

LIQUIDMETAL TECHNOLOGIES INC  
Form S-1/A  
July 03, 2007

As filed with the Securities and Exchange Commission on June 29, 2007

Registration No. 333-142442

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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Amendment No. 1 to

## FORM S-1

REGISTRATION STATEMENT  
Under

THE SECURITIES ACT OF 1933

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### LIQUIDMETAL TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**3399**  
(Primary Standard Industrial Classification Code  
Number)

**33-0264467**  
(I.R.S. Employer  
Identification No.)

**Liquidmetal Technologies, Inc.**

**30452 Esperanza**

**Rancho Santa Margarita, California 92688**

**(949) 635-2100**

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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**Larry Buffington**

**President and Chief Executive Officer**

**Liquidmetal Technologies, Inc.**

**30452 Esperanza**

**Rancho Santa Margarita, California 92688**

**Phone: (949) 635-2100**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

with a copy to:

**Curt P. Creely**  
 Foley & Lardner LLP  
 100 North Tampa Street, Suite 2700  
 Tampa, Florida 33602  
 Phone: (813) 229-2300/Fax: (813) 221-4210

**Approximate date of commencement of proposed sale to the public:** From time to time after the effective date of this Registration Statement, as determined by the selling stockholders.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933 check the following box.  X

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.  O

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.  O

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.  O

**CALCULATION OF REGISTRATION FEE**

Title of Each Class of Securities to Be Registered	Amount to Be Registered	Proposed Maximum Offering Price Per Share	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common Stock issuable upon conversion of Convertible Subordinated Notes Due January 2010	7,537,385 shares	\$ 1.10	(1) \$ 8,291,124	\$ [ ]
Common Stock issuable upon exercise of warrants	3,895,208 shares	\$ 1.55	(2) \$ 6,037,572	\$ [ ]
Common Stock issuable upon exercise of warrants	599,547 shares	\$ 2.13	(3) \$ 1,277,035	\$ [ ]
<b>TOTAL</b>	12,032,140 shares		\$ 15,605,731	\$ [ ] (4)

(1) The price is estimated in accordance with Rule 457(g) under the Securities Act solely for the purpose of calculating the registration fee and is \$1.10, the conversion price of the Convertible Subordinated Notes Due January 2010 as amended.

(2) The price is estimated in accordance with Rule 457(g) under the Securities Act solely for the purpose of calculating the registration fee and is \$1.55, the exercise price of the warrants issued in January 2007 as amended.

(3) The price is estimated in accordance with Rule 457(g) under the Securities Act solely for the purpose of calculating the registration fee and is \$2.13, the exercise price of the shares issuable upon exercise of the warrants issued between May 17, 2006 and December 1, 2006, as adjusted.

(4) Previously paid.

**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.**

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**PROSPECTUS**

**LIQUIDMETAL TECHNOLOGIES, INC.**

**12,032,140 Shares**

**Common Stock**

This prospectus covers a total aggregate of up to 12,032,140 shares of our common stock, par value \$0.001 per share, that may be offered from time to time by the selling stockholders identified on pages 27 of this prospectus. The shares being offered by this prospectus consist of:

- up to 7,537,385 shares issuable upon the conversion of our Convertible Subordinated Notes Due January 2010 issued by us in connection with a private placement in January 2007;
- up to 3,895,208 shares issuable upon the exercise of common stock purchase warrants issued by us in our January 2007 private placement; and
- up to 599,547 shares issuable upon the exercise of common stock purchase warrants issued by us between May 17, 2006 and December 1, 2006 in connection with a private placement of non-convertible subordinated notes.

We are registering these shares of our common stock for resale by the selling stockholders named in this prospectus, or their transferees, pledgees, donees or successors. We will not receive any proceeds from the sale of these shares by the selling stockholders. These shares are being registered to permit the selling stockholders to sell shares from time to time in the public market, in amounts, at prices and on terms determined at the time of offering. The selling stockholders may sell this common stock through ordinary brokerage transactions, directly to market makers of our shares or through any other means described in the section entitled "Plan of Distribution" beginning on page 93.

**Before purchasing any of the shares covered by this prospectus, carefully read and consider the risk factors in the section entitled "Risk Factors" beginning on page 1.**

Our common stock is quoted on the OTC Bulletin Board under the symbol LQMT.OB. On June 28, 2007, the last reported sales price of our common stock was \$0.86 per share.

Our principal executive offices are located at 30452 Esperanza, Rancho Santa Margarita, California 92688, and our telephone number at that address is (949) 635-2100.

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved the sale of this common stock or determined that the information in this prospectus is accurate and complete. Any representation to the contrary is a criminal offense.**

The date of this prospectus is \_\_\_\_\_, 2007.

The information in this prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

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This prospectus is a part of the registration statement that we filed with the Securities and Exchange Commission. The selling stockholders named in this prospectus may from time to time sell the securities described in this prospectus.

**You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with information different from that contained in this prospectus. The common stock is not being offered in any jurisdiction where the offer is not**

**permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or any sale of the common stock.**

We have registered the following trademark, which is used in this prospectus: Liquidmetal. In this prospectus, we use the terms company, we, us and our to refer to Liquidmetal Technologies, Inc. In this prospectus Liquidmetal or Liquidmetal Technologies refer to Liquidmetal Technologies, Inc.

**PROSPECTUS SUMMARY**



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*This summary highlights information contained elsewhere in this prospectus. Because this is a summary, it is not complete and does not contain all of the information that may be important to you. For a more complete understanding of us and this offering of our common stock, we encourage you to read this prospectus in its entirety, especially the risks of investing in our common stock discussed under Risk Factors and our consolidated financial statements, including the notes thereto, appearing elsewhere in this prospectus.*

### **Liquidmetal Technologies, Inc.**

We are a materials technology company that develops and commercializes products made from amorphous alloys. Our Liquidmetal® family of alloys consists of a variety of proprietary coatings, powders, bulk alloys, and composites that utilize the advantages offered by amorphous alloy technology. We develop, manufacture, and sell products and components from bulk amorphous alloys to customers in various industries, and we also partner with third-party licensees to develop and commercialize bulk Liquidmetal alloy products. We believe that our proprietary bulk alloys are the only commercially viable bulk amorphous alloys currently available in the marketplace. In addition to our bulk alloys, we market and sell a line of proprietary amorphous alloy-based industrial coatings under the Liquidmetal® Armacor™ coatings brand.

Amorphous alloys are unique materials that are distinguished by their ability to retain a random atomic structure when they solidify, in contrast to the crystalline atomic structure that forms in other metals and alloys when they solidify. Liquidmetal alloys possess a combination of performance, processing, and potential cost advantages that we believe can make them preferable to other materials in a variety of applications. The amorphous atomic structure of our alloys enables them to overcome certain performance limitations caused by inherent weaknesses in crystalline atomic structures, thus facilitating performance and processing characteristics superior in many ways to those of their crystalline counterparts. For example, our zirconium-titanium Liquidmetal alloys are approximately 250% stronger than commonly used titanium alloys such as Ti-6Al-4V, but they also have some of the beneficial processing characteristics more commonly associated with plastics. We believe these advantages could result in Liquidmetal alloys supplanting high-performance alloys, such as titanium and stainless steel, and other incumbent materials in a wide variety of applications. Moreover, we believe these advantages could enable the introduction of entirely new products and applications that are not possible or commercially viable with other materials.

### **Our Strategy**

Our goal is to develop and commercialize a wide variety of products made from Liquidmetal alloys. The key elements of our strategy include:

- Identifying and developing new applications for our Liquidmetal alloy technology;
- Focusing our marketing and internal manufacturing activities on select products with expected higher gross margins;
- Further developing our manufacturing processes, capabilities, and efficiencies for bulk Liquidmetal alloys;
- Pursuing strategic partnerships in order to more rapidly develop and commercialize products; and
- Advancing and further developing the Liquidmetal® brand to increase awareness of our company and technology.

#### **Applications for Liquidmetal Alloys**

We are focusing our commercialization efforts for Liquidmetal alloys on five identified product areas. We believe that these areas are consistent with our strategy in terms of market size, building brand recognition, and providing an opportunity to develop and refine our processing capabilities. Although we believe that strategic partnering transactions could create valuable opportunities beyond the parameters of these target markets, we anticipate continuing to pursue these markets both internally and in conjunction with partners.

- *Components for electronic products.* We produce components for electronic devices using our bulk Liquidmetal alloys and believe that our alloys offer enhanced performance and design benefits for these components in certain applications. Specifically, we currently produce internal hinge housings for certain Samsung cellular phone models and casings for certain SanDisk flash memory drives.

- *Sporting goods and leisure products.* We are developing a variety of applications for Liquidmetal alloys in the sporting goods and leisure products area. In 2003, Rawlings Sporting Goods Company launched a new line of baseball and softball bats that utilize a Liquidmetal alloy coating, and HEAD NV Sport launched a new line of HEAD® Liquidmetal® tennis racquets that incorporates Liquidmetal alloy in composite form in their racquet design. In 2005, we also launched goods that utilize Liquidmetal alloy including skis. Other potential applications for our alloys in this industry include golf clubs, eyewear, fishing, hunting, and other sport products.
- *Medical devices.* We are engaged in product development efforts relating to various medical devices that could be made from Liquidmetal alloys. We believe that the unique properties of bulk Liquidmetal alloys provide a combination of performance and cost benefits that could make them a desirable replacement to incumbent materials, such as stainless steel and titanium, currently used in various medical device applications.
- *Industrial coatings and powders.* We continue to market and sell amorphous alloy industrial coatings and powders under the Liquidmetal® Armacor™ coatings brand name. Liquidmetal alloy coatings are used primarily as a protective coating for industrial machinery and equipment.
- *Defense applications.* We are working with the U.S. Department of Defense, as well as a variety of defense-related research and development agencies and large defense contractors, to develop various defense-related applications for Liquidmetal alloys. For example, we are currently developing prototype kinetic energy penetrator rods for use in armor-piercing ammunition systems.

**Risk Factors / Going Concern**

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We are subject to a number of risks that you should be aware of before you decide to buy our common stock. These risks are discussed more fully in the RISK FACTORS section of this prospectus.

We have experienced significant operating losses since our inception. Our net loss for the fiscal years ended December 31, 2006 and 2005 was \$14.5 million and \$7.1 million, respectively. For the three months ended March 31, 2007 and 2006, we had a net income of \$0.5 million and a net loss of \$6.0 million, respectively. In the audit report on our financial statements for our fiscal years ended December 31, 2006 and 2005, our present auditors included a going-concern qualification indicating that our significant operating losses and working capital deficit cause substantial doubt about our ability to continue as a going concern. By issuing an opinion stating that there is substantial doubt about our ability to continue as a going concern, our auditors have indicated that they are uncertain as to whether we have the capability to continue our operations without additional funding. On January 3, 2007, we completed a private placement of \$16.3 million in principal amount of 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes). The January 2010 Notes were issued for aggregate cash in the amount of \$12.9 million and in payment of a total of \$3.4 million in principal and accrued but unpaid interest under our previously issued 7% Senior Secured Convertible Notes due August 2007 and our 8% Unsecured Subordinated Notes.

We anticipate that the \$12.9 million aggregate cash raised in the private placement will be sufficient to pursue our current operating plan only through the third quarter of 2007, and we will therefore require additional funding at or prior to that time. As a result, we are actively seeking additional sources of capital. The amount of funding that we seek and the timing of such fundraising efforts will depend on the extent to which we are able to increase revenues through obtaining additional purchase orders for our products and/or the extent to which we can restructure or modify our debt. Because we cannot be certain that we will be able to obtain adequate funding from debt, equity, or other traditional financing sources, we are also actively exploring several strategic financing options, including the possible sale of our manufacturing plant in South Korea (which would then be replaced with a smaller facility), potential licensing and outsourcing of manufacturing operations including those in South Korea and China, and the possible sale of all or a part of our Liquidmetal Coatings business or our interest in such business. In June 2007, we entered into an equipment sale and licensing agreement with Grace Metal, a South Korean corporation, providing for \$2.0 million in exchange for die casting machines and vacuum induction melters, and a 10-year exclusive license to manufacture Liquidmetal alloys for customers whose principal headquarters or major operations are based in South Korea. The principal purpose of the transactions with Grace Metal was to raise capital for the next-generation casting equipment and to shift the cost and burden of our manufacturing operations to a third party. Grace Metal was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company. We cannot guarantee that adequate funds will be available when needed, and if we do not receive sufficient capital, we may be required to alter or reduce the scope of our operations.

### Corporate Information

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We were originally incorporated in California in 1987, and we reincorporated in Delaware in May 2003. Our principal executive offices are located at 30452 Esperanza, Rancho Santa Margarita, California 92688. Our telephone number at that address is (949) 635-2100. Our Internet website address is [www.liquidmetal.com](http://www.liquidmetal.com), and all of our filings with the Securities and Exchange Commission are available free of charge on our website. Any information that is included on or linked to our Internet site is not a part of this prospectus.

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**The Offering**

Common stock offered	<p>Up to 12,032,140 shares are being offered by the selling stockholders. Of these shares:</p> <ul style="list-style-type: none"> <li>• up to 7,537,385 shares are issuable upon the conversion of our Convertible Subordinated Notes Due January 2010 (the January 2010 Notes ), which notes were issued by us to various selling stockholders in a private placement on January 3, 2007;</li> <li>• up to 3,895,208 shares are issuable to various selling stockholders upon the exercise of outstanding common stock purchase warrants issued by us in our January 2007 private placement and have an amended exercise price of \$1.55 per share; and</li> <li>• up to 599,547 shares are issuable to various selling stockholders upon the exercise of outstanding common stock purchase warrants issued by us on May 17, 2006, September 20, 2006, and December 1, 2006 in connection with a private placement of non-convertible subordinated notes and have an adjusted exercise price of \$2.13 per share.</li> </ul>
Shares outstanding after the offering	56,663,908 shares
Use of proceeds	We will not receive any proceeds from the sale of the shares offered by the selling stockholders. Any proceeds we receive from the selling stockholders upon their exercise of the warrants or option to purchase the shares included in the shares that are being offered by them hereunder will be used for general working capital.
Risk factors	See RISK FACTORS and other information included in this prospectus for a discussion of factors you should carefully consider before deciding to invest in the shares.
OTC Bulletin Board symbol	LQMT.OB

The number of shares of common stock that will be outstanding immediately after this offering is based on 44,631,768 shares outstanding as of June 1, 2007 and assumes the full conversion of the convertible promissory notes and the full exercise of the warrants identified above. There is no guarantee that all or any of such notes or warrants will be converted or exercised. The number of shares of common stock to be outstanding after this offering does not include 7,028,414 shares issuable pursuant to common stock options outstanding as of June 1, 2007 under our equity incentive plans, of which options to purchase 5,873,151 shares were exercisable as of such date at a weighted-average exercise price of \$5.15 per share, and 8,683,173 additional shares of common stock reserved for future grants under our equity compensation plans. The number of shares of common stock to be outstanding after this offering also does not include the shares underlying our 6% Senior Secured Notes Due July 29, 2007 (the July 2007 Notes ), our 7% Senior Secured Convertible Notes Due August 2, 2007 (the August 2007 Notes ), and the warrants issued in connection with such notes. As of June 1, 2007, an aggregate of 10,632,606 shares of our common stock were issuable pursuant to the conversion or exercise of such notes and warrants.

The convertible notes identified above are convertible into such number of shares of our common stock as is determined by dividing the outstanding principal balance of such notes by the conversion price of the notes. As of June 1, 2007, approximately \$2.1 million in aggregate principal amount of July 2007 Notes were outstanding at a conversion price of \$1.00 per share, approximately \$7.2 million in aggregate principal amount of August 2007 Notes were outstanding at an adjusted conversion price of \$1.75 per share, and approximately \$16.3 million in aggregate principal amount of January 2010 Notes were outstanding at a conversion price of \$1.10. The warrants identified above are exercisable at the price per share indicated above. However, the above-described notes and warrants contain anti-dilution provisions that may result in a reduction of these conversion and exercise prices if we issue shares in the future for consideration below the existing conversion or exercise prices. Such anti-dilution provisions may cause a decrease in the voting power and value of your investment in our shares. See

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DESCRIPTION OF CAPITAL STOCK Anti-Dilution Provisions in Notes and Warrants.

In this prospectus, unless otherwise stated or the context otherwise requires, references to Liquidmetal, we, us, our, our company, the Com and similar references refer to Liquidmetal Technologies, Inc. and its subsidiaries.

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## Summary Consolidated Financial Data

The following summary consolidated financial data as of and for our years ended December 31, 2006, 2005, 2004, 2003 and 2002 have been derived from our audited consolidated financial statements, and the summary consolidated financial data as of and for the three months ended March 31, 2006, and 2005 have been derived from our unaudited consolidated financial statements included elsewhere in this prospectus. Such unaudited interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( generally accepted accounting principles ). Operating results for the three months ended March 31, 2007 are not necessarily indicative of the results that may be expected for any future periods or the year ending December 31, 2007. In the opinion of management, all adjustments (consisting of only of normal recurring accruals) considered necessary for a fair presentation have been included. The following information should be read together with MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS and our Consolidated Financial Statements and Notes thereto included elsewhere in this prospectus. The historical results presented below are not necessarily indicative of future results. The summary consolidated financial data should be read in conjunction with notes to the fiscal year 2006 consolidated financial statements included in this prospectus and in the fiscal 2003 annual report on Form 10-K filed on November 10, 2004, which reflects the restatements of prior year transactions.

	Three Months Ended		Years Ended December 31,		2004	2003	2002
	2007	2006	2006	2005	(Restated)		(Restated)
	(Unaudited)	(Restated)		(Restated)			
	(In thousands, except per share data)						
<b>Consolidated Statements</b>							
<b>Of Operation Data:</b>							
Revenue	\$ 5,067	\$ 6,555	\$ 27,669	\$ 16,365	\$ 17,429	\$ 13,658	\$ 9,138
Cost of sales	6,441	5,324	22,418	15,129	12,168	18,162	5,656
Gross (loss) profit	(1,374 )	1,231	5,251	1,236	5,261	(4,504 )	3,482
Operating expenses:							
Selling, general, and administrative expenses	2,532	2,705	9,962	8,534	11,591	17,729	13,099
Research and development expenses	263	203	950	1,120	1,467	8,780	11,825
Impairment of Goodwill						184	
Impairment of long lived assets				4,487		2,684	
Total operating expenses	2,795	2,908	10,912	14,141	13,058	29,377	24,924
Loss before interest, other income, income taxes, minority interest and discontinued operations	(4,169 )	(1,677 )	(5,661 )	(12,905 )	(7,797 )	(33,881 )	(21,442 )
Loss from extinguishments of debt	(648 )			(1,247 )	(2,941 )		
Change in value of warrants, gain (loss)	3,692	(1,289 )	279	3,985	747		
Change in value of conversion feature, gain (loss)	4,344	(1,783 )	(226 )	9,118	2,093		
Other income		480	572		302		
Interest expense	(2,763 )	(1,782 )	(9,509 )	(6,021 )	(6,577 )	(390 )	(1,109 )
Interest income	61	2	23	17	37	304	506
Gain on sale of marketable securities held for sale						1,178	832
Income (loss) before minority interest and discontinued operations	517	(6,049 )	(14,522 )	(7,053 )	(14,136 )	(32,789 )	(21,213 )
Minority interest in loss of consolidated subsidiary						21	118
Income loss from continuing operations	517	(6,049 )	(14,522 )	(7,053 )	(14,136 )	(32,768 )	(21,095 )
Discontinued Operations:							
(Loss) gain income from discontinued operations, net					(749 )	(964 )	83



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Gain from disposal of discontinued operations, net						127	1,556
Net income (loss)	\$ 517	\$ (6,049 )	\$ (14,522 )	\$ (7,053 )	\$ (14,885 )	\$ (33,605 )	\$ (19,456 )
Income (loss) per share from continuing operations	\$ 0.01	\$ (0.14 )	\$ (0.33 )	\$ (0.17 )	\$ (0.34 )	\$ (0.79 )	\$ (0.54 )
(Loss) gain per share from discontinued operations	\$	\$	\$	\$	\$ (0.02 )	\$ (0.02 )	\$ 0.04
Net income (loss) per share	\$ 0.01	\$ (0.14 )	\$ (0.33 )	\$ (0.17 )	\$ (0.36 )	\$ (0.81 )	\$ (0.50 )
Weighted average shares - basic and diluted	44,925	42,817	43,809	41,833	41,610	41,505	38,714

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	As of March 31, 2007 (Unaudited) (In thousands)	As of December 31, 2006	2005 (Restated)	2004 (Restated)	2003	2002 (Restated)
<b>Consolidated Balance Sheet Data:</b>						
Cash and cash equivalents	\$ 2,937	\$ 144	\$ 1,392	\$ 742	\$ 3,127	\$ 25,058
Working capital (deficit)	(16,066 )	(23,157 )	(10,993 )	(14,910 )	(698 )	25,812
Total assets	25,735	22,244	21,563	28,508	30,852	24,845
Long-term debt, including current portion, net of discount	18,255	14,705	6,776	6,628	4,047	
Shareholders' equity (deficiency)	(9,322 )	(10,363 )	(1,320 )	4,191	16,163	50,599

## RISK FACTORS

*An investment in our common stock involves risk. You should carefully consider the risks we describe below before deciding to invest in our common stock. The market price of our common stock could decline due to any of these risks, in which case you could lose all or part of your investment. In assessing these risks, you should also refer to the other information included in this prospectus, including our consolidated financial statements, including the notes thereto, and appearing elsewhere in this prospectus. This discussion contains forward-looking statements. See *Forward-Looking Statements* for a discussion of uncertainties, risks and assumptions associated with these statements.*

### **We have incurred significant operating losses in the past and may not be able to achieve or sustain profitability in the future.**

We have experienced significant operating losses since our inception. Our net loss for the fiscal years ended December 31, 2006, 2005, and 2004, was \$14.5 million, \$7.1 million, and \$14.9 million, respectively. For the three months ended March 31, 2007 and 2006, we had a net income of \$0.5 million and a net loss of \$6.0 million, respectively. We had an accumulated deficit of approximately \$148.5 million at March 31, 2007. Of this accumulated deficit, \$44.5 million was attributable to losses generated by our discontinued equipment manufacturing and retail golf. We anticipate that we may continue to incur operating losses for the foreseeable future. Consequently, it is possible that we may never achieve positive earnings and, if we do achieve positive earnings, we may not be able to achieve them on a sustainable basis.

### **We will likely require additional funding, which may not be available on favorable terms or at all.**

Our future capital requirements will depend on the amount of cash generated by our operations. Our projections of cash flows from operations and, consequently, future cash needs are subject to substantial uncertainty. In addition, in our audit report on our financial statements for our fiscal years ended December 31, 2006 and 2005, our auditors included a going-concern qualification indicating that our significant operating losses and working capital deficit cause substantial doubt about our ability to continue as a going concern. By issuing an opinion stating that there is substantial doubt about our ability to continue as a going concern, our auditors have indicated that they are uncertain as to whether we have the capability to continue our operations without additional funding. On January 3, 2007, we completed a private placement of \$16.3 million in principal amount of 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes). The January 2010 Notes were issued for aggregate cash in the amount of \$12.9 million and in payment of a total of \$3.4 million in principal and accrued but unpaid interest under our previously issued 7% Senior Secured Convertible Notes Due August 2007 and our previously issued 8% Unsecured Subordinated Notes.

We anticipate that the \$12.9 million aggregate cash raised in the private placement will be sufficient to pursue our current operating plan only through the third quarter of 2007, and we will therefore require additional funding at or prior to that time. As a result, we are actively seeking additional sources of capital. The amount of funding that we seek and the timing of such fundraising efforts will depend on the extent to which we are able to increase revenues through obtaining additional purchase orders for our products and/or the extent to which we can restructure or modify our debt. Because we cannot be certain that we will be able to obtain adequate funding from debt, equity, or other traditional financing sources, we are also actively exploring several strategic financing options, including the possible sale of our manufacturing plant in South Korea (which would then be replaced with a smaller facility), potential licensing and outsourcing of manufacturing operations including those in South Korea and China, and the possible sale of our Liquidmetal Coatings business. In June 2007, we entered into an equipment sale and licensing agreement with Grace Metal, a South Korean corporation, providing for \$2.0 million in exchange for die casting machines and vacuum induction melters, and a 10-year exclusive license to manufacture Liquidmetal alloys for customers whose principal headquarters or major operations are based in South Korea. The principal purpose of the transactions with Grace Metal was to raise capital for the next-generation casting equipment and to shift the cost and burden of our manufacturing operations to a third party. Grace Metal was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company. We cannot guarantee that adequate funds will be available when needed, and if we do not receive sufficient capital, we may be required to alter or reduce the scope of our operations. If we raise additional funds by issuing equity securities, existing stockholders may be diluted. In addition, if shares of our common stock or securities convertible into or exercisable for our common stock are issued in consideration of such funds at an effective per share price lower than the conversion and exercise prices of our currently outstanding convertible notes and warrants, then anti-dilution provisions in such convertible notes and warrants would be triggered, thus possibly causing even greater dilution of our then-existing stockholders if the notes are converted or the warrants are exercised. See RISK FACTORS Our convertible notes and warrants contain anti-dilution provisions that, if triggered, could cause substantial dilution to our then-existing stockholders.

### **We have a limited history of developing, manufacturing, and selling products made from our bulk amorphous alloys.**

We have marketed and sold industrial coatings to distributors in the coatings industry since 1987. Prior to the third quarter of 2002, our experience selling products made from bulk amorphous alloys has been limited to our discontinued retail golf business, which had a different marketing strategy than the one we are currently employing. Therefore, we have a relatively limited



history of producing bulk amorphous alloy components and products on a mass-production basis. Furthermore, our ability to produce our products in desired quantities and at commercially reasonable prices is uncertain and is dependent on a variety of factors that are outside of our control, including the nature and design of the component, the customer's specifications, and required delivery timelines.

**We rely on assumptions about the markets for our products and components that, if incorrect, may adversely affect our profitability.**

We have a relatively short history producing bulk amorphous alloy components on a mass-production basis. We have made assumptions regarding the market size for, and the manufacturing requirements of, our products and components based in part on information we received from third parties and also from our limited history. If these assumptions prove to be incorrect, we may not achieve anticipated revenue targets or profitability.

**If we cannot establish and maintain relationships with customers that incorporate our components and products into their finished goods, we will not be able to increase our revenue and commercialize our products.**

Our business is based upon the commercialization of a new and unique materials technology. Our ability to increase our revenues will depend on our ability to successfully maintain and establish relationships with customers who are willing to incorporate our proprietary alloys and technology into their finished products. However, we believe that the size of our company and the newness of our technology and manufacturing process may continue to make it challenging to maintain and establish such relationships. In addition, we rely and will continue to rely to a large extent on the manufacturing, research, and development capabilities, as well as the marketing and distribution capabilities, of our customers in order to commercialize our products. Our future growth and success will depend in large part on our ability to enter into these relationships and the subsequent success of these relationships. If our products are selected for use in a customer's products, we still may not realize significant revenue from that customer if that customer's products are not commercially successful.

**It may take significant time and cost for us to develop new customer relationships, which may delay our ability to generate additional revenue or achieve profitability.**

Our ability to generate revenue from new customers is generally affected by the amount of time it takes for us to, among other things:

- identify a potential customer and introduce the customer to Liquidmetal alloys;
- work with the customer to select and design the parts to be fabricated from Liquidmetal alloys;
- make the molds and tooling to be used to produce the selected part;
- make prototypes and samples for customer testing;
- work with our customers to test and analyze prototypes and samples; and
- with respect to some types of products, such as medical devices, to obtain regulatory approval.

We currently do not have a sufficient history of selling products made from our bulk amorphous alloys to predict accurately the length of our average sales cycle. We believe that our average sales cycle from the time we deliver an active proposal to a customer until the time our customer fully integrates our bulk amorphous alloys into its product could be a significant period of time. Our history to date has demonstrated that the sales cycle could extend significantly longer than we anticipate. The time it takes to transition a customer from limited production to full-scale production runs will depend upon the nature of the processes and products into which our alloys are integrated. Moreover, we have found that customers often proceed very cautiously and slowly before incorporating a fundamentally new and unique type of material into their products.

**After we develop a customer relationship, it may take a significant amount of time for that customer to develop, manufacture, and sell finished goods that incorporate our components and products.**

Our experience has shown that our customers will perform numerous tests and extensively evaluate our components and products before incorporating them into their finished products. The time required for testing, evaluating, and designing our components and products into a customer's products, and in some cases, obtaining regulatory approval, can take a significant amount of time, with an additional period of time before a customer commences volume production of products incorporating our components and products, if ever. Moreover, because of this lengthy development cycle, we may experience a delay between the time we accrue expenses for research and development and sales and marketing efforts and the time when we generate revenue, if any. We may incur substantial costs in an attempt to transition a customer from initial testing to prototype and from prototype to final product. If we are unable to minimize these transition costs, or to recover the costs of these transitions from our customers, our operating results will be adversely affected.

**A limited number of our customers generate a significant portion of our revenue.**

For the near future, we expect that a significant portion of our revenue will be concentrated in a limited number of customers. For example, for the three months ended March 31, 2007, revenues from one customer, Flextronics Manufacturing LTD, represented approximately 17% of total revenues from continuing operations, for the year ended December 31, 2006, revenues from one customer, Flextronics Manufacturing LTD, represented approximately 13% of total revenues from continuing operations, for the year ended December 31, 2005, revenues from one customer, Samsung, represented approximately 10% of total revenue from continuing operations, and for the year ended December 31, 2004, revenue from two customers represented approximately 62% of total revenue from continuing operations. Revenues from direct suppliers to SanDisk were approximately 18% of total revenues from continuing operations for the three months ended March 31, 2007, and 22% of total revenues for the year ended December 31, 2006. Revenues from direct suppliers to Samsung represented approximately 0% of total revenues from continuing operations for the three months ended March 31, 2007 and 15%, 14% and 62% of total revenues from continuing operations, for the year ended December 31, 2006, 2005 and 2004, respectively. Also, revenues from defense related contracts with the United States of America represented 9% for the three months ended March 31, 2007 and 7%, 9%, and 10% for the year ended December 31, 2006, 2005, and 2004, respectively, and Growell Metal represented 0% of revenue from continuing operations for the three months ended March 31, 2007 and 0%, 0%, 12%, of revenue from continuing operations for the year ended December 31, 2006, 2005, and 2004. A reduction, delay, or cancellation of orders from one or more of these customers or the loss of one or more customer relationships could significantly reduce our revenue. Unless we establish long-term sales arrangements with these customers, they will have the ability to reduce or discontinue their purchases of our products on short notice.

**We expect to rely on our customers to market and sell finished goods that incorporate our products and components, a process over which we will have little control.**

Our future revenue growth and ultimate profitability will depend in part on the ability of our customers to successfully market and sell their finished goods that incorporate our products. We will have little control over our customers' marketing and sales efforts. These marketing and sales efforts may be unsuccessful for various reasons, any of which could hinder our ability to increase revenue or achieve profitability. For example, our customers may not have or devote sufficient resources to develop, market, and sell their finished goods that incorporate our products. Because we typically will not have exclusive sales arrangements with our customers, they will not be precluded from exploring and adopting competing technologies. Also, products incorporating competing technologies may be more successful for reasons unrelated to the performance of our customers' products or the marketing efforts of our customers.

**Our growth depends on our ability to identify, develop, and commercialize new applications for our technology.**

Our future growth and success will depend in part on our ability to identify, develop, and commercialize, either alone or in conjunction with our customers, new applications and uses for Liquidmetal alloys. If we are unable to identify and develop new applications, we may be unable to develop new products or generate additional revenue. Successful development of new applications for our products may require additional investment, including costs associated with research and development and the identification of new customers. In addition, difficulties in developing and achieving market acceptance of new products would harm our business.

**We may not be able to effectively compete with current suppliers of incumbent materials or producers of competing products.**

The future growth and success of our bulk amorphous alloy business will depend in part on our ability to establish and retain a technological advantage over other materials for our targeted applications. For many of our targeted applications, we will compete with manufacturers of similar products that use different materials. These different materials may include plastics, titanium alloys, or stainless steel, among others. For example, we have targeted the cellular phone component market as an application for bulk Liquidmetal alloys. In this market, we believe we will compete with other manufacturers of cellular phone components who use plastics or metal to construct their components. These other manufacturers may be able to manufacture their cellular phone components, particularly those made from plastics, at significantly less cost than our alloys. In other markets, we will compete directly with suppliers of the incumbent material. In addition, in each of our targeted markets, our success will depend in part on the ability of our customers to compete successfully in their respective markets. Thus, even if we are successful in replacing an incumbent material in a finished product, we will remain subject to the risk that our customer will not compete successfully in its own market.

**Our bulk amorphous alloy technology is still at an early stage of commercialization relative to many other materials.**

Our bulk amorphous alloy technology is a relatively new technology as compared to many other material technologies, such as plastics and widely-used high-performance crystalline alloys. Historically, the successful commercialization of a new materials technology has required the persistent improvement and refining of the technology over a sometimes lengthy period of time. Accordingly, we believe that our company's future success will be dependent on our ability to continue expanding and improving our technology platform by, among other things, constantly refining and improving our manufacturing processes, optimizing our existing amorphous alloy compositions for various applications, and developing and improving new bulk amorphous alloy compositions. Our failure to further expand our technology base could limit our growth opportunities and hamper our commercialization efforts.

**Future advances in materials science could render Liquidmetal alloys obsolete.**

Academic institutions and business enterprises frequently engage in the research and testing of new materials, including alloys and plastics. Advances in materials science could lead to new materials that have a more favorable combination of performance, processing, and cost characteristics than our alloys. The future development of any such new materials could render our alloys obsolete and unmarketable or may impair our ability to compete effectively.

**Our growth depends upon our ability to retain and attract a sufficient number of qualified employees.**

Our business is based upon the commercialization of a new and unique materials technology. Our future growth and success will depend in part on our ability to retain key members of our management and scientific staff, who are familiar with this technology and the potential applications and markets for it. For example, as a result of their experience and knowledge of our alloy technology, we believe that our future growth and success will depend in large part on the efforts of Larry Buffington, our President and Chief Executive Officer, and Dr. Atakan Peker, our Vice President of Technology. We do not have key man or similar insurance on any of these individuals. If we lose their services or the services of other key personnel, our financial results or business prospects may be harmed. Additionally, our future growth and success will depend in part on our ability to attract, train, and retain scientific engineering, manufacturing, sales, marketing, and management personnel. We cannot be certain that we will be able to attract and retain the personnel necessary to manage our operations effectively. Competition for experienced executives and scientists from numerous companies and academic and other research institutions may limit our ability to hire or retain personnel on acceptable terms. In addition, many of the companies with which we compete for experienced personnel have greater financial and other resources than we do. Moreover, the employment of non-citizens may be restricted by applicable immigration laws.

**We may not be able to successfully identify, consummate, or integrate strategic partnerships.**

As a part of our business strategy, we intend to pursue strategic partnering transactions that provide access to new technologies, products, markets, and manufacturing capabilities. These transactions could include licensing agreements, joint ventures, or even business combinations. We believe that these transactions will be particularly important to our future growth and success due to the size and resources of our company and the newness of our technology. For example, we may determine that we may need to license our technology to a larger manufacturer in order to penetrate a particular market. In addition, we may pursue transactions that will give us access to new technologies that are useful in connection with the composition, processing, or application of Liquidmetal alloys. We may not be able to successfully identify any potential strategic partnerships. Even if we do identify one or more potentially beneficial strategic partnering, we may not be able to consummate these transactions on favorable terms or obtain the benefits we anticipate from such a transaction.





**We may encounter manufacturing problems or delays or may be unable to produce high-quality products at acceptable costs.**

We have relatively limited experience in manufacturing our products and may be required to manufacture a range of products in high volumes while ensuring high quality and consistency. Although we currently own and operate a 166,000 square feet manufacturing facility in South Korea, we cannot guarantee that the facility will be able to produce the intended products with production yields, quality controls, and production costs that provide us with acceptable margins or profitability or satisfy the requirements of our customers.

**We expect to derive a substantial portion of our revenue from sales outside the United States, and problems associated with international business operations could affect our ability to manufacture and sell our products.**

We expect that we will continue to manufacture a substantial portion of our initial bulk Liquidmetal alloy products in our South Korean facility and derive a material portion of our revenues from customers in South Korea and revenues from products manufactured by our licensing partner in China. For our fiscal years ended December 31, 2006, 2005, and 2004, approximately 12%, 31%, and 54%, of our revenues came from customers located in South Korea, respectively. For the three months ended March 31, 2007 and 2006, approximately 11% and 47% of our revenues came from customers located in South Korea, respectively. As a result, our manufacturing operations and financial results are subject to risks of political instability, including the risk of conflict between North Korea and South Korea and tensions between the United States and North Korea. In addition, we anticipate that the trend of foreign customers accounting for a significant portion of our total revenues may continue. Specifically, we expect to continue to derive a significant amount of revenue from sales to customers located in Asia. A downturn in the economies of Asian countries where our products will be sold, particularly South Korea's economy, could materially harm our business.

