CVR ENERGY INC
Form 10-Q
November 03, 2010

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

Form 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2010

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to .

Commission file number: 001-33492

CVR ENERGY, INC.
(Exact name of registrant as specified in its charter)

Delaware	**61-1512186**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
2277 Plaza Drive, Suite 500 **Sugar Land, Texas**	**77479**
(Address of principal executive offices)	*(Zip Code)*

(281) 207-3200
(Registrant s telephone number, including area code)

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

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

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o Smaller reporting company o

(Do not check if a smaller reporting company)

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

There were 86,347,268 shares of the registrant s common stock outstanding at November 1, 2010.

CVR ENERGY, INC. AND SUBSIDIARIES

INDEX TO QUARTERLY REPORT ON FORM 10-Q
For The Quarter Ended September 30, 2010

		Page No.
	PART I. Financial Information	
Item 1.	Financial Statements	4
	Condensed Consolidated Balance Sheets September 30, 2010 (unaudited) and December 31, 2009	4
	Condensed Consolidated Statements of Operations Three and Nine Months Ended September 30, 2010 and 2009 (unaudited)	5
	Condensed Consolidated Statements of Cash Flows Nine Months Ended September 30, 2010 and 2009 (unaudited)	6
	Notes to the Condensed Consolidated Financial Statements September 30, 2010 (unaudited)	7
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	32
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	62
Item 4.	Controls and Procedures	63
	PART II. Other Information	
Item 1.	Legal Proceedings	64
Item 1A.	Risk Factors	64
Item 6.	Exhibits	64
Signatures		65

GLOSSARY OF SELECTED TERMS

The following are definitions of certain industry terms used in this Form 10-Q.

2-1-1 crack spread The approximate gross margin resulting from processing two barrels of crude oil to produce one barrel of gasoline and one barrel of distillate. The 2-1-1 crack spread is expressed in dollars per barrel.

Ammonia Ammonia is a direct application fertilizer and is primarily used as a building block for other nitrogen products for industrial applications and finished fertilizer products.

Backwardation market Market situation in which futures prices are lower in succeeding delivery months. Also known as an inverted market. The opposite of contango.

Barrel Common unit of measure in the oil industry which equates to 42 gallons.

Blendstocks Various compounds that are combined with gasoline or diesel from the crude oil refining process to make finished gasoline and diesel fuel; these may include natural gasoline, fluid catalytic cracking unit or FCCU gasoline, ethanol, reformate or butane, among others.

bpd Abbreviation for barrels per day.

Bulk sales Volume sales through third party pipelines, in contrast to tanker truck quantity sales.

Capacity Capacity is defined as the throughput a process unit is capable of sustaining, either on a calendar or stream day basis. The throughput may be expressed in terms of maximum sustainable, nameplate or economic capacity. The maximum sustainable or nameplate capacities may not be the most economical. The economic capacity is the throughput that generally provides the greatest economic benefit based on considerations such as feedstock costs, product values and downstream unit constraints.

Catalyst A substance that alters, accelerates, or instigates chemical changes, but is neither produced, consumed nor altered in the process.

Coker unit A refinery unit that utilizes the lowest value component of crude oil remaining after all higher value products are removed, further breaks down the component into more valuable products and converts the rest into pet coke.

Common units The class of interests issued under the limited liability company agreements governing Coffeyville Acquisition LLC, Coffeyville Acquisition II LLC and Coffeyville Acquisition III LLC, which provide for voting rights and have rights with respect to profits and losses of, and distributions from, the respective limited liability companies.

Contango market Market situation in which prices for future delivery are higher than the current or spot market price of the commodity. The opposite of backwardation.

Crack spread A simplified calculation that measures the difference between the price for light products and crude oil. For example, the 2-1-1 crack spread is often referenced and represents the approximate gross margin resulting from processing two barrels of crude oil to produce one barrel of gasoline and one barrel of distillate.

Distillates Primarily diesel fuel, kerosene and jet fuel.

Ethanol A clear, colorless, flammable oxygenated hydrocarbon. Ethanol is typically produced chemically from ethylene, or biologically from fermentation of various sugars from carbohydrates found in agricultural crops and cellulosic residues from crops or wood. It is used in the United States as a gasoline octane enhancer and oxygenate.

Farm belt Refers to the states of Illinois, Indiana, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, Ohio, Oklahoma, South Dakota, Texas and Wisconsin.

Feedstocks Petroleum products, such as crude oil and natural gas liquids, that are processed and blended into refined products.

Heavy crude oil A relatively inexpensive crude oil characterized by high relative density and viscosity. Heavy crude oils require greater levels of processing to produce high value products such as gasoline and diesel fuel.

Independent petroleum refiner A refiner that does not have crude oil exploration or production operations. An independent refiner purchases the crude oil used as feedstock in its refinery operations from third parties.

Light crude oil A relatively expensive crude oil characterized by low relative density and viscosity. Light crude oils require lower levels of processing to produce high value products such as gasoline and diesel fuel.

Magellan Magellan Midstream Partners L.P., a publicly traded company whose business is the transportation, storage and distribution of refined petroleum products.

MMBtu One million British thermal units or Btu is a measure of energy. One Btu of heat is required to raise the temperature of one pound of water one degree Fahrenheit.

Natural gas liquids Natural gas liquids, often referred to as NGLs, are both feedstocks used in the manufacture of refined fuels and are products of the refining process. Common NGLs used include propane, isobutane, normal butane and natural gasoline.

PADD II Midwest Petroleum Area for Defense District which includes Illinois, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, Oklahoma, South Dakota, Tennessee, and Wisconsin.

Petroleum coke (Pet coke) A coal-like substance that is produced during the refining process.

Refined products Petroleum products, such as gasoline, diesel fuel and jet fuel, that are produced by a refinery.

Sour crude oil A crude oil that is relatively high in sulfur content, requiring additional processing to remove the sulfur. Sour crude oil is typically less expensive than sweet crude oil.

Spot market A market in which commodities are bought and sold for cash and delivered immediately.

Sweet crude oil A crude oil that is relatively low in sulfur content, requiring less processing to remove the sulfur. Sweet crude oil is typically more expensive than sour crude oil.

