments, although differing amounts could be reported if there are changes in the assumptions and estimates. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventory allowances, impairment costs, depreciation and amortization, warranty costs, taxes and contingencies. Management has identified the following accounting policies as critical to an understanding of our financial statements and/or as areas most dependent on management s judgment and estimates.

Revenue Recognition

In accordance with Staff Accounting Bulletin No. 104, we recognize revenue from the sale of products when the products are shipped to the customer. Revenues from the sale of services consist of non-recurring engineering charges, which are recognized when the services have been rendered. Historically, sales returns have amounted to less than 1% of net income and all sales are recorded net of sales returns and discounts.

Impairment of Long-Lived Assets

We continually review the recoverability of the carrying value of long-lived assets using the methodology prescribed in Statement of Financial Accounting Standards (SFAS) 144, Accounting for the Impairment and Disposal of Long-Lived Assets. We also review long-lived assets and the related intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Upon such an occurrence, recoverability of these assets is determined by comparing the forecasted undiscounted net cash flows to which the assets relate, to the carrying amount. If the asset is determined to be unable to recover its carrying value, then intangible assets, if any, are written down first, followed by the other long-lived assets to fair value. Fair value is determined based on discounted cash flows, appraised values or management s estimates, depending on the nature of the assets.

Deferred Tax Asset Valuation Allowance

We record a deferred tax asset in jurisdictions where we generate a loss for income tax purposes. For all years prior to fiscal 2005, due to our history of operating losses, we had recorded a full valuation allowance against these deferred tax assets in accordance with SFAS 109, Accounting for Income Taxes, because, in management s judgment, the deferred tax assets would not be realized in the foreseeable future. In fiscal years 2004 and 2005, the Company returned to a position of continued profitability. Based on recent profit history and on anticipated future profits resulting from the Company s acquisition and merger with Picometrix, Inc. in May 2005, we reversed a portion of the valuation allowance for the year ended March 27, 2005, because, in our estimation, we believe that at least 50% of the deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible, and no assurance can be given that the Company will, in fact, generate future taxable income in amounts sufficient to fully realize the asset. We have considered the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making our assessment. The deferred tax assets are evaluated annually and the valuation allowance may be adjusted again in the future years if it is determined that any additional portion of the assets will or will not be realized.

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Inventories

Our inventories are stated at standard cost (which approximates the first-in, first-out method) or market. Slow moving and obsolete inventories are analyzed quarterly. To calculate a reserve for obsolescence, we begin with a review of our slow moving inventory. Any inventory which has not moved within the past 24 months is reserved for at 100% of book value; inventory which has not moved within the past 12 months is reserved for at 40%. The percentages applied to the reserve calculation are based on historical usage analyses. In addition, any residual inventory which is customer specific and remaining on hand at the time of contract completion is reserved for at the standard unit cost. The complete list of slow moving and obsolete inventory is then reviewed by the production, engineering and/or purchasing departments to identify items that can be utilized in the near future. These items are then excluded from the analysis and the remaining amount of slow-moving and obsolete inventory is then reserved for. Additionally, non-cancelable open purchase orders for parts we are obligated to purchase where demand has been reduced may be reserved. Reserves for open purchase orders where the market price is lower than the purchase order price are also established. If a product which had previously been reserved for is subsequently sold, the amount of reserve specific to that item is then reversed.

Accounts Receivable and Allowance for Doubtful Accounts

The Allowance for Doubtful Accounts is established by analyzing each account that has a balance over 90 days past due. Each account is individually assigned a probability of collection. The total amount determined to be uncollectible in the 90-days-past-due category is then reserved fully. The percentage of this reserve to the 90-days-past-due total is then established as a guideline and applied to the rest of the non-current accounts receivable balance where appropriate. When other circumstances suggest that a receivable may not be collectible, it is immediately reserved for, even if the receivable is not yet in the 90-days-past-due category.

TABLE OF CONTRACTUAL OBLIGATIONS

The following table sets forth the contractual obligations of the Company at March 27, 2005.