Consequently, our operations and revenue likely will be subject to a number of risks associated with foreign commerce, including:

- staffing and managing our manufacturing facility located in South Korea;
- product or material transportation delays or disruption, including the availability and costs of air and other transportation between our South Korean facility and the United States;
- political and economic instability, including instability involving China and North Korea that may disrupt our operations in South Korea;
- potentially adverse tax consequences, which may reduce the profitability of products manufactured overseas or sold to overseas customers;
- burden of complying with complex foreign laws and treaties, which could limit our ability to conduct our business as contemplated in South Korea; and
- trade protection laws, policies, and measures and other regulatory requirements affecting trade and investment that could adversely affect the profitability of our South Korean Operations, including loss or modification of exemptions for taxes and tariffs.

Moreover, customers may sell finished goods that incorporate our components and products outside of the United States, which exposes us indirectly to additional foreign commerce risks.

**A substantial increase in the price or interruption in the supply of raw materials for our alloys could have an adverse effect on our profitability.**

Our proprietary alloy compositions are comprised of many elements, all of which are available commodity products. Although we believe that each of these raw materials is currently readily available in sufficient quantities from multiple sources on commercially acceptable terms, if the prices of these materials substantially increases or there is an interruption in the supply of these materials, such increase or interruption could adversely affect our profitability. For example, if the price of one of the elements included in our alloys substantially increases, we may not be able to pass the price increase on to our customers.

**Our business is subject to the potential adverse consequences of exchange rate fluctuations.**

We expect to conduct business in various foreign currencies and will be exposed to market risk from changes in foreign currency exchange rates and interest rates. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material adverse effect on our business, results of operations, and financial condition and could specifically result in foreign exchange gains and losses. The impact of future exchange rate fluctuations on our operations cannot be accurately predicted. To the extent that the percentage of our non-U.S. dollar revenue derived from international sales increases in the future, our exposure to risks associated with fluctuations in foreign exchange rates will increase further. Moreover, as a result of operating a manufacturing facility in South Korea, a substantial portion of our costs are and will continue to be denominated in the South Korean won. Adverse changes in the exchange rates of the South Korean won to the U.S. dollar will affect our costs of goods sold and operating margins and could result in exchange losses. The average foreign exchange rates for the years ended December 31, 2006, 2005, and 2004 were 967, 1,028, and 1,151 South Korean Won to the U.S. dollar, respectively. The average foreign exchange rates for the three months ended March 31, 2007 and 2006 were 954 and 993 South Korean Won to the U.S. dollar, respectively. The fluctuations in the exchange rates resulted in foreign currency translation gains of \$0.3 million, \$0.3 million, and \$1.7 million, for the years ended December 31, 2006, 2005, and 2004, respectively, and loss of \$0.2 million and a gain of \$0.1 million for the three months ended March 31, 2007 and 2006, respectively.

**Our inability to protect our licenses, patents, and proprietary rights in the United States and foreign countries could harm our business because third parties may take advantage of our research and development efforts.**

We have an exclusive license from the California Institute of Technology, or Caltech, to several patents and patent applications relating to amorphous alloy technology, and we have obtained several of our own patents. Our success depends in part on our ability to obtain and maintain patent and other proprietary right protection for our technologies and products in the United States and other countries. If we are unable to obtain or maintain these protections, we may not be able to prevent third parties from using our proprietary rights. Specifically, we must:

- protect and enforce our owned and licensed patents and intellectual property;
- exploit our patented technology (owned and licensed); and
- operate our business without infringing on the intellectual property rights of third parties.

Our licensed technology comprises several issued United States patents covering the composition and method of manufacturing of the family of Liquidmetal alloys. We also hold several United States and corresponding foreign patents covering the manufacturing processes of Liquidmetal alloys and their use. The patents relating to our coatings have various expiration dates until 2022, and those relating to our bulk amorphous alloys have expiration dates between 2013 and 2025. Patents covering the sale of our Armacore™ coatings material expired during 2005. We continue to hold other coatings related patents; however, if we are unable to protect our proprietary rights prior to the expiration of these patents, we may lose the advantage we have established as being the first to market bulk amorphous alloy products. In addition, the laws of some foreign countries do not protect proprietary rights to the same extent as the laws of the United States, and we may encounter significant problems and costs in protecting our proprietary rights in these foreign countries.

Patent law is still evolving relative to the scope and enforceability of claims in the fields in which we operate. Our patent protection involves complex legal and technical questions. Our patents and those patents for which we have license rights may be challenged, narrowed, invalidated, or circumvented. We may be able to protect our proprietary rights from infringement by third parties only to the extent that our proprietary technologies are covered by valid and enforceable patents or are effectively maintained as trade secrets. Furthermore, others may independently develop similar or alternative technologies or design around our patented technologies. Litigation or other proceedings to defend or enforce our intellectual property rights could require us to spend significant time and money and could otherwise adversely affect our business.



**Other companies may claim that we infringe their intellectual property rights, which could cause us to incur significant expenses or prevent us from selling our products.**

Our success depends, in part, on our ability to operate without infringing on valid, enforceable patents or proprietary rights of third parties and not breaching any licenses that may relate to our technology and products. Future patents issued to third parties may contain claims that conflict with our patents and that compete with our products and technologies, and third parties could assert infringement claims against us. Any litigation or interference proceedings, regardless of their outcome, may be costly and may require significant time and attention of our management and technical personnel. Litigation or interference proceedings could also force us to:

- stop or delay using our technology;
- stop or delay our customers from selling, manufacturing or using products that incorporate the challenged intellectual property;
- pay damages; or
- enter into licensing or royalty agreements that may be unavailable on acceptable terms.

**Our level of indebtedness reduces our financial flexibility and could impede our ability to operate.**

As of March 31, 2007, our long-term debt was \$29.8 million net of debt discount, including the current portion of such debt. Our long-term debt (including the current portion) includes the following:

- \$1.2 million in principal outstanding under our Korean subsidiary's loan from Kookmin Bank of South Korea;
- \$2.1 million in principal outstanding under the 6% Senior Secured Notes due July 2007 (the July 2007 Notes) issued in our August 19, 2004 private exchange;
- \$7.2 million in principal outstanding under the 7% Senior Secured Convertible Notes due August 2007 (the August 2007 Notes) issued in our August 2, 2005 private placement;
- \$16.3 million in principal outstanding under the 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes) issued in our January 3, 2007 private placement, as amended; and
- \$3.0 million in principal outstanding under the 8% Unsecured Subordinated Notes issued in May 2006, September 2006, and December 2006 private placements.
- As of March 31, 2007, our short-term debt was \$1.5 million. Our short-term debt included the following:
  - \$1.5 million in outstanding advances received under a factoring, loan, and security agreement executed in April 2005, as amended, with a financing company.

Under our loan from Kookmin Bank, we are obligated to make equal monthly payments of principal and interest of \$0.11 million each through the period ending in February 2008. Under our July 2007 Notes, August 2007 Notes, and January 2010 Notes we are required to make cash interest payments to the noteholders of \$0.51 million per quarter until such notes are converted or paid. Unless such notes are converted, the \$2.1 million in aggregate principal amount under our July 2007 Notes will become due in July 2007, provided that the holders of such notes may demand payment thereunder at any time after July 2006. The \$7.2 million in aggregate principal amount under our August 2007 Notes will become due in August 2007, the \$3.0 million in aggregate principal amount under the 8% Unsecured Subordinated Notes will become due in August 2007, and \$16.3 million in aggregate principal amount under our January 2010 Notes will become due beginning July 31, 2008 through January 3, 2010.



Our level of debt affects our operations in several important ways, including the following:

- a significant portion of our cash flow from operations is likely to be dedicated to the payment of the principal of and interest on our indebtedness;
- we may be unable to refinance our indebtedness on terms acceptable to us or at all;
- our cash flow may be insufficient to meet our required principal and interest payments; and
- we may be unable to obtain additional loans as a result of covenants and agreements with existing debt holders.

In addition, our convertible notes and related documents contain restrictive covenants pursuant to which we generally may not (i) incur any indebtedness that would be senior to, or on the same rank as, the convertible notes with respect to payment or security, (ii) grant any liens or security interests in any of our assets which serve as collateral for the convertible notes (which collateral consists of substantially all of our assets), (iii) with certain exceptions, sell any of the assets that constitute collateral for the notes, (iv) become a guarantor for a third-party's obligation (other than guarantees in the ordinary course of business not in excess of \$500,000 in the aggregate), (v) acquire any shares or securities of any other person or entity in excess of an aggregate of \$1.0 million over any rolling 12-month period, (vi) purchase or otherwise acquire any assets in excess of an aggregate of \$3.0 million over any rolling 12-month period, (vii) engage in any transaction resulting in the issuance to any person of more than 40% of the equity of our company, or (viii) engage in any merger or sale of all or substantially all of our business assets. These covenants may curtail our ability to raise capital in the future or otherwise restrict our ability to enter into a transaction that we believe would be in the best interest of our stockholders.

**One of the investors in our January 2007 private placement has demanded the redemption of its note issued in the private placement.**

The January 2010 Notes issued in our January 2007 private placement were issued pursuant to a Securities Purchase Agreement, dated January 3, 2007, between our company and the purchasers of the January 2010 Notes (the "January Purchase Agreement"). Under the terms of the original January Purchase Agreement, we agreed to repay or otherwise satisfy, within 5 days after the closing of the private placement, approximately \$15.5 million of our outstanding debt under previously issued promissory notes, including the August 2007 Notes (the "Debt Satisfaction Covenant"). We originally agreed to this covenant based on assurances that a substantial number of holders of previously issued notes would elect to convert such notes at a reduced conversion price following the January 2007 private placement under a note conversion agreement proposed by us, but most of such holders ultimately elected not to proceed with such conversion. Accordingly, in an effort to preserve funds, we have not yet repaid the indebtedness as required by the original January Purchase Agreement, and in April 2007, we entered into an amendment to the January Purchase Agreement providing that we will have until October 1, 2007 (or such earlier date on which the indebtedness to be repaid is due) to comply with the Debt Satisfaction Covenant.

On March 22, 2007, one of the purchasers of the January 2010 Notes (holding January 2010 Notes in the aggregate amount of \$2.0 million) sent us an event of default notice ("Event of Default Notice") indicating that we had defaulted under the January Purchase Agreement (and therefore under the January 2010 Note) by failing to comply with the Debt Satisfaction Covenant. This holder did not execute the April 2007 amendment to the January Purchase Agreement, although that amendment was approved by a majority of the note holders. In general, upon a breach of the January 2010 Notes or January Purchase Agreement, a holder of the January 2010 Notes may require us to redeem the January 2010 Notes at a price equal to the greater of (i) the conversion amount to be redeemed and (ii) the product of (A) the conversion rate with respect to such conversion amount in effect at such time as the purchaser of the January 2010 Note delivers an Event of Default Redemption Notice (as defined below) and (B) the closing sale price of our common stock on the date immediately preceding such event of default. Under the terms of the January 2010 Notes and January Purchase Agreement, we have ten (10) business days after the receipt of an Event of Default Notice to cure a default. On April 6, 2007, the holder which sent the Event of Default Notice further sent us an event of default redemption notice ("Event of Default Redemption Notice"). The Event of Default Redemption Notice states that the holder has elected to require us to redeem its January 2010 Note for a price equal to \$2,000,000 (the amount of the January 2010 Note) plus accrued and unpaid interest. On April 16, 2007, we were served with a complaint filed by the holder in the Federal District Court in Minnesota to collect this amount. We have answered and denied that any amount is currently owed to the holder, because of the April 2007 amendment to the January Purchase Agreement. The holder has also moved for summary judgment and a hearing on that motion is scheduled for August 30, 2007. We are currently working to resolve this matter.



Also, because we repaid \$1.8 million in principal and interest in January and February 2007 under certain subordinated bridge notes without first repaying the August 2007 Notes and July 2007 Notes, we may also be deemed to be in breach of the August 2007 Notes and July 2007 Notes, which case they would also have the right to accelerate such notes and foreclose on their security interest if the breach is not cured within thirty days of notice of default. The August 2007 Notes and July 2007 Notes are secured by substantially all of the assets of our company. If we fail to pay such notes, either at maturity or upon acceleration, then the noteholders may elect to foreclose upon the assets securing the notes.

**Evolving regulation of corporate governance and public disclosure may result in additional expenses and continuing uncertainty.**

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002 and new SEC regulations, are creating uncertainty for public companies. As a result of these new rules and the size and limited resources of our company, we will incur additional costs associated with our public company reporting requirements, and we may not be able to comply with some of these new rules. For example, we were not able to comply with Section 404 of the Sarbanes-Oxley Act of 2002 for our 2005 and 2004 fiscal years. In addition, these new rules could make it more difficult or more costly for us to obtain certain types of insurance, including director and officer liability insurance, and this could make it difficult for us to attract and retain qualified persons to serve on our board of directors.

We are presently evaluating and monitoring developments with respect to new and proposed rules and cannot predict or estimate the amount of the additional costs we may incur or the timing of such costs. These new or changed laws, regulations, and standards are subject to varying interpretations, in many cases due to their lack of specificity, and as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices.

We are committed to maintaining high standards of corporate governance and public disclosure. As a result, we intend to invest resources to comply with evolving laws, regulations, and standards, and this investment may result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities. If our efforts to comply with new or changed laws, regulations, and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to practice, regulatory authorities may initiate legal proceedings against us and we may be harmed.

**The time and cost associated with complying with government regulations to which we could become subject could have a material adverse effect on our business.**

Some of the applications that we have identified or may identify in the future may be subject to government regulations. For example, any medical devices such as precision ophthalmic instruments and orthopedic devices made from our alloys likely will be subject to extensive government regulation in the United States by the Food and Drug Administration, or FDA. Any medical device manufacturers to whom we sell Liquidmetal alloy products may need to comply with FDA requirements, including premarket approval or clearance under Section 510(k) of the Food Drug and Cosmetic Act before marketing in the United States Liquidmetal alloy medical device products. These medical device manufacturers may be required to obtain similar approvals before marketing these medical devices in foreign countries. Any medical device manufacturers with which we jointly develop and sell medical device products may not provide significant assistance to us in obtaining required regulatory approvals. The process of obtaining and maintaining required FDA and foreign regulatory approvals could be lengthy, expensive, and uncertain. Additionally, regulatory agencies can delay or prevent product introductions. The failure to comply with applicable regulatory requirements can result in substantial fines, civil and criminal penalties, stop sale orders, loss or denial of approvals, recalls of products, and product seizures.

In addition, the processing of beryllium, a minor constituent element of some of our alloys, can result in the release of beryllium into the workplace and the environment and in the creation of beryllium oxide as a by-product. Beryllium is classified as a hazardous air pollutant, a toxic substance, a hazardous substance, and a probable human carcinogen under



environmental, safety, and health laws, and various acute and chronic health effects may result from exposure to beryllium. We are required to comply with certain regulatory requirements and to obtain a permit from the U.S. Environmental Protection Agency or other government agencies to process beryllium. Our failure to comply with present or future governmental regulations related to the processing of beryllium could result in suspension of manufacturing operations and substantial fines or criminal penalties.

To the extent that our products have the potential for dual use, such as military and non-military applications, they may be subject to import and export restrictions of the U.S. government, as well as other countries. The process of obtaining any required U.S. or foreign licenses or approvals could be time-consuming, costly, and uncertain. Failure to comply with import and export regulatory requirements can lead to substantial fines, civil and criminal penalties, and the loss of government contracting and export privileges.

**The existence of minority stockholders in our Liquidmetal Golf subsidiary creates potential for conflicts of interest.**

We directly own 79% of the outstanding capital stock of Liquidmetal Golf, our subsidiary that has the exclusive right to commercialize our technology in the golf market. The remaining 21% of Liquidmetal Golf stock is owned by approximately 95 stockholders of record. As a result, conflicts of interest may develop between us and the minority stockholders of Liquidmetal Golf. To the extent that our officers and directors are also officers or directors of Liquidmetal Golf, matters may arise that place the fiduciary duties of these individuals in conflicting positions. John Kang, our Chairman, is also director of Liquidmetal Golf.

**Our stock price has experienced volatility and may continue to experience volatility.**

During the first five months in 2007, the highest bid price for our common stock was \$1.55 per share, while the lowest bid price during that period was \$0.70 per share. The trading price of our common stock could continue to fluctuate widely due to:

- quarter-to-quarter variations in results of operations;
- loss of a major customer;
- announcements of technological innovations by us or our potential competitors;
- changes in, or our failure to meet, the expectations of securities analysts;
- new products offered by us or our competitors;
- announcements of strategic relationships or strategic partnerships; or
- other events or factors that may be beyond our control.

In addition, the securities markets in general have experienced extreme price and trading volume volatility in the past. The trading prices of securities of many companies at our stage of growth have fluctuated broadly, often for reasons unrelated to the operating performance of the specific companies. These general market and industry factors may adversely affect the trading price of our common stock, regardless of our actual operating performance. If our stock price is volatile, we could face securities class action litigation, which could result in substantial costs and a diversion of management's attention and resources and could cause our stock price to fall.

**Our convertible notes and warrants contain anti-dilution provisions that, if triggered, could cause substantial dilution to our then-existing stockholders.**

The convertible notes and warrants issued in our January 2007 private placement contain full-ratchet anti-dilution rights. As a result of these anti-dilution rights, under our January 2010 Notes, if we issue or grant in the future any rights to purchase any of our common stock, or other security convertible into our common stock, for an effective per share price less than the conversion price then in effect, the conversion price of all unconverted January 2010 Notes will be decreased to equal such lower price. With regard to the warrants issued in connection with the January 2010 Notes, if we, in the future, issue or grant any rights to purchase any of our common stock, or other security convertible into our common stock, for a per share price less than



the conversion price of the January 2010 Notes then in effect, the exercise price of the warrants will be reduced to equal such lower price and the number of shares of our common stock for which the warrants may be exercised will be increased so that the total aggregate exercise price remains constant. The foregoing adjustments to the conversion price of the notes and the exercise price of the warrants will not apply to certain exempt issuances, including issuances pursuant to employee stock option plans and strategic transactions

In addition to the above-described full-ratchet anti-dilution rights, certain other notes and warrants previously issued by us contain weighted-average anti-dilution provisions. As of December 31, 2006, we had outstanding \$2.1 million in aggregate principal amount of 6% Senior Convertible Notes Due July 2007 with a conversion price of \$1.00 per share, \$9.9 million in aggregate principal amount of 7% Senior Convertible Notes Due August 2007 with a conversion price of \$2.00 per share, warrants to purchase 973,064 shares at an exercise price of \$2.58 per share, and warrants to purchase 3,902,714 shares at an exercise price of \$2.00 per share, each of which notes and warrants contain weighted-average anti-dilution provisions. Under these provisions, if we issue shares in the future for consideration below the conversion or exercise prices then in effect, then (with certain exceptions, including the issuance of stock options) the conversion price for our convertible notes would automatically be reduced (allowing the holders of the notes to receive additional shares of common stock upon conversion) and the exercise price of the warrants would automatically be reduced (with a corresponding increase in the number of shares issuable pursuant to such warrants). To illustrate the impact of these weighted-average anti-dilution provisions, because of the issuance of the January 2010 Notes in January 2007 and the reduction of the conversion price of certain previously issued convertible notes in February 2007, the above-described warrants outstanding as of December 31, 2006 have been adjusted to represent warrants to purchase 1,178,651 shares at an exercise price of \$2.13 per share, warrants to purchase 4,317,409 shares at an exercise price of \$1.75 per share, and warrants to purchase 125,000 shares at an exercise price of \$2.00 per share as of April 4, 2007. Thus, an aggregate of 745,282 additional shares of our common stock have become issuable pursuant to such previously granted warrants subsequent to December 31, 2006 as a result of the operation of these weighted-average anti-dilution provisions. It is also possible that a future triggering of the full-ratchet anti-dilution rights in our January 2010 Notes could result in a corresponding triggering of the above-described weighted-average anti-dilution provisions in the other notes and warrants.

If our available funds and cash generated from operations are insufficient to satisfy our liquidity requirements in the future, then we may need to raise substantial additional funds in the future to support our working capital requirements and for other purposes. If shares of our common stock or securities convertible into or exercisable for our common stock are issued in consideration of such funds at an effective per share price lower than the conversion and exercise prices of our convertible notes and warrants, then these anti-dilution provisions would be triggered, thus possibly causing substantial dilution to our then-existing stockholders if the notes are converted or the warrants are exercised. Further, subsequent sales of the shares in the public market could depress the market price of our stock by creating an excess in supply of shares for sale.

**We have never paid dividends on our common stock, and we do not anticipate paying any cash dividends in the foreseeable future.**

We have paid no cash dividends on our common stock to date. We currently intend to retain our future earnings, if any, to fund the development and growth of our businesses, and upon the completion of this offering, we do not anticipate paying any cash dividends on our capital stock for the foreseeable future. In addition, the terms of existing or any future debts may preclude us from paying dividends on our stock. As a result, capital appreciation, if any, of our common stock will be your sole source of gain for the foreseeable future.

**Antitakeover provisions of our certificate of incorporation and bylaws and provisions of applicable corporate law could delay or prevent a change of control that you may favor.**

Provisions in our certificate of incorporation, our bylaws, and Delaware law could make it more difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders. These provisions could discourage potential takeover attempts and could adversely affect the market price of our shares. Because of these provisions, you might not be able to receive a premium on your investment. These provisions:

- authorize our board of directors, without stockholder approval, to issue up to 10,000,000 shares of blank check preferred stock that could be issued by our board of directors to increase the number of outstanding shares and prevent a takeover attempt;
- limit stockholders' ability to call a special meeting of our stockholders;
- provide for a classified board of directors; and
- establish advance notice requirements to nominate directors for election to our board of directors or to propose matters that can be acted on by stockholders at stockholder meetings.

The provisions described above could delay or make more difficult transactions involving a change in control of us or our management.

**An ongoing investigation by the Department of Justice could have a material adverse impact on our company.**

In August 2006, we received a federal grand jury subpoena for the production of documents related to the period from January 1, 1999 through the present. The documents being sought include accounting records, documents relating to our relationship with Growell Metal of Korea, and documents and records relating to transactions in company stock by officers and directors. The subpoena was issued in connection with a grand jury investigation being conducted by the U.S. Department of Justice, Criminal Division, in the Middle District of Florida concerning alleged accounting improprieties involving our company, among other things. We have been, and intend to continue to be, fully cooperative with the authorities in connection with the Department of Justice's subpoena and investigation. However, in the event that current or former members of our senior management were to be implicated in any wrongdoing, it could have a material adverse impact on our capital resources and business focus.

**FORWARD-LOOKING STATEMENTS**

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This prospectus may contain forward-looking statements that relate to our management's current expectations, estimates, forecasts, and projections about our company and its business. Any statement in this prospectus that is not a statement of historical fact is a forward-looking statement, and in some cases, words such as believe, estimate, project, expect, intend, may, anticipate, plans, seeks, and similar words identify forward-looking statements. Forward-looking statements involve risks and uncertainties that could cause actual outcomes and results to differ materially from the anticipated outcomes or result. These statements are not guarantees of future performance. It is important to note that our actual results could differ materially from what is expressed in our forward-looking statements due to, among other things, the matters discussed in the RISK FACTORS section of this prospectus, as well as the following risks and uncertainties:

- Our history of operating losses and uncertainty surrounding our ability to achieve or sustain profitability;
- Our limited history of developing, manufacturing, and selling products made from our bulk amorphous alloys;
- Lengthy customer adoption cycles and unpredictable customer adoption practices;
- Our ability to identify, develop, and commercialize new product applications for our technology;
- Competition from current suppliers of incumbent materials or producers of competing products;
- Our ability to identify, consummate, and/or integrate strategic partnerships;
- The potential for manufacturing problems or delays; and
- Potential difficulties associated with protecting or expanding our intellectual property position.

We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

**DESCRIPTION OF PRIVATE PLACEMENT AND CONVERTIBLE NOTES**

### Description of Private Placement

On January 3, 2007, we completed a private placement of \$16.3 million in principal amount of Convertible Subordinated Notes due January 2010 (the January 2010 Notes). This prospectus covers the resale of the shares of our common stock issuable upon the conversion of the January 2010 Notes and upon the exercise of the warrants issued in the private placement.

The January 2010 Notes were issued pursuant to a Securities Purchase Agreement dated January 3, 2007 among our company and the purchasers of the January 2010 Notes, as amended by Amendment No. 1 on April 23, 2007 (the Securities Purchase Agreement). The principal purposes of the private placement were to raise additional funding for working capital and to provide for the repayment of certain indebtedness of our company. The January 2010 Notes were issued for aggregate cash in the amount of \$12.9 million (before expenses and placement agent fees) and in payment of a total of \$3.4 million in principal and accrued but unpaid interest under our previously issued 7% Senior Secured Convertible Notes Due August 2007 (the 7% Senior Notes) and our 8% Unsecured Subordinated Notes (the Subordinated Notes).

The January 2010 Notes (as amended) are convertible at any time at the option of the holder into shares of our common stock at a conversion price of \$1.10 per share, subject to adjustment for stock splits, stock dividends, and the like. In the event that we issue or grant, in the future, any rights to purchase any of our common stock, or other security convertible into our common stock, for an effective per share price less than the conversion price then in effect, the conversion price of all unconverted January 2010 Notes will be decreased to equal such lower price, provided that such adjustment will not apply to certain exempt issuances, including stock issuances pursuant to employee stock option plans and strategic transactions. In the event that the average of the daily volume weighted average price of the shares of our common stock for any 20 consecutive trading days exceeds 250% of the conversion price, we will have the right, but not the obligation, to require the holders of the January 2010 Notes to convert the Notes into our common stock at the conversion price then in effect. Such a mandatory conversion is subject to specified conditions, including the existence of an effective registration statement covering the resale of the shares into which the January 2010 Notes are converted and certain minimum trading volumes in the stock to be issued.

Prior to maturity, the January 2010 Notes will bear interest at 8% per annum with interest payable quarterly in arrears in cash, or, at our option, in the form of additional January 2010 Notes (in which case the interest rate will be 10% per annum). Our ability to pay interest with additional January 2010 Notes is subject to specified conditions, including the existence of an effective registration statement covering the resale of the shares issued in payment of interest and certain minimum trading volumes in the stock to be issued. From and after an event of default under the January 2010 Notes and for so long as the event of default is continuing, the January 2010 Notes will bear default interest at a rate of 12% per annum (or 15% per annum if we elect to pay interest with additional January 2010 Notes).

Beginning on July 31, 2008, and at the end of each month thereafter, we will be required to redeem 1/36th of the principal amount of the January 2010 Notes in cash or, at our election, with shares of our common stock. Our ability to pay the redemption amounts with shares of our common stock will be subject to specified conditions, including the existence of an effective registration statement covering the resale of the shares issued in payment of the redemption amount and certain minimum trading volumes in the stock to be issued. Any unconverted January 2010 Notes will become due on January 3, 2010, although we will have the right at any time after 18 months following the issuance of the January 2010 Notes to redeem the January 2010 Notes in whole or in part for a cash redemption price of 105% of the portion of the principal amount being redeemed plus all accrued and unpaid interest thereon. The January 2010 Notes are unsecured and are subordinate to our 6% Senior Convertible Notes Due July 2007 (the 6% Senior Notes) and to certain secured financing from commercial lenders incurred by our company in the future.

As a part of the private placement, we issued warrants to the purchasers of the Notes giving them the right to purchase up to an aggregate of 7.4 million shares of our common stock at an amended exercise price of \$1.55 per share (the Warrants). The exercise price of the Warrants is subject to adjustment for stock splits, stock dividends, and the like. In the event that we, in the future, issue or grant any rights to purchase any of our common stock, or other security convertible into our common stock, for a per share price less than the conversion price of the Notes then in effect, the exercise price of the Warrant will be reduced to equal such lower price and the number of shares of our common stock for which the Warrant may be exercised will be increased so that the total aggregate exercise price remains constant. The foregoing adjustment to the exercise price will not apply to certain exempt



issuances, including issuances pursuant to employee stock option plans and strategic transactions. In connection with the private placement, we also issued to the placement agent for the transaction warrants to purchase an aggregate of 248,710 shares of our common stock at an exercise price of \$1.55 per share. All of the Warrants (including the warrants granted to the placement agent) are immediately exercisable and will expire on January 3, 2012.

In connection with the private placement, our company and the purchasers of the January 2010 Notes entered into a Registration Rights Agreement under which we were required, on or before 45 days after the closing of the private placement, to file a registration statement with the SEC covering the resale of the shares of our common stock issuable pursuant to the January 2010 Notes and Warrants and to use our best efforts to have the registration declared effective at the earliest date (but in no event later than 90 days after filing if there is no SEC review of the registration statement, or 120 days if there is an SEC review). We will be subject to certain monetary penalties, as set forth in the Registration Rights Agreement, up to a maximum amount of 18% of the aggregate amount of January 2010 Notes sold in the private placement if the registration statement is not filed or does not become effective on a timely basis. The monetary penalties will accrue at the rate of 1% per month of the then-outstanding principal amount of the January 2010 Notes. In the event that we are unable to include in the registration statement all shares of our common stock issuable pursuant to the January 2010 Notes and Warrants, then we will be required to file up to two additional registration statements to register the resale of any shares excluded from the originally filed registration statement and to pay monetary penalties on the January 2010 Notes convertible into the excluded shares until the resale of such excluded shares is covered by an effective registration statement or until such shares can be sold under SEC Rule 144. As of May 31, 2007, an aggregate of \$127,995 in monetary penalties under the Registration Rights Agreement had already been paid to investors as a result of the late filing of the required registration statement, while an additional \$263,193 in such penalties were accrued but unpaid. The registration statement of which this prospectus is a part was filed pursuant to this Registration Rights Agreement.

**Dollar Value of Underlying Securities and Potential Profits on Conversion**

The following table sets forth the potential profit to be realized upon conversion of the January 2010 Notes based on the conversion price at January 3, 2007 and the closing price of our common stock on January 3, 2007 (the date the Notes were issued). Although the original conversion price of the January 2010 Notes exceeded the market price of our common stock on that date, the holders of our nonconvertible subordinated notes issued in 2006 (the Bridge Notes) were, under the terms of the Bridge Notes, entitled to a discount on the purchase of the January 2010 Notes.

**Potential Profit from Conversion of Convertible Notes**

<b>Market price per share at January 3, 2007</b>	\$	1.54
<b>Conversion Price per share at January 3, 2007</b>	\$	1.55
<b>Total shares underlying January 2010 Notes based on conversion price</b>		10,515,818
<b>Aggregate market value of underlying shares based on market price as of January 3, 2007</b>	\$	16,194,360
<b>Aggregate conversion price of underlying shares</b>	\$	16,299,518
<b>Discount to holders of Bridge Notes</b>	\$	73,000
<b>Aggregate purchase price for Notes after discount for Bridge Note holders</b>	\$	16,226,518

Pursuant to the amendment of the January 2010 Notes on April 23, 2007, the conversion price of the January 2010 Notes was reduced to \$1.10, which is a premium over the \$0.89 per share closing price of our common on the date of such amendment. The exercise price of the Warrants issued in the private placement was initially \$1.93 per share prior to the April 23 amendment, and therefore the Warrants were granted at a premium (not a discount) to the market value of our common stock on the date of the closing of the private placement. Pursuant to the April 23 amendment, the exercise price of the Warrants was decreased to \$1.55, which is a premium over the \$0.89 per share closing price of our common on the date of the amendment.

**Payments to Selling Stockholders and Affiliates**

In connection with the January 2010 Notes and the related private placement, we are or may be required to make the following payments to the selling stockholders.

Payee	Maximum Interest Payments(1)	Maximum Redemption Premiums(2)	Maximum Registration Penalties(3)	Total Maximum Payments During First Year(4)
Fort Mason Master, LP	595,145	140,865	507,114	292,999
Fort Mason Partners, LP	38,595	9,135	32,886	19,001
The Tail Wind Fund Ltd.	264,058	62,500	225,000	130,000
Solomon Strategic Holdings, Inc.	52,812	12,500	45,000	26,000
Whitebox Intermarket Partners, LP	422,493	100,000	360,000	208,000
Castlerigg Master Investments Ltd.	422,493	100,000	360,000	208,000
Diamond Opportunity Fund, LLC	73,936	17,500	63,000	36,400
Rockmore Investment Master Fund, Ltd.	211,247	50,000	180,000	104,000
Abdi Mahamedi	105,623	25,000	90,000	52,000
BridgePointe Master Fund Ltd.	422,493	100,000	360,000	208,000
Iroquois Master Fund Ltd.	105,623	25,000	90,000	52,000
Kenneth Lisiak	35,460	8,393	30,215	17,458
Vestal Venture Capital	77,514	18,347	66,048	38,161
Charles (Hyun Ju) Kim	47,701	11,290	40,645	23,484
Chunhyong Myong	35,776	8,468	30,484	17,613
Rodd Friedman	31,449	7,444	26,797	15,483
Myron Neugeboren	6,106	1,445	5,203	3,006
Ricardo Salas	69,921	16,550	59,578	34,423
Chang Ki Cho	92,140	21,809	78,511	45,362
Eric Brachfeld	11,518	2,726	9,814	5,670
Ed Neugeboren	4,245	1,005	3,617	2,090
Wynnefield Partners Small Cap Value L.P.	88,724	21,000	75,600	43,680
Wynnefield Partners Small Cap Value LP I	116,186	27,500	99,000	57,200
Wynnefield Small Cap Value Offshore	111,961	26,500	95,400	55,120

(1) Represents maximum amount of interest payable by us to the selling stockholders under the January 2010 Notes assuming the January 2010 Notes remain outstanding until the maturity date and assuming that interest is paid in cash.

(2) Represents the cash amount that would be payable by us if we exercised the optional redemption right described above, but does not include the warrants that would be issuable upon the exercise of such right.

(3) Represents the maximum monetary penalties that would be payable if we failed to timely file or obtain a declaration of effectiveness with respect to the registration statement required under the above-described Registration Rights Agreement.

(4) Represents the maximum amounts payable in cash during the first year of the January 2010 Notes under the other columns in this table assuming that (i) the optional redemption right is not exercised during the first year and (ii) monetary penalties accrue under the Registration Rights Agreement by reason of the late filing and effectiveness registration statement required by the Registration Rights Agreement.

In addition to the foregoing, we reimbursed the placement agent for the January 2007 private placement an amount equal to \$37,500 for legal fees incurred by them in connection with the private placement.

**Net Proceeds from Private Placement of January 2010 Notes**

The following table sets forth the gross cash proceeds received from the private placement of the January 2010 Notes and calculates the net proceeds from the private placement of the January 2010 Notes after deduction of the anticipated payments pursuant to the Notes and the other private placement documents. The net proceeds do not include the payment of any contingent payments, such as liquidated damages or repayment premiums in the case of default or a change in control. The net proceeds assumes that all interest and principal will be paid in cash notwithstanding that we may pay interest and principal in additional January 2010 Notes or shares of our common stock under specified circumstances, as described above. The interest amount reflected below assumes that all payments are made when due without any event of default, and the table assumes that none of the January 2010 Notes are converted prior to maturity. Based on the foregoing assumptions, the net proceeds represent approximately 63% of the gross proceeds.

<b>Gross Cash Proceeds</b>	\$ 12,580,000
Approximate Aggregate Interest Payments	\$ 3,443,219
Approximate Transaction Costs (including Placement Agent Fees)	\$ 1,240,876
<b>Net Proceeds</b>	\$ 7,895,905

**Comparison of Issuer Proceeds to Potential Investor Profit**

We plan to use the proceeds from the sale of the January 2010 Notes for working capital and to provide for the repayment of certain indebtedness of our company. The following table summarizes the potential proceeds we will receive pursuant to the Securities Purchase Agreement, January 2010 Notes, and Warrants. For purposes of this table, we have assumed that the selling stockholders will exercise all of the Warrants on a cash basis, although there is no assurance that any of the Warrants will actually be exercised. We have also assumed that the January 2010 Notes will be held by the selling stockholders through the maturity date of the January 2010 Notes.

Total Gross Proceeds Payable to Company in January 2007 Private Placement(1)	\$	24,719,266	
All Payments that have been made or may be required to be made by Company until Maturity(2)	\$	3,834,407	
Net Proceeds to Company Assuming Maximum Payments made by Company(3)	\$	20,884,859	
Total Possible Profit to the Selling Stockholders(4)	\$	0	
Percentage (%) of Payments and Profit over Net Proceeds(5)		18	%
Percentage (%) of Payments and Profit over Net Proceeds per year of Term(6)		6	%

(1) Includes gross cash proceeds payable to our company on the sale of the January 2010 Notes in the amount of \$12,850,000 and assumes full exercise of the Warrants (including Warrants granted to placement agents) to yield an aggregate exercise price of \$11,869,266. However, there is no assurance that any Warrants will actually be exercised.

(2) Total possible payments (excluding repayment of principal) payable by us to the selling stockholders or their affiliates assuming the January 2010 Notes remain outstanding until the maturity date and that interest is paid in cash. Assumes that liquidated damages under the Registration Rights Agreement are incurred only through April 30, 2007 and that no redemption premium on the January 2010 Notes will be applicable.