Throughput The volume processed through a unit or a refinery or transported on a pipeline.

Turnaround A periodically required standard procedure to inspect, refurbish, repair and maintain the refinery and nitrogen fertilizer plant assets. This process involves the shutdown and inspection of major processing units and occurs every three to four years for the refinery and every two years for the nitrogen fertilizer plant.

UAN A solution of urea and ammonium nitrate in water used as a fertilizer.

WTI West Texas Intermediate crude oil, a light, sweet crude oil, characterized by an American Petroleum Institute gravity, or API gravity, between 39 and 41 degrees and a sulfur content of approximately 0.4 weight percent that is used as a benchmark for other crude oils.

WTS West Texas Sour crude oil, a relatively light, sour crude oil characterized by an API gravity of 30-32 degrees and a sulfur content of approximately 2.0 weight percent.

Yield The percentage of refined products that is produced from crude oil and other feedstocks.

PART I. FINANCIAL INFORMATION

ITEM 1. ***FINANCIAL STATEMENTS***

CVR ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2010 (unaudited)	December 31, 2009
	(in thousands, except share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 162,386	$ 36,905
Accounts receivable, net of allowance for doubtful accounts of $701 and $4,772, respectively	73,747	45,729
Inventories	237,938	274,838
Prepaid expenses and other current assets	32,335	26,141
Income tax receivable		20,858
Deferred income taxes	23,133	21,505
Total current assets	529,539	425,976
Property, plant, and equipment, net of accumulated depreciation	1,092,688	1,137,910
Intangible assets, net	353	377
Goodwill	40,969	40,969
Deferred financing costs, net	12,065	3,485
Insurance receivable	3,587	1,000
Other long-term assets	4,854	4,777
Total assets	$ 1,684,055	$ 1,614,494
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term debt	$	$ 4,777
Note payable and capital lease obligations	9,870	11,774
Accounts payable	114,953	106,471
Personnel accruals	25,923	14,916
Accrued taxes other than income taxes	21,361	15,904
Income taxes payable	5,260	
Deferred revenue	7,890	10,289
Other current liabilities	34,512	26,493
Total current liabilities	219,769	190,624

Long-term liabilities:		
Long-term debt, net of current portion	496,212	474,726
Accrued environmental liabilities, net of current portion	2,854	2,828
Deferred income taxes	279,814	278,008
Other long-term liabilities	3,799	3,893
Total long-term liabilities	782,679	759,455
Commitments and contingencies		
Equity:		
CVR stockholders equity:		
Common Stock $0.01 par value per share, 350,000,000 shares authorized, 86,354,508 and 86,344,508 shares issued, respectively	864	863
Additional paid-in-capital	451,442	446,263
Retained earnings	218,785	206,789
Treasury stock, 11,406 and 15,271 shares, respectively, at cost	(84)	(100)
Total CVR stockholders equity	671,007	653,815
Noncontrolling interest	10,600	10,600
Total equity	681,607	664,415
Total liabilities and equity	$ 1,684,055	$ 1,614,494

See accompanying notes to the condensed consolidated financial statements.

CVR ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(unaudited) (in thousands, except share data)			
Net sales	$ 1,031,174	$ 811,693	$ 2,931,584	$ 2,214,392
Operating costs and expenses:				
Cost of product sold (exclusive of depreciation and amortization)	889,850	712,730	2,584,392	1,721,970
Direct operating expenses (exclusive of depreciation and amortization)	53,504	58,419	176,545	169,100
Selling, general and administrative expenses (exclusive of depreciation and amortization)	16,397	29,165	48,584	70,443
Net costs associated with flood	(970)	529	(970)	609
Depreciation and amortization	21,943	21,634	64,756	63,650
Total operating costs and expenses	980,724	822,477	2,873,307	2,025,772
Operating income	50,450	(10,784)	58,277	188,620
Other income (expense):				
Interest expense and other financing costs	(13,863)	(10,932)	(36,551)	(33,593)
Interest income	549	475	1,608	1,142
Gain (loss) on derivatives, net	(1,014)	3,116	7,815	(62,978)
Loss on extinguishment of debt			(15,052)	(677)
Other income, net	17	82	701	280
Total other income (expense)	(14,311)	(7,259)	(41,479)	(95,826)
Income (loss) before income tax expense (benefit)	36,139	(18,043)	16,798	92,794
Income tax expense (benefit)	12,932	(4,604)	4,802	32,903
Net income (loss)	$ 23,207	$ (13,439)	$ 11,996	$ 59,891
Basic earnings (loss) per share	$ 0.27	$ (0.16)	$ 0.14	$ 0.69
Diluted earnings (loss) per share	$ 0.27	$ (0.16)	$ 0.14	$ 0.69
Weighted-average common shares outstanding:				
Basic	86,343,102	86,244,245	86,336,205	86,244,049
Diluted	87,013,575	86,244,245	86,677,325	86,333,437

See accompanying notes to the condensed consolidated financial statements.

CVR ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30,	
	2010	2009
	(unaudited) (in thousands)	
Cash flows from operating activities:		
Net income (loss)	$ 11,996	$ 59,891
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	64,756	63,650
Allowance for doubtful accounts	(4,070)	(41)
Amortization of deferred financing costs	2,386	1,510
Amortization of original issue discount	232	
Deferred income taxes	178	(4,339)
Loss on disposition of assets	2,179	36
Loss on extinguishment of debt	15,052	677
Share-based compensation	8,357	25,400
Unrealized (gain) loss on derivatives	(3,582)	34,664
Changes in assets and liabilities:		
Restricted cash		34,560
Accounts receivable	(23,948)	(20,725)
Inventories	36,900	(80,278)
Prepaid expenses and other current assets	(15,113)	11,061
Insurance receivable	(2,587)	
Insurance proceeds from flood		11,756
Other long-term assets	(574)	849
Accounts payable	10,282	1,378
Accrued income taxes	26,118	29,479
Deferred revenue	(2,399)	2,492
Other current liabilities	24,953	8,223
Payable to swap counterparty		(62,457)
Accrued environmental liabilities	26	(884)
Other long-term liabilities	(94)	1,260
Net cash provided by operating activities	151,048	118,162
Cash flows from investing activities:		
Capital expenditures	(23,003)	(36,495)
Proceeds from the sale of assets	11	
Net cash used in investing activities	(22,992)	(36,495)
Cash flows from financing activities:		
Revolving debt payments	(60,000)	(72,200)