CONTRACTUAL OBLIGATIONS	PAYMENTS DUE BY PERIOD				
	Total Restated	Less than 1 year	1 3 years	3 5 years	More than 5 years
Long-term debt	5,000,000		5,000,000		
Discount on convertible notes	(1,168,000)	(939,000)	(229,000)		
Capital lease obligations	13,000	11,000	2,000		
Operating lease obligations	1,488,000	434,000	1,054,000		
Purchase Obligations	875,000	875,000			
Other long-term liabilities reflected on the registrant s balance sheet under GAAP					
Total	6,208,000	381,000	5,827,000		

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RESULTS OF OPERATIONS

Fiscal year 2005 Compared to Fiscal Year 2004

REVENUES

The Company s revenues for the fiscal year ended March 27, 2005 (2005) were $14.8 million, an increase of $2.4 million, or 19% from revenues of $12.4 million for the fiscal year ended March 28, 2004 (2004). Approximately $500,000 of the increase was attributable to revenues from Photonic Detectors, Inc. (PDI), which the Company acquired in December 2004. The remaining increase reflects an overall increase in shipments to customers in each of the Company s major market segments over the prior year. As has been the trend for most of the current fiscal year, the most significant revenue increases are coming from the medical and industrial sensing segments, which increased by 34% and 17% respectively over the prior year and account for $1.5 million of the total increase. Similarly, sales to the military aerospace and automotive markets have also increased, by 5% and 17% respectively, and account for approximately $400,000 of the remaining increase in net revenues. Stated as a percentage of net revenues, sales to the industrial sensing markets represent 44%, sales to the military aerospace markets represent 33%, medical is 17% and automotive is 5%.

As expected, the increased diversification and larger customer base achieved through the Company s previous acquisitions resulted in net revenues which fully met our expectations for the most recent fiscal year. During the upcoming year, we expect to see continued revenue growth in our core silicon business, as well as a significant revenue increase resulting from our acquisition of Picometrix, Inc. which occurred in May 2005. As such, in fiscal 2006, we expect total revenues to increase by 65%-85% over fiscal 2005.

COSTS AND EXPENSES

Cost of product sales increased to $10.1 million in 2005 from $8.1 million in 2004. Stated as percent of net sales, cost of product sales increased 3 percentage points to 68%, reducing our gross profit margin to 32% in 2005 as compared to 35% in fiscal year 2004. The reduction in gross margin is primarily attributable to manufacturing issues, including labor inefficiencies and a significant increase in material costs related to scrap, rework and assembly yields. Stated as a percentage of net sales, material costs rose to 28% in 2005 as compared to 25% in 2004. In 2005, we were again faced with heightened competitiveness in certain markets which caused us to absorb increases in certain material costs while maintaining or reducing existing pricing in our efforts to generate new business as well as retain existing business. Direct labor and other overhead expenses as a percentage of net sales remained flat at 8% and 32%, respectively, in 2005 as compared to 2004. While our gross margins fell slightly short of our expectations for 2005, we are continually seeking ways to improve our cost and margin structure, and have made margin improvement a continued priority for 2006.

Research and development (R&D) costs decreased by $134,000 (48%) to $146,000 during 2005 compared to $280,000 in 2004. R & D costs decreased significantly over the past two years as we concentrated our efforts on projects offering the highest commercial potential per each dollar spent. We expect that R&D expenses will increase significantly in the upcoming fiscal year, as we focus on new opportunities brought to us as a result of the Picometrix acquisition.

Marketing and sales expenses increased by $205,000 (20%) to $1.2 million in 2005. Planned additions to the sales department staff during the year accounted for $113,000 of increased salary, travel and related expenses. In addition, increased sales contributed to a $68,000 increase in commission expense and overall advertising

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and marketing expenses increased by approximately $24,000. We remain committed to insuring that our customers receive excellent service. To that end, we will continue to build our sales department and anticipate further increases in salary, commissions, travel and related expenses during fiscal 2006, as we plan for the successful integration of the Picometrix business.