(3) Total net proceeds to us calculated by subtracting the result in footnote (2) from the results in footnote (1) (excluding transaction costs and placement agent fees).

(4) Total possible profit to the selling stockholders based on the aggregate discount to market price of the shares underlying the January 2010 Notes and Warrants as indicated above in the table entitled Potential Profit from Conversion of Convertible Notes.

(5) Percentage of the total possible payments to the selling stockholders as calculated in footnote (2) plus profit calculated in footnote (4) compared to net proceeds disclosed in footnote (3).

(6) Based on three year term.

**Comparison of Registered Shares to Outstanding Shares**

The following table compares the number of shares held by persons other than the selling stockholders, affiliates of our company, and affiliates of the selling stockholders with the number of shares registered for resale and sold by such parties in prior transactions as well as in January 2007:

Shares Outstanding Prior to January 2007 Private Placement Held by Persons Other than Selling Stockholders, or Affiliates of Company or Selling Stockholders	33,629,122
Shares Registered for Resale by Selling Stockholders, or Affiliates of Company or Selling Stockholders in Prior Registration Statements	100,500
Shares Registered for Resale by Selling Stockholders, or Affiliates of Company or Selling Stockholders, under Prior Registration Statements that Continue to be Held by Such Persons	0
Shares Sold in Registered Resale Transactions by the Selling Stockholders or Affiliates of the Selling Stockholders	100,500
Shares Registered for Resale on behalf of the Selling Stockholders or Affiliates of the Selling Stockholders in connection with the January 2007 Private Placement	12,032,140

**Other Information**

We currently intend, and we have a reasonable basis to believe that, we will have the financial ability to make all payments on the January 2010 Notes when they are due.

We have not received any information from the selling stockholders indicating that any selling shareholder has an existing short position our common stock.

With the exception of the following, we have not had any material relationships or arrangements with any of the selling stockholders, their affiliates, or any person with whom any selling shareholder has a contractual relationship regarding the January 2007 private placement (or any predecessors of those persons):

- Kenneth Lisiak, Vestal Venture Capital, Charles (Hyun Ju) Kim, Chunhyong Myong, and Ricardo Salas were investors in our May 2006 private placement and were therefore issued Bridge Notes in that transaction. These investors have exchanged their Bridge Notes for the January 2010 Notes.
- Rodd Friedman, Myron Neugeboren, Ricardo Salas, Chang Ki Cho, Eric Brachfeld, Ed Neugeboren, Wynnefield Partners Small Cap Value L.P., Wynnefield Partners Small Cap Value LP I, and Wynnefield Small Cap Value Offshore were investors in our August 2005 private placement and were therefore issued 7% Senior Secured Convertible Notes due August 2007 in that transaction. These investors have exchanged their 7% Senior Secured Convertible Notes for January 2010 Notes.
- Ricardo Salas was a former President, Chief Executive Officer, and director of our company.
- Chang Ki Cho was appointed as a director of our company in December of 2004.

**SELLING STOCKHOLDERS**



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On behalf of the selling stockholders named in the table below (including their donees, pledgees, transferees or other successors-in-interest who receive any of the shares covered by this prospectus), we are registering, pursuant to the registration statement of which this prospectus is a part, all 12,032,140 shares of our common stock which will become issuable upon:

- the conversion of Convertible Subordinated Notes Due January 2010 (the January 2010 Notes), which notes were issued by us to such selling stockholders in connection with a private placement in January 2007;
- the exercise of outstanding common stock purchase warrants issued by us in our January 2007 private placement and having an exercise price of \$1.55 per share; and
- the exercise of outstanding common stock purchase warrants issued by us between May 17, 2006 and December 1, 2006 and having an adjusted exercise price of \$2.13 per share.

The selling stockholders are investors that provided financing to us or are those that acted as placement agents in our private placement financings. We are registering the shares to permit the selling stockholders to offer these shares for resale from time to time. The selling stockholders may sell all, some or none of the shares covered by this prospectus. All information with respect to beneficial ownership has been furnished to us by the respective selling stockholders. For more information, see Plan of Distribution. As of May 14, 2007, the January 2010 Notes and the above-described warrants are convertible or exercisable for an aggregate of 23,653,994 shares of our common stock, although we are registering only 12,032,140 of this shares in the registration statement of which this prospectus is a part. The selling stockholders will have the right to determine whether the shares registered on their behalf will be allocated to the conversion of January 2010 Notes, the exercise of warrants, or a combination of the two.

The table below lists the selling stockholders and information regarding their ownership of common stock as of June 1, 2007:

SELLING STOCKHOLDER	NUMBER OF SHARES BENEFICIALLY OWNED PRIOR TO THIS OFFERING	NUMBER OF SHARES BEING OFFERED HEREBY(1)	SHARES OWNED AFTER OFFERING(1) NUMBER	PERCENTAGE(2)	
Fort Mason Master, LP(3)(5)	2,227,125	1,954,205	(4) 1,887,568	4.06	%
Fort Mason Partners, LP(3)(5)	249,137	126,729	(4) 122,408	*	
The Tail Wind Fund Ltd.(3)(6)	1,704,546	867,056	(4) 837,490	1.84	%
Solomon Strategic Holdings, Inc. (3)(7)	340,910	174,412	(4) 166,498	*	
Whitebox Intermarket Partners, LP(3)(8)	2,227,125	1,387,290	(4) 1,339,983	2.91	%
Castlerigg Master Investments Ltd. (3)(9)	2,227,125	1,387,290	(4) 1,339,983	2.91	%
Diamond Opportunity Fund, LLC (3)(10)	477,273	242,775	(4) 234,498	*	
Rockmore Investment Master Fund, Ltd. (3)(11)	1,363,637	693,645	(4) 669,992	1.48	%
Abdi Mahamedi(3)	2,227,125	346,823	(4) 2,227,125	4.97	%
BridgePointe Master Fund Ltd. (3)(12)	2,227,125	1,387,290	(4) 1,339,983	2.91	%
Iroquois Master Fund Ltd. (3)(13)	681,819	346,823	(4) 334,996	*	

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<b>SELLING STOCKHOLDER</b>	<b>NUMBER OF SHARES BENEFICIALLY OWNED PRIOR TO THIS OFFERING</b>	<b>NUMBER OF SHARES BEING OFFERED HEREBY(1)</b>	<b>SHARES OWNED AFTER OFFERING(1)</b>		
Gryphon Master Fund, L.P. (14)	234,742	119,407	115,335	*	
GSSF Master Fund, LP(15)	117,371	59,703	57,668	*	
Triage Capital Management L.P. (16)	28,170	14,329	13,841	*	
Leon Frenkel	89,203	45,375	43,828	*	
Stratford Partners, LP(17)	70,424	35,823	34,601	*	
Kenneth Lisiak(3)	269,045	136,855	(4) 132,190	*	
Vestal Venture Capital(3)(18)	576,658	293,330	(4) 283,328	*	
James Kang	6,164,322	41,793	6,122,529	12.88	%
Kurtis Jang	23,475	11,941	11,534	*	
Charles (Hyun Ju) Kim(3) (23)	354,868	180,512	(4) 174,356	*	
Chunhyong Myong(3)	266,151	135,384	(4) 130,767	*	
Hamilton Investment Partners, LLC(19)	58,686	29,852	28,834	*	
Rockport Funding, LLC(20)	23,475	11,941	11,534	*	
Jay P. Deahna	23,475	11,941	11,534	*	
Indigo Securities, LLC(21)(24)	346,481	176,245	170,236	*	
Rodd Friedman(3)	245,546	103,266	(4) 142,280	*	
Myron Neugeboren(3)	70,274	20,049	(4) 50,225	*	
Ricardo Salas(3)	1,726,425	296,279	(4) 1,430,146	3.17	%
Chang Ki Cho (3)	1,214,192	302,550	(4) 911,642	2.01	%
Eric Brachfeld(3)(23)	118,826	37,819	(4) 81,007	*	
Ed Neugeboren(3)(23)	63,120	13,940	(4) 49,180	*	
Wynnefield Partners Small Cap Value L.P.(3)(22)	692,729	291,322	(4) 401,407	*	
Wynnefield Partners Small Cap Value LP I(3) (22)	907,143	381,504	(4) 525,639	1.16	%
Wynnefield Small Cap Value Offshore(3) (22)	874,158	367,632	(4) 506,526	1.12	%

\* Less than 1.0%.

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- (1) Assumes that the stockholders dispose of all the shares of common stock covered by this prospectus and do not acquire or dispose of any additional shares of common stock. The selling stockholders are not representing, however, that any of the shares covered by this prospectus will be offered for sale, and the selling stockholders reserve the right to accept or reject, in whole or in part, any proposed sale of shares.
- (2) The percentage of common stock beneficially owned is based on 44,631,768 shares of common stock outstanding on June 1, 2007.
- (3) On January 3, 2007, we entered into a registration rights agreement with these selling stockholders. See the section of this prospectus entitled DESCRIPTION OF CAPITAL STOCK Registration Rights. Under the registration rights agreement, we are required to file a resale registration statement for the shares underlying the Convertible Subordinated Notes due January 2010 and the related Common Stock Purchase Warrants to enable the resale of such shares by these selling stockholders on a delayed or continuous basis under Rule 415 of the Securities Act.
- (4) Represents a good faith estimate of the maximum number of shares of common stock issuable pursuant to the Convertible Subordinated Notes due January 2010 and the related Common Stock Purchase Warrants. These Convertible Subordinated Notes and the related Common Stock Purchase Warrants contain conversion and exercise limitations providing that a selling stockholder may not at any time, unless waived by the selling stockholder upon no less than 61 days prior written notice, convert such notes or exercise such warrants into shares of our common stock if and to the extent that such conversion or exercise would result in the selling stockholder having beneficial ownership (calculated in accordance with Section 13(d) of the Securities Exchange Act of 1934, as amended) of more than 4.99% of our common stock. Accordingly, the number of shares of common stock set forth in the table as being registered for a selling shareholder may exceed the number of shares of common stock that the selling shareholder could own beneficially at any given time through its ownership of the convertible debentures and warrants.
- (5) The shares listed herein are owned by Fort Mason Master, L.P. and Fort Mason Partners, L.P. (collectively, the Fort Mason Funds ). Fort Mason Capital, LLC serves as the general partner of each of the Fort Mason Funds and, in such capacity, exercises sole voting and investment authority with respect to such shares. Mr. Daniel German serves as the sole managing member of Fort Mason Capital, LLC. Fort Mason Capital, LLC and Mr. German each disclaim beneficial ownership of such shares, except to the extent of its or his pecuniary interest therein, if any.
- (6) Tail Wind Advisory & Management Ltd., a UK corporation authorized and regulated by the Financial Services Authority of Great Britain ( TWAM ), is the investment manager for The Tail Wind Fund Ltd., and David Crook is the CEO and controlling shareholder of TWAM. Each of TWAM and David Crook expressly disclaims any equitable or beneficial ownership of the shares being registered hereunder and held by The Tail Wind Fund Ltd.
- (7) Andrew P. Mackellar has been authorized by the Board of Directors of Solomon Strategic Holdings, Inc. ( SSH ) to make voting and disposition decisions with respect to the shares on behalf of SSH. By reason of such delegated authority, Mr. Mackellar may be deemed to share dispositive power over the shares of common stock owned by SSH. Mr. Mackellar expressly disclaims any equitable or beneficial ownership of the shares being registered hereunder and held by SSH, and he does not have any legal right to maintain such delegated authority.
- (8) Andrew Redleaf, managing member of the GP, has the power to vote and dispose of the shares held by Whitebox Intermarket Partners, LP.

(9) Mr. Thomas E. Sandell has the power to vote and dispose of the shares held by Castlerigg Master Investments Ltd. ( Castlerigg ). Thomas Sandell is the controlling person of Sandell Asset Management Corp. ( SAMC ).

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Castlerigg International Ltd. ( CIL ) is the controlling shareholder of Castlerigg International Holdings Limited ( Holdings ). Holdings is the controlling shareholder of Castlerigg. Each of Holdings and CIL may be deemed to share beneficial ownership of the shares beneficially owned by Castlerigg. SAMC, Mr. Sandell, Holdings and CIL each disclaims beneficial ownership of the securities with respect to which indirect beneficial ownership is described.

(10) Mr. David Hokin, Mr. Rob Rubin, and Mr. Richard Marks in their capacities as Manager and Managing Directors, respectively, of Diamond Opportunity Fund, have the shared power to vote and dispose of the shares. Each of Messrs. Hokin, Rubin and Marks disclaim beneficial ownership of the shares.

(11) Rockmore Capital, LLC ( Rockmore Capital ) and Rockmore Partners, LLC ( Rockmore Partners ), each a limited liability company formed under the laws of the State of Delaware, serve as the investment manager and general partner, respectively, to Rockmore Investments (US) LP, a Delaware limited partnership, which invests all of its assets through Rockmore Investment Master Fund Ltd., an exempted company formed under the laws of Bermuda ( Rockmore Master Fund ). By reason of such relationships, Rockmore Capital and Rockmore Partners may be deemed to share dispositive power over the shares of our common stock owned by Rockmore Master Fund. Rockmore Capital and Rockmore Partners disclaim beneficial ownership of such shares of our common stock. Rockmore Partners has delegated authority to Rockmore Capital regarding the portfolio management decisions with respect to the shares of common stock owned by Rockmore Master Fund and, as of April 4, 2007, Mr. Bruce T. Bernstein and Mr. Brian Daly, as officers of Rockmore Capital, are responsible for the portfolio management decisions of the shares of common stock owned by Rockmore Master Fund. By reason of such authority, Messrs. Bernstein and Daly may be deemed to share dispositive power over the shares of our common stock owned by Rockmore Master Fund. Messrs. Bernstein and Daly disclaim beneficial ownership of such shares of our common stock and neither of such persons has any legal right to maintain such authority. No other person has sole or shared voting or dispositive power with respect to the shares of our common stock as those terms are used for purposes under Regulation 13D-G of the Securities Exchange Act of 1934, as amended. No person or group (as that term is used in Section 13(d) of the Securities Exchange Act of 1934, as amended, or the SEC's Regulation 13D-G) controls Rockmore Master Fund.

(12) Mr. Eric S. Swartz has the power to vote and dispose of the shares held by BridgePointe Master Fund Ltd.

(13) Mr. Joshua Silverman has voting and investment control over the shares held by Iroquois Master Fund Ltd. Mr. Silverman disclaims beneficial ownership of these shares.

(14) Mr. E.B. Lyon, IV has the power to vote and dispose of the shares held by Gryphon Master Fund, L.P.

(15) Mr. Tom C Davis has the power to vote and dispose of the shares held by GSSF Master Fund, LP.

(16) Mr. Leon Frenkel has the power to vote and dispose of the shares held by Triage Capital Management L.P.

(17) Mr. Mark Fain has the power to vote and dispose of the shares held by Stratford Partners, LP.

(18) Mr. Allan R. Lyons has the power to vote and dispose of the shares held by Vestal Venture Capital.

(19) Mr. Doug Hamilton, managing member of Hamilton Investment Partners, LLC, has the power to vote and dispose of the shares held by Hamilton Investment Partners, LLC.

(20) Mr. Richard Trepp, as member of Rockport Funding, LLC, has the power to vote and dispose of the shares held by Rockport Funding, LLC.



- (21) Mr. Eric Brachfeld has the power to vote and dispose of the shares held by Indigo Securities, LLC.
- (22) Nelson Obus, Managing Member of the selling stockholder, exercises sole voting and investment power over such shares.
- (23) These selling stockholders (or their ultimate beneficial owners) have represented to us that they are affiliates of broker-dealers and that they each acquired the notes, warrants, or underlying shares to be resold in the ordinary course of business and that, at the time of acquisition, each had no agreements or understandings, directly or indirectly, with any person to distribute the securities.
- (24) These selling stockholders are broker-dealers who acquired their warrants as compensation for serving as placement agents in the private placements in which the notes and warrants were issued.

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**USE OF PROCEEDS**

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The selling stockholders will receive all of the proceeds from the sale of the common stock offered by this prospectus. We will not receive any of the proceeds from the sale of common stock by the selling stockholders, although we may receive proceeds from the exercise of warrants by the selling stockholders, if exercised. We cannot guarantee that the warrants or the option will be exercised by the selling stockholders.

### **DIVIDEND POLICY**

Historically, we have not paid any dividends on our common stock, and we do not anticipate paying any dividends on our common stock in the foreseeable future. We expect to retain any earnings generated from our operations for use in our business. Any future determination as to the payment of dividends will be at the discretion of our Board of Directors and will depend upon our future operating results, financial condition and capital requirements, general business conditions and such other factors as our Board of Directors deems relevant.

**MARKET FOR AND PRICE RANGE OF THE COMMON STOCK**

## Edgar Filing: LIQUIDMETAL TECHNOLOGIES INC - Form S-1/A

Our common stock is currently quoted on the OTC Bulletin Board under the symbol LQMT. On June 28, 2007, the last reported sales price of our common stock was \$0.86 per share. As of June 28, 2007, we had 247 record holders of our common stock.

The following table sets forth, on a per share basis, the range of high and low bid information for the shares of our common stock for each full quarterly period within the two most recent fiscal years and any subsequent interim period for which financial statements are included. These quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

2007	High	Low
First Quarter	\$ 1.63	\$ 0.82

2006	High	Low
Fourth Quarter	\$ 1.80	\$ 1.42
Third Quarter	\$ 2.01	\$ 1.31
Second Quarter	\$ 2.34	\$ 1.31
First Quarter	\$ 1.75	\$ 0.87

2005	High	Low
Fourth Quarter	\$ 1.76	\$ 0.64
Third Quarter	\$ 2.13	\$ 1.52
Second Quarter	\$ 2.25	\$ 1.28
First Quarter	\$ 2.85	\$ 1.10

**SELECTED FINANCIAL DATA**

## Edgar Filing: LIQUIDMETAL TECHNOLOGIES INC - Form S-1/A

The following table shows our selected consolidated financial data as of and for the years ended December 31, 2002 through 2006. The selected consolidated financial data as of and for the years ended December 31, 2004, 2005, and 2006 are derived from our audited consolidated financial statements included elsewhere in this prospectus. The summary consolidated financial data as of and for the three months ended March 31, 2007 and 2006 have been derived from our unaudited consolidated financial statements included elsewhere in this prospectus. Such unaudited interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( generally accepted accounting principles ). Operating results for the three months ended March 31, 2007 are not necessarily indicative of the results that may be expected for any future periods or the year ending December 31, 2007. In the opinion of management, all adjustments (consisting of only of normal recurring accruals) considered necessary for a fair presentation have been included. The following information should be read with MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS and our Consolidated Financial Statements and Notes thereto included elsewhere in this prospectus.

These statements should be read in conjunction with restatement footnote 2 in the notes to the fiscal year 2006 consolidated financial statements included in the INDEX TO THE FINANCIAL STATEMENTS of this prospectus and in the fiscal 2003 annual report on Form 10-K filed on November 10, 2004, which reflects the restatements of prior year transactions.

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	Three Months Ended		Years Ended December 31,				
	2007	2006	2006	2005	2004	2003	2002
	(Unaudited)	(Restated)		(Restated)	(Restated)		(Restated)
(In thousands, except per share data)							
<b>Consolidated Statements Of Operation Data:</b>							
Revenue	\$ 5,067	\$ 6,555	\$ 27,669	\$ 16,365	\$ 17,429	\$ 13,658	\$ 9,138
Cost of sales	6,441	5,324	22,418	15,129	12,168	18,162	5,656
Gross (loss) profit	(1,374 )	1,231	5,251	1,236	5,261	(4,504 )	3,482
Operating expenses:							
Selling, general, and administrative expenses	2,532	2,705	9,962	8,534	11,591	17,729	13,099
Research and development expenses	263	203	950	1,120	1,467	8,780	11,825
Impairment of Goodwill						184	
Impairment of long lived assets				4,487		2,684	
Total operating expenses	2,795	2,908	10,912	14,141	13,058	29,377	24,924
Loss before interest, other income, income taxes, minority interest and discontinued operations	(4,169 )	(1,677 )	(5,661 )	(12,905 )	(7,797 )	(33,881 )	(21,442 )
Loss from extinguishments of debt	(648 )			(1,247 )	(2,941 )		
Change in value of warrants, gain (loss)	3,692	(1,289 )	279	3,985	747		
Change in value of conversion feature, gain (loss)	4,344	(1,783 )	(226 )	9,118	2,093		
Other income		480	572		302		
Interest expense	(2,763 )	(1,782 )	(9,509 )	(6,021 )	(6,577 )	(390 )	(1,109 )
Interest income	61	2	23	17	37	304	506
Gain on sale of marketable securities held for sale						1,178	832
Income (loss) before minority interest and discontinued operations	517	(6,049 )	(14,522 )	(7,053 )	(14,136 )	(32,789 )	(21,213 )
Minority interest in loss of consolidated subsidiary						21	118
Income loss from continuing operations	517	(6,049 )	(14,522 )	(7,053 )	(14,136 )	(32,768 )	(21,095 )
Discontinued Operations:							
(Loss) gain income from discontinued operations, net					(749 )	(964 )	83
Gain from disposal of discontinued operations, net						127	1,556
Net income (loss)	\$ 517	\$ (6,049 )	\$ (14,522 )	\$ (7,053 )	\$ (14,885 )	\$ (33,605 )	\$ (19,456 )
Income (loss) per share from continuing operations	\$ 0.01	\$ (0.14 )	\$ (0.33 )	\$ (0.17 )	\$ (0.34 )	\$ (0.79 )	\$ (0.54 )
(Loss) gain per share from discontinued operations	\$	\$	\$	\$	\$ (0.02 )	\$ (0.02 )	\$ 0.04
Net income (loss) per share	\$ 0.01	\$ (0.14 )	\$ (0.33 )	\$ (0.17 )	\$ (0.36 )	\$ (0.81 )	\$ (0.50 )
Weighted average shares - basic and diluted	44,925	42,817	43,809	41,833	41,610	41,505	38,714



	As of March 31, 2007 (Unaudited) (In thousands)	2006	As of December 31, 2005 (Restated)	2004 (Restated)	2003	2002 (Restated)
<b>Consolidated Balance Sheet Data:</b>						
Cash and cash equivalents	\$ 2,937	\$ 144	\$ 1,392	\$ 742	\$ 3,127	\$ 25,058
Working capital (deficit)	(16,066 )	(23,157 )	(10,993 )	(14,910 )	(698 )	25,812
Total assets	25,735	22,244	21,563	28,508	30,852	24,845
Long-term debt, including current portion, net of discount	18,255	14,705	6,776	6,628	4,047	
Shareholders' equity (deficiency)	(9,322 )	(10,363 )	(1,320 )	4,191	16,163	50,599

**SUPPLEMENTARY FINANCIAL INFORMATION**

## Edgar Filing: LIQUIDMETAL TECHNOLOGIES INC - Form S-1/A

The following information presents our unaudited quarterly operating results for 2007, 2006, and 2005. The data has been prepared by Liquidmetal Technologies, Inc. on a basis consistent with the Consolidated Financial Statements included elsewhere in this prospectus, and includes all adjustments, consisting of normal recurring accruals, that we consider necessary for a fair presentation thereof. These operating results are not necessarily indicative of our future performance.

Consolidated Statements of Operations Data:	For the Three Months Ended 3/31/07 (In thousands, except per share data) (Unaudited)	
Revenue	\$	5,067
Cost of sales		6,441
Gross loss		(1,374)
Operating expenses		
Selling, general, and administrative		2,532
Research and development		263
Total operating expenses		2,795
Loss from operations		(4,169)
Loss from extinguishments of debt		(648)
Change in value of warrants, gain		3,692
Change in value of conversion feature, gain		4,344
Interest expense, net		(2,702)
Income from operation before income taxes		517
Income taxes		
Net Income	\$	517
Income per share from operations - basic and diluted		0.01
Weighted average common shares used to compute loss per share from operations - basic and diluted		44,925

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Consolidated Statements of Operations Data:	For the Three Months Ended			
	12/31/06	9/30/06	6/30/06	3/31/06 (Restated)
	(In thousands, except per share data) (Unaudited)			
Revenue	\$ 5,984	\$ 8,040	7,090	\$ 6,555
Cost of sales	5,081	6,449	5,564	5,324
Gross profit	903	1,591	1,526	1,231
Operating expenses				
Selling, general, and administrative	2,599	2,290	2,368	2,705
Research and development	197	269	281	203
Total operating expenses	2,796	2,559	2,649	2,908
Loss from operations	(1,893 )	(968 )	(1,123 )	(1,677 )
Change in value of warrants, gain (loss)	1,633	1,361	(1,426 )	(1,289 )
Change in value of conversion feature, gain (loss)	1,707	1,987	(2,137 )	(1,783 )
Other income			92	480
Interest expense, net	(2,142 )	(2,294 )	(3,270 )	(1,780 )
Income (loss) from operation before income taxes	(695 )	86	(7,864 )	(6,049 )
Income taxes				
Net Income (loss)	\$ (695 )	\$ 86	\$ (7,864 )	\$ (6,049 )
Income (loss) per share from operations - basic and diluted	(0.02 )	0.00	(0.18 )	(0.14 )
Weighted average common shares used to compute loss per share from operations - basic and diluted	44,245	44,100	44,075	42,817

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Consolidated Statements of Operations Data:	For the Three Months Ended			
	12/31/05 (Restated) (In thousands, except per share data) (Unaudited)	9/30/05 (Restated)	6/30/05 (Restated)	3/31/05 (Restated)
Revenue	\$ 5,453	\$ 4,342	\$ 3,727	\$ 2,843
Cost of sales	4,576	3,756	3,962	2,835
Gross (loss) profit	877	586	(235 )	8
Operating expenses				
Selling, general, and administrative	2,013	2,364	1,567	2,590
Research and development	314	196	213	397
Impairment of long lived assets	260	833	3,394	
Total operating expenses	2,587	3,393	5,174	2,987
Loss from operations	(1,710 )	(2,807 )	(5,409 )	(2,979 )
Loss from extinguishments of debt		(1,247 )		
Change in value of warrants, gain (loss)	2,840	1,112	(100 )	133
Change in value of conversion feature, gain	4,621	2,215	1,167	1,115
Interest expense, net	(1,641 )	(1,652 )	(1,180 )	(1,531 )
Income (loss) from operation before income taxes and discontinued operations	4,110	(2,379 )	(5,522 )	(3,262 )
Income taxes				
Net income (loss)	\$ 4,110	\$ (2,379 )	\$ (5,522 )	\$ (3,262 )
Income (loss) per share from continuing operations - basic and diluted	\$ 0.10	\$ (0.06 )	\$ (0.13 )	\$ (0.08 )
Weighted average common shares used to compute income (loss) per share from continuing operations - basic and diluted	42,180	41,933	41,610	41,610

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements included elsewhere in this prospectus. This discussion contains forward-looking statements. See Forward-Looking Statements for a discussion of uncertainties, risks and assumptions associated with these statements.*

### Overview

Our revenues are derived from two principal operating segments: Liquidmetal alloy industrial coatings and bulk Liquidmetal alloy products. Liquidmetal alloy industrial coatings are used primarily as a protective coating for industrial machinery and equipment, such as drill pipe used by the oil drilling industry and boiler tubes used in coal-burning power plants. Bulk Liquidmetal alloy segment revenue includes sales of parts or components of electronic devices, medical products, and sports and leisure goods; tooling and prototype parts (including demonstration parts and test samples) for customers with products in development, product licensing and arrangements, and research and development revenue relating primarily to defense and medical applications. We expect that these sources of revenue will continue to significantly change the character of our revenue mix.

The cost of sales for our Liquidmetal coatings segment consists primarily of the costs of outsourcing our manufacturing to third parties. Consistent with our expectations, our cost of sales has been increasing over historical results as we further build our bulk Liquidmetal alloy business. Although we plan to continue outsourcing the manufacturing of our coatings, we will internally manufacture many products derived from our bulk Liquidmetal alloys.

Selling, general, and administrative expenses currently consist primarily of salaries and related benefits, severance costs, travel, consulting and professional fees, depreciation and amortization, insurance, office and administrative expenses, and other expenses related to our operations.

Research and development expenses represent salaries, related benefits expense, stock-based compensation, depreciation of research equipment, consulting and contract services, expenses incurred for the design and testing of new processing methods, expenses for the development of sample and prototype products, and other expenses related to the research and development of Liquidmetal alloys. Costs associated with research and development activities are expensed as incurred. We plan to enhance our competitive position by improving our existing technologies and developing advances in amorphous alloy technologies. We believe that our research and development efforts will focus on the discovery of new alloy compositions, the development of improved processing technology, and the identification of new applications for our alloys.

We maintain certain of our raw material inventories in amounts in excess of our operating cycle of one year due to the nature of our manufacturing process, production lead time, and the recyclability of our raw material. These inventories were classified as long-term inventory as of December 31, 2004. We have determined that its current and projected raw material requirements are not sufficient enough to warrant the use of such raw materials in the foreseeable future. As a result, we determined that the carrying value of raw materials held by our South Korea subsidiary, Liquidmetal Korea, exceeded its fair value in the amount of \$2.7 million during the fiscal year 2005.

Idle equipment consists of certain equipment held by us for use in expansion of bulk alloy parts manufacturing. Due to excess manufacturing capacity, we classified the equipment as idle equipment as of December 31, 2005 and 2004. While the equipment may be used internally to meet future capacity requirements, considering our current revenue and foreseeable production requirements, we do not anticipate utilizing this equipment internally in the near future. As a result, we determined that the carrying value of idle equipment held by its subsidiary, Liquidmetal Technologies Korea, exceeded its fair value in the amount of \$1.7 million during the second quarter of fiscal year 2005.

Impairment of Long-Lived Assets consists of a write-down of \$2.7 million of raw materials considered to be long term inventory and \$1.7 million of idle equipment. During 2005, while we may use the excess raw materials beyond one year to fulfill future customer order, we determined that our capacity was not significant enough to warrant holding this inventory as a long term asset. Further, while we have actively marketed the idle equipment for ultimate sale since early 2004, we were unable to sell

this equipment. In addition, while the equipment may be used internally to meet future capacity requirements, considering the revenues during 2005, we did not anticipate utilizing this equipment internally in the near future. As such, during 2005 we have reduced the carrying values of the excess raw material and idle equipment.

Change in Value of Warrants consists of changes to the fair value of warrants outstanding at each period. The warrants have been accounted for as a liability in accordance with Emerging Issues Task Force Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock, with the change in fair values reported in earnings. The fair values are determined using a Black-Scholes pricing model and fluctuations in our stock price have had the greatest impact on the valuation of outstanding warrants.

Change in Value of Conversion Feature consists of changes to the fair value of the embedded conversion feature of our senior convertible notes. The embedded conversion feature has been accounted for as a separate derivative instrument in accordance with SFAS 133 with a change in fair values reported in earnings. The change in fair values is determined using a Black-Scholes pricing model and fluctuations in our stock price have had the greatest impact on the valuation of outstanding conversion features.

On May 21, 2003, we completed a reincorporation by transitioning from a California corporation to a Delaware corporation. The reincorporation was effected through the merger of the former California entity into a newly created wholly owned Delaware subsidiary. The reincorporation changed the legal domicile of our company but did not result in any change to our business, management, employees, fiscal year, assets or liabilities, or location of facilities. As part of the reincorporation, each share of the California corporation was automatically converted into one share of the Delaware corporation. In addition, total authorized shares decreased from 200,000,000 shares to 100,000,000 shares.

In conjunction with the divestiture of our Dongyang and Taesung subsidiaries in March and June 2004, respectively, we decided to discontinue our equipment manufacturing business in order to conform our operations to our broader corporate business strategy. Pursuant to Accounting Principles Board Opinion No. 30, Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, we reclassified our consolidated financial statements to reflect the discontinuation of our equipment manufacturing operations. The revenue, costs and expenses, assets and liabilities, and cash flows of the equipment manufacturing business were segregated in our financial statements.

On August 4, 2004, we established a post-processing plant in the city of Weihai in Shandong province of China under Weihai Liquidmetal Company Limited, which is 100 percent owned by Liquidmetal Technologies Korea, to facilitate our bulk alloy manufacturing business. Weihai Liquidmetal is consolidated into Liquidmetal Technologies with all intercompany transactions eliminated. Effective June 1, 2007, we discontinued our operation in Weihai and transferred our manufacturing staff and equipment in Weihai to Grace Metal, a South Korean corporation, as result of a strategy to shift the cost and burden of our manufacturing operations to a third party. Grace Metal was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company. As part of this strategy, in June 2007, we changed the name of our South Korean subsidiary to Liquidmetal Technologies Korea Co., Ltd, which was formerly Liquidmetal Korea Co., Ltd. Grace Metal will assume the name of Liquidmetal Korea to conduct business in South Korea.

On June 26, 2006, we entered into a joint venture agreement with SAGA, SpA in Padova, Italy, ( SAGA ) a specialist precision parts manufacturer. The joint venture is named Liquidmetal SAGA Italy, Srl ( LSI ). We also entered into an exclusive manufacturing license agreement for the eyewear industry with LSI. Under the joint venture agreement, we have the option to buy ownership interest in LSI, initially, of 19.9% to up to 50%. In December 2006, we have purchased 19.9% interest in the joint venture.

## **Results of Operations**

### ***Comparison of the three months ended March 31, 2007 and 2006***

*Revenue.* Revenue decreased \$1.5 million to \$5.1 million for the three months ended March 31, 2007 from \$6.6 million for the three months ended March 31, 2006. The decrease consisted of a decrease of \$1.8 million from the sales and prototyping of parts manufactured from bulk Liquidmetal alloys to consumer electronics customers as a result of decreased demand from electronic casings applications, offset by an increase of \$0.3 million from sales of our coatings products as a result of increase in demand from oil drilling applications.

*Cost of Sales.* Cost of sales increased to \$6.4 million, or 127% of revenue, for the three months ended March 31, 2007 from \$5.3 million, or 81% of revenue, for the three months ended March 31, 2006. The increase was a result of decreases in





bulk Liquidmetal alloy business. Significant portions of our manufacturing costs continue to remain fixed. We believe that higher manufacturing volumes and greater mix of higher-margin products in the future will cause the gross profit to improve over time. The cost to manufacture parts from our bulk Liquidmetal alloys is variable and differs based on the unique design of each product. However, the cost of sales for the products sold by the coatings business segment is generally consistent because the Liquidmetal coatings products are produced by third parties and sold wholesale to various industries.

*Selling, General, and Administrative Expenses.* Selling, general, and administrative expenses decreased to \$2.5 million, or 50% of revenue, for the three months ended March 31, 2007 from \$2.7 million, or 41% of revenue, for the three months ended March 31, 2006. This decrease was primarily a result of decrease in wages and expenses of \$0.1 million, and a decrease in travel and advertising expenses \$0.1 million.

*Research and Development Expenses.* Research and development expenses increased to \$0.3 million, or 5% of revenue, for the three months ended March 31, 2007 from \$0.2 million, or 3% of revenue, for the three months ended March 31, 2006. The increase is primarily due to an increase in wages and expenses and professional fees of \$0.1 million. We continue to perform research and development of new Liquidmetal alloys and related processing capabilities, develop new manufacturing techniques, and contract with consultants to advance the development of Liquidmetal alloys.

*Loss from Extinguishments of Debt.* Loss from extinguishments of debt increased to \$0.6 million, or 13% of revenue, for the three months ended March 31, 2007 from \$0 for the three months ended March 31, 2006. The \$0.6 million loss from extinguishment of debt was recognized from the extinguishment of certain of our convertible and subordinated notes in January 2007.

*Change in Value of Warrants.* Change in value of warrants increased to a gain of \$3.7 million, or 73% of revenue, for the three months ended March 31, 2007 from a loss of \$1.3 million, or 20% of revenue, for the three months ended March 31, 2006. The change in value of warrants consisted of warrants issued from convertible notes and subordinated notes funded between 2004 and 2007 primarily as a result of fluctuations in our stock price.

*Change in Value of Conversion Feature.* Change in the value of our conversion feature liability from our senior convertible debt funded in March 2004 and exchanged in August 2004, August 2005 and January 2007 resulted in a change in value of conversion feature gain of \$4.3 million, or 86% of revenue, during the three months ended March 31, 2007 from a loss of \$1.8 million or 27% of revenue, for the three months ended March 31, 2006, primarily as a result of fluctuations in our stock price.

*Other Income.* Other income was \$0.5 million, or 7% of revenue, for the three months ended March 31, 2006 from termination of a distribution agreement with a Japanese sporting goods distributor originally entered into in March 1996. There were no amounts recognized as other income during the three months ended March 31, 2007.

*Interest Expense.* Interest expense was \$2.8 million, or 55% of revenue, for the three months ended March 31, 2007 and was \$1.8 million, or 27% of revenue, for the three months ended March 31, 2006. Interest expense consists primarily of interest accrued on the Kookmin Bank loan funded in 2003, convertible debts funded in 2004, 2005, and 2007, subordinated notes funded in 2006, fees charged from short-term borrowings under the April 2005 factoring, loan, and security agreement, as well as amortization of debt issuance costs and discount on the convertible and subordinated debt. The increase was primarily due to higher debt balance, increased debt discount amortization, increases in fees from borrowings made under the April 2005 factoring, loan, and security agreement, and interest costs accrued for late filing penalties during the three months ended March 31, 2007.