Revolving debt borrowings	60,000	72,200
Proceeds net of original issue discount on issuance of senior notes	485,853	
Principal payments on term debt	(479,503)	(3,623)
Payment of financing costs	(8,765)	(17)
Payment of capital lease obligation	(111)	(80)
Payment of treasury stock	(49)	
Net cash used in financing activities	(2,575)	(3,720)
Net increase in cash and cash equivalents	125,481	77,947
Cash and cash equivalents, beginning of period	36,905	8,923
Cash and cash equivalents, end of period	$ 162,386	$ 86,870
Supplemental disclosures:		
Cash paid for income taxes, net of refunds (received)	$ (21,493)	$ 7,764
Cash paid for interest, net of capitalized interest of $1,740 and $1,338 in 2010 and 2009, respectively	20,478	30,084
Cash funding of margin account for other derivative activities, net of withdrawals (received)	(1,896)	3,934
Non-cash investing and financing activities:		
Accrual of construction in progress additions	(1,800)	(4,427)
Reduction of senior notes for underwriting discount and financing costs	10,127	
Receipt of marketable securities	23	

See accompanying notes to the condensed consolidated financial statements.

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2010
(unaudited)

(1) Organization and History of the Company and Basis of Presentation

Organization

The Company or CVR may be used to refer to CVR Energy, Inc. and, unless the context otherwise requires, its subsidiaries. Any references to the Company as of a date prior to October 16, 2007 (the date of the restructuring as further discussed in this note) and subsequent to June 24, 2005 are to Coffeyville Acquisition LLC (CALLC) and its subsidiaries.

The Company, through its wholly-owned subsidiaries, acts as an independent petroleum refiner and marketer of high value transportation fuels in the mid-continental United States. In addition, the Company, through its majority-owned subsidiaries, acts as an independent producer and marketer of upgraded nitrogen fertilizer products in North America. The Company s operations include two business segments: the petroleum segment and the nitrogen fertilizer segment.

CALLC formed CVR Energy, Inc. as a wholly-owned subsidiary, incorporated in Delaware in September 2006, in order to effect an initial public offering. The initial public offering of CVR was consummated on October 26, 2007. In conjunction with the initial public offering, a restructuring occurred in which CVR became a direct or indirect owner of all of the subsidiaries of CALLC. Additionally, in connection with the initial public offering, CALLC was split into two entities: CALLC and Coffeyville Acquisition II LLC (CALLC II).

CVR is a controlled company under the rules and regulations of the New York Stock Exchange where its shares are traded under the symbol CVI. As of September 30, 2010, approximately 64% of its outstanding shares were beneficially owned by GS Capital Partners V, L.P. and related entities (GS or Goldman Sachs Funds) and Kelso Investment Associates VII, L.P. and related entities (Kelso or Kelso Funds).

Nitrogen Fertilizer Limited Partnership

In conjunction with the consummation of CVR s initial public offering in 2007, CVR transferred Coffeyville Resources Nitrogen Fertilizers, LLC (CRNF), its nitrogen fertilizer business, to a then newly created limited partnership, CVR Partners, LP (the Partnership), in exchange for a managing general partner interest (managing GP interest), a special general partner interest (special GP interest) represented by special GP units and a de minimis limited partner interest represented by special LP units. This transfer was not considered a business combination as it was a transfer of assets among entities under common control and, accordingly, balances were transferred at their historical cost. CVR concurrently sold the managing GP interest to Coffeyville Acquisition III LLC (CALLC III), an entity owned by its controlling stockholders and senior management, at fair market value. The board of directors of CVR determined, after consultation with management, that the fair market value of the managing GP interest was $10,600,000. This interest has been classified as a noncontrolling interest included as a separate component of equity in the Condensed Consolidated Balance Sheets at September 30, 2010 and December 31, 2009.

CVR owns all of the interests in the Partnership (other than the managing GP interest and the associated incentive distribution rights (IDRs)) and is entitled to all cash distributed by the Partnership except with respect to IDRs. The managing general partner is not entitled to participate in Partnership distributions except with respect to its IDRs, which entitle the managing general partner to receive increasing percentages (up to 48%) of the cash the Partnership

distributes in excess of $0.4313 per unit in a quarter. However, the Partnership is not permitted to make any distributions with respect to the IDRs until the aggregate Adjusted Operating Surplus, as defined in the Partnership s partnership agreement, generated by the Partnership through December 31, 2009, has been distributed in respect of the units held by CVR and any common units issued by the Partnership if it elects to pursue an initial public offering. In addition, the Partnership and its subsidiaries

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

are currently guarantors under the first priority credit facility of Coffeyville Resources, LLC (CRLLC), a wholly-owned subsidiary of CVR. There will be no distributions paid with respect to the IDRs for so long as the Partnership or its subsidiaries are guarantors under the first priority credit facility.

The Partnership is operated by CVR s senior management pursuant to a services agreement among CVR, the managing general partner, and the Partnership. The Partnership is managed by the managing general partner and, to the extent described below, CVR, as special general partner. As special general partner of the Partnership, CVR has joint management rights regarding the appointment, termination, and compensation of the chief executive officer and chief financial officer of the managing general partner, has the right to designate two members of the board of directors of the managing general partner, and has joint management rights regarding specified major business decisions relating to the Partnership. CVR, the Partnership, and the managing general partner also entered into a number of agreements to regulate certain business relations between the parties.

At September 30, 2010, the Partnership had 30,333 special LP units outstanding, representing 0.1% of the total Partnership units outstanding, and 30,303,000 special GP units outstanding, representing 99.9% of the total Partnership units outstanding. In addition, the managing general partner owned the managing GP interest and the IDRs. The managing general partner contributed 1% of CRNF s interest to the Partnership in exchange for its managing GP interest and the IDRs.