Total general and administrative expenses increased by $541,000 (25%) to $2.7 million in 2005 as compared to $2.2 million in 2004. Approximately 50% of the increase in general and administrative expenses is due to increased personnel and related expenses, including salaries, bonuses and benefits to support our growth objectives. In addition, total payroll was increased during the fourth quarter of fiscal 2005 as a direct result of the PDI acquisition, which was consummated on December 21, 2004. As part of our integration plan, selected PDI personnel were either offered a permanent position or requested to remain as an employee until a date specified by the Company. The net effect of the additional PDI personnel accounted for approximately $160,000 of the year to date increase. The remaining increases in general and administrative expenses were primarily due to acquisition investigation and related expenses, including consultants, legal, financing and other related expenses, which amounted to approximately $246,000 in total. In the upcoming year, general and administrative expenses will increase as needed to provide the infrastructure necessary to support the Company s growth objectives

Interest income for 2005 totaled $43,000, an increase of $23,000 over 2004, due primarily to capital financing activities which resulted in higher cash balances available for short-term investment. Interest expense for the year was $330,000 as compared to $30,000 in 2004, also a result of capital financing activities, amortization of convertible notes discount of $176,000 and the related interest liabilities.

At March 27, 2005, the Company reversed 50% of its deferred tax valuation allowance, in the amount of $4,749,000. The deferred tax valuation allowance had previously been recorded at full value against its deferred tax assets, reducing the net value of the asset to zero. With the acquisition of both Photonic Detectors Inc. in December 2004 and Picometrix, Inc. in May 2005, the Company s management has projected that the Company will generate sufficient future taxable income to utilize at least a portion of its accumulated NOL s before they expire and has accordingly reduced the deferred tax asset valuation allowance to $4.7 million against a deferred tax asset of $9.5 million, bringing the net value of the deferred tax asset to $4.7 million at March 27, 2005. The reduction in the valuation allowance has been recorded as a deferred tax benefit in the statement of operations.

Net income for fiscal year 2005 was $5.1 million, including the $4.7 million adjustment made to reduce the deferred tax valuation allowance, as compared to $794,000 in 2004. Total acquisition-related expenses for fiscal year 2005 which were necessary to support our growth objectives amounted to $736,000 (which includes interest expense of $154,000, $176,000 amortization of convertible note discount, plus the $406,000 increased general and administrative expenses associated with PDI and other acquisition investigation activities, as noted above). Thus, excluding the net impact of the deferred tax asset adjustment and acquisition-related expenses, net income for fiscal 2005 would have been $1.1 million, or $0.08 per share.

Fiscal year 2004 Compared to Fiscal Year 2003

REVENUES

The Company s revenues for the fiscal year ended March 28, 2004 (2004) were $12.401 million, an increase of $3.254 million, or 36%, from revenues of $9.147 million for the fiscal year ended March 30, 2003 (2003).

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The increase was primarily attributable to the Company s acquisitions of Silicon Sensors, Inc. and Texas Optoelectronics, Inc., both of which occurred during fiscal 2003. The increase in net product sales reflects significant increases in shipments to customers in each of the Company s major market segments, the most notable coming from the military/aerospace segments, which increased 41% over the prior year and represent 37% of total revenues, or $4.64 million. Similarly, sales to the industrial sensing segments increased 28% over the prior year and represent 41% of total revenues, or $5.13 million. Sales to the medical markets, representing 15% of total revenues, increased 22% to $1.86 million, and sales to the automotive segment, which are directly attributable to the Texas Optoelectronics, Inc. acquisition, increased to $717,000 and represent 6% of total revenues, as compared to $203,000 representing 2% of total revenues in fiscal year 2003.

Revenues fell somewhat short of expectations because of changes in customer delivery schedules and other manufacturing issues. Nonetheless, we are pleased with the market stability and increased diversification that has been achieved as a result of our acquisitions and consolidation of the three companies.