*Interest Income.* Interest income was \$61 thousand for the three months ended March 31, 2007 and was \$2 thousand for the three months ended March 31, 2006 from interest earned on cash deposits.

*Comparison of the years ended December 31, 2006 and 2005*

*Revenue.* Revenue increased to \$27.7 million in the twelve months ended December 31, 2006 from \$16.4 million in the twelve months ended December 31, 2005. The increase included a \$7.3 million increase in sales and prototyping of parts manufactured from bulk Liquidmetal alloys to consumer electronics customers as a result of increased demand in electronic casings

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applications, and increase of \$3.5 million in sale of our coatings products as a result of increased demand in oil drilling applications, and an increase of \$0.5 million in research and development services as a result of increased research and development services primarily from defense applications.

*Cost of Sales.* Cost of sales increased to \$22.4 million, or 81% of revenue, during the twelve months ended December 31, 2006 from \$15.1 million, or 92% of revenue, in the twelve months ended December 31, 2005. The increase was a result of increases in bulk Liquidmetal alloy business and coatings business. Cost of sales as a percentage of revenue has decreased as a result of continued maturing of our manufacturing process, which represents our company's efforts to manage costs and focus on our core business, and an increase in revenues generated from our higher margin coatings products. We believe that higher manufacturing volumes and greater mix of higher-margin products in the future will cause the gross profit to improve over time. The cost to manufacture parts from our bulk Liquidmetal alloys is variable and differs based on the unique design of each product. However, cost of sales for the products sold by the coatings business segment is generally consistent because the Liquidmetal coatings products are produced by third parties and sold wholesale to various industries.

*Selling, General, and Administrative Expenses.* Selling, general, and administrative expenses increased to \$10.0 million, or 36% of revenue, in the twelve months ended December 31, 2006 from \$8.5 million, or 52% of revenue, in the twelve months ended December 31, 2005. This increase was primarily a result of increase in wages and expenses of \$1.4 million, increase in professional and contracted services of \$0.4 million, increase in travel expenses of \$0.3 million, and increase in advertising and promotions expense of \$0.2 million offset by a decrease in insurance expense of \$0.7 million and decrease in rent expense of \$0.1 million. The decrease in selling, general and administrative expenses as a percentage of revenue represent our company's efforts to manage costs and focus on our core business while continuing to build our corporate infrastructure required to prepare for and support the anticipated growth of our bulk Liquidmetal alloy business.

*Research and Development Expenses.* Research and development expenses decreases to \$1.0 million, or 3% of revenue, in the twelve months ended December 31, 2006 from \$1.1 million, or 7% of revenue, in the twelve months ended December 31, 2005. The decrease was a result of our company focusing primarily on our core business associated with our bulk Liquidmetal alloy business while managing our costs. Our company continues to perform research and development efforts on new Liquidmetal alloys and related processing capabilities, develop new manufacturing techniques, and contract with consultants and provide research grants to various institutions to advance the development of Liquidmetal alloys.

*Impairment of Long Lived Assets.* Impairment of long lived assets decreased to \$0, in the twelve months ended December 31, 2006 from \$4.5 million, or 27% of revenue, in the twelve months ended December 31, 2005. Impairment expense during 2005 represent primarily write-down of \$2.7 million of raw materials considered to be long term inventory and \$1.7 million of idle equipment which were written down due to our projected capacity for 2006 as not being significant enough to warrant holding this inventory as a long term asset. Further, while we have actively marketed the idle equipment for ultimate sale since early 2004, we were unable to sell this equipment. While the equipment may be used internally to meet future capacity requirements we did not anticipate utilizing this equipment internally in the near future. As such, we reduced the carrying values of the excess raw material and idle equipment in 2005. No such reductions were needed in 2006.

*Loss from Extinguishments of Debt.* Loss from extinguishments of debt decreased to \$0 in the twelve months ended December 31, 2006 from \$1.2 million, or 8% of revenue, in the twelve months ended December 31, 2005. The \$1.2 million loss from extinguishments of debt was recognized from the exchange of our 6% Convertible Notes due 2006 in August 2005.

*Change in Value of Warrants.* Change in value of warrants was a gain of \$0.3 million, or 1% of revenue during the twelve months ended December 31, 2006, and \$4.0 million, or 24% of revenue, during the twelve months ended December 31, 2005, from the change in value of warrants issued primarily as a result of fluctuations in our stock price.

*Change in Value of Conversion Feature.* Change in the value of our conversion feature liability from our senior convertible debt funded in March 2004 and exchanged in August 2004 and August 2005 resulted in a change in value of conversion feature loss of \$0.2 million, or 1% of revenue, in the twelve months ended December 31, 2006, and a gain of \$9.1 million, or 56% of revenue, in the twelve months ended December 31, 2005, primarily due to fluctuations in our stock price.

*Other Income.* Other income was \$0.6 million, or 2% of revenue, in the twelve months ended December 31, 2006 from \$0.1 million of gain recognized from disposal of idle equipment and \$0.5 million gain recognized from termination of a distribution agreement with a Japanese sporting goods distributor originally entered into in March 1996. There were no amounts recognized as other income in the twelve months ended December 31, 2005.

*Interest Expense.* Interest expense was \$9.5 million or 34% of revenue, in the twelve months ended December 31, 2006 and was \$6.0 million, or 37% of revenue, in the twelve months ended December 31, 2005. Interest expense consists primarily of interest accrued on the Kookmin Bank loan funded in 2003, convertible debt funded in 2004 and 2005, subordinated notes funded in 2006, fees charged from short-term borrowings under the 2005 factoring, loan, and security agreement, as well as amortization of debt issuance costs and discount on the convertible debt. The increase in interest expense was primarily due to costs accrued for late registration penalties of \$1.6 million, higher debt balances and increased debt discount amortization during the twelve months ended December 31, 2006.

*Interest Income.* Interest income was \$23 thousand and \$17 thousand for the twelve months ended December 31, 2006 and 2005, respectively, from interest earned on cash deposits.

***Comparison of the years ended December 31, 2005 and 2004***

*Revenue.* Revenue decreased to \$16.4 million in the twelve months ended December 31, 2005 from \$17.4 million in the twelve months ended December 31, 2004. The decrease included a \$2.6 million decrease from restatement of revenues from 2003 to 2004 as part of our 2003 financial statement restatement which resulted in one-time recognition of revenues during the first quarter of 2004, and \$0.9 million decrease from our research and development services related primarily to reduced activity from defense, leisure, and luxury goods applications during 2005. The decreases were offset by a \$0.4 million increase in bulk alloy parts primarily to increased sales to sporting goods manufacturers and \$1.9 million increase from sale of our coatings products from increased demand for drill pipe coatings during 2005.

*Cost of Sales.* Cost of sales increased to \$15.1 million, or 92% of revenue, during the twelve months ended December 31, 2005 from \$12.2 million, or 70% of revenue, in the twelve months ended December 31, 2004. The increase was a result of decreases in bulk Liquidmetal alloy business. Cost of sales as a percentage of revenue has increased as a result of ramp up of lower margin electronic casing and prototypes during the year. Further, significant portion of our manufacturing costs continue to remain fixed. We believe that higher manufacturing volumes and greater mix of higher margin products in the future will cause the gross profit to improve over time. The cost to manufacture parts from our bulk Liquidmetal alloys is variable and differs based on the unique design of each product. However, the cost of sales for the products sold by the coatings business segment is generally consistent because the Liquidmetal coatings products are produced by third parties and sold wholesale to various industries.

*Selling, General, and Administrative Expenses.* Selling, general, and administrative expenses decreased to \$8.5 million, or 52% of revenue, in the twelve months ended December 31, 2005 from \$11.6 million, or 67% of revenue, in the twelve months ended December 31, 2004. This decrease was primarily a result of decrease in professional and contracted services of \$1.8 million, decrease in advertising and promotions expense of \$0.2 million, decrease in bad debt expenses of \$0.1 million, decrease in product warranty expense of \$0.2 million, decrease in insurance costs of \$0.6 million, and decrease in amortization and depreciation costs of \$0.2 million. These and other decreases in selling, general and administrative expenses represent our efforts to manage costs and focus on our core business while continuing to build our corporate infrastructure required to prepare for and support the anticipated growth of our bulk Liquidmetal alloy business.

*Research and Development Expenses.* Research and development expenses decreased to \$1.1 million, or 7% of revenue, in the twelve months ended December 31, 2005 from \$1.5 million, or 8% of revenue, in the twelve months ended December 31, 2004. The decrease was primarily a result of decreases in salaries, wages and related expenses by \$0.3 million and decrease in laboratory and prototyping expenses by \$0.1 million. The decreases were a result of our company focusing primarily on our core business associated with our bulk Liquidmetal alloy business while managing our costs. We continue to perform research and development efforts on new Liquidmetal alloys and related processing capabilities, develop new manufacturing techniques, and contract with consultants and provide research

grants to various institutions to advance the development of Liquidmetal alloys.

*Impairment of Long Lived Assets.* Impairment of long lived assets increased to \$4.5 million, or 27% of revenue, for the twelve months ended December 31, 2005 from \$0 for the twelve months ended December 31, 2004. Impairment expense represents primarily write-down of \$2.7 million of raw materials considered to be long term inventory and \$1.7 million of idle

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equipment. While we may use the excess raw materials beyond one year to fulfill future customer order, we have determined that our current capacity was not significant enough to warrant holding this inventory as a long term asset. Further, while we have actively marketed the idle equipment for ultimate sale since early 2004, we were unable to sell this equipment. In addition, while the equipment may be used internally to meet future capacity requirements, considering our current revenue, we do not anticipate utilizing this equipment internally in the near future. As such, we have reduced the carrying values of the excess raw material and idle equipment.

*Loss from Extinguishments of Debt.* Loss from extinguishments of debt decreased to \$1.2 million, or 8% of revenue, for the twelve months ended December 31, 2005 from \$2.9 million, or 17% of revenue, for the twelve months ended December 31, 2004. The \$1.2 million loss from extinguishments of debt was recognized from the exchange of our 6% Convertible Notes due 2006 in August 2005. The \$1.7 million loss from extinguishments of debt was recognized from exchange of our 6% Senior Convertible Notes due March 2007 in August 2004.

*Change in Value of Warrants.* Change in value of warrants was a net gain of \$4.0 million, or 24% of revenue, and \$0.7 million, or 4.3% of revenue, during the twelve months ended December 31, 2005 and 2004, respectively from the change in value of warrants issued from the senior convertible notes issued in March 2004 and exchanged in August 2004, convertible debt funded in June 2005, and senior convertible debt funded in August 2005 primarily as a result of fluctuations in our stock price.

*Change in Value of Conversion Feature.* Change in the value of our conversion feature liability from our senior convertible notes issued in March 2004 and exchanged in August 2004 and August 2005 resulted in a change in value of conversion feature gain of \$9.1 million, or 56% of revenue, and a gain of \$2.1 million, or 12% of revenue, for the twelve months ended December 31, 2005 and 2004, respectively, primarily due to fluctuations in our stock price.

*Other Income.* Other income was \$0.3 million, or 2% of revenue, during the twelve months ended December 31, 2004 from certain stock transactions with John Kang, our Chairman, President, and Chief Executive Officer during 2002 (see CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS ). There were no amounts recorded as other income for the twelve months ended December 31, 2005.

*Interest Expense.* Interest expense was \$6.0 million, or 37% of revenue, for the twelve months ended December 31, 2005 and was \$6.6 million, or 38% of revenue, for the twelve months ended December 31, 2004. During each of the twelve months ended December 31, 2005 and 2004, the interest expense was primarily due to the interest accrued on the Kookmin Bank loan funded on February 4, 2003, senior convertible debt funded on March 3, 2004 and exchanged in August 2004, convertible debt funded on June 13, 2005, and senior convertible debt funded in August 9, 2005, as well as amortization of debt issuance costs and discount on the convertible debt. During 2005, \$0.1 million of interest expense was accrued from default interest rates applied to the senior convertible notes effective April 1, 2005 from non-payment of quarterly scheduled interest payments and \$1.0 million of late registration penalty fee of our senior convertible debt was accrued as interest expense. The default interest and late registration penalty were paid as of December 31, 2005.

*Interest Income.* Interest income was \$17 thousand for the twelve months ended December 31, 2005, and \$37 thousand for the twelve months ended December 31, 2004 from interest earned on cash deposits.

### **Liquidity and Capital Resources**

Since our inception, we have funded our operations through the sale of equity securities in private placements and our initial public offering, the sale of convertible notes and warrants in private placements, debt financing, and cash generated from operations.

Our cash used for operating activities was \$5.4 million for the three months ended March 31, 2007 and \$1.2 million for the three months ended March 31, 2006. Our working capital deficit decreased from \$ \$23.2 million at December 31, 2006 to \$16.1 million at March 31, 2007. Our working capital deficit decrease of \$7.1 million was primarily attributable to increase in cash and cash equivalent of \$2.8 million, increase in restricted cash of \$2.1 million, increase in other assets of \$1 million decrease in accounts payable and accrued liability of \$2.1 million, decrease

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in short term debt of \$1.2 million, decrease in current portion of long-term debt of \$2.6 million, offset by decrease in trade accounts receivable of \$0.9 million, inventories of \$1.2 million, decrease in property, plant and equipment of \$1.0 million, and increase in conversion feature liabilities of \$1.6 million.

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Our cash used in investing activities was \$0.2 million for the three months ended March 31, 2007 primarily for investments in joint venture.

Our cash provided by financing activities was \$8.5 million for the three months ended March 31, 2007. We received net \$3.7 million in borrowings from factoring agreement executed in April 2005. The proceeds from borrowings have been used to meet working capital requirements. We have \$3.5 million available for future borrowings under the factoring agreement, which is contingent on approval of eligible receivables by the financing company. As of March 31, 2007, we had cash of \$2.9 million.

Our capital requirements during the next twelve months will depend on numerous factors, including the success of existing products either in manufacturing or development, the development of new applications for Liquidmetal alloys, and the resources we devote to develop and support our Liquidmetal alloy products, the success of pursuing strategic licensing and funded product development relationships with external partners.

We have experienced significant operating losses since our inception. Our net loss for the fiscal years ended December 31, 2006 and 2005 was \$14.5 million and \$7.1 million, respectively. For the three months ended March 31, 2007 and 2006, we had a net income of \$0.5 million and a net loss of \$6.0 million, respectively. In the audit report on our financial statements for our fiscal years ended December 31, 2006 and 2005, our auditors included a going-concern qualification indicating that our significant operating losses and working capital deficit cause substantial doubt about our ability to continue as a going concern. By issuing an opinion stating that there is substantial doubt about our ability to continue as a going concern, our auditors have indicated that they are uncertain as to whether we have the capability to continue our operations without additional funding. On January 3, 2007, we completed a private placement of \$16.3 million in principal amount of 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes). The January 2010 Notes were issued for aggregate cash in the amount of \$12.9 million and in payment of a total of \$3.4 million in principal and accrued but unpaid interest under our previously issued 7% Senior Secured Convertible Notes Due August 2007 and our 8% Unsecured Subordinated Notes.

We anticipate that the \$12.9 million aggregate cash raised in the January 2007 private placement will be sufficient to pursue our current operating plan only through the third quarter of 2007, and we will therefore require additional funding at or prior to that time. As a result, we are actively seeking additional sources of capital. The amount of funding that we seek and the timing of such fundraising efforts will depend on the extent to which we are able to increase revenues through obtaining additional purchase orders for our products and/or the extent to which we can restructure or modify our debt. Because we cannot be certain that we will be able to obtain adequate funding from debt, equity, or other traditional financing sources, we are also actively exploring several strategic financing options, including the possible sale of our manufacturing plant in South Korea (which would then be replaced with a smaller facility), potential licensing and outsourcing of manufacturing operations including those in South Korea and China, and the possible sale of our Liquidmetal Coatings business. In June 2007, we entered into an equipment sale and licensing agreement with Grace Metal, a South Korean corporation, providing for \$2.0 million in exchange for die casting machines and vacuum induction melters, and a 10-year exclusive license to manufacture Liquidmetal alloys for customers whose principal headquarters or major operations are based in South Korea. The principal purpose of the transactions with Grace Metal was to raise capital for the next-generation casting equipment and to shift the cost and burden of our manufacturing operations to a third party. Grace Metal was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company. We cannot guarantee that adequate funds will be available when needed, and if we do not receive sufficient capital, we may be required to alter or reduce the scope of our operations.

As of March 31, 2007, we had accrued \$1.6 million and paid \$0.9 million of the late filing and registration fees as a result of the late fee provisions of a restated registration rights agreement, dated August 2, 2005. We are currently in negotiations with the holders to settle the outstanding late filing and registration fees. However, we cannot predict the outcome of the negotiations, and the resolution of this issue may harm our business and have a material adverse impact on our financial condition.

#### ***Initial Public Offering Proceeds***

Pursuant to our Registration Statement on Form S-1 (Registration No. 333-73716), as amended, initially filed with the Securities and Exchange Commission on November 20, 2001 and declared effective May 21, 2002, we closed an initial public offering of 5,000,000 shares of common stock on May 28, 2002, plus an additional 229,000 shares on June 10, 2002 pursuant to an over allotment option, at a price of \$15.00 per share (which sale is referred to herein as the Offering). The Offering generated aggregate cash proceeds during the second quarter 2002 of \$78.4 million. The net proceeds were \$70.7 million after deducting underwriting commissions of \$5.5 million and other transaction fees of \$2.2 million. The managing underwriters for the Offering were Merrill Lynch & Co., UBS Warburg, and Robert W. Baird & Co.

As of December 31, 2003, we used all \$70.7 million of net proceeds from the Offering. In 2002, we used approximately \$7.8 million of the net proceeds from the Offering to repay all outstanding promissory notes and accrued interest, \$11.1 million to fund the construction of our manufacturing facility in South Korea, \$14.3 million to purchase equipment used to manufacture Liquidmetal parts, \$0.4 million to purchase assets related to production and sale of equipment used in the production process of Liquidmetal alloy products, and \$0.3 million to purchase the 51% interest in our majority owned Dongyang subsidiary. During the third quarter of 2002, we used \$2.0 million to invest in the common stock of Growell Metal, which supplied a portion of the Liquidmetal alloy ingots used in our manufacturing operations in Korea. We have since sold such stock, realizing a gain on the sale. We used the remaining proceeds of \$32.7 million for working capital in 2002 and 2003, excluding \$2.1 million paid to Paul Azinger in 2002 and 2003 for amounts due under the terms of his terminated endorsement agreement with our discontinued retail golf operations.

***Private Placements of Convertible Notes and Bridge Notes***

On March 3, 2004, we sold \$9.9 million of 6.0% Senior Convertible Notes due 2007 (the Initial Notes ) and warrants to purchase approximately 1.2 million shares of our common stock to accredited investors in a private placement. The notes were convertible at any time into our common stock at a price of \$3.00 per share, and the warrants granted in this transaction expired on various dates through March 1, 2006.

On August 19, 2004, we completed a private placement in which the investors in the March 2004 private placement exchanged approximately \$5.46 million in aggregate principal amount of the Initial Notes for an aggregate of (i) \$2.73 million of new 6% Senior Secured Notes Due 2007 (the July 2007 Notes ) and (ii) \$2.73 million of new 10% Senior Secured Notes Due 2005 (the July 2005 Notes ). The remaining Initial Notes were redeemed for cash in connection with the transaction. The July 2007 Notes and July 2005 Notes were secured by certain patents owned by our company and a second priority mortgage interest in plant facilities and certain equipment at our plant in South Korea. The July 2005 Notes had a maturity date of July 29, 2005, and a conversion price of \$2.00 per share. The July 2007 Notes had a maturity date of July 29, 2007, and a conversion price of \$1.00 per share.

On June 13, 2005, we completed a private placement of 10% Convertible Unsecured Notes Due June 13, 2006 in the aggregate principal amount of \$3.25 million (the June 2006 Bridge Notes ), together with warrants to purchase up to an aggregate of 893,750 shares of our company's common stock. The June 2006 Bridge Notes were unsecured and were due on the earlier of June 13, 2006 or the consummation of a follow-on equity or debt offering or restructuring transaction pursuant to which our company receives gross proceeds of at least \$4.0 million.

On August 9, 2005, we completed a private placement of \$9.9 million in principal amount of new 7% Senior Secured Convertible Notes due August 2007 (the August 2007 Notes ). The August 2007 Notes were issued in consideration of \$5.0 million in cash, the exchange of \$1.3 million in principal amount of the July 2005 Notes, the exchange of \$3.0 million in principal amount of the June 2006 Bridge Notes (resulting in the full satisfaction of the June 2006 Bridge Notes), satisfaction of accrued interest and late registration fees in the amount of \$0.6 million on the July 2005 Notes, and satisfaction of accrued interest of \$9 thousand on the June 2006 Bridge Notes. Interest of 7% per annum on the August 2007 Notes was due quarterly. The August 2007 Notes were convertible into shares of our common stock at \$2.00 per share and were secured by substantially all of our assets. We also issued warrants to the purchasers of the August 2007 Notes and placement agents giving them the right to purchase up to 2,469,470 and 414,495 shares of our common stock, respectively, with an exercise price of \$2.00 per share. The warrants will expire on August 2, 2010.

On March 17, 2006, in exchange for a \$1.0 million loan, we issued a \$1.0 million 10% subordinated promissory note due October 16, 2006 (the Atlantic Note ) to Atlantic Realty Group, Inc., a company controlled by Jack Chitayat, a former director of our company. The Atlantic Note was unsecured and subordinated to all prior indebtedness of our company. All accrued interest and unpaid principal was due on October 16, 2006. In connection with the March 2006 Note, we issued warrants to Atlantic Realty to purchase an aggregate amount of up to 125,000 shares of common stock exercisable at \$2.00 per share. The warrants will expire on March 17, 2009.

On May 17, 2006, September 21, 2006, and December 1, 2006, we completed a private placement of 8% Unsecured Subordinated Notes in the aggregate principal amount of \$4.6 million (the New Bridge Notes), together with warrants to purchase up to an aggregate of 973,064 shares of our common stock. The New Bridge Notes were unsecured and were scheduled to become due on the earlier of August 17, 2007 or the consummation of a follow-on equity or debt offering pursuant to which we receive gross proceeds of at least \$6.0 million, but in no event will the New Bridge Notes become due any earlier than the payment in full of the August 2007 Notes and July 2007 Notes. Interest on the New Bridge Notes accrues at the rate of 8% per annum. The New Bridge Notes are subordinate in right of payment and in all other respects to the previously issued July 2007 Notes and August 2007 Notes. As a part of the private placement of the New Bridge Notes, we issued warrants to the purchasers of the New Bridge Notes giving them the right to purchase up to an aggregate of 890,990 shares of our common stock, and warrants to purchase 82,074 shares of our common stock were issued to the placement agent in the transaction. The warrants have an exercise price of \$2.58 per share and will expire on May 17, 2011.

As of December 31, 2006, \$9.9 million in aggregate principal amount of August 2007 Notes were still outstanding with accrued but unpaid interest in the amount of approximately \$173 thousand, and \$2.1 million in aggregate principal amount of July 2007 Notes were also outstanding with accrued but unpaid interest in the amount of approximately \$32 thousand. As of December 31, 2006, \$4.6 million in aggregate principal amount of New Bridge Notes were still outstanding with accrued but unpaid interest in the amount of approximately \$195 thousand.

On January 3, 2007, we completed a private placement of new 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes). As a result of an April 2007 amendment to this transaction, we ultimately issued \$16.3 million in principal amount of January 2010 Notes, which supersedes the aggregate note amount indicated in our prior announcements regarding the private placement. Under the amended transaction, the January 2010 Notes were issued for aggregate cash in the amount of \$12.9 million and in payment of a total of \$3.4 million in principal and accrued but unpaid interest under the August 2007 Notes and New Bridge Notes. The January 2010 Notes have a maturity date of January 3, 2010.

The January 2010 Notes were issued pursuant to a Securities Purchase Agreement, dated January 3, 2007, between our company and the purchasers of the January 2010 Notes (the January Purchase Agreement). Under the terms of the original January Purchase Agreement, we agreed to repay or otherwise satisfy, within 5 days after the closing of the private placement, approximately \$15.5 million of our outstanding debt under previously issued promissory notes, including the August 2007 Notes, the Atlantic Note, and New Bridge Notes (the Debt Satisfaction Covenant). We originally agreed to this covenant based on assurances that a substantial number of holders of the August 2007 Notes would elect to convert their August 2007 Notes at a reduced conversion price following the private placement under a note conversion agreement proposed by us, but most of such holders ultimately elected not to proceed with such conversion. Accordingly, in an effort to preserve funds, we have not yet repaid the indebtedness as required by the original January Purchase Agreement, and in April 2007, we entered into an amendment to the January Purchase Agreement providing that we will have until October 1, 2007 (or such earlier date on which the indebtedness to be repaid is due) to comply with the Debt Satisfaction Covenant. In addition, the April 2007 amendment provides that the purchasers of the January 2010 Notes have the right to require us to redeem such notes prior to maturity in the event that we sell our Liquidmetal Coatings business unit, sell our manufacturing facility in South Korea, and/or engage in any debt or equity financing, provided that the foregoing transactions result in aggregate cumulative proceeds of \$25,000,000, and it also provides that we will be obligated to grant to the purchasers of such notes a *par passu* security interest in any collateral (if any) that is used to secure our next private placement of convertible notes. As required by the January Purchase Agreement, the April 2007 amendment was executed by the holders of more than fifty percent (50%) of the outstanding principal amount of the Notes.

The January 2010 Notes, as amended by the April 2007 amendment, are convertible at any time at the option of the holder into shares of our common stock at a conversion price of \$1.10 per share (compared to an original conversion price of \$1.55 per share), subject to adjustment for anti-dilution. The January 2010 Notes bear interest at 8% per annum with interest payable quarterly in arrears in cash, or, at our option, in the form of additional January 2010 Notes (in which case the interest rate will be 10% per annum). Our ability to pay interest with additional January 2010 Notes is subject to specified conditions, including the existence of an effective registration statement covering the resale of the shares issued in payment of interest and certain minimum trading volumes in the stock to be issued. From and after an event of default under the January 2010 Notes and for so long as the event of default is continuing, the January 2010 Notes will bear default interest at a rate of 12% per annum (or 15% per annum if we elect to pay interest with additional January 2010 Notes).

Beginning July 31, 2008 and at the end of each month thereafter, we will be required to redeem 1/36th of the principal amount of the January 2010 Notes in cash or, at our election, with shares of our common stock. Our ability to pay the redemption amounts with shares of our common stock will be subject to specified conditions, including the existence of an effective registration statement covering the resale of the shares issued in payment of the redemption amount and certain minimum trading volumes in the stock to be issued. Any unconverted January 2010 Notes will become due on December 31, 2009, although we will have the right at any time after 18 months following the issuance of the January 2010 Notes to redeem the January 2010 Notes in whole or in part for a cash redemption price of 105% of the portion of the principal amount being redeemed plus all accrued and unpaid interest thereon. The January 2010 Notes are unsecured and are subordinate to our July 2007 Notes and to certain secured financing from commercial lenders incurred by us in the future. The terms of the 2010 Notes also provide that we will be required to maintain a sufficient bank balance to provide for the timely repayment of our July 2007 Notes.

As a part of the January 2007 private placement, we issued warrants to the purchasers of the January 2010 Notes giving them the right following the April 2007 amendment to purchase up to an aggregate of 7,408,881 shares of our common stock at an exercise price of \$1.55 per share. In connection with the private placement, we also issued to the placement agent for the transaction warrants to purchase an aggregate of 248,710 shares of our common stock at an exercise price of \$1.55 per share. All of the warrants (including the warrants granted to the placement agent in the transaction) are immediately exercisable and will expire in January 2012.

In connection with the January 2007 private placement, we entered into a Registration Rights Agreement with the purchasers of the January 2010 Notes under which we are required, on or before 45 days after the closing of the private placement, to use our commercially reasonable efforts to file a registration statement with the SEC covering the resale of the shares of our common stock issuable pursuant to the January 2010 Notes and warrants and to use our commercially reasonable efforts to have the registration declared effective at the earliest date (but in no event later than 90 days after filing if there is no SEC review of the registration statement, or 120 days if there is an SEC review). We will be subject to certain monetary penalties, as set forth in the Registration Rights Agreement, up to a maximum amount of 18% of the aggregate amount of Notes sold in the Private Placement if the registration statement is not filed or does not become effective on a timely basis. The monetary penalties will accrue at the rate of 1% per month of the then-outstanding principal amount of the January 2010 Notes. In the event that we are unable to include in the registration statement all shares of our common stock issuable pursuant to the January 2010 Notes and warrants, then we will be required to file up to two additional registration statements to register the resale of any shares excluded from the originally filed registration statement and to pay the foregoing monetary penalties on the January 2010 Notes convertible into the excluded shares until the resale of such excluded shares is covered by an effective registration statement or until such shares can be sold under SEC Rule 144. As of April 23, 2007, an aggregate of \$148 thousand in monetary penalties under the Registration Rights Agreement had already been paid to investors, while an additional \$178 thousand in such penalties were accrued but unpaid.

On March 22, 2007, one of the purchasers of the January 2010 Notes (holding January 2010 Notes in the aggregate amount of \$2.0 million) sent us an event of default notice ( "Event of Default Notice" ) indicating that we had defaulted under the January Purchase Agreement (and therefore under the January 2010 Note) by failing to comply with the Debt Satisfaction Covenant. This holder did not execute the April 2007 amendment to the January Purchase Agreement, although the amendment was approved by a majority of the noteholders. In general, upon a breach of the January 2010 Notes or January Purchase Agreement, a holder of the January 2010 Notes may require us to redeem the January 2010 Notes at a price equal to the greater of (i) the conversion amount to be redeemed and (ii) the product of (A) the conversion rate with respect to such conversion amount in effect at such time as the purchaser of the January 2010 Note delivers an Event of Default Redemption Notice (as defined below) and (B) the closing sale price of our common stock on the date immediately preceding such event of default. Under the terms of the January 2010 Notes and January Purchase Agreement, we have ten (10) business days after the receipt of an Event of Default Notice to cure a default. On April 6, 2007, the holder which sent the Event of Default Notice further sent us an event of default redemption notice ( "Event of Default Redemption Notice" ). The Event of Default Redemption Notice states that the holder has elected to require us to redeem its January 2010 Note for a price equal to \$2.0 million (the amount of the January 2010 Note) plus accrued and unpaid interest. On April 16, 2007, we were served with a complaint filed by the holder in the Federal District Court in Minnesota to collect this amount. We have answered and denied that any amount is currently owed to the holder, because of the April 2007 amendment to the January Purchase Agreement. The holder has also moved for summary judgment and a hearing on that motion is scheduled for August 30, 2007. We are currently working to resolve this matter.

In addition, because we repaid \$1.8 million of principal and interest under the Atlantic Note and certain New Bridge Notes in January and February 2007 without first repaying the August 2007 Notes and July 2007 Notes, we may also be in breach of the August 2007 Notes and July 2007 Notes. In February 2007, we entered into conversion agreements with the holders of the August 2007 Notes holding \$0.4 million of principal providing for the conversion of such notes at a reduced conversion price of \$1.25 per share and issued 320,000 shares of our common stock.

**Loan from Kookmin Bank**

Our Liquidmetal Technologies Korea Co., Ltd. subsidiary has an outstanding loan from Kookmin Bank in the Republic of Korea. As of March 31, 2007, the outstanding balance under this loan was \$1.2 million. The loan is payable in monthly installments of \$0.11 million per month through February 2008.

**Off Balance Sheet Arrangements**

An off-balance sheet arrangement is any transaction, agreement or other contractual arrangement involving an unconsolidated entity under which a company has (1) made guarantees, (2) a retained or a contingent interest in transferred assets, (3) an obligation under derivative instruments classified as equity, or (4) any obligation arising out of a material variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to our company, or that engages in leasing, hedging, or research and development arrangements with our company.

On June 26, 2006, we entered into a joint venture agreement with SAGA, SpA in Padova, Italy, ( SAGA ) a specialist precision parts manufacturer. The joint venture is named Liquidmetal SAGA Italy, Srl ( LSI ). We also entered into an exclusive manufacturing license agreement for the eyewear industry with LSI. Under the joint venture agreement, we have the option to buy ownership interest in LSI, initially, of 19.9% to up to 50%. In December 2006, we have purchased 19.9% interest in the joint venture. Under the licensing agreement, at any time following 18 months after the effective date of the agreement, LSI may exercise its option to sell us certain business assets including manufacturing equipment acquired under the joint venture. During the year ended December 31, 2006, we recognized revenues of \$0.7 million of Liquidmetal alloys sold to SAGA for use in the joint venture. We anticipate the alloys to be fully utilized by the joint venture prior to the 18 month period.

**Contractual Obligations**

The following table summarizes our company's obligations and commitments as of March 31, 2007:

Contractual Cash Obligations (1)	Payments Due by Period (in thousands)				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	After 5 Years
Long-term debt (2)	\$ 29,796	\$ 13,496	\$ 16,300	\$	\$
Short-term debt (3)	1,493	1,493			
Operating leases and rents	1,701	94	1,095	512	
Consulting services payable	47	47			
Dongyang	12	12			
Nichimen	335	335			
	\$ 33,384	\$ 15,477	\$ 17,395	\$ 512	\$

(1) Contractual cash obligations include Long-Term Debt comprised of: \$2,083 of Senior Convertible Notes issued in 2004 and \$7,186 of Senior Convertible Notes issued in 2005, \$3,009 of Unsecured Subordinated Notes issued in 2006, \$16,300 of Convertible Unsecured Notes issued in 2007, and \$1,218 of Kookmin Bank Loan, Short-Term Debt comprised of \$1,493 outstanding advances received under factoring, loan, and security agreement, future minimum lease payments under capital and operating leases, and purchase commitments from consultants, payments due from our discontinued equipment manufacturing business (Dongyang), and minimum payments due under a distribution agreement (Nichimen).

(2) Does not include interest payments of \$4,055; and un-amortized discounts for conversion feature and warrants of \$11,540 of our notes.

(3) Does not include minimum interest and fee payments of \$30.

### Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results could differ materially from these estimates under different assumptions or conditions.

We believe that the following accounting policies are the most critical to our consolidated financial statements since these policies require significant judgment or involve complex estimates that are important to the portrayal of our financial condition and operating results:

- Our earnings and cash flows are subject to fluctuations due to changes in non-U.S. currency exchange rates. We are exposed to non-U.S. exchange rate fluctuations as the financial results of non-U.S. subsidiaries, Korea and China, are translated into U.S. dollars. As exchange rates vary, those results, when translated, may vary from expectations and adversely impact overall expected profitability. The cumulative translation effects for subsidiaries using functional currencies other than the U.S. dollar are included in accumulated foreign exchange translation in stockholders' equity. Movements in non-U.S. currency exchange rates may affect our competitive position, as exchange rate changes may affect business practices and/or pricing strategies of non-U.S. based competitors.
- We record an accrual for potential product warranty costs. Due to the lack of historical information for warranty expense related to bulk alloy products, management estimates product warranties as a percentage of bulk alloy product sales earned during the period. In the event in future periods the actual product warranty costs consistently exceed the estimate for product warranty costs, an adjustment would be made and income would decrease in the period of such determination. Likewise, in the event we determine that actual product warranty costs are consistently lower than the estimate for product warranty costs, an adjustment would be made and income would increase in the period of such determination.
- We record an allowance for doubtful accounts as a contra-asset to our trade receivables for estimated uncollectible accounts. Management estimates the amount of potentially uncollectible accounts by reviewing significantly past due customer balances relative to historical information available for those customers. In the event, in future periods, actual uncollectible accounts exceed the estimate for uncollectible accounts, an adjustment would be made and income would decrease in the period of such determination. Likewise, in the event, in future periods, actual uncollectible accounts are lower than the estimate for uncollectible accounts, an adjustment would be made and income would increase in the period of such determination.
- We value inventories at lower of cost or net realizable value. Management has determined net realizable value to be equal to the selling price of the products to be produced and sold less the cost of disposal. In the event, in future periods, the actual selling prices exceed the estimate for selling prices less cost to sell, an adjustment would be made and income would increase in the period of such determination. Likewise, in the event, in future periods, actual selling prices are lower than the estimate for selling prices, an adjustment would be made and income would decrease in the period of such determination.
- We value our assets at lower of cost or fair market value. Management has determined fair market to be equal to the selling price of the assets to be sold less the cost of disposal. In the event, in future periods, actual selling prices are lower than the estimate for selling prices, an adjustment would be made and income would decrease in the period of such determination.