In accordance with the Contribution, Conveyance, and Assumption Agreement, by and between the Partnership and the partners, dated as of October 24, 2007, since an initial private or public offering of the Partnership was not consummated by October 24, 2009, the managing general partner of the Partnership can require the Company to purchase the managing GP interest. This put right expires on the earlier of (1) October 24, 2012 or (2) the closing of the Partnership s initial private or public offering. If the Partnership s initial private or public offering is not consummated by October 24, 2012, the Company has the right to require the managing general partner to sell the managing GP interest to the Company. This call right expires on the closing of the Partnership s initial private or public offering. In the event of an exercise of a put right or a call right, the purchase price will be the fair market value of the managing GP interest at the time of the purchase determined by an independent investment banking firm selected by the Company and the managing general partner.

As of September 30, 2010, the Partnership has distributed $50,000,000 to CVR. This distribution occurred in 2008.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements were prepared in accordance with U.S. generally accepted accounting principles (GAAP) and in accordance with the rules and regulations of the Securities and Exchange Commission (SEC). The condensed consolidated financial statements include the accounts of CVR and its majority-owned direct and indirect subsidiaries. The ownership interests of noncontrolling investors in its subsidiaries are recorded as a noncontrolling interest included as a separate component of equity for all periods presented. All intercompany account balances and transactions have been eliminated in consolidation. Certain information and footnotes required for complete financial statements under GAAP have been condensed or omitted pursuant to SEC rules and regulations. These unaudited condensed consolidated financial statements should be read in conjunction with the December 31, 2009 audited consolidated financial statements and notes thereto included in CVR s Annual Report on Form 10-K for the year ended December 31, 2009, which was filed with the SEC on March 12, 2010.

In the opinion of the Company s management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) that are necessary to fairly present the financial position of the Company as of September 30, 2010 and December 31, 2009, the

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

results of operations for the three and nine months ended September 30, 2010 and 2009, and the cash flows for the nine months ended September 30, 2010 and 2009. Certain prior year amounts have been reclassified to conform to current year presentation.

Results of operations and cash flows for the interim periods presented are not necessarily indicative of the results that will be realized for the year ending December 31, 2010 or any other interim period. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

The Company evaluated subsequent events that would require an adjustment to the Company s condensed consolidated financial statements or require disclosure in the notes to the condensed consolidated financial statements through the date of issuance of the condensed consolidated financial statements.

(2) Recent Accounting Pronouncements

In January 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-06, Improving Disclosures about Fair Value Measurements, an amendment to Accounting Standards Codification (ASC) Topic 820, Fair Value Measurements and Disclosures. This amendment requires an entity to: (i) disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers, (ii) present separate information for Level 3 activity pertaining to gross purchases, sales, issuances, and settlements and (iii) enhance disclosures of assets and liabilities subject to fair value measurements. The provisions of ASU No. 2010-06 are effective for the Company for interim and annual reporting beginning after December 15, 2009, with one new disclosure effective after December 15, 2010. The Company adopted this ASU as of January 1, 2010. The adoption of this standard did not impact the Company s financial position or results of operations.

In June 2009, the FASB issued an amendment to a previously issued standard regarding consolidation of variable interest entities. This amendment was intended to improve financial reporting by enterprises involved with variable interest entities. Overall, the amendment revises the test for determining the primary beneficiary of a variable interest entity from a primarily quantitative analysis to a qualitative analysis. The provisions of the amendment are effective as of the beginning of the entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. The Company adopted this standard as of January 1, 2010. The adoption of this standard did not impact the Company s financial position or results of operations.

(3) Share-Based Compensation

Prior to CVR s initial public offering in October 2007, CVR s subsidiaries were held and operated by CALLC. Management of CVR holds an equity interest in CALLC. CALLC issued non-voting override units to certain management members who held common units of CALLC. There were no required capital contributions for the override operating units. In connection with CVR s initial public offering, CALLC was split into two entities: CALLC and CALLC II. In connection with this split, management s equity interest in CALLC, including both their common units and non-voting override units, was split so that half of management s equity interest was in CALLC and half was in CALLC II. CALLC was historically the primary reporting company and CVR s predecessor. In addition, in

connection with the transfer of the managing GP interest of the Partnership to CALLC III in October 2007, CALLC III issued non-voting override units to certain management members of CALLC III.

CVR, CALLC, CALLC II and CALLC III account for share-based compensation in accordance with standards issued by the FASB regarding the treatment of share-based compensation, as well as guidance

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

regarding the accounting for share-based compensation granted to employees of an equity method investee. CVR has been allocated non-cash share-based compensation expense from CALLC, CALLC II and CALLC III.

In accordance with these standards, CVR, CALLC, CALLC II and CALLC III apply a fair-value based measurement method in accounting for share-based compensation. In addition, CVR recognizes the costs of the share-based compensation incurred by CALLC, CALLC II and CALLC III on its behalf, primarily in selling, general, and administrative expenses (exclusive of depreciation and amortization), and a corresponding capital contribution, as the costs are incurred on its behalf, following the guidance issued by the FASB regarding the accounting for equity instruments that are issued to other than employees, for acquiring, or in conjunction with selling goods or services, which requires remeasurement at each reporting period through the performance commitment period, or in CVR s case, through the vesting period.

At September 30, 2010, the value of the override units of CALLC and CALLC II was derived from a probability-weighted expected return method. The probability-weighted expected return method involves a forward-looking analysis of possible future outcomes, the estimation of ranges of future and present value under each outcome, and the application of a probability factor to each outcome in conjunction with the application of the current value of the Company s common stock price with a Black-Scholes option pricing formula, as remeasured at each reporting date until the awards are vested.

The estimated fair value of the override units of CALLC III has been determined using a probability-weighted expected return method which utilizes CALLC III s cash flow projections, which are representative of the nature of the interests held by CALLC III in the Partnership.

The following table provides key information for the share-based compensation plans related to the override units of CALLC, CALLC II, and CALLC III. Compensation expense amounts are disclosed in thousands.