COSTS AND EXPENSES

Cost of product sales increased to $8.10 million in 2004 from $6.45 million in 2003. Stated as percent of net sales, cost of product sales decreased 5 percentage points to 65%, bringing gross profit margin to 35% in 2004 as compared to 30% in fiscal year 2003. The improvement in gross margin is primarily attributable to a reduction in material costs which decreased to 25% as compared to 30% in the prior year. In addition, margins benefited from the consolidation of the Company s acquired businesses and steps taken by the Company to maximize production efficiencies between its two facilities, including load and inventory sharing, inventory reduction plans, and other cost management techniques. Direct labor as a percentage of net sales remained relatively flat at 8% in 2004 as compared to 7% in 2003, as did other fixed and variable overhead expenses, which amounted to 32% for 2004 compared to 33% in 2003. The Company continually seeks ways to improve gross margin, and expects that the current margin of 35% is indicative of what can be expected in the future, given the current operational structure. Research and development (R&D) costs decreased by $231,000 (45%) to $280,000 during 2004 compared to $511,000 in 2003. R & D costs have fluctuated significantly over the past two years as we have restructured and refocused our efforts. During 2004, the Company discontinued projects which did not have a clearly identified customer demand in our current market segments. We expect R&D expenditures for fiscal year 2005 to be slightly higher than in 2004.

Marketing and sales expenses decreased slightly, by $59,000 (5%) to $1.026 million in 2004. During 2004, the Company focused on bringing more sales and marketing functions in-house and improving the effectiveness and utilization of its internal sales force, thereby decreasing the use of outside sales representatives and advertising/marketing services. As a result, decreases in bad debt expense ($78,000) and advertising and marketing expenses ($40,000) were offset by increases in travel, salary and benefit expenses. To insure that we can continue to provide excellent service to our consolidated customer base, we will continue to build our sales department and expect that marketing and sales expenses will increase in 2005, due primarily to planned additions to the sales department staff.

Total general and administrative expenses increased by $174,000 (9%) to $2.148 million in 2004 as compared to $1.974 million in 2003. The net increase in general and administrative expenses is primarily due to increased software support and travel costs, representing approximately $105,000. In addition, the Company posted increased consultant and non-compete expenses of $40,000 as well as an increase to its Directors & Officers liability insurance of $24,000. General and administrative expenses are expected to increase in fiscal year 2005, due to the addition of an in-house information technology specialist and the continued strengthening of the administrative infrastructure necessary to support the Company s growth.

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Interest income for 2004 totaled $20,000, a decrease of $50,000 over 2003. Interest expense for the year was $30,000 as compared to $13,000 in 2004. The decrease in interest income is primarily due to consistently low interest rates available throughout the past year and the increase in interest expense is due to obligations assumed through the acquisition of Texas Optoelectronics, Inc. as well as expenses associated with the Company s secured line of credit. In addition, the Company reported a $40,000 net loss on sale of fixed assets, due primarily to the disposal or sale of select assets acquired from Texas Optoelectronics, Inc. for which the Company had no useful application.

Net income for fiscal year 2004 was $794,000, an improvement of $1.597 million, or 199%, over the net loss of ($803,000) reported in 2003.

LIQUIDITY AND CAPITAL RESOURCES

On December 21, 2004, the Company purchased the business and all of the outstanding stock of Photonic Detectors, Inc., a privately owned manufacturer of optoelectronic components and assemblies, located in Simi Valley, California. In connection with the transaction, the Company acquired certain net assets, including $44,000 cash, and assumed certain outstanding liabilities of Photonic Detectors, Inc. $1,073,000 net cash was expended for the transaction, which included the agreed purchase price of $1,075,000, plus additional expenses incurred of $42,000, less the $44,000 cash received.

In addition, in March 2005, approximately $4.2 million was used to fund a pre-acquisition loan made to Picometrix, Inc. The loan was contributed to the capital of the newly formed limited liability company upon closing of the acquisition and merger transaction on May 2, 2005 (see Note 13 to the Consolidated Financial Statements for information concerning additional debt incurred by the Company in connection with the Picometrix acquisition).