- We record valuation allowances to reduce the deferred tax assets to the amounts estimated to be realized. While we consider taxable income in assessing the need for a valuation allowance, in the event we determine we would be able to realize our deferred tax assets in the future in excess of the net recorded amount, an adjustment would be made and income increased in the period of such determination. Likewise, in the event we determine we would not be able to realize all or part of our deferred tax assets in the future, an adjustment would be made and charged to income in the period of such determination.
- We account for the warrants and the embedded conversion feature of our senior convertible notes as derivatives in accordance with Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, and Emerging Issues Task Force Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock. Fair values of warrants and embedded conversion features are measured at each period end using Black-Scholes pricing models and changes in fair value during the period are reported in our earnings.
- We adopted Statement of Financial Accounting Standards No. 123, Share-Based Payment ( SFAS 123R ), on January 1, 2006. This new standard requires companies to expense the fair value of employee stock options and similar awards. We adopted SFAS 123R using the modified prospective transition method. Therefore, stock based compensation expense measured in accordance with SFAS 123R was recorded starting with the first quarter of 2006, but the prior year consolidated statement of income was not restated. The adoption of SFAS 123R resulted in incremental expense of \$1.1 million for the year ended December 31, 2006, and \$0.2 million for each of the three months ended March 31, 2007 and 2006.

#### **Recent Accounting Pronouncements**

In February 2006, the FASB issued SFAS No. 155, ( SFAS No. 155 ), Accounting for Certain Hybrid Instruments, which amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. SFAS No. 155 also clarifies and amends certain other provisions of SFAS No. 133 and SFAS No. 140. This statement is effective for all financial instruments acquired or issued in fiscal years beginning after September 15, 2006. We do not expect the adoption of this new standard to have a material impact on its financial position, results of operations or cash flows.

In July 2006, the FASB issued FASB interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB statement No. 109, which prescribes a recognition threshold and measurement process for recording in the financial statements, uncertain tax positions taken or expected to be taken in a tax return. In addition, FIN 48 provides guidance on the derecognizing, classification, accounting in interim periods and disclosure requirements for uncertain tax positions. We are currently evaluating the impact, if any, that FIN 48 will have on its financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurement, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The effective date of SFAS No. 157 will be the first quarter of 2008. While we are currently evaluating the provisions of SFAS 157, the adoption is not expected to have a material impact on its consolidated financial statements.

In September 2006, the SEC issued SAB No. 108, Guidance re: the Use of a Cumulative Effect Adjustment to Correct Immaterial Misstatements ( SAB 108 ). Registrants are required to apply the provisions of SAB 108 no later than the annual financial statements for their first fiscal year ending after November 15, 2006. The application of SAB 108 is not expected to have a material impact on our financial statements.

In February 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The effective date of SFAS 159 will be the first quarter of 2008. We are currently evaluating the provisions of SFAS 159 and do not expect the adoption of this new standard to have a material impact on our consolidated financial statements.





Other recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the AICPA and the SEC did not or are not believed by management to have a material impact on our company's present or future consolidated financial statements.

#### **Quantitative and Qualitative Disclosures About Market Risks**

We are exposed to various market risks in conducting the business of our company, and we anticipate that this exposure will increase if our business and revenues grow. In an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. These may take the form of forward sales contracts, option contracts, foreign currency exchange contracts, and interest rate swaps. We have not, and do not intend to, engage in the practice of trading derivative securities for profit.

*Interest Rates.* We are exposed to market risks relating to changes in interest rates. Fluctuations in interest rates may have a negative impact to existing short-term borrowings and future borrowings.

*Commodity Prices.* We are exposed to price risk related to anticipated purchases of certain commodities used as raw materials by our businesses, including titanium and zirconium. Although we do not currently enter into commodity future, forward, and option contracts to manage the fluctuations in prices of anticipated purchases, we may enter into such contracts in the future as our business grows and as our purchases of these raw materials increases.

*Foreign Exchange Rates.* As a result of our manufacturing presence in South Korea, a substantial portion of our costs will be denominated in South Korean won. Consequently, fluctuations in the exchange rates of the South Korean won to the U.S. dollar will affect our costs of goods sold and operating margins and could result in exchange losses. Although we do not currently enter into foreign exchange hedge transactions, we may do so in the future as our business grows. Fluctuations in exchange rates resulted in foreign currency translation gains of \$0.3 million, \$0.3 million, and \$1.7 million for the years ended December 31, 2006, 2005, and 2004, respectively, and a loss of \$0.2 million and a gain of \$0.1 million for the three months ended March 31, 2007 and 2006, respectively..

## **BUSINESS**

### **Overview**

We are a materials technology company that develops and commercializes products made from amorphous alloys. Our Liquidmetal® family of alloys consists of a variety of proprietary coatings, powders, bulk alloys, and composites that utilize the advantages offered by amorphous alloy technology. We develop, manufacture, and sell products and components from bulk amorphous alloys to customers in various industries, and we also partner with third-party licensees and distributors to develop and commercialize bulk Liquidmetal alloy products. We believe that our proprietary bulk alloys are the only commercially viable bulk amorphous alloys currently available in the marketplace. In addition to our bulk alloys, we market and sell a line of proprietary amorphous alloy-based industrial coatings under the Liquidmetal® Armacor™ Coatings brand.

Amorphous alloys are unique materials that are distinguished by their ability to retain a random atomic structure when they solidify, in contrast to the crystalline atomic structure that forms in other metals and alloys when they solidify. Liquidmetal alloys possess a combination of performance, processing, and potential cost advantages that we believe will make them preferable to other materials in a variety of applications. The amorphous atomic structure of our alloys enables them to overcome certain performance limitations caused by inherent weaknesses in crystalline atomic structures, thus facilitating performance and processing characteristics superior in many ways to those of their crystalline counterparts. For example, our zirconium-titanium Liquidmetal alloys are approximately 250% stronger than commonly used titanium alloys such as Ti-6Al-4V, but they also have some of the beneficial processing characteristics more commonly associated with plastics. We believe these advantages could result in Liquidmetal alloys supplanting high-performance alloys, such as titanium and stainless steel, and other incumbent materials in a wide variety of applications. Moreover, we believe these advantages could enable the introduction of entirely new products and applications that are not possible or commercially viable with other materials.

### **General Corporate Information**

We were originally incorporated in California in 1987, and we reincorporated in Delaware in May 2003. Our principal executive offices are located at 30452 Esperanza, Rancho Santa Margarita, California 92688. Our telephone number at that address is (949) 635-2100. Previously, our principal executive offices were located in Lake Forest, California. In May 2007, we relocated all corporate and research and development functions into our new facility in Rancho Santa Margarita. Our Internet website address is [www.liquidmetal.com](http://www.liquidmetal.com) and all of our filings with the Securities and Exchange Commission are available free of charge on our website.

### **Subsidiaries and Other Locations**

We currently own and operate a manufacturing facility in Pyongtaek, South Korea, which became operational in the third quarter of 2002. This Korean subsidiary handles our Bulk Liquidmetal alloy business which includes market opportunities to manufacture and sell casing components for electronic devices, medical devices, sporting goods, tooling, prototype sampling, defense applications and metal processing equipment. We operate a distribution warehouse division in Conroe, Texas to handle our Liquidmetal alloy industrial coatings which are used primarily as protective coatings for industrial machinery and equipment, such as drill pipe used by the oil drilling industry and boiler tubes used by coal burning power plants. Lastly, we acquired a coatings application business based in Dothan, Alabama in the second quarter of 2007 which will be used to support our industrial coatings business.

### **Our Technology**

The performance, processing, and potential cost advantages of Liquidmetal alloys are a function of their unique atomic structure and their proprietary material composition.

#### ***Unique Atomic Structure***

The atomic structure of Liquidmetal alloys is the fundamental feature that differentiates them from other alloys and metals. In the molten state, the atomic particles of all alloys and metals have an amorphous atomic structure, which means that

the atomic particles appear in a completely random structure with no discernible patterns. However, when non-amorphous alloys and metals are cooled to a solid state, their atoms bond together in a repeating pattern of regular and predictable shapes, or crystalline grains. This process is analogous to the way ice forms when water freezes and crystallizes. In non-amorphous metals and alloys, the individual crystalline grains contain naturally occurring structural defects that limit the potential strength and performance characteristics of the material. These defects, known as dislocations, consist of discontinuities or inconsistencies in the patterned atomic structure of each grain. Unlike other alloys and metals, bulk Liquidmetal alloys can retain their amorphous atomic structure throughout the solidification process and therefore do not develop crystalline grains and the associated dislocations. Consequently, bulk Liquidmetal alloys exhibit superior strength and other superior performance characteristics compared to their crystalline counterparts. Our Liquidmetal alloy coatings, in contrast to our bulk alloys, have a crystalline atomic structure when initially applied, but their atomic structure becomes amorphous as the coatings rub against surfaces under force, thus improving their performance over time.

Prior to 1993, commercially viable amorphous alloys could be created only in thin forms, such as coatings, films, or ribbons. However, in 1993, researchers at the California Institute of Technology (Caltech) developed the first commercially viable amorphous alloy in a bulk form. Today, bulk Liquidmetal alloys can be formed into objects that are up to one inch thick, and we are not aware of any other commercially available amorphous alloys that can achieve this thickness. We have the exclusive right to commercialize bulk amorphous alloy technology through a license agreement with Caltech and other patents that we own.

#### ***Proprietary Material Composition***

The constituent elements and percentage composition of Liquidmetal alloys are critical to their ability to solidify into an amorphous atomic structure. We have several different alloy compositions that have different constituent elements in varying percentages. These compositions are protected by various patents that we own or exclusively license from third parties, including Caltech. The raw materials that we use in Liquidmetal alloys are readily available and can be purchased from multiple suppliers.

#### **Advantages of Liquidmetal Alloys**

Liquidmetal alloys possess a unique combination of performance, processing and cost advantages that we believe makes them superior in many ways to other commercially available materials for a variety of existing and potential future product applications.

#### ***Performance Advantages***

Our bulk Liquidmetal alloys provide several distinct performance advantages over other materials, and we believe that these advantages make the alloys desirable in applications that require high yield strength, strength-to-weight ratio, elasticity and hardness.

The high yield strength of bulk Liquidmetal alloys means that a high amount of stress must be exerted to create permanent deformation. However, because the yield strength is so high, the yield strength of many of our bulk Liquidmetal alloy compositions is very near their ultimate strength, which is the measure of stress at which total breakage occurs. Therefore, very little additional stress may be required to break an object made of bulk Liquidmetal alloys once the yield strength is exceeded. Although we believe that the yield strength of many of our bulk alloys exceeds the ultimate strength of most other commonly used alloys and metals, our bulk alloys may not be suitable for certain applications, such as pressurized tanks, in which the ability of the material to yield significantly before it breaks is more important than its strength advantage. Additionally, although our bulk alloys show a high resistance to crack initiation because of their very high strength and hardness, certain of our bulk alloys are sensitive to crack propagation under certain long-term, cyclical loading conditions. Crack propagation is the tendency of a crack to grow after it forms. We are currently developing new alloy compositions that have improved material properties to overcome these limitations.

#### ***Processing Advantages***

The processing of a material generally refers to how a material is shaped, formed, or combined with other materials to create a finished product. Bulk Liquidmetal alloys possess processing characteristics that we believe make them preferable to other materials in a wide variety of applications. In particular, our alloys are amenable to processing options that are

similar in many respects to those associated with plastics. For example, we believe that bulk Liquidmetal alloys have superior net-shape casting capabilities as compared to high-strength crystalline metals and alloys. Net-shape casting is a type of casting that permits the creation of near-to-net shaped products that reduce costly post-cast processing or machining. Additionally, unlike most metals and alloys, our bulk Liquidmetal alloys are capable of being thermoplastically molded in bulk form. Thermoplastic molding consists of heating a solid piece of material until it is transformed into a moldable state, although at temperatures much lower than the melting temperature, and then introducing it into a mold to form near-to-net shaped products. Accordingly, thermoplastic molding can be beneficial and economical for net shape fabrication of high-strength products.

Bulk Liquidmetal alloys also permit the creation of composite materials that cannot be created with most non-amorphous metals and alloys. A composite is a material that is made from two or more different types of materials. In general, the ability to create composites is beneficial because constituent materials can be combined with one another to optimize the composite's performance characteristics for different applications. In other metals and alloys, the high temperatures required for processing could damage some of the composite's constituent materials and therefore limit their utility. However, the relatively low melting temperatures of bulk Liquidmetal alloys allow mild processing conditions that eliminate or limit damage to the constituent materials when creating composites. In addition to composites, we believe that the processing advantages of Liquidmetal alloys will ultimately allow for a variety of other finished forms, including a coating or a spray. Most high-strength metals and alloys cannot be processed into these forms.

Notwithstanding the foregoing advantages, our bulk Liquidmetal alloys possess certain limitations relative to processing. The beneficial processing features of our bulk alloys are made possible in part by the alloys' relatively low melting temperatures. Although a lower melting temperature is a beneficial characteristic for processing purposes, it renders certain bulk alloy compositions unsuitable for certain high-temperature applications, such as jet engine exhaust components. Additionally, the current one-inch thickness limitation of our zirconium-titanium bulk alloy renders our alloys currently unsuitable for use as structural materials in large-scale applications, such as load-bearing beams in building construction. We are currently engaged in research and development with the goal of developing processing technology and new alloy compositions that will enable our bulk alloys to be formed into thicker objects.

#### ***Cost Advantages***

Liquidmetal alloys have the potential to provide cost advantages over other high-strength metals and alloys in certain applications. Because bulk Liquidmetal alloy has processing characteristics similar in some respects to plastics, which lends itself to near-to-net shape casting and molding, Liquidmetal alloys can in many cases be shaped efficiently into intricate, engineered products. This capability can eliminate or reduce certain post-casting steps, such as machining and re-forming, and therefore has the potential to significantly reduce processing costs associated with making parts in high volume.

Additionally, because the near-to-net shape processing of Liquidmetal alloys reduces the need for capital-intensive heavy industrial equipment such as that found in foundry and forging operations, Liquidmetal alloys can be processed with a smaller machinery footprint, which allows for more efficient development of facilities and reduced permitting and regulatory costs. We believe that these advantages may allow our customers an opportunity to maintain or improve the performance of their products without a commensurate increase in cost.

#### ***Our Strategy***

As a result of the experience and knowledge that we have gained through our activities to date, and recognizing that developing and commercializing a revolutionary new technology is an evolutionary process, we are continually modifying our business strategy to enable us to better capitalize on our evolving core strengths and more effectively pursue revenue growth and profitability. The key elements of our strategy include:

- *Identifying and Developing New Applications for Our Liquidmetal Alloy Technology.* We intend to continue to identify and develop new applications that will benefit from the performance, processing, and cost advantages of Liquidmetal alloys.
- *Focusing Our Marketing and Internal Manufacturing Activities on Select Products with Expected Higher Gross-Margins.* We intend to focus our marketing and internal manufacturing activities on select products



with anticipated higher gross margins. This strategy is designed to align our product development initiatives with our manufacturing processes and manufacturing cost structure, and to reduce our exposure to more commodity-type product applications that are prone to unpredictable demand and fluctuating pricing. Our focus is primarily on higher-margin products that possess design features that take optimal advantage of our existing and developing manufacturing technology and that command a price commensurate with the performance advantages of our alloys. In addition to our focus on products with higher gross margins, we will continue to engage in prototype manufacturing, both for internally manufactured products and for products that will ultimately be licensed to or manufactured by third parties.

- *Further Developing Our Manufacturing Processes, Capabilities, and Efficiencies for Bulk Liquidmetal Alloys.* We intend to improve and enhance our internal manufacturing processes, capabilities, and efficiencies in order to maintain quality control over products made from bulk Liquidmetal alloys, to focus on improvements to the processing of our alloys, and to protect our intellectual property. As our alloys become more pervasive, however, we expect to enter into additional strategic relationships that would involve the licensing of Liquidmetal technology to third parties for certain market segments.
- *Pursuing Strategic Partnerships In Order to More Rapidly Develop and Commercialize Products.* We intend to actively pursue and support strategic partnerships that will enable us to leverage the resources, strength, and technologies of other companies in order to more rapidly develop and commercialize products. These partnerships may include licensing transactions in which we license full commercial rights to our technology in a specific application area, or they may include transactions of a more limited scope in which, for example, we outsource manufacturing activities or grant distribution rights. We believe that utilizing such a partnering strategy will enable us to reduce our working capital burden, better fund product development efforts, better understand customer adoption practices, leverage the technical and financial resources of our partners, and more effectively handle product design and process challenges. As this partnering strategy evolves, a growing portion of our revenue mix may be comprised of revenue from the provision of product development services, technical support, and engineering services, as well as revenues from royalties on the sale of Liquidmetal alloy products by our partners.
- *Advancing the Liquidmetal® Brand.* We believe that building our corporate brand will foster continued adoption of our technology. Our goal is to position Liquidmetal alloys as a superior substitute for materials currently used in a variety of products across a range of industries. Furthermore, we seek to establish Liquidmetal alloys as an enabling technology that will facilitate the creation of a broad range of commercially viable new products. To enhance industry awareness of our company and increase demand for Liquidmetal alloys, we are reviewing various brand development strategies that could include collaborative advertising and promotional campaigns with select customers, industry conference and trade show appearances, public relations, and other means.

#### **Applications for Liquidmetal Alloys**

We have focused our commercialization efforts for Liquidmetal alloys on five identified product areas. We believe that these areas are consistent with our strategy in terms of market size, building brand recognition, and providing an opportunity to develop and refine our processing capabilities. Although we believe that strategic partnering transactions could create valuable opportunities beyond the parameters of these target markets, we anticipate continuing to pursue these markets both internally and in conjunction with partners.

#### **Components for Electronic Products**

We produce components for electronic devices using our bulk Liquidmetal alloys and believe that our alloys offer enhanced performance and design benefits for these components in certain applications. Bulk Liquidmetal alloys can be used for various structural components of a cellular phone, including the shield, faceplate, hinge, hinge housings, back plate, side plates, brackets, and the cover on the phones. We initially targeted the electronic casings market because of its potential for high product volumes and branding opportunities; however, unpredictable customer adoption practices, short product model lives, processing limitations, and intense pricing pressures make it very challenging to compete in this high-volume market. Accordingly, we are





currently limiting our focus in this market to higher-margin applications that have the potential to benefit from the unique performance characteristics of bulk Liquidmetal alloys. We continue to believe that the high strength-to-weight ratio and elastic limit of bulk Liquidmetal alloys enable the production of stronger and thinner electronic devices as compared to plastic, zinc, and magnesium, and we intend to focus on products that require these design and performance benefits.

Through our shipments to date, we have demonstrated that bulk Liquidmetal alloys can be used for structural components of cellular phones and other electronic devices. During 2007, 2006, 2005, and 2004, we shipped production quantities of cell phone components to Samsung Electronics Company, Motorola, and Vertu Limited, the luxury communication products subsidiary of Nokia, for inclusion in various cellular phone models.

### *Sporting Goods and Leisure Products*

We are developing a variety of applications for Liquidmetal alloys in the sporting goods and leisure products area.

In the sporting goods industry, we believe that the high strength, hardness, and elasticity of our bulk alloys have the potential to enhance performance in a variety of products, and we further believe that many sporting goods products are conducive to our internal manufacturing strategy of focusing on high-margin products that meet our design criteria. Substantial opportunities also exist for our amorphous alloy coatings, powders and composites. In 2003, Rawlings Sporting Goods Company launched a new line of baseball and softball bats that utilize a Liquidmetal alloy coating, and HEAD NV Sport launched a new line of HEAD® Liquidmetal® tennis racquets that incorporates Liquidmetal alloy in composite form in their racquet design. In 2005, we have also launched goods that utilize Liquidmetal alloy including skis. Other potential applications for our alloys in this industry include golf clubs, eyewear, fishing, hunting, and other sport products.

In the leisure products category, we believe that bulk Liquidmetal alloys can be used to efficiently produce intricately engineered designs with high-quality finishes, such as premium watchcases, and we further believe that Liquidmetal alloy technology can be used to make high-quality, high-strength jewelry from precious metals. We have successfully produced prototype rings made from an amorphous Liquidmetal platinum alloy that is harder (and hence more scratch resistant) than conventional platinum jewelry.

In order to accelerate the commercialization of Liquidmetal alloys in the jewelry and high-end luxury products market, in June 2003, we entered into an exclusive, ten-year license agreement with LLPG, Inc. ( LLPG ), a corporation headed by, Jack Chitayat, a former director of our company. Under the terms of the agreement, LLPG has the right to commercialize Liquidmetal alloys, particularly precious-metal based compositions, in jewelry and high-end luxury product markets. We, in turn, will receive royalty payments over the life of the contract on all Liquidmetal products produced and sold by LLPG. In conjunction with its technology licensing contract, LLPG purchased two proprietary Liquidmetal alloy melting machines and three proprietary Liquidmetal alloy casting machines for a total purchase price of \$2.0 million. We recognized \$0.1 million of revenues as minimum royalty fees under the license agreement during the year ended December 31, 2006.

In December 2006, we entered into an amended the license agreement with LLPG, which extends the license agreement to fifteen years at reduced royalty rates. Additionally, the amended license agreement includes a \$0.4 million termination fee to be paid out in quarterly installments in 2007. The termination fee will be recognized as revenue when received in 2007.

In order to accelerate the commercialization of Liquidmetal alloys in the eyewear industry, in June of 2006, we entered into a joint venture agreement with SAGA, SpA in Padova, Italy, a specialist precision part manufacturer. The joint venture is named Liquidmetal SAGA Italy, Srl ( LSI ), and it will have an exclusive manufacturing license for the eyewear industry. Its initial focus will be on the development and commercialization of eyewear with Safilo SpA, a worldwide leader in luxury eyewear, supplying frames and sunglasses for most of the luxury brands with operations in more than 120 countries worldwide.

### *Medical Devices*

We are engaged in product development efforts relating to various medical devices that could be made from Liquidmetal alloys. We believe that the unique properties of bulk Liquidmetal alloys provide a combination of performance and cost benefits that could make them a desirable replacement to incumbent materials, such as stainless steel and titanium, currently used in



various medical device applications. Our ongoing emphasis in 2006 and 2007 has been on surgical instrument applications for Liquidmetal alloys. These include, but are not limited to, specialized blades, orthopedic instruments utilized for implant surgery procedures, dental devices, and general surgery devices. The potential value offered by our alloys is high performance in some cases and cost reduction in others, the latter stemming from the ability of Liquidmetal alloys to be net shape cast into components, thus reducing costs of secondary processing. The status of most components in the prototyping phase is subject to non-disclosure agreements with our customers.

We believe that our future success in the medical device market will be driven largely by strategically aligning ourselves with well-established companies that are uniquely positioned to facilitate the introduction of Liquidmetal alloys into this market, especially as it relates to the unique processing challenges and stringent material qualification requirements that are prevalent in this industry. We also believe that our prospects for success in this market will be enhanced through our focus on optimizing existing alloy compositions and developing new alloy compositions to satisfy the industry's rigorous material qualification standards.

#### ***Industrial Coatings and Powders***

We continue to market and sell amorphous alloy industrial coatings and powders under the Liquidmetal® Armacor™ Coatings brand name. Liquidmetal alloy coatings are used primarily as a protective coating for industrial machinery and equipment. Since the inception of this business in the late 1980s, our proprietary coatings have demonstrated a high degree of hardness and low coefficient of friction which, when combined with their strong adhesion properties, reduce the wear and consequent failure of the machinery and equipment on which they are used. In contrast to our bulk alloys, we sell Liquidmetal coatings primarily in the form of a wire or powder feedstock that is melted and applied to machinery or equipment through welding or thermal spray processes.

Our Liquidmetal coatings are widely used in the oil drilling industry as a protective coating on drill pipe and casings, and we estimate that our coatings represent a dominant share of annual worldwide sales of hard band coatings for new oil drill pipe. Drilling often places tremendous stress on pipes and casings, especially whenever the drill changes direction. Both the drill pipe and casing experience excessive wear, which leads to higher replacement costs and greater failure rates. Liquidmetal coatings are used to provide a protective coating, or hard band, around the outside of the drill pipe and the inside of casings to reduce wear and failure rates and accordingly reduce operating costs.

Liquidmetal coatings have also been sold into the power generation industry specifically for the purpose of coating boiler tubes in coal-burning power plants in order to extend the lives of these boilers. Boiler tubes are subject to high heat, erosion, and corrosion and often require costly replacement, both in terms of replacement parts and length of downtime for installation. Additionally, residue build-up in boiler tubes of coal burning power plants creates operating inefficiencies. Historic performance and testing of Liquidmetal coatings have demonstrated that our coatings extend the life of these boiler tubes meaningfully beyond their current average life depending on the specific environment. In addition, our coatings have demonstrated the ability to reduce build-up of residue on boiler tubes, helping to improve the efficiencies of the boilers. Historically, we have not concentrated sales efforts on the boiler tube market in a substantial way. However, given the size of the market and potential opportunities for our coatings, we have recently dedicated greater effort to this area.

#### ***Defense Applications***

We are working with the U.S. Department of Defense, as well as a variety of defense-related research and development agencies and large defense contractors, to develop various defense-related applications for Liquidmetal alloys. For example, we are currently developing prototype kinetic energy penetrator rods for use in armor-piercing ammunition systems. Kinetic energy penetrators, or KEPs, are armor piercing munitions that are currently made primarily from depleted uranium or tungsten alloys. Initial ballistic tests under the Liquidmetal KEP program have demonstrated that tungsten KEPs perform better whenever Liquidmetal alloy is combined with the tungsten to create a composite material. In August 2003, we signed a new \$3.0 million research and development contract with the U.S. Army for the development of KEPs, which was later supplemented by additional \$2.7 million. Our strategy is to orient the KEP program toward future systems such as the Joint Strike Fighter program and the Army's Future Combat System.

We also continue to work with a number of defense-related research and development agencies and large defense companies to identify additional military applications that may benefit from using Liquidmetal alloys. We believe that our alloys can present opportunities that we can capitalize on the trend toward lighter but stronger weapon systems in the U.S. military, and our strategy is to align ourselves with the largest and most significant players in this industry. Product development programs for defense applications are currently underway with several leading defense contractors, including Alliant Techsystems and General Dynamics.

### **Going Concern / Liquidity**

We have experienced significant operating losses since our inception. Our net loss for the fiscal years ended December 31, 2006 and 2005 was \$14.5 million and \$7.1 million, respectively. For the three months ended March 31, 2007 and 2006, we had a net income of \$0.5 million and a net loss of \$6.0 million, respectively. In the audit report on our financial statements for our fiscal years ended December 31, 2006 and 2005, our present auditors included a going-concern qualification indicating that our significant operating losses and working capital deficit cause substantial doubt about our ability to continue as a going concern. By issuing an opinion stating that there is substantial doubt about our ability to continue as a going concern, our auditors have indicated that they are uncertain as to whether we have the capability to continue our operations without additional funding. On January 3, 2007, we completed a private placement of \$16.3 million in principal amount of 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes). The January 2010 Notes were issued for aggregate cash in the amount of \$12.9 million and in payment of a total of \$3.4 million in principal and accrued but unpaid interest under our previously issued 7% Senior Secured Convertible Notes due August 2007 and our 8% Unsecured Subordinated Notes.

We anticipate that the \$12.9 million aggregate cash raised in the private placement will be sufficient to pursue our current operating plan only through the third quarter of 2007, and we will therefore require additional funding at or prior to that time. As a result, we are actively seeking additional sources of capital. The amount of funding that we seek and the timing of such fundraising efforts will depend on the extent to which we are able to increase revenues through obtaining additional purchase orders for our products and/or the extent to which we can restructure or modify our debt. Because we cannot be certain that we will be able to obtain adequate funding from debt, equity, or other traditional financing sources, we are also actively exploring several strategic financing options, including the possible sale of our manufacturing plant in South Korea (which would then be replaced with a smaller facility), potential licensing and outsourcing of manufacturing operations including those in South Korea and China, and the possible sale of our Liquidmetal Coatings business. In June 2007, we entered into an equipment sale and licensing agreement with Grace Metal, a South Korean corporation, providing for \$2.0 million in exchange for die casting machines and vacuum induction melters, and a 10-year exclusive license to manufacture Liquidmetal alloys for customers whose principal headquarters or major operations are based in South Korea. The principal purpose of the transactions with Grace Metal was to raise capital for the next-generation casting equipment and to shift the cost and burden of our manufacturing operations to a third party. Grace Metal was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company. We cannot guarantee that adequate funds will be available when needed, and if we do not receive sufficient capital, we may be required to alter or reduce the scope of our operations.

### **Liquidmetal Golf**

From 1997 until September 2001, we were engaged in the retail marketing and sale of golf clubs through a majority owned subsidiary, Liquidmetal Golf. The retail business of Liquidmetal Golf was discontinued in September 2001. Although the retail golf club business has been discontinued, Liquidmetal Golf is engaged in the development of golf club components for golf original equipment manufacturers that will integrate these components into their own clubs and then sell them under their respective brand names. Liquidmetal Technologies owns 79% of the outstanding common stock in Liquidmetal Golf.

Our Liquidmetal Golf subsidiary has the exclusive right and license to utilize our Liquidmetal alloy technology for purposes of golf equipment applications. This right and license is set forth in an intercompany license agreement between Liquidmetal Technologies and Liquidmetal Golf. This license agreement provides that Liquidmetal Golf has a perpetual and exclusive license to use Liquidmetal alloy technology for the purpose of manufacturing, marketing, and selling golf club components and other products used in the sport of golf. In consideration of this license, Liquidmetal Golf has issued 4,500,000 shares of Liquidmetal Golf common stock to Liquidmetal Technologies.

### **Our Intellectual Property**

Our intellectual property consists of patents, trade secrets, know-how, and trademarks. Protection of our intellectual property is a strategic priority for our business, and we intend to vigorously protect our patents and other intellectual property. Our intellectual property portfolio includes 32 owned or licensed U.S. patents and numerous patent applications relating to the composition, processing, and application of our alloys, as well as various foreign counterpart patents and patent applications.



Our initial bulk amorphous alloy technology was developed by researchers at the California Institute of Technology ( Caltech ). We have purchased patent rights that provide us with the exclusive right to commercialize the amorphous alloy and other amorphous alloy technology acquired from Caltech through a license agreement ( Caltech License Agreement ) with Caltech. Under the Caltech license agreement, we have the exclusive worldwide right to make, use, and sell products from all of Caltech 's inventions, proprietary information, know-how, and other technology relating to amorphous alloys existing as of September 1, 2001. We also have an exclusive worldwide license to eleven issued patents and two patent applications held by Caltech relating to amorphous alloy technology, as well as all related foreign counterpart patents and patent applications. Of the patents currently issued to Caltech and licensed by us, the earliest expiration date is 2013 and the latest expiration date is 2021. Furthermore, the license agreement gives us the exclusive right to make, use, and sell products from substantially all amorphous alloy technology that was developed in Professor William Johnson 's Caltech laboratory during the period September 1, 2001 through August 31, 2005. All fees and other amounts payable by us for these rights and licenses have been paid in full, and no further royalties, license fees, or other amounts will be payable in the future under this license agreement.

Our rights under the license agreement are perpetual in duration. However, Caltech has the right to convert the license to a non-exclusive license if we fail to utilize the licensed technology for a period of 18 or more consecutive months, provided that Caltech must give us 180-days advance written notice of the conversion and we may cure the failure at any time during the 180-day notice period. If we cure the failure, then the license will not be converted into a non-exclusive license.

Under the license agreement, we have the right to sublicense any of the licensed technology or patents. The license agreement also provides that Caltech reserves the right to use the licensed technology and patents for noncommercial educational and research purposes. The patents and patent applications that we license from Caltech relate primarily to the composition and processing of our alloys. The currently issued U.S. patents covered by the license agreement will expire between 2012 and 2013.

Under the Caltech license agreement, the parties are obligated to provide reasonable cooperation to each other in connection with any threatened or actual infringement of the licensed technology by third parties. We have the right to commence an action for infringement of any of the licensed technology, and although Caltech is not obligated to bring suit or take action against infringers, Caltech is obligated to join in any such lawsuit upon our request.

In addition to the patents and patent applications that we license from Caltech, we are building a portfolio of our own patents to expand and enhance our technology position. These patents and patent applications primarily relate to various applications of our bulk amorphous alloys, the composition of our coatings and powders, and the processing of our alloys. The patents relating to our coatings expire on various dates between 2006 and 2017, and the patents relating to our bulk amorphous alloys expire on various dates between 2013 and 2021. Our policy is to seek patent protection for all technology, inventions, and improvements that are of commercial importance to the development of our business, except to the extent that we believe it is advisable to maintain such technology or invention as a trade secret.

In order to protect the confidentiality of our technology, including trade secrets, know-how, and other proprietary technical and business information, we require that all of our employees, consultants, advisors and collaborators enter into confidentiality agreements that prohibit the use or disclosure of information that is deemed confidential. The agreements also obligate our employees, consultants, advisors and collaborators to assign to us developments, discoveries and inventions made by such persons in connection with their work with us.

## Research and Development

We are engaged in ongoing research and development programs that are driven by the following key objectives:

- *Enhance Material Processing and Manufacturing Efficiencies.* We plan to continue research and development of processes and compositions that will decrease our cost of making products from Liquidmetal alloys.
- *Optimize Existing Alloys and Develop New Compositions.* We believe that the primary technology driver of our business will continue to be our proprietary alloy compositions. We plan to continue research and development on new alloy compositions to generate a broader class of amorphous alloys with a wider range of

specialized performance characteristics. During 2003 and continuing into 2006, we have successfully expanded our portfolio of bulk amorphous alloys to include additional zirconium-titanium alloys, as well as alloys based on other metals, such as iron, gold, and platinum. Although these various compositions are at different stages of development and only a few are currently suitable for commercial use, we believe that a larger alloy portfolio will enable us to increase the attractiveness of our alloys as an alternative to incumbent materials and, in certain cases, drive down product costs. We also believe that our ability to optimize our existing alloy compositions will enable us to better tailor our alloys to our customers' specific application requirements.

- *Develop New Applications.* We will continue research and development of new applications for Liquidmetal alloys. We believe the range of potential applications will broaden by expanding the forms, compositions, and methods of processing of our alloys.

We conduct our research and development programs internally and also through strategic relationships that we enter into with third parties. Our internal research and development efforts are conducted by a team of 12 scientists and engineers whom we either employ directly or engage as consultants. Included among this team are Professor William Johnson, who discovered our initial bulk amorphous alloy at Caltech in 1993, and his graduate student at the time, Atakan Peker, who is employed as our Vice President of Technology. Professor Johnson was an employee of our company from October 2001 through December 2003 and then became a consultant to our company. Professor Johnson continues to be a member of our board of directors.

In addition to our internal research and development efforts, we enter into cooperative research and development relationships with leading academic institutions. We have entered into development relationships with other companies for the purpose of identifying new applications for our alloys and establishing customer relationships with such companies. Some of our product development programs are partially funded by our customers. We are also engaged in negotiations with other potential customers regarding possible product development relationships. Our research and development expenses for the years ended December 31, 2006, 2005, and 2004, were \$1.0 million, \$1.1 million, and \$1.5 million, respectively, and \$0.3 million and \$0.2 million for the three months ended March 31, 2007 and 2006, respectively.

## **Manufacturing**

We currently own and operate a 166,000 square foot manufacturing facility in Pyongtaek, South Korea, which became operational in the third quarter of 2002. We opened a 14,400 square foot facility in Weihai, China in August 2004 to facilitate our bulk alloy manufacturing business. Effective June 1, 2007, we discontinued our operation in Weihai and transferred our manufacturing staff and equipment in Weihai to Grace Metal ( GM ), a South Korean corporation, as result of a strategy to shift the cost and burden of our manufacturing operations to a third party. We believe that these facilities will meet our anticipated manufacturing needs for the foreseeable future, although these needs may change depending upon the actual and forecasted orders we receive for our products. We currently intend to develop supplemental research and development, prototyping and manufacturing capabilities elsewhere, including the United States, for purposes of meeting our long-term manufacturing needs and our customers' requirements. In December 2003, we entered into a license agreement with Florida Custom Mold, Inc., a Clearwater, Florida-based company that specializes in high-quality mold design and injection molding services, under which Florida Custom Mold is currently acting as a contract manufacturer to our company for purposes of producing prototypes of certain defense and medical products in the US. In June 2006, we entered into a joint venture agreement with SAGA, SpA in Padova, Italy, ( SAGA ) a specialist precision parts manufacturer. The joint venture is named Liquidmetal SAGA Italy, Srl ( LSI ), under which LSI is currently acting as a contract manufacturer to our company for the purpose of producing prototypes and certain consumer electronics products in Europe. In June 2007, we entered into a licensing agreement with GM a 10-year exclusive license to manufacture Liquidmetal alloys for customers whose principal headquarters or major operations are based in South Korea. GM was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company.

## **Raw Materials**

Liquidmetal alloy compositions are comprised of many elements, all of which are available commodity products. We believe that each of these raw materials is readily available in sufficient quantities from multiple sources on commercially acceptable terms. However, any substantial increase in the price or interruption in the supply of these materials could have an adverse effect on our profitability.

## **Customers**

During the three months ended March 31, 2007, revenues from one customer, Flextronics Manufacturing LTD, represented approximately 17%, of total revenues from continuing operations. During 2006, one customer, Flextronics Manufacturing LTD, who is a direct supplier to SanDisk, accounted for 10% or more of our revenue from continuing operations.