Award Type	Benchmark Value (per Unit)	Original Awards Issued	Grant Date	*Compensation Expense Increase (Decrease) for the Three Months Ended September 30, 2010	2009	*Compensation Expense Increase (Decrease) for the Nine Months Ended September 30, 2010	2009
Override Operating Units(a)	$ 11.31	919,630	June 2005	$	$ 962	$ 338	$ 2,449
Override Operating Units(b)	$ 34.72	72,492	December 2006		43	12	95
Override Value Units(c)	$ 11.31	1,839,265	June 2005	1,730	6,353	3,728	9,442
Override Value Units(d)	$ 34.72	144,966	December 2006	16	271	96	405
Override Units(e)	$ 10.00	138,281	October 2007				

Override Units(f)	$ 10.00	642,219	February 2008	1	1	3	5
			Total	$ 1,747	$ 7,630	$ 4,177	$ 12,396

* As CVR s common stock price increases or decreases, compensation expense increases or is reversed in correlation with the calculation of the fair value under the probability-weighted expected return method.

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Valuation Assumptions

Significant assumptions used in the valuation of the Override Operating Units (a) and (b) were as follows:

	(a) Override Operating Units September 30, 2009	(b) Override Operating Units September 30, 2009
Estimated forfeiture rate	None	None
CVR closing stock price	$12.44	$12.44
Estimated weighted-average fair value (per unit)	$24.01	$8.60
Marketability and minority interest discounts	20.0%	20.0%
Volatility	54.3%	54.3%

On the tenth anniversary of the issuance of override operating units, such units convert into an equivalent number of override value units. Override operating units are forfeited upon termination of employment for cause. As of September 30, 2010 these units were fully vested.

Significant assumptions used in the valuation of the Override Value Units (c) and (d) were as follows:

	(c) Override Value Units September 30,		(d) Override Value Units September 30,	
	2010	2009	2010	2009
Estimated forfeiture rate	None	None	None	None
Derived service period	6 years	6 years	6 years	6 years
CVR closing stock price	$8.25	$12.44	$8.25	$12.44
Estimated weighted-average fair value (per unit)	$8.53	$18.52	$2.04	$8.60
Marketability and minority interest discounts	20.0%	20.0%	20.0%	20.0%
Volatility	45.4%	54.3%	45.4%	54.3%

Unless the compensation committee of the board of directors of CVR takes an action to prevent forfeiture, override value units are forfeited upon termination of employment for any reason, except that in the event of termination of employment by reason of death or disability, all override value units are initially subject to forfeiture as follows:

Minimum Period Held	Forfeiture Percentage
2 years	75%
3 years	50%

4 years	25%
5 years	0%

(e) *Override Units* Using a binomial and a probability-weighted expected return method that utilized CALLC III s cash flow projections which includes expected future earnings and the anticipated timing of IDRs, the estimated grant date fair value of the override units was approximately $3,000. As a non-contributing investor, CVR also recognized income equal to the amount that its interest in the investee s net book value has increased (that is its percentage share of the contributed capital recognized by the investee) as a result of the disproportionate funding of the compensation cost. As of September 30, 2010 these units were fully vested.

(f) *Override Units* Using a probability-weighted expected return method that utilized CALLC III s cash flow projections which includes expected future earnings and the anticipated timing of IDRs, the estimated

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

grant date fair value of the override units was approximately $3,000. As a non-contributing investor, CVR also recognized income equal to the amount that its interest in the investee s net book value has increased (that is its percentage share of the contributed capital recognized by the investee) as a result of the disproportionate funding of the compensation cost. Of the 642,219 units issued, 109,720 were immediately vested upon issuance and the remaining units are subject to a forfeiture schedule. Significant assumptions used in the valuation were as follows:

	September 30,	
	2010	**2009**
Estimated forfeiture rate	None	None
Derived Service Period	Based on forfeiture schedule	Based on forfeiture schedule
Estimated fair value (per unit)	$0.08	$0.03
Marketability and minority interest discount	20.0%	20.0%
Volatility	59.7%	47.0%

Based upon the estimated fair value at September 30, 2010, there was approximately $1,855,000 of unrecognized compensation expense related to non-voting override units. This expense is expected to be recognized over a remaining period of approximately one year as follows (in thousands):

	Override Value Units
Three months ending December 31, 2010	$ 642,000
Year ending December 31, 2011	1,213,000
	$ 1,855,000

Phantom Unit Plans

CVR, through a wholly-owned subsidiary, has two Phantom Unit Appreciation Plans (the Phantom Unit Plans) whereby directors, employees, and service providers may be awarded phantom points at the discretion of the board of directors or the compensation committee. Holders of service phantom points have rights to receive distributions when holders of override operating units receive distributions. Holders of performance phantom points have rights to receive distributions when CALLC and CALLC II holders of override value units receive distributions. There are no other rights or guarantees and the plan expires on July 25, 2015, or at the discretion of the compensation committee of the board of directors. As of September 30, 2010, the issued Profits Interest (combined phantom points and override units) represented 15.0% of combined common unit interest and Profits Interest of CALLC and CALLC II. The Profits Interest was comprised of approximately 11.1% of override interest and approximately 3.9% of phantom interest. The expense associated with these awards is based on the current fair value of the awards which was derived from a probability-weighted expected return method. The probability-weighted expected return method involves a forward-looking analysis of possible future outcomes, the estimation of ranges of future and present value under each

outcome, and the application of a probability factor to each outcome in conjunction with the application of the current value of the Company s common stock price with a Black-Scholes option pricing formula, as remeasured at each reporting date until the awards are settled. Based upon this methodology, the service phantom interest and performance phantom interest were valued at $13.66 and $8.36 per point, respectively, at September 30, 2010. Using the September 30, 2009, CVR stock closing price to determine the Company s equity value, through an independent valuation process, the service phantom interest and performance phantom interest were valued at $23.44 and $18.28 per point, respectively. CVR has recorded approximately $9,835,000 and $6,723,000 in personnel accruals as of September 30, 2010 and December 31, 2009, respectively. Compensation expense for

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

the three months ended September 30, 2010 and 2009 related to the Phantom Unit Plans was $1,469,000 and $8,166,000, respectively. Compensation expense for the nine months ended September 30, 2010 and 2009 related to the Phantom Unit Plans was $3,112,000 and $12,665,000, respectively.

Based upon the estimated fair value at September 30, 2010, there was approximately $553,000 of unrecognized compensation expense related to the Phantom Unit Plans. This is expected to be recognized over a remaining period of approximately one year.