In July 2004, the Company established a revolving line of credit with a regional bank which provides for borrowings up to $3,000,000, based on 80% of the Company s eligible accounts receivable and 40% of the Company s eligible inventory, subject to certain limitations as defined by the agreement. At March 27, 2005, the outstanding balance on the line was $1.0 million. The line is secured by all business assets of the Company. Repayment is interest only, monthly, with principal due at maturity, July 20, 2005. Interest is computed at the Wall Street Journal Prime plus 1.00% which was 6.00% at March 27, 2005 (see Note 6 to the Consolidated Financial Statements).

At March 27, 2005, the Company had cash and cash equivalents of $1.5 million and working capital of $11.3 million. The Company s cash and cash equivalents increased by $204,000 during the twelve months ended March 27, 2005, including $1.7 million transferred from short-term investments into cash. $5.0 million was obtained through private placement of a convertible note, of which $1.25 million remained in a restricted cash collateral account subject to release upon satisfaction of certain conditions (which conditions were subsequently met) (see Note 7 to the Consolidated Financial Statements for further information concerning this debt), and the balance was available for working capital and other requirements. Cash provided by operating activities totaled $228,000, which was net of significant outlays for inventories and prepaid capital finance expenses. $30,000 was derived through net increases in accounts payable, accrued expenses, and customer deposit liabilities. $193,000 was used for capital expenditures required primarily for necessary computer and manufacturing equipment upgrades or replacements.

The Company is exposed to interest rate risk for marketable securities. Due to anticipated cash needs during the year, the Company held funds in highly liquid income and money fund accounts, considered to be cash equivalents, which carried an average interest rate of 1.3%. At March 27, 2005, the Company did not hold

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any funds in either short-term or long term investment accounts. We continually monitor interest rates and will attempt to utilize the best possible avenues of investment as excess cash becomes available.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

At March 27, 2005, all of our interest rate exposure is linked to the prime rate, subject to certain limitations. As such, we are at risk to the extent of changes in the prime rate and do not believe that moderate changes in the prime rate will materially affect our operating results or financial condition.

FORWARD LOOKING STATEMENTS

The information contained herein includes forward looking statements that are based on assumptions that management believes to be reasonable but are subject to inherent uncertainties and risks including, but not limited to, risks associated with the integration of newly acquired businesses, unforeseen technological obstacles which may prevent or slow the development and/or manufacture of new products, limited (or slower than anticipated) customer acceptance of new products which have been and are being developed by the Company, the availability of other competing technologies and a decline in the general demand for optoelectronic products.

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Item 8. Financial Statements and Supplementary Data

The following financial statements of Advanced Photonix, Inc. are included in Item 8:

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
of Advanced Photonix, Inc.:

We have audited the accompanying consolidated balance sheets of Advanced Photonix, Inc. (the Company) as of March 27, 2005 and March 28, 2004 and the related consolidated statements of operations, shareholders equity and cash flows for each of the years ended March 27, 2005, March 28, 2004 and March 30, 2003. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the Standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company at March 27, 2005 and March 28, 2004 and the results of its operations and its cash flows for the years ended March 27, 2005, March 28, 2004 and March 30, 2003 in conformity with accounting principles generally accepted in the United States.

/s/ Farber Hass Hurley McEwen, LLP
Formerly Farber & Hass LLP
May 27, 2005
except for note 2, as to which the date is November 8, 2006

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ADVANCED PHOTONIX, INC.
CONSOLIDATED BALANCE SHEET

	Restated March 27, 2005	March 28, 2004
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 1,503,000	$ 1,299,000
Restricted cash	1,254,000	
Investments		1,700,000
Accounts receivable, less allowance of $24,000 in 2005 and $56,000 in 2004	2,610,000	2,442,000
Note receivable from Picometrix, Inc.	4,228,000	
Inventories, less allowance of $1,032,000 in 2005 and $925,000 in 2004	3,644,000	2,929,000
Deferred tax asset, current portion	644,000	
Prepaid expenses and other current assets	563,000	290,000