During 2005, one customer, Samsung, accounted for 10% or more of our revenue from continuing operations. During 2004, four customers accounted for 10% or more of our revenue from continuing operations. Revenues from Charm Tech and Pntel, both of which are direct suppliers to Samsung, represented 62% of revenue from continuing operations for the year ended 2004. Also, revenues from defense related contracts with the United States of America represented 10% and Growell Metal represented 12% of revenue from continuing operations for the year ended 2004. We expect that a significant portion of our revenue may continue to be concentrated in a limited number of customers, even as our bulk Liquidmetal alloy business grows.

### **Competition**

We are not aware of any other company or business that manufactures, markets, distributes, or sells bulk amorphous alloys or products made from bulk amorphous alloys. We believe it would be difficult to develop a competitive bulk amorphous alloy without infringing our patents. However, our bulk Liquidmetal alloys face competition from other materials, including metals, alloys, plastics and composites, which are currently used in the commercial applications that we pursue. For example, we face significant competition from plastics and zinc in our electronics components business, and titanium and composites will continue to be used widely in medical devices and sporting goods. Based on our experience with developing products for a variety of customers, we believe that the selection of materials by potential customers will continue to be product-specific in nature, with the decision for each product being driven primarily by the performance needs of the application and secondarily by cost considerations and design flexibility. Because of the relatively high strength of our alloys and the design flexibility of our process, we are most competitive when the customer is seeking a higher strength as well as greater design flexibility than currently available with other materials. However, if currently available materials, such as plastics, are strong enough for the application, our alloys are often not competitive those applications with respect to price. We also believe that our alloys are generally not competitive with the cost of some of the basic metals, such as steel, aluminum or copper, when such basic metals can be used in specific applications, but our alloys are generally more competitive with price on more exotic metals, such as titanium. Our alloys could also face competition from new materials that may be developed in the future, including new materials that could render our alloys obsolete.

Our Liquidmetal alloy coatings face competition from industrial coatings currently manufactured or sold by other companies. At present, the primary competitors of our coatings business are Varco International, Inc. and Arco Technology Trust, Limited. Although we believe, based on market data gathered by us, that our coatings compete favorably with these companies' products and that we continue to maintain the dominant market share with respect to protective coatings for oil drill pipe and casings, these competitors are larger well-established businesses that have substantially greater financial, marketing, and other resources than we do.

We will also experience indirect competition from the competitors of our customers. Because we will rely on our customers to market and sell finished goods that incorporate our components or products, our success will depend in part on the ability of our customers to effectively market and sell their own products and compete in their respective markets.

### **Backlog**

In our bulk alloy segment, because of the minimal lead-time associated with orders of bulk alloy parts, we generally do not carry a significant backlog. In our coatings segment, we typically ship our coating products shortly after receipt of an order, and our coatings backlog is therefore also insignificant. In both our bulk alloy segment and coatings segment, the backlog as of any particular date gives no indication of actual sales for any succeeding period.

### **Sales and Marketing**

We direct our marketing efforts towards customers that will incorporate our components and products into their finished goods. To that end, we will continue to hire business development personnel who, in conjunction with engineers and scientists, will actively identify potential customers that may be able to benefit from the introduction of Liquidmetal alloys to their products. In some cases, we will develop applications in conjunction with existing or potential customers. By adopting this strategy, we intend to take advantage of the sales and marketing forces and distribution channels of our customers to facilitate the commercialization of our alloys. We also direct business development efforts toward companies who we believe could be viable candidates for potential partnering transactions, such as licensing relationships, distribution arrangements, joint ventures, and the like.

## **Employees**

As of June 1, 2007, we had 98 full-time and 63 part-time employees. As of that date, 52 of our Korean operation employees were represented by a labor union. We have not experienced any work stoppages and we consider our employee relations to be favorable.

## **Governmental Regulation**

Medical instruments incorporating our Liquidmetal alloys will be subject to regulation in the United States by the FDA and corresponding state and foreign regulatory agencies. Any orthopedic devices that we develop will be regulated in a similar manner. Medical device manufacturers to whom we intend to sell our products may need to obtain FDA approval before marketing their medical devices that incorporate our products. Medical device manufacturers may need to obtain similar approvals before marketing these medical device products in foreign countries.

Because we intend to sell our medical device products to medical device manufacturers, we do not believe that we will need to obtain FDA approval or similar foreign approvals before selling products to medical device manufacturers. Nonetheless, as a manufacturer of medical device components, we would be subject to quality control and record keeping requirements of FDA and other federal and state statutes and regulations, as well as similar regulations in foreign countries.

The process of obtaining and maintaining required FDA and foreign regulatory approvals for medical devices that incorporate our products could be lengthy, expensive, and uncertain for our customers. Additionally, regulatory agencies can delay or prevent product introductions. Generally, before a medical device manufacturer can market a product incorporating one of our products, our customer must obtain for their finished product marketing clearance through a 510(k) premarket notification or approval of a pre-market approval application, or PMA. The FDA will typically grant a 510(k) clearance if the applicant can establish that the device is substantially equivalent to a predicate device. It generally takes a number of months from the date of a 510(k) submission to obtain clearance, but it may take longer, particularly if a clinical trial is required.

The FDA may find that a 510(k) is not appropriate for a medical device that incorporates our product or that substantial equivalence has not been shown and as a result will require a PMA. A PMA application must be submitted if a proposed medical device does not qualify for a 510(k) pre-market clearance procedure. PMA applications must be supported by valid scientific evidence to demonstrate the safety and effectiveness of the device, typically including the results of clinical trials, bench tests, and laboratory and animal studies. The PMA process can be expensive, uncertain and lengthy, requires detailed and comprehensive data, and generally takes significantly longer than the 510(k) process. Additionally, the FDA may never approve the PMA.

Similar regulations in foreign countries vary significantly from country to country and with respect to the nature of the particular medical device. The time required to obtain these foreign approvals to market our products may be longer or shorter than that required in the United States, and requirements for such approval may differ from FDA requirements.

## **Environmental Law Compliance**

Our manufacturing operations are subject to national, state, and local environmental laws in each of China, South Korea, and the United States. We believe that we are in material compliance with all applicable environmental regulations. While we continue to incur costs to comply with environmental regulations, we do not believe that such costs will have a material effect on our capital expenditures, earnings, or competitive position.

## **Material Legal Proceedings**

### *Securities Class Action and Shareholder Derivative Actions*

In April 2006, we reached agreements-in-principle to settle our previously-disclosed consolidated securities class action and shareholder derivative actions for a total of \$7.5 million; \$7.0 million for the class action and \$0.5 million for the derivative actions. In addition, we will commit to maintain or implement various corporate governance measures in connection with the settlement of the derivative actions.

The consolidated class action arose from a number of lawsuits filed in 2004 against our company and certain of our former and current directors and officers on behalf of persons who purchased our common stock between May 21, 2002 and May 13, 2004. These actions, which were brought under the federal securities laws, alleged that the Prospectus issued in connection with our initial public offering in May 2002 contained material misrepresentations and omissions regarding our historical financial condition and regarding a personal stock transaction by our former chief executive officer. They also alleged that our company and certain of our present and former officers and directors engaged in improper revenue recognition with respect to certain of our business transactions, failed to maintain adequate internal controls, and knowingly disclosed unrealistic but favorable information about market demand for and commercial viability of our products to artificially inflate the value of our stock. On October 19, 2006, the presiding judge entered an Order giving final approval of the class action settlement. In connection with the settlement, our directors and officers' liability insurers contributed \$7.0 million to a settlement fund, from which approved claims of eligible class members will be paid in accordance with a court-approved plan of allocation. Taking into account the insurance contribution, the net cost of the settlement to our company is approximately \$0.5 million, which is the insurance deductible we paid over several quarters ending in the third quarter of 2005, and which was previously recorded as a charge.

In addition, in May 2004, two shareholder derivative actions were filed in the Superior Court of Orange County, California and later consolidated. Shortly thereafter, one additional shareholder derivative action was filed in the United States District Court for the Middle District of Florida, Tampa Division. These derivative actions were brought by certain shareholders against certain of our present and former officers and directors as well as our company (as a nominal defendant). The suits alleged that the defendants breached various fiduciary duties and otherwise violated state law based primarily upon the same facts and circumstances underlying the federal securities class action. On August 2, 2006, plaintiffs' counsel in the California derivative action filed a Notice of Settlement in the Superior Court. The parties' counsel have executed a Stipulation of Settlement, and plaintiffs' counsel have filed a Motion to Approve Settlement and Award of Attorneys' Fees and Expenses. A settlement approval hearing is scheduled for July 13, 2007.

#### *Department of Justice Investigation*

In August 2006, the United States Department of Justice (DOJ) instituted a grand jury proceeding in the Middle District of Florida to investigate, among other things, alleged accounting improprieties in relation to certain of our business transactions and a personal stock transaction by our former chief executive officer. The grand jury proceeding is based primarily upon the same underlying facts and circumstances as alleged in the federal class action and shareholder derivative actions. To date, subpoenas for the production of documents and/or grand jury testimony have been issued to our company and several present and former officers and directors. We are cooperating with the DOJ in its investigation.

#### *Noteholder Lawsuit*

On January 3, 2007, we completed a private placement of new 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes) that, as amended, provided for the issuance of \$16.3 million in principal amount of January 2010 Notes. The January 2010 Notes were issued pursuant to a Securities Purchase Agreement, dated January 3, 2007, between our company and the purchasers of the January 2010 Notes (the January Purchase Agreement). Under the terms of the original January Purchase Agreement, we agreed to repay or otherwise satisfy, within 5 days after the closing of the private placement, approximately \$15.5 million of our outstanding debt under previously issued promissory notes, including the August 2007 Notes, the Atlantic Note, and New Bridge Notes (the Debt Satisfaction Covenant). We originally agreed to this covenant based on assurances that a substantial number of holders of the August 2007 Notes would elect to convert their August 2007 Notes at a reduced conversion price following the private placement under a note conversion agreement proposed by us, but most of such holders ultimately elected not to proceed with such conversion. Accordingly, in an effort to preserve funds, we have not yet repaid the indebtedness as required by the original January Purchase Agreement, and in April 2007, we entered into an amendment to the January Purchase Agreement providing that we will have until October 1, 2007 (or such earlier date on which the indebtedness to be repaid is due) to comply with the Debt Satisfaction Covenant.

On March 22, 2007, one of the purchasers of the January 2010 Notes (holding January 2010 Notes in the aggregate amount of \$2.0 million) sent us an event of default notice (Event of Default Notice) indicating that we had defaulted under the January Purchase Agreement (and therefore under the January 2010 Note) by failing to comply with the Debt Satisfaction Covenant. This holder did not execute the April 2007 amendment to the January Purchase Agreement, although that amendment was approved by a majority of the noteholders. In general, upon a breach of

the January 2010 Notes or January Purchase Agreement, a holder of the January 2010 Notes may require us to redeem the January 2010 Notes at a price equal to the greater of (i) the conversion amount to be redeemed and (ii) the product of (A) the conversion rate with respect to such conversion amount in effect at such time as the purchaser of the January 2010 Note delivers an Event of Default Redemption Notice (as defined below) and (B) the closing sale price of our common stock on the date immediately preceding such event of default. Under the terms of the January 2010 Notes and January Purchase Agreement, we have ten (10) business days after the receipt of an Event of Default Notice to cure a default. On April 6, 2007, the holder which sent the Event of Default Notice further sent us an event of default redemption notice ( Event of Default Redemption Notice ). The Event of Default Redemption Notice states that the holder has elected to require us to redeem its January 2010 Note for a price equal to \$2.0 million (the amount of the January 2010 Note) plus accrued and unpaid interest. On April 16, 2007, we were served with a complaint filed by the holder in the Federal District Court in Minnesota to collect this amount. We have answered and denied that any amount is currently owed to the holder, because of the April 2007 amendment to the January Purchase Agreement. The holder has also moved for summary judgment and a hearing on that motion is scheduled for August 30, 2007. We are currently working to resolve this matter.

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### PROPERTIES

Our principal executive offices and principal research and development offices are located in Rancho Santa Margarita, California and consist of approximately 15,000 square feet. This facility is occupied pursuant to a lease agreement that expires in April 20, 2012.

In Conroe, Texas, we lease an office and warehouse for our coatings business segment. This facility, which is approximately 10,000 square feet, is leased through September 2007.

Effective as of March 19, 2007, we entered into a lease agreement in Huntsville, Texas, commencing on August 1, 2007. This facility, which is approximately 4,500 square feet, is leased through August 1, 2012.

Our principal prototyping and manufacturing facility is in Pyongtaek, South Korea, and consists of approximately 166,000 square feet. We lease the land on which this facility is located, although we own the buildings, fixtures, and all personal property located on the land. The parcel of land consists of approximately four acres and is leased through 2022.

On August 2004, we entered into a 3-year lease for a post-processing facility located in Weihai, China, which consists of approximately 14,400 square feet, to facilitate our bulk alloy manufacturing. Effective June 1, 2007, we discontinued our operation in Weihai and transferred our manufacturing staff and equipment in Weihai to Grace Metal, a South Korean corporation, as result of a strategy to shift the cost and burden of our manufacturing operations to a third party. Grace Metal was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company.

We currently expect that the foregoing facilities will meet our anticipated internal manufacturing, research, warehousing, and administrative needs for the foreseeable future.

**MANAGEMENT****Executive Officers**

The executive officers of our company as of June 1, 2007, are as follows:

NAME	AGE	POSITION
Larry Buffington	59	President and Chief Executive Officer
Won Chung	29	Vice President of Finance
John Kang	43	Chairman of the Board

*Larry Buffington.* Larry Buffington was elected by our Board of Director to serve as the President and Chief Executive Officer of our company in October 2006. Mr. Buffington has been serving as full-time consultant to our company since July 2006. He is also the president of Buffington Consulting, a consulting firm that Mr. Buffington started in 1997 focusing on the assessment and turnaround of manufacturing operations. Prior to starting Buffington Consulting, Mr. Buffington was the General Manager of the Communications Products Business Unit of Augat, Inc., a public company with worldwide manufacturing operations in communication, automotive and electronic products. Mr. Buffington received a bachelor's degree in Industrial Engineering from Pennsylvania State University in 1969.

*Won Chung.* Won Chung was elected by our Board of Directors to serve as the Vice President of Finance of our company in May 2006, and in that capacity, Mr. Chung will serve as our principal financial and accounting officer. Prior to then, Mr. Chung worked for us since October 2004 as our company's Financial Reporting Manager. Prior to joining our company, he worked for KPMG, LLP as a senior auditor since September 2001. Mr. Chung is a certified public accountant and a graduate of California State University at Fullerton, where he received his B.A. specializing Accounting in 2001.

John Kang's biographical information is set forth below.

Our executive officers are elected by, and serve at the discretion of, our board of directors. There are no family relationships among our directors and executive officers.

**Change in Principal Financial Officer**

On April 30, 2007, Young Ham resigned as our Chief Financial Officer and ceased to be our principal financial officer. On May 1, 2007, our board elected Won Chung to serve as our Vice President of Finance and become our company's principal financial and accounting officer. Additional information regarding Mr. Chung is set forth above.

**Directors**

Listed below are the names of each of our directors, together with certain additional information concerning each such director as of June 1, 2007 are as follows:

**Directors with Terms Expiring at 2008 Annual Meeting**

Name	Age	Business Experience During Last Five Years	Director Since
Patrick Caruana	67	Patrick Caruana was elected as a director in October 2006. Mr. Caruana is a retired United States Air Force General and a recently retired vice president for Northrop Grumman Space Technology. From 2002 through February 2005, he had served as Vice President of Northrop Grumman Space	2006



Technology and was the Corporate lead for Missile and Defense business development in the Asia market. Mr. Caruana served as Vice President and Program Manager for TRW Space & Electronics from August 1999 until the company was acquired by Northrup Grumman in 2002. Prior to joining TRW, Mr. Caruana served 36 years in the U.S. Air Force, retiring the grade of Lieutenant General. Mr. Caruana is a graduate of the U.S. Air Force Academy, where he earned a bachelor's degree in engineering. In 1972, Mr. Caruana received a Master of Science degree in Mathematics from Texas A&M University.

#### Directors with Terms Expiring at 2007 Annual Meeting

Dean Tanella	46	Dean G. Tanella was elected as a director in February 2004. Mr. Tanella is a 20-year veteran of the institutional investment business and has worked for such leading firms as Raymond James & Associates, CS First Boston Corp., Adams Harkness & Hill, Drexel Burnham Lambert, Inc., Kidder Peabody & Co. and the Vanguard Group. Since 1999, Mr. Tanella has served as President of Safe Harbor Capital, LLC and, since 2003, as President of HarborLight Capital, LLC, both of which are private investment firms. Mr. Tanella received his bachelors degree from Princeton University and his MBA from the Harvard Graduate School of Business Administration. In December 2004, Mr. Tanella was also named Executive Vice President Capital Markets Group and a member of the Board of Directors at GunnAllen Financial Inc., a leading independent brokerage firm headquartered in Tampa, Florida.	2004
CK Cho	51	CK Cho was elected as a director in January 2005. Mr. Cho has over 18 years of experience with Samsung Electronics and managed over \$700 million annual procurement budget responsible for semi-conductor and telecommunication equipment and other electronic components. He also served as CEO and President of Winvest Venture Partners Inc. and is currently serving as President and CEO of ATIC, an IT Venture Capital Company based in Korea. Mr. Cho received his bachelors degree majoring in Business Administration and Material Sciences from the Korea University of Seoul.	2005

#### Directors with Terms Expiring at 2006 Annual Meeting or the First Annual Meeting Thereafter

John Kang	43	John Kang has been a director of our company since 1994. From December 1994 to June 2001, he served as Chairman of our Board of Directors in various capacities. From June 2001 until December 30, 2005, Mr. Kang had served variously as our Chief Executive Officer and President. From July 1996 to September 2000, Mr. Kang served variously as Chief Executive Officer, President, and a director of Medical Manager Corporation, a public company traded on the Nasdaq National Market until its sale in September 2000 to WebMD Corporation. From 1988 to	1994
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1995, he was Chairman of the board of directors of Clayton Group, Inc., a private company engaged in the distribution of waterworks equipment. Mr. Kang received a B.A. degree in Economics from Harvard College in 1985. Mr. Kang is the brother of James Kang, one of our directors. On December 15, 2005, an indictment naming as defendants ten former officers and directors of Medical Manager Corporation, including our Chairman, John Kang, was filed in the United States District Court for the District of South Carolina (Beaufort Division). Medical Manager Corporation was a publicly traded company in which Mr. Kang was formerly the President and Chief Executive Officer. Mr. Kang was charged in counts for conspiracy to commit securities fraud, conspiracy to commit mail fraud and conspiracy to launder money instruments relating to a series of acquisitions that were made by Medical Manager during the years 1996 through 2003, the accounting practices of Medical Manager during that time frame, and the filing of various financial statements during that time frame. Although the indictment is unrelated to Mr. Kang's services as a director and officer of our company, Mr. Kang resigned as our President and Chief Executive Officer on December 30, 2005; however, he continues to serve as Chairman of the Board of our company and continues to work for us on a full-time basis. Mr. Kang has pled not guilty to the indictment and plans to contest the charges vigorously.

William Johnson, Ph.D.	57	William Johnson, Ph.D., has served as a director since June 2000. From October 2001 to September 2003, he was employed as our executive Vice Chairman of Technology. Since 1988, Professor Johnson has been the Mettler Professor of Engineering and Applied Physics at Caltech. He held a Visiting Professor appointment at the Metal Physics Institute in Gottingen, Germany (1983) and received a Von Humbolt Distinguished Scientist Fellowship in Gottingen (1988). He is the 1995 recipient of the TMS/AIME Hume Rothery Award for his experimental work. He received a B.A. degree in Physics from Hamilton College and a Ph.D. degree in Applied Physics from Caltech. He spent two years at IBM's Research Center (1975-1977). At Caltech, Professor Johnson directed the research that led to the discovery of our bulk Liquidmetal alloy. Professor Johnson is currently a consultant to our company.	2000
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Robert Biehl	62	Robert Biehl has served as a director since January 2005. Mr. Biehl is an executive mentor. In 1976, he founded Masterplanning Group International. As President, he has personally consulted with over 400 clients ranging from start up to multi-billion dollar organizations. He has published 20 books in the area of personal and organizational development. He is a frequent key note speaker at various conferences. Prior to starting Masterplanning Group, Mr. Biehl was an executive staff of World Vision International where he designed and developed the Love Loaf Program, which has raised millions of dollars for hunger worldwide. Mr. Biehl received his B.A. degree in psychology and a Masters Degree in Counseling from Michigan State University.	2005
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### **Term of Directors**

Our board of directors is divided into three classes (designated CLASS I, CLASS II, and CLASS III), as nearly equal in number as possible, with each class serving three-year terms expiring at the third annual meeting of stockholders after their elections or until their respective successors have been elected and qualified. CLASS I currently consist of the following directors whose term is scheduled to expire at the 2006 annual meeting of stockholders or the first annual meeting thereafter: John Kang, William Johnson, and Robert Biehl. CLASS II currently consists of the following directors whose term is scheduled to expire at the 2007 annual meeting of stockholders: Dean Tanella and CK Cho. CLASS III currently consists of the following directors whose term will expire at the 2008 annual meeting of stockholders: Patrick Caruana.

### **Audit Committee**

Our board of directors has an Audit Committee that is currently comprised of Mr. Tanella, and Mr. Biehl. The Audit Committee is responsible for reviewing the independence, qualifications, and activities of our independent certified accountants and our financial policies, control procedures, and accounting staff. The Audit Committee is also responsible for the review of transactions between us and any officer, director, or entity in which an officer or director of our company has a material interest. Our board of directors has determined that Mr. Tanella qualifies as an audit committee financial expert as defined by the regulations of the Securities and Exchange Commission. In addition, our board of directors has determined that Mr. Tanella is an independent director within the meaning of Rule 10A-3(b)(i) under the Securities Exchange Act of 1934. The Audit Committee is governed by a written charter approved by the board of directors.

### **Compensation Committee**

The Compensation Committee is comprised of Mr. Cho and Mr. Biehl. All of the members of the Compensation Committee are independent directors, as defined by the rules applicable to members of the Compensation Committee. The Compensation Committee is responsible for establishing the compensation of our senior management, including salaries, bonuses, termination arrangements, and other executive officer benefits. The Compensation Committee also administers our equity incentive plans.

### **Corporate Governance and Nominating Committee**

A Corporate Governance and Nominating Committee (the Committee) was formed on February 18, 2003, and is comprised of Mr. Tanella and Mr. Biehl. All members of the Committee are independent directors, as defined by the rules applicable to members of the Committee. The Committee is generally responsible for adopting policies, procedures, and practices designed to help ensure that our corporate governance policies, procedures, and practices continue to assist the board and our management in effectively and efficiently promoting the best interests of our stockholders. The Committee is also responsible for selecting and recommending for approval by the Board and our company's stockholders a slate of director nominees for election at each of our company's annual meetings of stockholders, and otherwise for determining the Board committee members and chairmen, subject to Board ratification, as well as recommending to the Board director nominees to fill vacancies or new positions on the Board or its committees that may occur or be created from time to time, all in accordance with our company's Bylaws and applicable law.

The Corporate Governance Committee's principal functions include:

- developing and maintaining our corporate governance policy guidelines;
- developing and maintaining our codes of conduct and ethics;

- overseeing the interpretation and enforcement of our Code of Conduct and our Code of Ethics for Chief Executive Officer and Senior Financial and Accounting Officers; and
- evaluating the performance of our board, its committees, and committee chairmen and our directors.
- selecting and recommending a slate of director nominees for election at each of our annual meetings of the stockholders and recommending to the Board director nominees to fill vacancies or new positions on the Board or its committees that may occur from time to time.

#### **Compensation Committee Interlocks and Insider Participation**

None of the members of our compensation committee serves, or has at any time served, as an officer or employee of us or any of our subsidiaries. None of our executive officers has served as a member of the compensation committee, or other committee serving an equivalent function, of any other entity, one of whose executive officers served as a member of our compensation committee.

#### **Limitation of Liability and Indemnification of Officers and Directors**

Our by-laws provide that our directors, officers and employees shall be indemnified by us to the fullest extent authorized by Delaware law, as it now exists or may in the future be amended, against all expense, liability and loss reasonably incurred or suffered by them in connection with their service for or on behalf of us. In addition, we have entered into separate indemnification agreements with our directors and executive officers. We believe that these provisions and agreements are necessary to attract and retain qualified persons as directors and executive officers. These indemnification agreements may require us to indemnify our directors and executive officers for related expenses, including attorneys fees, judgments, fines and amounts paid in settlement that were actually and reasonably incurred or suffered by a director or executive officer in an action or proceeding arising out of his or her service as one of our directors or executive officers. In order to cover the foregoing potential expenses and liability, we have obtained insurance that insures our directors and officers against specified losses.

#### **Code of Ethics**

Our board of directors has adopted a Code of Ethics that is applicable to its principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. The Code of Ethics is attached as Exhibit 14 to our Annual Report on Form 10-K filed on November 10, 2004. In addition, we intend to promptly disclose (1) the nature of any amendment to our Code that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions and (2) the nature of any waiver, including an implicit waiver, from a provision of our Code that is granted to one of these specified officers, the name of such person who is granted the waiver and the date of the waiver on our website in the future. You may also request a copy of the Code by sending the request to [information@liquidmetal.com](mailto:information@liquidmetal.com).

## COMPENSATION DISCUSSION AND ANALYSIS

This compensation discussion describes the material elements of compensation awarded to, earned by, or paid to each of our executive officers who served as named executive officers during the last completed fiscal year. This compensation discussion focuses on the information contained in the following tables and related footnotes and narrative for primarily the last completed fiscal year, but we also describe compensation actions taken before or after the last completed fiscal year to the extent it enhances the understanding of our executive compensation disclosure.

The compensation committee currently oversees the design and administration of our executive compensation program.

The principal elements of our executive compensation program are base salary, annual cash incentives, long-term equity incentives in the form of stock options, other benefits and perquisites, post-termination severance and acceleration of stock option vesting for certain named executive officers upon termination and/or a change in control. Our other benefits and perquisites consist of reimbursement for certain automobile payments and health insurance benefits. Our philosophy is to position the aggregate of these elements at a level that is commensurate with our size and sustained performance.

### Compensation Program Objectives and Philosophy

The objectives of our compensation programs are to:

- attract, motivate and retain talented and dedicated executive officers;
- provide our executive officers with both cash and equity incentives to further the interests of us and our stockholders; and
- provide employees with long-term incentives so we can retain them and provide stability during our growth stage.

Generally, the compensation of our executive officers is composed of a base salary, an annual incentive compensation award and equity awards in the form of stock options. In setting base salaries, the compensation committee reviewed the individual contributions of the particular executive. The management incentive program for 2006 is a discretionary award determined by the compensation committee based on company performance. In addition, stock options are granted to provide the opportunity for long-term compensation based upon the performance of our common stock over time.

For each of our named executive officers, the compensation committee reviews and approves all elements of compensation taking into consideration recommendations from our principal executive officer (for compensation other than his own), as well as competitive market guidance provided at the request of the compensation committee.

We have designed our management incentive program so that bonuses paid thereunder will qualify as performance-based compensation under Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code). Given the compensation cost to us of awarding stock options under recent accounting pronouncements, we will consider the size and frequency of any future stock option awards under our long-term equity incentive program.

### Base Salaries

We provide the opportunity for our named executive officers and other executives to earn a competitive annual base salary. We provide this opportunity to attract and retain an appropriate caliber of talent for the position, and to provide a base wage that is not subject to our performance risk. We review base salaries for our named executive officers annually in January and increases are based on our performance and individual performance. The salary of our principal executive officer is set by our compensation committee.

### Cash Incentives

We provide the opportunity for our named executive officers and other executives to earn cash incentive award. We provide this opportunity to attract and retain an appropriate caliber of talent for the position and to motivate executives to achieve our annual business goals. We plan to review cash incentive awards for our named executive officers and other executives annually in March to determine award payments for the last

completed fiscal year, as well as to establish award opportunities for the current fiscal year.

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Awards are subject to the compensation committee's discretion and may take into account corporate performance measures, including, but not limited to, revenues, EBITDA and net income. The compensation committee establishes award criteria, generally, as a percentage of annual growth.

For the year ended December 31, 2006, John Kang, our chairman of the board was eligible to receive cash awards under the 2006 management incentive program based on revenue and profit growth over 2005. Mr. Kang is eligible for cash awards of 5% of revenues that exceed annual revenues in 2005. The awards are subject to final approval by the compensation committee based on overall performance of our company. There were no such awards declared or paid to our named executive officers during 2006 and 2007.

In setting the target bonus amounts, our Board took into consideration that our named executive officers have significant equity interests in us through direct ownership of shares or prior option grants, which already provide them with performance incentives.

### Equity-Based Compensation

Our equity-based awards to our executive officers consist principally of stock options granted from time to time under our 2002 Equity Incentive Plan and our 1996 Stock Option Plan. Stock option grants are based on various factors, including the executive officer's position, responsibility and tenure, each executive officer's ability to contribute to our future success, and the other elements of such executive officer's compensation. Generally, we use equity-based compensation to better align the interests of our executive officers with those of our stockholders.

For our named executive officers, our stock option program is based on grants that are individually negotiated in connection with employment agreements and other grants to our executives. We have traditionally used stock options as its form of equity compensation because stock options provide a relatively straightforward incentive for our executives, result in less immediate dilution of existing shareholders' interests and, prior to our adoption of FAS 123(R), resulted in less compensation expense for us relative to other types of equity awards. During 2006, all grants of stock options to our employees were granted with exercise prices equal to or greater than the fair market value of our common stock on the respective grant dates. For a discussion of the determination of the fair market value of these grants, see Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies .

We do not time stock option grants to executives in coordination with the release of material non-public information. Our stock options have a 10-year contractual exercise term or 5-year contractual term if the optionee owns more than 10% of voting power of the company. In general, the option grants are also subject to the following post-termination and change in control provisions:

Event	Award Vesting	Exercise Term
Termination by Us Reason Other than Cause, Disability or Death	Forfeit Unvested (1)	3 months from Date of Termination (1)
Disability or Death	Forfeit Unvested	12 months from Date of Termination
Termination for Cause	Forfeit Vested and Unvested	
Other Termination	Forfeit Unvested	90 days from Date of Termination
Change in Control	Accelerated (2)	Accelerated (2)

(1) Options granted under the 2002 Non-employee Director Option Plan will continue to vest and be exercisable for 12 months following the termination.

(2) The Board of Directors may, at its discretion, may amend vesting rights including additional grant additional shares in case of mergers or reorganizations for anti-dilution purposes.

The vesting of certain of our named executive officers' stock options may be accelerated pursuant to the terms of their employment agreements in certain termination and/or change in control events. These terms are more fully described in Employment Agreements and Potential Payments upon Termination or Change in Control.

### Executive Benefits and Perquisites

We provide the opportunity for our named executive officers and other executives to receive certain perquisites and general health and welfare benefits. We also offer participation in our defined contribution 401(k) savings plan. We do not match employee contributions under our 401(k) plan. Participation in general health and welfare benefits and the 401(k) plan are voluntary and are available to all eligible employees of the company. We provide these benefits to provide an additional incentive for our executives and to remain competitive in the general marketplace for executive talent. For the last completed fiscal year, perquisites other than general health and welfare benefits consisted of car payment reimbursements provided to John Kang, our chairman of the board, and CK Cho, our director.

Set forth below is information regarding compensation earned by or paid or awarded to the following executive officers of the company during the year ended December 31, 2006: (i) Larry Buffington, our president and chief executive officer; (ii) Won Chung, our vice president of finance; and (iii) John Kang, who is our chairman of the board, James Kang, who is a former founder and director of the board, and Ricardo Salas, who is a former president and chief executive officer, which persons are the three most highly compensated executives whose total compensation exceeded \$200,000, other than Messrs. Buffington and Chung, who were serving as executive officers. The identification of such named executive officers is determined based on the individual's total compensation for the year ended December 31, 2006, as reported below in the Summary Compensation Table.

### Summary Compensation Table

The following table sets forth for each of the named executive officers: (i) the dollar value of base salary and bonus earned during the year ended December 31, 2006; (ii) the aggregate grant date fair value of stock and option awards granted during the year, computed in accordance with SFAS 123 (R); (iii) the dollar value of earnings for services pursuant to awards granted during the year under non-equity incentive plans; (iv) the change in pension value and non-qualified deferred compensation earnings during the year; (v) all other compensation for the year; and, finally, (vi) the dollar value of total compensation for the year.

Name and Principal Position	Year	Salary	Bonus	Stock Awards	Option Awards (1)	Non-Equity Incentive Plan Compensation	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compensation	Total
Larry Buffington (2)	2006	\$ 41,667							\$ 41,667
Won Chung (6)	2006	\$ 84,583	\$ 6,800		\$ 10,210				\$ 91,383
John Kang	2006	\$ 213,750						\$ 11,752 (3)	\$ 225,502
James Kang (5)	2006	\$ 250,000							\$ 250,000
Ricardo Salas (4)	2006	\$ 222,418			\$ 51,052				\$ 273,470



- (1) Amounts represent the expensed fair value of stock options granted in 2006 under SFAS 123(R) as discussed in Note 17, Stock Compensation Plan to our financial statements included in our annual report on Form 10-K filed with the SEC on March 16, 2007.
- (2) Mr. Buffington commenced employment in October 2006 at an initial annual salary of \$200,000, which was subsequently adjusted to \$250,000 in January 2007.
- (3) Amount represents automobile lease payments.
- (4) Mr. Salas resigned as our president and chief executive officer in October 2006 and ceased to be an executive officer as of that date.
- (5) James Kang ceased to be an executive officer of our company as of October 2006. James Kang is the brother of John Kang, our Chairman
- (6) Mr. Chung was elected as our vice president of finance by our board and commenced serving as our principal financial and accounting officer in May 2007 at an initial annual salary of \$125,000. During 2006, Mr. Chung served as our company's controller.

For a description of the material terms of employment agreements with our named executive officers, see Employment Agreements.

#### Grants of Plan-Based Awards

The following table sets forth information regarding all incentive plan awards that were made to the named executive officers during 2006, including incentive plan awards (equity-based and non-equity based) and other planned-based awards. Disclosure on a separate line item is provided for each grant of an award made to a named executive officer during the year. The information supplements the dollar value disclosure of stock, option and non-stock awards in the Summary Compensation Table by providing additional details about such awards. Equity incentive-based awards are subject to a performance condition or a market condition as those terms are defined by SFAS 123(R). Non-equity incentive plan awards are awards that are not subject to SFAS 123(R) and are intended to serve as an incentive for performance to occur over a specified period.

Name	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares or Units	All Other Option Awards: Number of Securities Underlying Options	Exercise or Base Price of Option Awards
		Threshold	Target	Maximum	Threshold	Target	Maximum			
Larry Buffington										
Won Chung	4/1/06							10,000		\$ 1.44
John Kang										
James Kang										
Ricardo Salas	4/1/06								500,000	\$ 1.44

**Outstanding Equity Awards at Fiscal Year-End**

The following table sets forth information on outstanding option and stock awards held by the named executive officers at December 31, 2006, including the number of shares underlying both exercisable and unexercisable portions of each stock option as well as the exercise price and expiration date of each outstanding option.

Name	Option Awards				Stock Awards			Equity Incentive Plan Awards: Number of Unearned Shares, Units or Rights That Have Not Vested	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested
	Number of Securities Underlying Unexercised Options Exercisable	Number of Securities Underlying Unexercised Options Unexercisable	Equity Incentive Plan Awards Number of Securities Underlying Unexercised Unearned Options	Option Exercise Price	Option Expiration Date	Vesting Commencement Date	Number of Shares or Units of Stock That Have Not Vested	Market Value of Shares or Units of Stock That Have Not Vested	
Larry Buffington									
Won	3,000	4,500		\$ 2.15	10/10/2014	10/11/2005	(1)		
Chung	20,000	16,000		\$ 2.33	12/31/2014	1/1/2006	(1)		
	1,000	4,000		\$ 1.56	01/31/2015	2/1/2006	(1)		
		10,000		1.44	03/31/2016	3/31/2007	(1)		
John Kang	21,505			\$ 4.65	12/30/2010	12/30/2000	(2)		
	1,591,399			\$ 4.65	12/30/2010	12/30/2000	(2)		
	10,000	40,000		\$ 2.33	12/31/2014	12/31//2005	(1)		
James Kang	43,010			\$ 2.33	4/7/2008	4/7/1999	(3)		
	253,764			\$ 2.33	4/7/2008	4/7/1999	(3)		
	2,532,259			\$ 6.20	5/20/2011	5/20/2002	(4)		
	48,387			\$ 6.20	5/20/2011	5/20/2002	(4)		
Ricardo Salas		153,260		\$ 1.44	3/31/2016	3/31/2007	(1)		
		346,740		\$ 1.44	3/31/2016	3/31/2007	(1)		

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- (1) The shares underlying this option vest 20% per year starting with the vesting commencement date and thereafter.
  - (2) The shares underlying this option vest 100% immediately on grant date.
  - (3) The shares underlying this option vest 25% per year starting with the vesting commencement date and thereafter.
  - (4) The shares underlying this option vest 33% per year starting with the vesting commencement date and thereafter.

#### **Option Exercises and Stock Vested**

There were no exercise of stock options and vesting of restricted stock during 2006.