Long-Term Incentive Plan

CVR has a Long-Term Incentive Plan (LTIP) that permits the grant of options, stock appreciation rights, non-vested shares, non-vested share units, dividend equivalent rights, share awards and performance awards (including performance share units, performance units and performance based restricted stock).

Stock Options

As of September 30, 2010, there have been a total of 32,350 stock options granted, of which 21,569 have vested. However, 6,301 vested options have expired, resulting in a net total of 15,268 outstanding options that have vested. Additionally, 3,149 unvested stock options were forfeited in the second quarter of 2010. During the three months ended September 30, 2010, 3,033 stock options vested and 6,301 stock options expired. There were no grants of stock options for the nine months ended September 30, 2010. The fair value of stock options is estimated on the date of grant using the Black-Scholes option pricing model. As of September 30, 2010, there was approximately $13,000 of total unrecognized compensation cost related to stock options to be recognized over a weighted-average period of less than one year.

Non-Vested Stock

A summary of non-vested stock grant activity and changes during the nine months ended September 30, 2010 is presented below:

Non-Vested Stock	Shares	Weighted-Average Grant-Date Fair Value
Outstanding at January 1, 2010 (non-vested)	177,060	$ 6.59
Vested	(20,013)	8.90
Granted	613,643	7.20
Forfeited	(1,799)	4.14
Outstanding at September 30, 2010 (non-vested)	768,891	$ 7.03

Through the LTIP, shares of non-vested stock have been granted to employees and directors of the Company. Non-vested shares, when granted, are valued at the closing market price of CVR s common stock on the date of issuance and amortized to compensation expense on a straight-line basis over the vesting period of the stock. These shares generally vest over a three-year period. As of September 30, 2010, there was approximately $4,242,000 of total unrecognized compensation cost related to non-vested shares to be recognized over a weighted-average period of approximately two and one-half years.

Compensation expense recorded for the three months ended September 30, 2010 and 2009 related to the non-vested stock and stock options was $707,000 and $125,000, respectively. Compensation expense recorded for the nine months ended September 30, 2010 and 2009 related to the non-vested stock and stock options was $1,068,000 and $340,000, respectively.

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) Inventories

Inventories consist primarily of domestic and foreign crude oil, blending stock and components, work-in-progress, fertilizer products, and refined fuels and by-products. Inventories are valued at the lower of the first-in, first-out (FIFO) cost or market for fertilizer products, refined fuels and by-products for all periods presented. Refinery unfinished and finished products inventory values were determined using the ability-to-bear process, whereby raw materials and production costs are allocated to work-in-process and finished products based on their relative fair values. Other inventories, including other raw materials, spare parts, and supplies, are valued at the lower of moving-average cost, which approximates FIFO, or market. The cost of inventories includes inbound freight costs.

Inventories consisted of the following (in thousands):

	September 30, 2010	December 31, 2009
Finished goods	$ 105,084	$ 123,548
Raw materials and catalysts	91,148	107,840
In-process inventories	16,639	19,401
Parts and supplies	25,067	24,049
	$ 237,938	$ 274,838

(5) Property, Plant, and Equipment

A summary of costs for property, plant, and equipment is as follows (in thousands):

	September 30, 2010	December 31, 2009
Land and improvements	$ 18,545	$ 18,016
Buildings	25,599	23,316
Machinery and equipment	1,354,312	1,305,362
Automotive equipment	8,826	8,796
Furniture and fixtures	9,251	8,095
Leasehold improvements	1,247	1,301
Construction in progress	43,291	77,818
	1,461,071	1,442,704
Accumulated depreciation	368,383	304,794
	$ 1,092,688	$ 1,137,910

Capitalized interest recognized as a reduction in interest expense for the three months ended September 30, 2010 and 2009, totaled approximately $93,000 and $536,000, respectively. Capitalized interest recognized as a reduction in interest expense for the nine months ended September 30, 2010 and 2009, totaled approximately $1,740,000 and $1,338,000, respectively. Land, buildings and equipment that are under a capital lease obligation approximated $5,242,000 as of September 30, 2010. Amortization of assets held under capital leases is included in depreciation expense.

(6) Cost Classifications

Cost of product sold (exclusive of depreciation and amortization) includes cost of crude oil, other feedstocks, blendstocks, pet coke expense and freight and distribution expenses. Cost of product sold excludes depreciation and amortization of $697,000 and $727,000 for the three months ended September 30, 2010 and

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2009, respectively. For the nine months ended September 30, 2010 and 2009 cost of product sold excludes depreciation and amortization of $2,163,000 and $2,157,000, respectively.

Direct operating expenses (exclusive of depreciation and amortization) includes direct costs of labor, maintenance and services, energy and utility costs, as well as chemicals and catalysts and other direct operating expenses. Direct operating expenses exclude depreciation and amortization of $20,703,000 and $20,312,000 for the three months ended September 30, 2010 and 2009, respectively. For the nine months ended September 30, 2010 and 2009, direct operating expenses exclude depreciation and amortization of $61,023,000 and $59,975,000, respectively.

Selling, general and administrative expenses (exclusive of depreciation and amortization) consist primarily of legal expenses, treasury, accounting, marketing, human resources and costs associated with maintaining the corporate and administrative office in Texas and the administrative office in Kansas. Selling, general and administrative expenses exclude depreciation and amortization of $542,000 and $595,000 for the three months ended September 30, 2010 and 2009, respectively. For the nine months ended September 30, 2010 and 2009, selling, general and administrative expenses exclude depreciation and amortization of $1,570,000 and $1,518,000, respectively.

(7) Note Payable and Capital Lease Obligations

The Company entered into an insurance premium finance agreement in July 2010 to finance a portion of the purchase of its 2010/2011 property insurance policies. The original balance of the note provided by the Company under such agreement was $5,000,000. This note will be paid in equal installments commencing October 1, 2010. In July 2009, the Company entered into an insurance premium finance agreement to finance a portion of the purchase of its 2009/2010 property, liability, cargo and terrorism insurance policies. The original balance of the note provided by the Company under such agreement was $10,000,000. This note was paid in full in June 2010. As of December 31, 2009, the Company owed $7,500,000 related to this note.