#### **Employment Agreements**

We have entered into the following employment agreements with the executive officers identified above.

Larry Buffington, who was elected as our President and Chief Executive Officer on October 8, 2006, received an initial base salary of \$200,000 for serving as President and Chief Executive Officer of our company. Effective January 1, 2007, the Compensation Committee approved an increase in the base salary to \$250,000. We and Mr. Buffington have not yet entered into an employment agreement relating to Mr. Buffington's employment with us, but we may determine to do so in the future.

Won Chung, who was elected as our Vice President of Finance on May 1, 2007, receives an initial base salary of \$125,000 for serving as principal financial and accounting officer of our company. We and Mr. Chung have not yet entered into an employment agreement relating to Mr. Chung's employment with us, but we may determine to do so in the future.

**John Kang.** On December 31, 2000, we entered into an employment agreement with John Kang that, as amended, provides for his employment as our Chief Executive Officer and President, and on August 22, 2003, Mr. Kang was named Chairman of our Board of Directors. On December 30, 2005, Mr. Kang ceased to serve as our President and Chief Executive Officer, and Mr. Kang's employment agreement has an expiration date of December 31, 2005, although the agreement automatically renews on a year-to-year basis until Mr. Kang resigns or his employment is terminated by us with or without cause. Mr. Kang receives an annual base salary equal to \$200,000 per year, and his employment will terminate upon the earlier of his death, resignation, disability, or termination by the board of directors for any reason. If we terminate Mr. Kang's employment without cause, or if Mr. Kang terminates his own employment upon a change of control of our company or for other good reason, as defined in the agreement, we are responsible for paying Mr. Kang a lump-sum cash payment equal to 200% of Mr. Kang's annual base salary plus the average cash bonus during the two full fiscal years immediately preceding the termination. Pursuant to the agreement, Mr. Kang was issued options to purchase 1,612,904 shares of our common stock at an exercise price of \$4.65 per share. The options expire on December 31, 2010 and vested immediately upon grant. In addition, Mr. Kang is prohibited, during his employment with us and for one year after he is no longer employed by us, from soliciting any of our employees or competing with us in any manner. Starting in May 2003, Mr. Kang and other members of senior management took a 10% voluntary decrease in their base salary and returned to full salary in June 2004.

#### **Equity Incentive / Equity Compensation Plans**

Our executive officers, directors, and all of our employees are allowed to participate in our equity incentive plans. We believe that providing them with the ability to participate in such plans provides them with a further incentive towards ensuring our success and accomplishing our corporate goals.



Securities authorized for issuance under equity compensation plans as of June 1, 2007 were as follows:

<b>Plan Category</b>	<b>Number of securities to be issued upon exercise of outstanding options, warrants, and rights [a]</b>	<b>Weighted-average exercise price of outstanding options, warrants, and rights [b]</b>	<b>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column [a]) [c]</b>
Equity compensation plans approved by stockholders	7,763,341	4.36	8,683,173
Equity compensation plans not approved by stockholders	13,654,996	\$ 1.62	
<b>Total</b>	<b>21,418,337</b>		<b>8,683,173</b>

Equity compensation plans not approved by stockholders consist of:

- Warrants to purchase up to 1,021,434 shares issued on June 13, 2005 with an exercise price of \$1.75 per share and an expiration date of June 13, 2010, as adjusted;
- Warrants to purchase up to 3,295,975 shares issued on August 2, 2005 with an exercise price of \$1.75 per share and an expiration date of August 2, 2010, as adjusted;
- Warrants to purchase up to 125,000 shares issued on March 17, 2006 with an exercise price of \$2.00 per share and an expiration date of March 17, 2009;
- Warrants to purchase up to 1,178,651 shares issued between May 17, 2006 and December 1, 2006 with an exercise price of \$2.13 per share and an expiration date of May 17, 2011, as adjusted;
- Warrants to purchase up to 7,657,591 shares issued on January 3, 2007 with an exercise price of \$1.55 per share and an expiration date of January 3, 2012, as amended; and
- Warrants to purchase up to 376,345 shares issued to Paul Azinger on January 1, 2001 with an exercise price of \$1.16 per share and an expiration date of January 1, 2008.

The number of securities and type of plans available for future issuance of stock options as of December 31, 2006 were as follows:

Plan Name	Options and Warrants for Common Shares			
	Authorized	Exercised	Outstanding	Available
1996 Stock Option Plan	12,903,226	1,974,365	3,225,006	
2002 Equity Incentive Plan	10,000,000		1,916,827	8,083,173
2002 Non-employee Director Stock Option Plan	1,000,000		400,000	600,000
Total Stock Options	23,903,226	1,974,365	5,541,833	8,683,173

### *1996 Stock Option Plan*

Our 1996 Stock Option Plan provides for the grant of stock options to employees, directors, and consultants of our company and its affiliates. The purpose of the plan is to retain the services of existing employees, directors, and consultants; to secure and retain the services of new employees, directors, and consultants; and to provide incentives for such persons to exert maximum efforts for our success. The plan provides for the granting to employees of incentive stock options within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended, and for the granting to employees and consultants of nonstatutory stock options. Our board of directors terminated the 1996 Stock Option Plan on April 4, 2002. The termination will not affect any outstanding options under the plan, and all such options will continue to remain outstanding and be governed by the plan.

Options granted under the 1996 Stock Option Plan are generally not transferable by the optionee except by will or the laws of descent and distribution, and each option is exercisable, during the lifetime of the optionee, only by the optionee. Options generally must be exercised within 90 days after the optionee's termination for cause, three months following the end of the optionee's status as an employee or consultant, other than for cause or for death or disability, or within six months after the optionee's termination by disability or twelve months following the optionee's termination by death. However, in no event may an option be exercised later than the earlier of the expiration of the term of the option or ten years from the date of the grant of the option or, where an optionee owns stock representing more than 10% of the voting power, five years from the date of the grant of the option in the case of incentive stock options.

As of June 1, 2007, options to purchase 3,225,006 shares of common stock were outstanding at a weighted average price of \$6.14 per share under the 1996 Stock Option Plan. As of June 1, 2007, options to purchase 1,974,365 shares had been issued upon exercise of options under the plan. There were 3,225,006 options exercisable under the 1996 Stock Option Plan as of June 1, 2007.

### *2002 Equity Incentive Plan*

Our 2002 Equity Incentive Plan, which was adopted by our board of directors and approved by our stockholders in April 2002, provides for the grant of stock options to officers, employees, consultants, and directors of our company and its subsidiaries. The purpose of the plan is to advance the interests of our stockholders by enhancing our ability to attract, retain, and motivate persons who make or are expected to make important contributions to our company and its subsidiaries by providing such persons with equity ownership opportunities and performance-based incentives, thereby better aligning their interests with those of our stockholders. The plan provides for the granting to employees of incentive stock options within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended, and for the granting to employees and consultants of nonstatutory stock options. In addition, the plan permits the granting of stock appreciation rights, or SARs, with or independently of options, as well as stock bonuses and rights to purchase restricted stock. A total of ten million shares of our common stock may be granted under the plan.

The plan is administered by our board of directors or a committee appointed by our board of directors. All members of such a committee must be a non-employee director and an outside director, as defined in the plan. Subject to the limitations set forth in the plan, the administrator has the authority to select the persons to whom grants are to be made, to designate the number of shares to be covered by each stock award, to determine whether an option is to be an incentive stock option or a nonstatutory stock option, to establish vesting schedules, to specify the option exercise price and the type of consideration to be paid upon exercise, and, subject to some restrictions, to specify other terms of stock awards.

The administrator establishes the option exercise price, which in the case of incentive stock options, must be at least the fair market value of the common stock on the date of the grant or, with respect to optionees who own at least 10% of our outstanding common stock, 110% of fair market value. If our common stock is listed and traded on a registered national or regional securities exchange, or quoted on the National Association of Securities Dealers Automated Quotation System, fair market value is the average closing price of a share of our common stock on such exchange or quotation system for the five trading days prior to the date of grant. If our common stock is not traded on a registered securities exchange or quoted in such a quotation system, fair market value is determined in good faith by the administrator.

Options granted under the plan are generally not transferable by the optionee except by will or the laws of descent and distribution, and to certain related individuals with the consent of the administrator. Options generally must be exercised within three months after the optionee's termination of employment for any reason other than disability or death, or within 12 months after the optionee's termination by disability. Options granted under the plan vest at the rate specified in the option agreement. However, in no event may an option be exercised later than the earlier of the expiration of the term of the option or 10 years from the date of the grant of the option, or when an optionee owns stock representing more than 10% of the voting power, five years from the date of the grant of the option in the case of incentive stock options.

Any incentive stock options granted to an optionee which, when combined with all other incentive stock options becoming exercisable for the first time in any calendar year that are held by that person, would have an aggregate fair market value in excess of \$0.1 million, shall automatically be treated as nonstatutory stock options.

The plan may be amended, altered, suspended or terminated by our board of directors at any time, but no such amendment, alteration, suspension or termination may adversely affect the terms of any option previously granted without the consent of the affected optionee. Unless terminated sooner, the plan will terminate automatically in September 2012. As of June 1, 2007, there were 1,916,827 outstanding options or stock awards at a weighted average price of \$2.49 under the plan. There were 1,051,564 options exercisable under the 2002 Equity Incentive Plan as of June 1, 2007.

In September 2005, the non-employee directors of our company were given the opportunity to receive shares of stock under the plan in lieu of past-due director and committee fees that were due to them for periods through September 30, 2005. Such shares were issuable to such directors at an average price of \$1.89 per share. As of December 31, 2005, a total of 92,219 shares were issued to non-employee directors in lieu of these past-due fees.

In February 2006, the non-employee directors of our company were given the opportunity to receive shares of stock under the plan in lieu of director and committee fees that were due for fiscal year 2006. Such shares were issuable to such directors at an average price of \$0.88 per share, the effective closing price of our stock on January 1, 2006 when the fees became due. In April 2006, we issued a total of 99,432 shares to non-employee directors in lieu of these fees.

In March 2006, one of the former non-employee directors of our company, Vincent Addonisio, was given the opportunity to receive shares of stock under the plan in lieu of past-due director and committee fees that were due to him for periods through December 31, 2005 at an average price of \$1.50. We issued a total of 10,000 shares at an average price of \$1.50 in March 2006.

In April 2006, the non-employee directors of our company were given the opportunity to receive shares of stock under the plan in lieu of past-due director and committee fees that were due to them for director fees for fiscal year 2006 due to them as of January 1, 2006. Such shares were issuable to such directors at an average price of \$0.88 per share. In April 2006, a total of 109,437 shares were issued to non-employee directors in lieu of these past-due fees.

In May 2006, our former President and Chief Operating Officer, Ricardo Salas, was given the opportunity to receive shares of stock under the plan in lieu of past-due salaries and fees that were due to him for services rendered through March 31, 2006. Such shares were issuable to Mr. Salas at an average price of \$1.41 per share. In May 2006, a total of 28,960 shares were issued to Mr. Salas in lieu of these past-due salaries and fees.

#### ***2002 Non-employee Director Stock Option Plan***

Our 2002 Non-employee Director Stock Option Plan was adopted by our board of directors and by our stockholders in April 2002. We have reserved a total of one million shares of our common stock for issuance under the plan. The option grants under the plan are automatic and nondiscretionary, and the exercise price of the options is equal to 100% of the fair market value of our common stock on the grant date.

Only non-employee directors are eligible for grants under the plan. The plan will provide for an initial grant to a new non-employee director of an option to purchase 50,000 shares of our common stock. Subsequent to the initial grants, each non-employee director will be automatically granted on the first business day of January commencing January 1, 2003, an option to purchase 10,000 shares of our common stock.

The term of the options granted under the plan is 10 years, but the options expire 12 months after the termination of the optionee's status as a director or three months if the termination is due to the voluntary resignation of the optionee. The option grants will vest and become exercisable as to one-fifth of the shares on the date that is one year after the date of grant and an additional one-fifth of the shares subject to the option on a cumulative basis will vest and become exercisable annually thereafter.

As of June 1, 2007, options to purchase 400,000 shares of common stock were outstanding at a weighted average price of \$2.05 per share under the 2002 Non-employee Director Stock Option Plan. There were 54,000 options exercisable under the 2002 Non-employee Director Stock Option Plan as of June 1, 2007.

The plan will terminate in October 2012, unless our board of directors terminates it sooner.

#### ***401(k) Savings Plan***

We have adopted a tax-qualified employee savings and retirement plan, or 401(k) plan, that covers all of our employees. Pursuant to our 401(k) plan, participants may elect to reduce their current compensation, on a pre-tax basis, by up to 15% of their taxable compensation or of the statutorily prescribed annual limit, whichever is lower, and have the amount of the reduction contributed to the 401(k) plan. The 401(k) plan permits us, in our sole discretion, to make additional employer contributions to the 401(k) plan. However, we do not currently make employer contributions to the 401(k) plan and may not do so in the future. As such, contributions by employees or by us to the 401(k) plan, and the income earned on plan contributions, are not taxable to employees until withdrawn from the 401(k) plan, and we can deduct our contributions, if any, at the time they are made.

#### **Pension Benefits**

We do not sponsor any qualified or non-qualified defined benefit plans.

#### **Nonqualified Deferred Compensation**

We do not maintain any non-qualified defined contribution or deferred compensation plans. The compensation committee, which is comprised solely of outside directors as defined for purposes of Section 162(m) of the Code, may elect to provide our officers and other employees with non-qualified defined contribution or deferred compensation benefits if the compensation committee determines that doing so is in our best interests. We sponsor a tax qualified defined contribution 401(k) savings plan.



**Disclosure Regarding Termination and Change Control Provisions**

Potential payments payable to our executive officers upon termination of employment following a change in control of us is discussed under Employment Agreements . The compensation committee of our board of directors may, at their discretion, amend or add benefits to these arrangements as they deem advisable.

**Director Compensation**

The following table sets forth information regarding the compensation received by each of our directors during the year ended December 31, 2006;

Name	Fees Earned or Paid in Cash	Stock Awards	Option Awards (1)	Non-Equity Incentive Plan Compensation	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compensation	Total
John Kang			(2)				
William Johnson			\$ 5,469 (3)				\$ 5,469
Dean Tanella	\$ 75,000		\$ 16,388 (4)				\$ 91,388
Robert Biehl			\$ 5,469 (5)			\$ 47,500 (8)	\$ 52,969
CK Cho			\$ 5,469 (6)			\$ 76,365 (9)	\$ 81,834
Patrick Caruana	\$ 1,667		\$ 60,867 (7)				\$ 62,534

(1) Amounts represent the expensed fair value of stock options granted in 2006 under SFAS 123(R) as discussed in Note 15, Stock Compensation Plan , to our consolidated financial statements included in our annual report on Form 10K filed with the SEC on March 16, 2007.

(2) 1,662,904 shares of options were outstanding as of December 31, 2006.

(3) 70,000 shares of options were outstanding as of December 31, 2006.

(4) 90,000 shares of options were outstanding as of December 31, 2006.

(5) 60,000 shares of options were outstanding as of December 31, 2006.

(6) 60,000 shares of options were outstanding as of December 31, 2006.

- (7) 50,000 shares of options were outstanding as of December 31, 2006.
- (8) Amount represents shares of stock issued in lieu of cash payment.
- (9) Amount represents \$20,639 of automobile lease payments, \$15,726 of purchases made using company credit card, and \$40,000 shares of stock issued in lieu of cash payment.

Our non-employee directors receive an annual fee of \$10,000 for their service to our board and are reimbursed for expenses incurred in attending board and committee meetings. Non-employee directors are also entitled to receive a \$10,000 annual cash stipend for each standing board committee (excluding the Audit Committee) on which the director serves. For Audit Committee service, the Audit Committee chairman is entitled to a \$35,000 annual stipend, and the other members of the Audit Committee are entitled to a \$27,500 annual stipend. In addition to the annual stipends, each non-employee director is entitled to receive a per-meeting fee of \$1,000 for each meeting of the board of directors or any board committee attended in person. Effective December 30, 2005, Dean Tanella was elected as the lead independent director of our company. The lead independent director is entitled to a \$30,000 annual stipend.

We also have a 2002 Non-employee Director Stock Option Plan pursuant to which our non-employee directors are entitled to receive stock options. Under this plan, when a director is first elected or appointed to our board of directors, the non-employee director is entitled to receive an initial stock option grant to purchase 50,000 shares of our common stock. Thereafter, on the first business day of January of each year in which the director continues to serve as a member of our board, the director is entitled to an annual stock option grant to purchase 10,000 shares of our common stock. All options granted under the plan have an exercise price equal to the fair market value of our common stock on the date of the grant. These stock options have a 10-year term, vest, and are exercisable pursuant to an equal 5-year vesting schedule, and remain exercisable for certain periods of time after a person is no longer a director.

No director who is an employee will receive separate compensation for services rendered as a director. However, our employee directors are eligible to participate in our 2002 Equity Incentive Plan.

**PRINCIPAL STOCKHOLDERS**

The following table sets forth certain information regarding the beneficial ownership of our common stock as of June 1, 2007 by:

- each person known by us to be a beneficial owner of more than 5.0% of our outstanding common stock;
- each of our directors;
- each of our named executive officers; and
- all directors and executive officers as a group.

The number and percentage of shares beneficially owned is determined under rules of the SEC and the information is not necessarily indicative of beneficial ownership for any other purpose. Under such rules, beneficial ownership includes any shares as to which the individual has sole or shared voting power or investment power and also any shares which the individual has the right to acquire beneficial ownership of within 60 days of June 1, 2007 through the exercise of any stock option or other right. Unless otherwise indicated in the footnotes, each person has sole voting and investment power with respect to the shares shown as beneficially owned. A total of 44,631,768 shares of our common stock were issued and outstanding as of June 1, 2007. Unless otherwise indicated, the address of all directors and named executive officers is 30452 Esperanza, Rancho Santa Margarita, California 92688.

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Name of Beneficial Owner	Shares	Percent of Class	
<b>5% Stockholders</b>			
Tjoa Thian Song(1) 16 Raffles Quay #B1-14A Hong Leong Building Singapore 0101	4,008,523	9	%
Jack Chitayat(2) 1133 Park Avenue, Suite 1W New York, NY 10128	2,669,289	6	%
James Kang(3) Hyundai Hyperion Apt. 101-403 Youngsan-Gu, Hannam-Dong Seoul, Korea	6,164,322	14	%
<b>Directors and Named Executive Officers</b>			
John Kang(4)	5,084,973	11	%
William Johnson(5)	1,176,650	3	%
Dean Tanella(6)	67,620	*	
Robert Biehl(7)	116,059	*	
CK Cho(8)	1,214,192	3	%
Patrick Caruana(9)			
Won Chung(10)	15,000	*	
All directors and executive officers as a group (7 persons)	7,674,494	17	%

\* Less than one percent.

(1) 3,874,585 of these shares are held of record by a revocable grantor trust established by Mr. Tjoa for himself and his family members. Mr. Tjoa continues to beneficially own all such shares.

(2) Includes 125,000 shares issuable pursuant to currently exercisable warrants held by Atlantic Realty Group, Inc., a company controlled by Mr. Chitayat, and 91,792 shares held of record by a trust established by Mr. Chitayat for his family members. Mr. Chitayat continues to beneficially own all such shares.

(3) Also includes 2,877,420 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of June 1, 2007 and includes 969 shares held by James Kang's minor children. Does not include the 1,700,000 shares that Mr. Kang has agreed to personally purchase on October 31, 2006 from Innometal Co., Ltd. as an inducement for Innometal to enter into a Settlement Agreement with us. Innometal agreed to accept these shares in full satisfaction of all of our obligations to them under January 2004 settlement agreement.

(4) As of August 22, 2003, John Kang was named Chairman of our board of directors. Mr. Kang resigned from his position as President and Chief Executive Officer of our company on December 30, 2005. However, he continues to serve as Chairman of the Board and continues to work for our company on a full-time basis. The beneficial shares include:

(a) 1,632,904 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of June 1, 2007. Does not include 30,000 shares that are issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of June 1, 2007; and

(b) 152,400 shares held by Mr. Kang's minor children.

(5) Includes 26,000 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of June 1, 2007. Does not include 54,000 shares that are issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of June 1, 2007.

(6) Includes 16,130 shares held by Mr. Tanella's investment firm, HarborLight Diversified Fund, LP. Also, includes 2,890 shares held by Mr. Tanella's family. Includes 40,000 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of June 1, 2007. Does not include 80,000 shares that are issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of June 1, 2007.

(7) Includes 22,000 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of June 1, 2007. Does not include 48,000 shares that are issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of June 1, 2007.

(8) Includes 304,072 shares issuable pursuant to currently exercisable warrants and 646,522 shares issuable pursuant to currently convertible notes. Also, includes 22,000 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of June 1, 2007. Does not include 48,000 shares that are issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of June 1, 2007.

(9) Mr. Caruana holds 60,000 shares issuable pursuant to outstanding stock options, none of which are exercisable currently or within 60 days of June 1, 2007.

(10) Includes 15,000 shares issuable pursuant to outstanding stock options exercisable currently or within 60 days of June 1, 2007. Does not include 27,500 shares that are issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of June 1, 2007.

## DESCRIPTION OF CAPITAL STOCK

### General

We are authorized to issue up to 100,000,000 shares of common stock, par value \$0.001 per share, of which 44,631,768 shares were issued and outstanding as of June 1, 2007. We are also authorized to issue up to 10,000,000 shares of preferred stock, par value \$0.001 per share, of which no shares were issued and outstanding as of June 1, 2007.

### Common Stock

The holders of our common stock are entitled to one vote per share on all matters to be voted upon by the stockholders. Subject to preferences that may be applicable to any outstanding preferred stock, the holders of common stock are entitled to receive ratably any dividends that may be declared from time to time by the board of directors out of funds legally available for that purpose. In the event of our liquidation, dissolution or winding up, the holders of common stock are entitled to share ratably in all assets remaining after payment of liabilities, subject to prior distribution rights of preferred stock then outstanding. The common stock has no preemptive or conversion rights or other subscription rights. There are no redemption or sinking fund provisions applicable to the common stock. All outstanding shares of common stock are fully paid and nonassessable, and the shares of common stock to be issued upon the closing of this offering will be fully paid and nonassessable.

### Preferred Stock

Our board of directors has the authority, without action by our stockholders, to designate and issue up to 10,000,000 shares of preferred stock in one or more series. The board of directors may also designate the rights, preferences, and privileges of each series of preferred stock, any or all of which may be greater than the rights of the common stock. It is not possible to state the actual effect of the issuance of any shares of preferred stock upon the rights of holders of the common stock until the board of directors determines the specific rights of the holders of the preferred stock. However, these effects might include restricting dividends on the common stock; diluting the voting power of the common stock; impairing the liquidation rights of the common stock; and delaying or preventing a change in control of our company without further action by the stockholders. We have no present plans to issue any shares of preferred stock.

### Convertible Notes

As of June 1, 2007, we had convertible promissory notes outstanding in the aggregate principal amount of \$25.6 million. The notes consist of \$2.1 million in aggregate principal amount of 6% Senior Secured Notes Due July 2007 (the July 2007 Notes), \$7.2 million in aggregate principal amount of 7% Senior Secured Convertible Notes due August 2007 (the August 2007 Notes), and \$16.3 million in aggregate principal amount of 8% Convertible Subordinated Notes due January 2010 (the January 2010 Notes).

The July 2007 Notes were issued in a private placement on July 29, 2004 and have a maturity date of July 29, 2007. The July 2007 Notes are convertible into shares of our common stock at a conversion price of \$1.00 per share, subject to specified anti-dilution adjustments. Under the July 2007 Notes, the noteholders have the right to call for repayment of such notes prior to maturity at any time after the second anniversary of the date of the issuance of the notes. The July 2007 Notes bear interest at a rate equal to 6% per annum, with interest being payable in cash on a quarterly basis.

The August 2007 Notes were issued in a private placement on August 2, 2005. In February 2007, we entered into conversion agreements with the holders of \$0.4 million in principal and accrued interest of the August 2007 Notes providing for the conversion of such notes at a reduced conversion price of \$1.25 per share.

The January 2010 Notes have a maturity date of January 3, 2010. The January 2010 Notes are convertible into shares of our common stock at a conversion price of \$1.10 per share, subject to specified anti-dilution adjustments. The January 2010 Notes bear interest at 8% per annum with interest payable quarterly in arrears in cash, or, at our option and subject to specified conditions, in the form of additional January 2010 Notes (in which case the interest rate will be 10% per annum).

### **Warrants and Special Stock Option**

As of June 1, 2007, we had warrants outstanding to purchase up to 13,278,651 shares of our common stock issued to investors and placement agents in several private placement transactions occurring between 2005 and 2007. Of these warrants:

- Warrants to purchase up to 1,021,434 shares were issued on June 13, 2005 and had an exercise price of \$1.75 per share as of June 1, 2007 (these warrants expire on June 13, 2010), as adjusted;
- Warrants to purchase up to 3,295,975 shares were issued on August 2, 2005 and had an exercise price of \$1.75 per share as of June 1, 2007 (these warrants expire on August 2, 2010), as adjusted;
- Warrants to purchase an aggregate amount of up to 125,000 shares of common stock were issued on March 17, 2006 and had an exercise price of \$2.00 per share as of June 1, 2007 (these warrants expire on March 17, 2009), as adjusted;
- Warrants to purchase an aggregate amount of up to 1,178,651 shares of common stock were issued on May 17, September 21, October 24, and December 1, 2006 and had an exercise price of \$2.13 per share as of June 1, 2007 (these warrants expire on May 17, 2011), as adjusted; and
- Warrants to purchase an aggregate amount of up to 7,657,591 shares of common stock were issued on January 3, 2007 and had an exercise price of \$1.55 per share as of June 1, 2007 (these warrants expire on January 3, 2012), as amended;

In addition to the above-described warrants, on January 1, 2001, we granted Paul Azinger, a professional golf player, a non-qualified stock option to purchase up to 1,021,507 shares of our common stock at an exercise price of \$1.16 per share. This option was granted to Mr. Azinger in consideration of Mr. Azinger entering into an endorsement agreement with our Liquidmetal Golf subsidiary, although the endorsement agreement was terminated effective January 1, 2003. As a result of the termination of the endorsement agreement, Mr. Azinger's option immediately vested as to 376,345 shares upon such termination, and the option was terminated as to the remaining shares. This stock option will expire on January 1, 2008, and as of June 1, 2007, no portion of this option has been exercised.

### **Anti-Dilution Provisions in Notes and Warrants**

Our convertible notes and warrants issued prior to January 2007 contain weighted-average anti-dilution provisions whereby, if we issue shares in the future for consideration below the conversion or exercise prices or such notes or warrants, then (with certain exceptions, including the issuance of stock options) the conversion price for our convertible notes would automatically be reduced (allowing the holders of the notes to receive additional shares of common stock upon conversion) and the exercise price of the warrants would automatically be reduced. The amount of the reduction would be equal to a portion of the difference between the conversion price of the notes and exercise price of the warrants, on the one hand, and the lower price at which the common stock was, or could effectively be acquired, in the subsequent transaction. The percentage by which the conversion price and exercise price could be reduced depends not only on the lower price at which our common stock was, or could be, acquired in the subsequent transaction, but also by the ratio that the number of shares of our common stock that were, or could be, acquired in such transaction bears to the total number of shares of our common stock that would be outstanding after such subsequent transaction.

In addition, under the January 2010 Notes (issued on January 3, 2007), if we issue or grant in the future any rights to purchase any of our common stock, or other security convertible into our common stock, for an effective per share price less than the conversion price then in effect, the conversion price of all unconverted January 2010 Notes will be decreased to equal such lower price, provided that such adjustment will not apply to certain exempt issuances, including stock issuances pursuant to employee stock option plans and strategic transactions. With regard to the warrants issued in connection with the January 2010 Notes, if we, in the future, issue or grant any rights to purchase any of our common stock, or other security convertible into our common stock, for a per share price less than the conversion price of the January 2010 Notes then in effect, the exercise price of the





warrants will be reduced to equal such lower price and the number of shares of our common stock for which the warrants may be exercised will be increased so that the total aggregate exercise price remains constant. The foregoing adjustment to the exercise price of the warrants will not apply to certain exempt issuances, including issuances pursuant to employee stock option plans and strategic transactions.

If our available funds and cash generated from operations are insufficient to satisfy our liquidity requirements in the future, then we may need to raise substantial additional funds in the future to support our working capital requirements and for other purposes. If shares of our common stock or securities convertible into or exercisable for our common stock are issued in consideration of such funds at an effective per share price lower than the conversion and exercise prices of our convertible notes and warrants, then these anti-dilution provisions would be triggered, thus possibly causing substantial dilution to our then-existing stockholders if the notes are converted or the warrants are exercised. Further, subsequent sales of the shares in the public market could depress the market price of our stock by creating an excess in supply of shares for sale.

### **Registration Rights**

On August 2, 2005, we entered into an amended and restated registration rights agreement with the holders of the July 2007 Notes, the holders of the August 2007 Notes, and the holders of the outstanding warrants issued in connection with the private placement of the July 2007 Notes and August 2007 Notes. This amended and restated registration rights agreement replaced all other registration rights agreements previously entered into by us in connection with the private sale by us of convertible notes and warrants. Under the amended and restated registration rights agreement, we were required to file a resale registration statement for the shares underlying all of our outstanding convertible notes and warrants, as described above, by October 31, 2005, to enable the resale of such shares by the selling stockholders on a delayed or continuous basis under Rule 415 of the Securities Act. We were then required to cause such registration statement to become effective within 60 days after we received the first written comments on the registration statement from the SEC, or if the SEC notified us that it would not review the registration statement, within five days after such notification. We were subject to certain monetary penalties, as set forth in the registration rights agreement, because the registration statement was not filed and did not become effective on a timely basis. Specifically, because we did not file the registration statement on a timely basis, we were obligated to pay a late filing fee to the selling stockholders in the amount of 3% of the warrant exercise price on each of the warrants held by them plus 3% of the principal amount of the outstanding notes held by them. This fee was payable for each period of 30 business days that the filing of the registration statement was made past the required filing date, and the payments were due 10 business days following the end of each 30-day period. Because the registration statement was not declared effective by the required effective date, we were obligated to pay a monthly late registration fee to the selling stockholders in the amount of 2% of the aggregate warrant exercise prices and aggregate note principal amounts for the first 30 business days after the required effective date, and 1% for each 30-business day period thereafter until the registration statement was declared effective. Notwithstanding the foregoing, the late filing fees and late registration fees could not and did not exceed 18% of the aggregate warrant exercise prices and aggregate note principal amounts.

We filed our Registration Statement on December 9, 2005 and on August 7, 2006, the registration statement became effective. As of March 31, 2007, we have accrued \$1.6 million and paid \$0.9 million of the late filing and registration fees. As of March 31, 2007, \$7.2 million in aggregate principal amount of August 2007 Notes was still outstanding with accrued but unpaid interest in the amount of approximately \$129 thousand. In addition, \$2.1 million in aggregate principal amount of July 2007 Notes was also outstanding with accrued but unpaid interest in the amount of approximately \$31 thousand.

On May 17, 2006, we entered into a registration rights agreement with the holders of the warrants issued in connection with a private placement of 8% Unsecured Subordinated Notes due August 17, 2007 relating to the resale of the shares of our common stock issuable upon exercise of such warrants. Under the registration rights agreement, we must file a registration statement with the Securities and Exchange Commission covering the resale of the shares issuable under the warrants, if, following the 180th day after the date of the registration rights agreement, we receive a written request to do so from the holders of fifty percent or more of the warrants then outstanding. The warrant holders also have piggyback registration rights under the registration rights agreement, which requires us to register, upon request by a warrant holder, the shares issuable upon exercise of such warrants in any registration statement filed in connection with the public offering of the our common stock.

On January 3, 2007, we entered into a registration rights agreement with the holders of the January 2010 Notes and warrants issued in connection with the private placement of January 2010 Notes, under which we are required, on or before 45 days after the closing of the private placement, to file a registration statement with the SEC covering the resale of the shares of our



common stock issuable pursuant to the January 2010 Notes and warrants and to use our best efforts to have the registration declared effective at the earliest date (but in no event later than 90 days after filing if there is no SEC review of the registration statement, or 120 days if there is an SEC review). We will be subject to certain monetary penalties, as set forth in the Registration Rights Agreement, up to a maximum amount of 18% of the aggregate amount of Notes sold in the Private Placement if the registration statement is not filed or does not become effective on a timely basis. The monetary penalties will accrue at the rate of 1% per month of the then-outstanding principal amount of the January 2010 Notes. In the event that we are unable to include in the registration statement all shares of our common stock issuable pursuant to the January 2010 Notes and warrants, then we will be required to file up to two additional registration statements to register the resale of any shares excluded from the originally filed registration statement and to pay the foregoing monetary penalties on the January 2010 Notes convertible into the excluded shares until the resale of such excluded shares is covered by an effective registration statement or until such shares can be sold under SEC Rule 144.

All of the above registration rights are subject to conditions and limitations, among them the right of the underwriters of any offering to limit the number of shares of common stock held by these security holders to be included in the registration. We are generally required to bear all of the expenses of all registrations, except underwriting discounts and selling commissions. Registration of the shares of common stock held by security holders with registration rights would result in these shares becoming freely tradeable without restriction under the Securities Act of 1933 immediately upon effectiveness of this registration. Other than the above-described registration rights, we have not granted any registration rights with respect to any shares of our capital stock.

### **Stock Options**

As of June 1, 2007, we had stock options outstanding under our equity incentive plans to purchase up to 7,028,414 shares of our common stock. Of these options, options to purchase 5,873,151 shares of common stock were exercisable at June 1, 2007 at a weighted-average exercise price of \$5.15 per share.

### **Anti-Takeover Effect**

Provisions of Delaware law and our certificate of incorporation and amended bylaws could make the acquisition of our company through a tender offer, a proxy contest or other means more difficult and could make the removal of incumbent officers and directors more difficult. We expect these provisions to discourage coercive takeover practices and inadequate takeover bids and to encourage persons seeking to acquire control of our company to first negotiate with our board of directors. We believe that the benefits provided by our ability to negotiate with the proponent of an unfriendly or unsolicited proposal outweigh the disadvantages of discouraging these proposals. We believe the negotiation of an unfriendly or unsolicited proposal could result in an improvement of its terms.

*Delaware Law.* Upon the closing of this offering, we will be subject to Section 203 of the Delaware General Corporation Law, an anti-takeover law. In general, Section 203 prohibits a publicly held Delaware corporation from engaging in a business combination with an interested stockholder for a period of three years following the date the person became an interested stockholder, unless:

- prior to the date of the transaction, the board of directors of the corporation approved either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder;
- the stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the number of shares outstanding (a) shares owned by persons who are directors and also officers, and (b) shares owned by employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer; or
- on or subsequent to the date of the transaction, the business combination is approved by the board and authorized at an annual or special meeting of stockholders, and not by written consent, by the affirmative vote of at least 66% of the outstanding voting stock which is not owned by the interested stockholder.



Generally, a business combination for these purposes includes a merger, asset or stock sale, or other transaction resulting in a financial benefit to the interested stockholder. An interested stockholder for these purposes is a person who, together with affiliates and associates, owns or, within three years prior to the determination of interested stockholder status, did own 15% or more of a corporation's outstanding voting securities. We expect the existence of this provision to have an anti-takeover effect with respect to transactions our board of directors does not approve in advance. We also anticipate that Section 203 may also discourage attempts that might result in a premium over the market price for the shares of common stock held by stockholders.

*Certificate of Incorporation and Bylaw Provisions.* Our certificate of incorporation to be in effect provides for our board of directors to be divided into three classes serving staggered terms. Approximately one-third of the board of directors will be elected each year. The provision for a classified board could prevent a party who acquires control of a majority of the outstanding voting stock from obtaining control of the board of directors until the second annual stockholders meeting following the date the acquiring party obtains the controlling stock interest. The classified board provision could discourage a potential acquiror from making a tender offer or otherwise attempting to obtain control of our company and could increase the likelihood that incumbent directors will retain their positions. Our bylaws also provides that directors may be removed with cause by the affirmative vote of the holders of the outstanding shares of common stock.

Our bylaws establish an advance notice procedure for stockholder proposals to be brought before an annual meeting of our stockholders, including proposed nominations of persons for election to the board of directors. At an annual meeting, stockholders may only consider proposals or nominations specified in the notice of meeting or brought before the meeting by or at the direction of the board of directors. Stockholders may also consider a proposal or nomination by a person who was a stockholder of record on the record date for the meeting, who is entitled to vote at the meeting and who has given to our Secretary timely written notice, in proper form, of his or her intention to bring that business before the meeting. The bylaws do not give the board of directors the power to approve or disapprove stockholder nominations of candidates or proposals regarding other business to be conducted at a special or annual meeting of the stockholders. However, our bylaws may have the effect of precluding the conduct of business at a meeting if the proper procedures are not followed. These provisions may also discourage or deter a potential acquirer from conducting a solicitation of proxies to elect the acquirer's own slate of directors or otherwise attempting to obtain control of our company.

Under Delaware law, a special meeting of stockholders may be called by the board of directors or by any other person authorized to do so in the certificate of incorporation or the bylaws. Our certificate of incorporation authorizes a majority of our board of directors to call a special meeting of stockholders, and it requires the President or Secretary to call a special meeting upon the written request of stockholders who own an aggregate of least 25% of the outstanding shares of voting stock. Because our stockholders owning less than an aggregate of 25% of our voting stock do not have the right to call a special meeting, such stockholders could not force stockholder consideration of a proposal over the opposition of the board of directors by calling a special meeting of stockholders prior to such time as a majority of the board of directors believed or the chief executive officer believed the matter should be considered or until the next annual meeting provided that the requestor met the notice requirements. The restriction on the ability of stockholders to call a special meeting means that a proposal to replace the board also could be delayed until the next annual meeting.

#### **Transfer Agent and Registrar**

The Transfer Agent and Registrar for the common stock is American Stock Transfer & Trust Company, New York, New York.

### PLAN OF DISTRIBUTION

The selling stockholders and any of their pledgees, donees, assignees and successors-in-interest may, from time to time, sell any or all of their shares of common stock registered hereunder on any stock exchange, market or trading facility on which the shares are traded or in private transactions. These sales may be at fixed or negotiated prices. The selling stockholders may use any one or more of the following methods when selling shares:

- ordinary brokerage transactions and transactions in which the broker-dealer solicits investors;
- block trades in which the broker-dealer will attempt to sell the shares as agent but may position and resell a portion of the block as principal to facilitate the transaction;
- purchases by a broker-dealer as principal and resale by the broker-dealer for its account;
- an exchange distribution in accordance with the rules of the applicable exchange;
- pledge, hypothecation, or assignment of shares;
- privately negotiated transactions;
- settlement of short sales (other than short sales established prior to the effectiveness of the registration statement to which this prospectus is a part);
- broker-dealers may agree with the selling stockholders to sell a specified number of such shares at a stipulated price per share;
- a combination of any such methods of sale; and
- any other method permitted pursuant to applicable law.

The selling stockholders may also sell shares under Rule 144 under the Securities Act of 1933 (the Securities Act ), if available, rather than under this prospectus.

Broker-dealers engaged by the selling stockholders may arrange for other brokers-dealers to participate in sales. Broker-dealers may receive commissions or discounts from the selling stockholders (or, if any broker-dealer acts as agent for the purchaser of shares, from the purchaser) in amounts to be negotiated. The selling stockholders do not expect these commissions and discounts to exceed what is customary in the types of transactions involved.

The selling stockholders may from time to time pledge or grant a security interest in some or all of their shares of common stock that are covered by this prospectus and, if they default in the performance of their secured obligations, the pledgees or secured parties may offer and sell such shares of common stock from time to time under this prospectus, or under an amendment to this prospectus under Rule 424(b)(3) or other applicable provision of the Securities Act amending the list of selling stockholders to include the pledgee, transferee or other successors in interest as selling stockholders under this prospectus.

Upon our company being notified in writing by a selling stockholder that any material arrangement has been entered into with a broker-dealer for the sale of common stock through a block trade, special offering, exchange distribution or secondary distribution or a purchase by a broker or dealer, a supplement to this prospectus will be filed, if required, pursuant to Rule 424(b) under the Securities Act, disclosing (i) the name of each such selling stockholder and of the participating broker-dealer(s), (ii) the number of shares involved, (iii) the price at which such the shares of common stock were sold, (iv) the commissions paid or discounts or concessions allowed to such broker-dealer(s), where applicable, (v) that such broker-dealer(s) did not conduct any investigation to verify the information set out or incorporated by reference in this prospectus, and (vi) other facts material to the transaction. In addition, upon our company being notified in writing by a selling stockholder that a donee or pledgee intends to sell more than 500 shares of common stock, a supplement to this prospectus will be filed if then required in accordance with applicable securities law.



The selling stockholders also may transfer the shares of common stock in other circumstances, in which case the transferees, pledgees or other successors in interest may be the selling beneficial owners for purposes of this prospectus.

The selling stockholders and any broker-dealers or agents that are involved in selling the shares may be deemed to be underwriters within the meaning of the Securities Act in connection with such sales. In such event, any commissions received by such broker-dealers or agents and any profit on the resale of the shares purchased by them may be deemed to be underwriting commissions or discounts under the Securities Act. Discounts, concessions, commissions and similar selling expenses, if any, that can be attributed to the sale of securities will be paid by the selling stockholder and/or the purchasers. Each selling stockholder has represented and warranted to us that it acquired the securities subject to this registration statement in the ordinary course of such selling stockholder's business and, at the time of its purchase of such securities such selling stockholder had no agreements or understandings, directly or indirectly, with any person to distribute any such securities.

We are required to pay our fees and expenses incident to the registration of the shares. We have agreed to indemnify the selling stockholders against certain losses, claims, damages and liabilities, including liabilities under the Securities Act.

We have advised each selling stockholder that it may not use shares registered on this registration statement to cover short sales of common stock made prior to the date on which this registration statement shall have been declared effective by the SEC. If a selling stockholder uses this prospectus for any sale of the common stock, it will be subject to the prospectus delivery requirements of the Securities Act. The selling stockholders will be responsible to comply with the applicable provisions of the Securities Act and Exchange Act, and the rules and regulations thereunder promulgated, including, without limitation, Regulation M, as applicable to such selling stockholders in connection with resales of their respective shares under this registration statement.



## CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

In June 2003, we entered into an exclusive, ten-year license agreement with LLPG, Inc. ( LLPG ), a corporation headed by, Jack Chitayat, a former director of our company. Under the terms of the agreement, LLPG has the right to commercialize Liquidmetal alloys, particularly precious-metal based compositions, in jewelry and high-end luxury product markets. Our company, in turn, will receive royalty payments over the life of the contract on all Liquidmetal products produced and sold by LLPG. In conjunction with its technology licensing contract, LLPG purchased two proprietary Liquidmetal alloy melting machines and three proprietary Liquidmetal alloy casting machines for a total purchase price of \$2.0 million. We recognized \$0.1 million of revenues as minimum royalty fees under the license agreement during the year ended December 31, 2006.

In December 2006, we entered into an amended the license agreement with LLPG, which extends the license agreement to fifteen years at reduced royalty rates. Additionally, the amended license agreement includes a \$0.4 million termination fee to be paid out in quarterly installments in 2007. The termination fee will be recognized as revenue when received in 2007. There were no revenues recognized under the licensing agreement during the three months ended March 31, 2007.

We have a license agreement with California Institute of Technology ( Caltech ) under which we exclusively license from Caltech certain inventions and technology relating to amorphous alloys. Professor William Johnson, a member of our board of directors, is a professor at Caltech, and substantially all of the amorphous alloy technology licensed to us under the Caltech license agreement was developed in Professor Johnson's Caltech laboratory. Additionally, we reimburse Caltech for laboratory expenses incurred by Professor Johnson's Caltech laboratory, which during the three months ended March 31, 2007 and 2006 amounted to \$0 and \$30 thousand, respectively and for the years ended December 31, 2006, 2005 and 2004, amounted to \$0.1 million and \$20 thousand, respectively.

Additionally, we are a party to a consulting agreement with Mr. Johnson. Under this agreement, Mr. Johnson provides consulting services on an as-needed basis through 2004 as it relates to marketing and development Liquidmetal alloy. During 2005, the agreement continued on a month to month basis. In April 2006, we entered into an agreement with Mr. Johnson effective from January 1, 2006 through December 31, 2006. During the three months ended March 31, 2007 and 2006, we incurred \$16 thousand and \$15 thousand, respectively, in consulting fees from Mr. Johnson. During the years ended December 31, 2006, 2005 and 2004, we incurred \$0.1 million, \$15 thousand, and \$0.1 million, respectively, in consulting fees from Mr. Johnson.

We are a party to a consulting agreement with Chitnis Consulting, Inc., which is owned 100% by Shekhar Chitnis, a former director and executive officer of our company. Under this agreement, we engaged Chitnis Consulting to provide consulting services on an as-needed basis through December 31, 2005. On January 1, 2006, the term of the agreement was extended to December 31, 2006 and on January 1, 2007, the term of the agreement was once again extended to December 31, 2007. During the three months ended March 31, 2007 and 2006, we incurred \$0 in consulting fees from Chitnis Consulting for both periods. During the years ended December 31, 2006, 2005 and 2004, we incurred \$0, \$0.1 million and \$0.1 million in consulting fees from Chitnis Consulting, respectively.

Soo Buchanan, the sister of John Kang and James Kang, was employed by us and was paid aggregate compensation of approximately \$0 and \$0.1 million as of December 31, 2006 and 2005, respectively. Effective, July 31, 2005, Ms. Buchanan was terminated as an employee and began providing services to us as a consultant. For the three months ended March 31, 2007 and 2006, we incurred \$4 thousand and \$24 thousand for her services as consultant. During 2006, 2005 and 2004, we incurred \$0.1 million, \$24 thousand and \$0, respectively, for her services as a consultant. Additionally, Otis Buchanan, the husband of Ms. Buchanan, was employed by us and was paid aggregate compensation of approximately \$32 thousand as of both March 31, 2007 and 2006, and \$0.1 million as of December 31, 2006, 2005 and 2004.

In November 2004, we entered into an agreement with John Kang, our Chairman of the Board, in which Mr. Kang agreed that certain stock transactions by him in 2002 involving our company's common stock should have resulted in a liability under Section 16(b) of the Securities Exchange Act of 1934, as amended ( Section 16(b) ). These transactions include Mr. Kang's private sale of 285,715 shares of his personal Liquidmetal Technologies common stock to Growell Metal Co., Ltd. in February 2002, prior to our initial public offering. They also include Mr. Kang's subsequent indirect purchase and disposition of Liquidmetal Technologies common stock in order to satisfy a personal agreement Mr. Kang made to Growell Metal in February 2002 regarding the guaranteed minimum value of the stock purchased by Growell Metal in February 2002 (the purchases and dispositions incident to this agreement occurred in August and November 2002, respectively). Lastly, the transactions include open-market purchases of an aggregate of 89,300 shares of our company's common stock made by Mr. Kang in August 2002.

The Audit Committee of our Board of Directors conducted an independent inquiry into the above-described transactions with the aid of independent legal counsel and, as a result of such inquiry, the Audit Committee concluded that the transactions should have resulted in a liability to us under Section 16(b) in the amount of \$0.3 million. Mr. Kang has acknowledged this liability, and in an agreement negotiated between Mr. Kang and the Audit Committee and approved by the full Board, Mr. Kang will pay this liability through periodic installments in 2005 and 2006. As a result, we accrued for the \$0.3 million receivable in other assets and other income as of December 31, 2004. The above-described transactions involving Growell Metal was reported on a new Form 4 filed by Mr. Kang on November 15, 2004, and the open-market purchases were previously reported on a timely basis in August 2002. As of December 31, 2006, the outstanding amount of the receivable was \$0.2 million, which is included in other assets, and has remained unchanged as of March 31, 2007. Mr. Kang has paid \$0 and \$0.1 million during 2006 and 2005 and is currently in negotiation with the Board of Directors on a payment plan for the remaining liability.

During the year ended December 31, 2005, we executed a \$0.2 million promissory note with CK Cho, member of our Board of Directors, for working capital purposes. The note was due and paid in full as of June 20, 2005. The note had an annual rate of interest of 6% resulting in us paying approximately \$2 thousand in interest. Further, during the year ended December 31, 2005 Mr. Cho advanced approximately \$1.3 million to cover short-term liquidity needs. The advance was made without interest and was repaid as of December 31, 2005. Mr. Cho holds \$0.3 million of Senior Convertible Notes, \$0.4 million of Convertible Notes and held 237,649 exercisable warrants as of March 31, 2007 and held \$0.6 million of Senior Convertible Notes and 92,584 exercisable warrants at both, December 31, 2006 and 2005.

During the year ended December 31, 2005, Ricardo Salas, our former President and Chief Executive Officer, and Young Ham, our former Chief Financial Officer, advanced us \$0.1 million and \$0.1 million to cover short-term liquidity needs, respectively. The advances were made without interest and were repaid as of December 31, 2005. During the year ended December 31, 2006, Mr. Salas advanced us \$0.6 million to cover short-term liquidity need. We paid \$0.1 million to Mr. Salas using 7.75% interest rate and on December 1 2006, the remaining balance of \$0.5 million and its accrued interest of \$9 thousand was converted into the 8% Unsecured Subordinated Notes. Effective January 1, 2007, Mr. Salas began providing services to the Company as a consultant. For the three months ended March 31, 2007, the Company incurred \$30 thousand for his services as consultant. As of March 31, 2007, Mr. Salas holds \$0.1 million of Senior Convertible Notes, \$0.3 million of Convertible Notes, and \$0.3 million of Unsecured Subordinated Notes as well as a total of 275,098 exercisable warrants. During the year ended December 31, 2006 Mr. Salas held \$0.3 million of Senior Convertible Notes and \$0.6 million of Unsecured Subordinated Notes as well as a total of 154,529 exercisable warrants.

During 2006, we purchased production supplies and molds from Grace Metal, Lead Metal, and SDM, which are controlled by James Kang, a former director and officer of our company. Mr. Kang is also a brother of John Kang, Chairman of the Board of our company. We purchased a total of \$0.1 million for the three months ended March 31, 2007, of which \$0.1 million is included in accounts payable and accrued liabilities as of March 31, 2007. We purchased a total of \$0.5 million for the year ended December 31, 2006, of which, \$10 thousand is included in accounts payable and accrued liabilities at December 31, 2006. Effective October 20, 2006, Mr. Kang began providing services to the Company as a consultant. For the three months ended March 31, 2007, the Company incurred \$50 thousand for his services as consultant. During 2006, the Company incurred \$33 thousand for his services as consultant.

During the second quarter of 2007, we entered into a transaction with Grace Metal, a South Korean corporation ( GM ), under which (i) GM agreed to purchase from us various equipment (including die casting machines and vacuum induction melters) used in the Company's bulk amorphous alloy business segment and (ii) we granted GM a 10-year exclusive license to manufacture products made from bulk Liquidmetal alloys for customers whose principal headquarters or whose major operations are located in the South Korea. The principal purposes of the transaction ( GM Transaction ), which closed on June 1, 2007, were to raise capital for us, to shift the cost and burden of our South Korean manufacturing operations to a third party as we prepares to shift manufacturing activities to China, and to provide a way to dispose of older casting equipment as we prepares to implement next-generation casting equipment. Under an equipment purchase agreement between us and GM, GM agreed to buy the purchased equipment for a total purchase price of \$2.0 million, of which \$0.4 million is due in June 2007, with the balance being payable upon the commissioning of the purchased equipment, which we anticipate will be completed on or around the end of the third quarter of 2007. The equipment purchase agreement provides that delivery of the equipment can be delayed to accommodate our continuing manufacturing needs, and it also provides that we will retain a security interest in the purchased equipment until full payment of the purchase price.

In consideration of the license agreement with GM, we will be entitled to royalty of 10% of GM's net sales of licensed products (unless GM's margin on the products falls below specified levels, in which case a new royalty will be negotiated in good faith). The agreement provides that we may convert the license to a non-exclusive license in the event that the net sales in the second year of the contract or thereafter are not sufficient to result in royalties of \$0.5 million or more per year. The agreement also provides that GM will be required to purchase all alloy feedstock from us, and we will have the right to continue to manufacture Liquidmetal alloy products for South Korean customers until all purchased equipment has been commissioned.

Additionally, effective June 1, 2007, we discontinued our post-processing operation in Weihai, China and transferred our manufacturing staff and equipment in Weihai to GM under an amendment to the equipment purchase agreement with GM. Further, we transferred certain of our

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manufacturing staff from our South Korean plant to GM. As a result, GM assumed \$0.4 million of accrued severance liability for the transferred employees. GM was formed by an investor group that includes the former Founder and director of our company, James Kang, who is also the brother of John Kang, Chairman of the Board of our company. We have also changed the name of our South Korean subsidiary to Liquidmetal Technologies Korea Co., Ltd, which was formerly Liquidmetal Korea Co., Ltd. GM will assume the name of Liquidmetal Korea to conduct business in South Korea.

We believe that each of the foregoing transactions was consummated on terms at least as favorable to us as we would expect to negotiate with unrelated third parties.

### **CHANGES OF ACCOUNTANTS**

On November 23, 2005, Stonefield Josephson, Inc. ( Stonefield ), the Company's independent registered public accounting firm, notified the Company that Stonefield would resign as the Company's independent registered public accounting firm upon the completion of Stonefield's review of the Company's interim unaudited financial statements as of and for the three and nine month periods ended September 30, 2005. The Company's interim unaudited financial statements as of and for the three and nine month periods ended September 30, 2005 were included in the Company's report on Form 10-Q for the third quarter ended September 30, 2005 filed with the SEC on December 1, 2005, and the Company's relationship with Stonefield was therefore effectively terminated as of December 1, 2005.

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The reports of Stonefield with respect to the Company's financial statements for the fiscal years ended December 31, 2003 and 2004 contained no adverse opinion or disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope, or accounting principles, except for an explanatory paragraph regarding the Company's ability to continue as a going concern contained in Stonefield's report on the Company's financial statements and for a disclaimer of opinion made by Stonefield with respect to the Company's internal controls over financial reporting and the Company's assessment of those controls as of December 31, 2004.

From May 21, 2004, the date Stonefield was appointed as the Company's independent auditors, through the date of Stonefield's resignation, there were no disagreements between the Company and Stonefield on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Stonefield, would have caused Stonefield to make reference to the subject matter of the disagreements in connection with its report on the Company's financial statements for such years.

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There were no reportable events as described under Item 304(a)(1)(v) of Regulation S-K occurring within the two most recent fiscal years of the Company ended December 31, 2004 and 2003 or within the subsequent interim period through the date of Stonefield's resignation, except as follows:

Stonefield has advised the Company that there are material weaknesses in its internal controls, mainly related to internal controls of its South Korean operations. Therefore, Stonefield has expanded the scope of its review of the interim unaudited financial statements as of and for the three and nine month periods ended September 30, 2005. The material deficiencies in the Company's internal controls over financial reporting include the following:

- a) Lack of adequate segregation of duties in the Company's South Korean operations in accounts receivable, involving cash receipts, shipping, delivery of products, and customer invoice reconciliations;
- b) Lack of adequate segregation of duties in the Company's Coatings Division in Texas in order processing and invoicing;
- c) Lack of adequate controls and documentation in the Company's South Korean operations to evidence proper customer invoicing and revenue recognition in the proper period;
- d) Lack of progress in documenting, assessing and evaluating the Company's internal controls in our South Korean Operations evidenced by aforementioned deficiencies of which remediations will need to be completed as of December 31, 2005.
- e) Lack of sufficient controls over internal access to the Company's SAP system of reporting by unauthorized users; and
- f) The manual performance of numerous procedures that could be automated using current reporting systems.

In connection with the foregoing, Stonefield has also advised the Company that it believes that the Company has made insufficient progress in documenting, assessing, and evaluating the Company's internal controls over financial reporting for purposes of timely complying with Section 404 of the Sarbanes-Oxley Act of 2002.

The Company's Audit Committee has discussed with Stonefield the matters disclosed above regarding Stonefield's resignation. The Company has authorized Stonefield to respond fully to the inquiries of the Company's successor accountant concerning the matters disclosed above.

Upon Stonefield's resignation, the Company's Audit Committee commenced an immediate search and on January 20, 2006, hired Choi Kim & Park LLP (CKP) as its new registered independent public accounting firm.

As of December 31, 2006, the Company has completed its documentation, assessment, and evaluation of the Company's internal controls over financial reporting and has complied with Section 404 of the Sarbanes-Oxley Act of 2002.

## **UNITED STATES FEDERAL INCOME TAX CONSIDERATION**

### **General**

The following is a summary of certain material United States federal income tax considerations related to the ownership and disposition of our common stock that may be relevant to you if you acquire our common stock pursuant to this offering. This summary is based on the Internal Revenue Code of 1986, as amended (the Code), existing and proposed Treasury regulations promulgated under the Code and administrative and judicial interpretations of the Code, all as of the date of this prospectus and all of which are subject to change, possibly with retroactive effect. The Internal Revenue Service is referred to as IRS in this summary.



This summary discusses only the tax consequences to the investors who purchase our common stock pursuant to this offering and does not discuss the tax consequences applicable to subsequent purchasers of our common stock. This summary deals only with common stock held as capital assets within the meaning of Section 1221 of the Code. It does not discuss all of the tax considerations that may be relevant to holders of our common stock in light of their particular circumstances or to holders of common stock subject to special rules, such as financial institutions, regulated investment companies, holders subject to the alternative minimum tax, insurance companies, pension funds, tax-exempt organizations, partnerships or other pass-through entities, dealers in securities or currencies, traders who elect to mark to market their securities or persons holding the common stock as part of a hedging or constructive sale transaction, straddle, conversion transaction, or other integrated transaction, or holders of the common stock whose functional currency is not the United States dollar or persons who acquired our common stock in compensatory transactions. In addition, this summary does not discuss any United States tax consequences to a Non-U.S. Holder (as defined below) that is a controlled foreign corporation, passive foreign investment company, foreign personal holding company, corporation that accumulates earnings to avoid U.S. federal income tax, or a U.S. expatriate. This summary does not address any state, local or non-United States tax considerations, or tax considerations under other federal tax laws (such as estate and gift tax laws).

We have not requested a ruling from the IRS on the tax consequences of owning our common stock. As a result, the IRS could disagree with portions of this discussion. Persons considering the purchase of our common stock should consult with their own tax advisors about the application of the United States federal income tax laws to their particular situations, as well as any tax considerations under other United States federal tax laws, and the laws of any state, local or foreign jurisdiction.

As used in this prospectus, the term **U.S. Holder** means a beneficial owner of common stock that is, for United States federal income tax purposes:

- a citizen or individual resident of the United States;
- a corporation, partnership or other entity treated as a corporation, created in or under the laws of the United States or of any political subdivision thereof;
- an estate the income of which is subject to United States federal income taxation regardless of its source; or
- a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust, or a trust that has a valid election in effect under applicable United States Treasury Regulations to be treated as a U.S. person.

As used in this prospectus, the term **Non-U.S. Holder** means a beneficial owner of common stock that is an individual, corporation, trust or estate that is not a U.S. Holder.

If an entity treated as a partnership for U.S. federal income tax purposes holds shares of common stock, the tax treatment of a partner will generally depend on the status of the partner and upon the activity of the partnership. If you are a partner of a partnership holding shares of common stock, we suggest you consult your own tax advisor.

## **U.S. Holders**

### ***Distributions to U.S. Holders***

If distributions are paid on the shares of our common stock (other than distributions in liquidation and distributions in redemption of our common stock), these distributions generally will constitute dividends for U.S. federal income tax purposes to the extent paid from our current or accumulated earnings and profits, as determined under U.S. federal income tax principles, and will constitute a tax-free return of capital that is applied against your tax basis in the common stock to the extent these distributions exceed those earnings and profits. Distributions in excess of our current and accumulated earnings and profits and your tax basis in the common stock will be treated as a gain from the sale or exchange of the common stock, the treatment of which is discussed below. For the tax years 2004 through 2008, non-corporate U.S. Holders are subject to a maximum tax rate on





dividends equal to 15%, which corresponds to the maximum tax rate for long-term capital gains; however, certain holding period requirements and other limitations may apply. Under current law for tax years beginning after December 31, 2008, dividends will be taxed at the same rate as other items of ordinary income. U.S. Holders that are corporations may be eligible for a dividend-received deduction in respect of a dividend distribution by us.

***Gain on Disposition of Common Stock by U.S. Holders***

A U.S. Holder will recognize gain or loss on the sale, exchange or other taxable disposition of our common stock to the extent of the difference between the amount realized on such sale, exchange or other disposition and the holder's adjusted tax basis in such shares. Such gain or loss generally will constitute capital gain or loss, and will be long-term capital gain or loss, if the holder has held such shares for more than one year at the time of sale or disposition. Non-corporate U.S. Holders are subject to a maximum tax rate of 15% on long-term capital gain (increased to 20% for years after 2008). The deductibility of capital losses by a U.S. Holder is subject to limitations.

**Non-U.S. Holders**

***Distributions to Non-U.S. Holders***

Dividends paid to a Non-U.S. Holder that are not effectively connected with the conduct of a U.S. trade or business of the Non-U.S. Holder generally will be subject to U.S. federal withholding tax at a 30% rate or, if an income tax treaty applies and certain certification requirements described below are satisfied, a lower rate specified by the treaty. A Non-U.S. Holder who wishes to claim the benefits of an applicable income tax treaty will be required to provide the appropriate IRS Form W-8 certifying its entitlement to benefits under an income tax treaty. Non-U.S. Holders should consult their tax advisors regarding their entitlement to benefits under a relevant tax treaty.

Withholding generally is imposed on the gross amount of a distribution, regardless of whether we have sufficient earnings and profits to cause the distribution to be a dividend for U.S. federal income tax purposes. However, we may elect to withhold on less than the gross amount of the distribution if we determine that the distribution is not paid out of our current or accumulated earnings and profits, based on our reasonable estimates.

A Non-U.S. Holder eligible for a reduced rate of U.S. federal withholding tax under a tax treaty may obtain a refund of any excess amounts withheld by filing an appropriate claim for a refund together with the required information with the IRS.

Dividends that are effectively connected with a Non-U.S. Holder's conduct of a trade or business within the United States and, if a tax treaty applies, attributable to a Non-U.S. Holder's U.S. permanent establishment, are exempt from U.S. federal withholding tax if the Non-U.S. Holder furnishes to us or our paying agent the appropriate IRS form and other applicable requirements are met. However, dividends exempt from U.S. federal withholding tax because they are effectively connected or attributable to a U.S. permanent establishment under an applicable tax treaty are subject to U.S. federal income tax on a net income basis at the regular graduated U.S. federal income tax rates. Any such effectively connected dividends received by a foreign corporation may, under certain circumstances, be subject to an additional branch profits tax at a 30% rate or a lower rate specified by an applicable tax treaty.

***Gain on Disposition of Common Stock by Non-U.S. Holders***

Subject to the discussion below concerning backup withholding, a Non-U.S. Holder generally will not be subject to U.S. federal income tax with respect to gain recognized on a sale or other disposition of our common stock unless one of the following applies:

- The gain is effectively connected with a Non-U.S. Holder's conduct of a trade or business within the United States and, if a tax treaty applies, the gain is attributable to a Non-U.S. Holder's U.S. permanent establishment. In such case, the Non-U.S. Holder will, unless an applicable tax treaty provides otherwise, generally be taxed on its net gain derived from the sale at regular graduated U.S. federal income tax rates, and in the case of a foreign corporation, may also be subject to the branch profits tax described above;

- A Non-U.S. Holder who is an individual holds our common stock as a capital asset, is present in the United States for 183 or more days in the taxable year of the sale or other disposition, and certain other conditions are met. In such a case, the Non-U.S. Holder will be subject to a flat 30% tax on the gain derived from the sale, which may be offset by certain U.S. capital losses; or
- We are or have been a United States real property holding corporation (a USRPHC) for United States federal income tax purposes at any time during the shorter of the five-year period ending on the date of the sale or other disposition and the period such Non-U.S. Holder held our common stock (the shorter period hereinafter referred to as the lookback period); provided that if our common stock is regularly traded on an established securities market, this rule will generally not cause any gain to be taxable unless the Non-U.S. Holder owned more than 5% of our common stock at some time during the lookback period. We do not believe that we are a USRPHC and do not expect to become one in the future. However, we could become a USRPHC as a result of future changes in assets or operations.

#### **Information Reporting and Backup Withholding Tax**

The amount of dividends paid to each U.S. Holder will be reported annually to the IRS and to each U.S. Holder. A U.S. Holder may be subject to backup withholding (currently at a rate of 28%) with respect to dividends on, and the proceeds from the sale or redemption of, common stock, unless such holder (a) is an entity that is exempt from withholding (including, among others, corporations and certain tax-exempt organizations) and when required, demonstrates this fact, or (b) provides the payor with its correct taxpayer identification number, which, for an individual, is ordinarily his or her social security number, and otherwise complies with applicable requirements of the backup withholding rules.

Generally, we must report annually to the IRS and to each Non-U.S. Holder the amount of dividends paid to, and the tax withheld with respect to, each Non-U.S. Holder. These reporting requirements apply regardless of whether withholding was reduced or eliminated by an applicable tax treaty. Copies of this information also may be available under the provisions of a specific tax treaty or agreement with the tax authorities in the country in which the Non-U.S. Holder resides or is established.

In general, backup withholding will not apply to dividends paid to a Non-U.S. Holder and to proceeds from the disposition of our common stock paid to a Non-U.S. Holder if the holder has provided the required certification that it is a Non-U.S. Holder and neither we nor our paying agents have actual knowledge or reason to know that the holder is a United States person.

Under United States Treasury Regulations, the payment of proceeds from the disposition of our common stock by a Non-U.S. Holder made to or through a foreign office of a broker to its customer generally are not subject to information reporting or backup withholding. However, if the broker is a U.S. person, a controlled foreign corporation for U.S. federal income tax purposes, a foreign person 50% or more of whose gross income from certain periods is effectively connected with a United States trade or business, or a foreign partnership with significant United States ownership, then information reporting (but not backup withholding) will be required, unless the broker has in its records documentary evidence that the beneficial owner of the payment is not a U.S. person or is otherwise entitled to an exemption, and other applicable certification requirements are met (and the broker has no actual knowledge to the contrary). Information reporting and backup withholding generally will apply to proceeds of a disposition of our common stock effected at a United States office of any United States or foreign broker, unless the broker has in its records documentary evidence that the beneficial owner of the payment is not a U.S. person or is otherwise entitled to an exemption, and other applicable certification requirements are met.

Backup withholding does not represent an additional income tax. Any amounts withheld from a payment to a holder under the backup withholding rules will be allowed as a credit against the holder's United States federal income tax liability and may entitle the holder to a refund, provided that the required information or returns are timely furnished by the holder to the IRS.

**The foregoing discussion of certain U.S. federal income tax considerations is for general information only and is not tax advice. Accordingly, each prospective investor should consult with his own tax adviser regarding U.S. federal, state, local and non-U.S. income and other tax consequences of the acquisition, holding and disposing of our common stock.**

## **LEGAL MATTERS**

The validity of the shares of common stock issued in this offering will be passed upon for us by the law firm of Foley & Lardner LLP, Tampa, Florida.

## **EXPERTS**

The consolidated financial statements as of and for the years ended December 31, 2006 and 2005 included in this prospectus have been audited by Choi, Kim & Park, LLP., our current independent auditors, as stated in their report appearing herein and are included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing. The consolidated financial statements as of and for the year ended December 31, 2004 included in this prospectus have been audited by Stonefield Josephson, Inc., our former independent auditors, as stated in their report appearing herein and are included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

## **WHERE YOU CAN FIND MORE INFORMATION**

We are subject to the informational reporting requirements of the Securities Exchange Act of 1934, as amended. In accordance with the Exchange Act, we file reports, proxy statements and other information with the Securities and Exchange Commission. You can inspect and copy these reports, proxy statements and other information at the Public Reference Room of the Securities and Exchange Commission at 100 F Street N.E., Washington, D.C. 20549, at prescribed rates. Please call the Securities and Exchange Commission at 1-800-SEC-0330 for further information on the operation of the Public Reference Room. Our Securities and Exchange Commission filings are also available on the Securities and Exchange Commission's web site. The address of this site is <http://www.sec.gov>.

We have filed with the Securities and Exchange Commission a registration statement (which term includes all amendments, exhibits and schedules thereto) on Form S-1 under the Securities Act of 1933, as amended, with respect to the shares offered by this prospectus. This prospectus is part of that registration statement and, as allowed by Securities and Exchange Commission's rules, does not contain all the information set forth in the registration statement and the exhibits to the registration statement. The registration statement may be inspected at the public reference facilities maintained by the Securities and Exchange Commission at 100 F Street, N.E., Washington, D.C. 20549-0102 and is available to you on the Securities and Exchange Commission's web site.

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of Liquidmetal Technologies, Inc.

We have audited the accompanying consolidated balance sheet of Liquidmetal Technologies, Inc. and subsidiaries (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of operations and comprehensive loss, shareholders' equity (deficiency), and cash flows for the years ended December 31, 2006 and 2005 as well as the effects of the adjustments for the correction of the error described in Note 2 as of and for the year ended December 31, 2004. Our audits also included the financial statement schedule listed at index in Item 15(a) as of and for the years ended December 31, 2006 and 2005. Our responsibility is to express an opinion on the financial statements and financial statement schedule 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Liquidmetal Technologies, Inc. and subsidiaries as of December 31, 2006 and 2005, and the results of their operations and cash flows for the years ended December 31, 2006 and 2005, as well as the effects of the adjustments for the correction of the error described in Note 2 as of and for the year ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 3 to the consolidated financial statements, the Company's significant operating losses and working capital deficit raise substantial doubt about its ability to continue as a going concern. Management's plans regarding those matters also are described in Note 3. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Choi, Kim & Park  
LLP

Los Angeles, California

Certified Public Accountants

February 15, 2007, except for Note 2, as to which the date is July 17, 2006

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of Liquidmetal Technologies, Inc.

We have audited, before the effects of the adjustments for the correction of the error described in Note 2, the consolidated statements of operations and comprehensive loss, shareholders' equity (deficiency), and cash flows of Liquidmetal Technologies, Inc. and subsidiaries (the Company) for the year ended December 31, 2004 (the 2004 financial statements before the effects of the adjustments discussed in Note 2 are not presented herein). Our audit also included the financial statement schedule listed at index in Item 15(a), except for the correction of the error described in Note 2, as of and for the year ended December 31, 2004. Our responsibility is to express an opinion on the financial statements and financial statement schedule 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, except for the error described in Note 2, such consolidated financial statements present fairly, in all material respects, the financial position of Liquidmetal Technologies, Inc. and subsidiaries as of December 31, 2004, and the results of their operations and cash flows for each of the two years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, except for the error described in Note 2, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We were not engaged to audit, review, or apply any procedures to the adjustments for the correction of the error described in Note 2, and accordingly, we do not express an opinion or any other form of assurance about whether such adjustments are appropriate and have been properly applied. Those adjustments were audited by Choi, Kim & Park LLP.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 3 to the consolidated financial statements, the Company's significant operating losses and working capital deficit raise substantial doubt about its ability to continue as a going concern. Management's plans regarding those matters also are described in Note 3. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Stonefield Josephson,  
Inc.

Irvine, California

Certified Public Accountants

March 3, 2005

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## LIQUIDMETAL TECHNOLOGIES, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	March 31, 2007 (Unaudited)	December 31, 2006	2005 (Restated)
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$ 2,937	\$ 144	\$ 1,392
Restricted cash	2,083		
Trade accounts receivables, net of allowance for doubtful accounts of \$65, \$82 and \$61 at March 31, 2007, December 31, 2006 and 2005, respectively	3,086	3,934	2,360
Inventories	2,541	3,765	1,748
Prepaid expenses and other current assets	996	830	609
Total current assets	11,643	8,673	6,109
Property, plant and equipment, net	11,077	12,095	13,437
Idle equipment	191	194	193
Other intangibles, net	1,156	1,170	1,185
Investment in joint venture	220	3	
Other assets	1,088	109	639
Total assets	\$ 25,375	\$ 22,244	\$ 21,563
<b>LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIENCY)</b>			
Current liabilities:			
Accounts payable and accrued expenses	\$ 7,696	\$ 9,802	\$ 6,530
Settlement payable			3,331
Deferred revenue	125	202	1,275
Short-term debt	1,493	2,669	550
Long-term debt, current portion, net of debt discounts of \$1,647, \$3,636 and \$0 at March 31, 2007, December 31, 2006 and 2005, respectively	11,849	14,480	1,343
Warrant liabilities	2,934	2,662	1,792
Conversion feature liabilities	3,434	1,838	1,798
Other liabilities, current portion	178	177	483
Total current liabilities	27,709	31,830	17,102
Long-term debt, net of current portion and debt discounts of \$9,893, \$0 and \$8,259 at March 31, 2007, December 31, 2006 and 2005, respectively	6,406	225	5,433
Other long-term liabilities, net of current portion	582	552	348
Total liabilities	34,697	32,607	22,883
Shareholders' deficiency:			
Common stock, \$0.001 par value; 100,000,000 shares authorized and 44,631,768, 44,311,768 and 42,187,621 issued and outstanding at March 31, 2007, December 31, 2006 and 2005, respectively	45	44	42
Additional paid-in capital	136,776	136,031	130,893
Accumulated deficit	(148,530)	(149,047)	(134,525)
Accumulated other comprehensive income	2,387	2,609	2,270
Total shareholders' deficiency	(9,322)	(10,363)	(1,320)
Total liabilities and shareholders' deficiency	\$ 25,375	\$ 22,244	\$ 21,563

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





**LIQUIDMETAL TECHNOLOGIES, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS**

**(in thousands, except per share data)**

<b>Three Months Ended</b>		<b>Years Ended December 31,</b>		
<b>March 31,</b>		<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>2007</b>	<b>2006</b>		<b>(Restated)</b>	<b>(Restated)</b>
<b>(Unaudited)</b>	<b>(Restated)</b>			