The Company also entered into a capital lease for real property used for corporate purposes on May 29, 2008. The lease had an initial lease term of one year with an option to renew for three additional one-year periods. During the second quarter of 2010, the Company renewed the lease for a one-year period commencing June 5, 2010. The Company makes quarterly lease payments that total $80,000 annually. The Company also has the option to purchase the property during the term of the lease, including the renewal periods. The Company originally recorded a capital asset and capital lease obligation of $4,827,000. The capital lease obligation was $4,506,000 and $4,274,000 as of September 30, 2010 and December 31, 2009, respectively.

(8) Flood, Crude Oil Discharge and Insurance Related Matters

For the three months ended September 30, 2010 and 2009, the Company recorded pre-tax expenses, net of anticipated insurance recoveries of $(970,000) and $529,000, respectively, associated with the June/July 2007 flood and associated crude oil discharge. For the nine months ended September 30, 2010 and 2009, the Company recorded pre-tax expenses, net of anticipated insurance recoveries of $(970,000) and $609,000, respectively, associated with the June/July 2007 flood and associated crude oil discharge. The costs are reported in net costs associated with flood in the Condensed Consolidated Statements of Operations. With the final insurance proceeds received under the Company s property insurance policy and builders risk policy during the first quarter of 2009, in the amount of $11,756,000, all property insurance claims and builders risk claims were fully settled, with all remaining claims closed under these policies only.

As of September 30, 2010, the remaining receivable from environmental insurance carriers was not anticipated to be collected in the next twelve months, and therefore has been classified as a non-current asset. See Note 12 (Commitments and Contingent Liabilities) for additional information regarding environmental and other contingencies related to the crude oil discharge that occurred on July 1, 2007.

CVR ENERGY, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(9) Nitrogen Fertilizer Incident

On September 30, 2010, the nitrogen fertilizer plant experienced an interruption in operations due to a rupture of a high-pressure Urea Ammonium Nitrate vessel. All operations at the nitrogen fertilizer facility were immediately shut down. No one was injured in the incident.

The nitrogen fertilizer facility had previously scheduled a major turnaround to begin on October 5, 2010. To minimize disruption and impact to the production schedule, the turnaround was accelerated. The turnaround was completed on October 29, 2010 with the gasification and ammonia units in operation. Repairs continue at the UAN unit due to the incident.

Based upon a preliminary internal investigation, the Company currently estimates that the cost to repair the damage caused by the incident will be in the range of $7.0 million to $10.0 million and repairs are expected to be completed prior to the end of November 2010. To the extent additional damage is discovered during the completion of the investigation or during completion of repairs, the cost to repair could increase or repairs could take longer to complete.

The Company maintains property damage insurance with a deductible of $2.5 million. The Company anticipates that substantially all of the repair costs in excess of the $2.5 million deductible should be covered by insurance. The Company s insurance policies also provide coverage for interruption to the business, including lost profits, and reimbursement for other expenses and costs the Company has incurred relating to the damage and losses suffered for business interruption. This coverage, however, only applies to losses incurred after a business interruption of 45 days.

As of September 30, 2010, the Company has written off $390,000 of net book value of property and $24,000 of catalysts destroyed as a result of the incident. These amounts were recorded in selling, general and administrative expenses (exclusive of depreciation and amortization) and direct operating expenses (exclusive of depreciation and amortization), respectively. The Company did not record an insurance receivable for these expenses due to the associated deductible.

Cash paid to owners	$16,673	
Contingent consideration	5,253	
Cash acquired	(680	)
Total fair value of consideration transferred	$21,246	

8

Table of Contents

ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table summarizes estimated fair values of the assets acquired and liabilities assumed as of November 8, 2012 (in thousands):

Cash	$680	
Accounts receivable	1,074	
Inventories	57	
Other receivables	32	
Other current assets	46	
Property and equipment	43	
Accounts payable	(390	)
Accrued payroll and employee benefits	(186	)
Other accrued expenses	(159	)
Customer deposits	(38	)
Deferred tax liabilities	(1,628	)
	(469	)
Amortizable intangible assets:		
Trademarks	106	
Technology	2,723	
Customer relationships	5,398	
Total amortizable intangible assets	8,227	
Total identifiable net assets	7,758	
Goodwill	13,488	
Total fair value of consideration transferred	$21,246	

A summary of the intangible assets acquired, amortization method and estimated useful lives as of November 8, 2012 follows (in thousands, except useful life):

	Amount	Amortization Method	Useful Life
Trademarks	$106	Straight-line	3
Technology	2,723	Straight-line	9
Customer relationships - other	744	Straight-line	7
Customer relationships - design	4,643	Straight-line	12
	$8,216		

Goodwill and intangible assets are recorded in the functional currency of the entity and are subject to changes due to translation at each balance sheet date.

The cost of the acquisition may increase or decrease based on the final amount payable to the former owner of Solvix related to the financial targets to be met during the three years ending December 31, 2015. Advanced Energy is in the process of finalizing valuations of other intangibles, estimates of the fair value of liabilities associated with the acquisition and deferred taxes and expects to complete the acquisition accounting and required disclosures prior to December 31, 2013.

The results of Solvix operations are included in our Condensed Consolidated Statements of Operations beginning November 8, 2012. The results of Solvix's operations for the three months ended March 31, 2013 are as follows (in thousands):

Sales	$1,222	
Net loss	(234	)

Pro Forma Results for Solvix Acquisition

The following unaudited pro forma financial information presents the combined results of operations of Advanced Energy and Solvix as if the acquisition had occurred as of January 1, 2012. The pro forma financial information is presented for informational purposes and is not indicative of the results of operations that would have been achieved if the acquisition had taken place at

9

January 1, 2012. The unaudited pro forma financial information for the three months ended March 31, 2012 includes the historical results of Advanced Energy for the three months ended March 31, 2012 and the historical results of Solvix for the same periods.

The unaudited pro forma results for all periods presented include amortization charges for acquired intangible assets and related tax effects. These pro forma results consider the sale of the gas flow control business and related product lines as discontinued operations. The unaudited pro forma results follow (in thousands, except per share data):

	(Unaudited) Three Months Ended March 31, 2012
Sales	$107,317
Net income	1,070
Earnings per share:	
Basic	$0.03
Diluted	0.03

Disposition

On October 15, 2010, we completed the sale of our gas flow control business, which included the Aera® mass flow control and related product lines to Hitachi Metals, Ltd. ("Hitachi"), for approximately $43.3 million. Assets and liabilities sold included, without limitation, inventories, real property in Hachioji, Japan, equipment, certain contracts, intellectual property rights related to the gas flow control business and certain warranty liability obligations.

In connection with the closing of this asset disposition, we entered into a Master Services Agreement and a Supplemental Transition Services Agreement pursuant to which we provided certain transition services until October 2011 and we became an authorized service provider for Hitachi in all countries other than Japan. In March 2012, we entered into an agreement to sell certain fixed assets to Hitachi and cease providing contract manufacturing services. As of May 31, 2012, we ceased providing contract manufacturing services to Hitachi and completed the sale of certain fixed assets related to that manufacturing. The sale of these assets resulted in a $1.9 million gain, which is recorded in Other income (expense), net in our Condensed Consolidated Statements of Operations. As of June 30, 2012, all manufacturing activities and relationships with Hitachi related to the previously owned gas flow control business have ended. We do not anticipate any additional activity with Hitachi in respect of these assets that would materially impact our financial statements in the future.

In accordance with authoritative accounting guidance for reporting discontinued operations, for the periods reported in this Form 10-Q, the results of continuing operations were reduced by the revenue and costs associated with the gas flow control business, which are included in the Income from discontinued operations, net of income taxes, in our Condensed Consolidated Statements of Operations.

Operating results of discontinued operations are as follows (in thousands):

	Three Months Ended March 31, 2012	
Sales	$4,576	
Cost of sales	5,145	
Gross profit (loss)	(569	)
Operating expenses:		
Research and development	—	
Selling, general, and administrative	45	
Total operating expenses	45	
Operating income (loss) from discontinued operations	(614	)
Other income	1,023	

Income from discontinued operations before income taxes	409
Provision for income taxes	106
Income from discontinued operations, net of income taxes	$303

10

Table of Contents
ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

NOTE 3. INCOME TAXES
The following table sets out the tax expense and the effective tax rate for our income from continuing operations (in thousands):

	Three Months Ended March 31,	
	2013	2012
Income from continuing operations before income taxes	$7,516	$1,034
Provision for income taxes	690	268
Effective tax rate	9.2 %	25.9 %

Our tax rate is lower than the U.S. federal income tax rate primarily due to the benefit of earnings in foreign jurisdictions which are subject to lower tax rates. In addition, during the three months ended March 31, 2013, we recognized a discrete tax benefit of $1.4 million related to the January 2, 2013 reinstatement of the 2012 U.S. research and development tax credit.
Undistributed earnings of foreign subsidiaries are considered to be permanently reinvested and accordingly, no provision for U.S. federal and state income taxes or foreign withholding taxes has been made.
Our policy is to classify accrued penalties and interest related to unrecognized tax benefits in our income tax provision. For the three months ended March 31, 2013 and 2012, the amount of interest and penalties accrued related to our unrecognized tax benefits was not significant.
NOTE 4. EARNINGS PER SHARE FOR CONTINUING OPERATIONS
Basic earnings per share (“EPS”) is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding during the period. The computation of diluted EPS is similar to the computation of basic EPS except that the numerator is increased to exclude charges that would not have been incurred, and the denominator is increased to include the number of additional common shares that would have been outstanding (using the if-converted and treasury stock methods), if securities containing potentially dilutive common shares (e.g., stock options and restricted stock units) had been converted to common shares, and if such assumed conversion is dilutive.
The following is a reconciliation of the weighted-average shares outstanding used in the calculation of basic and diluted EPS (in thousands, except per share data):

	Three Months Ended March 31,	
	2013	2012
Income from continuing operations, net of income taxes	$6,826	$766
Basic weighted-average common shares outstanding	38,775	40,781
Assumed exercise of dilutive stock options and restricted stock units	823	511
Diluted weighted-average common shares outstanding	39,598	41,292
Income from continuing operations:		
Basic earnings per share	$0.18	$0.02
Diluted earnings per share	$0.17	$0.02

The following stock options and restricted units were excluded in the computation of diluted earnings per share because they were anti-dilutive:

	Three Months Ended March 31,	
	2013	2012
Stock options	853	5,847
Restricted stock units	—	23

11

Share Repurchases

In October 2012, our Board of Directors authorized a program to repurchase up to $25.0 million of our stock over a twelve-month period. Under this program, during the three months ended March 31, 2013, we have not yet repurchased any shares.

NOTE 5. MARKETABLE SECURITIES

Our investments with original maturities of more than three months at time of purchase are considered marketable securities available for sale.

The composition of our marketable securities is as follows (in thousands):

	March 31, 2013		December 31, 2012	
	Cost	Fair Value	Cost	Fair Value
Commercial paper	$—	$—	$749	$749
Certificates of deposit	12,260	12,260	12,498	12,498
Corporate bonds/notes	—	—	11,274	11,253
Municipal bonds/notes	283	283	285	285
Agency bonds/notes	—	—	900	898
Total marketable securities	$12,543	$12,543	$25,706	$25,683

The maturities of our marketable securities available for sale as of March 31, 2013 are as follows:

	Earliest		Latest
Certificates of deposit	4/2/2013	to	2/17/2015
Municipal bonds/notes	9/1/2013	to	9/1/2013

The value and liquidity of the marketable securities we hold are affected by market conditions, as well as the ability of the issuers of such securities to make principal and interest payments when due, and the functioning of the markets in which these securities are traded. Our current investments in marketable securities are expected to be liquidated during the next twelve months.

As of March 31, 2013, we do not believe any of the underlying issuers of our marketable securities are presently at risk of default.

NOTE 6. DERIVATIVE FINANCIAL INSTRUMENTS

We are impacted by changes in foreign currency exchange rates. We manage these risks through the use of derivative financial instruments, primarily forward contracts. During the three months ended March 31, 2013 and 2012, we entered into foreign currency exchange forward contracts to manage the exchange rate risk associated with intercompany debt denominated in nonfunctional currencies. These derivative instruments are not designated as hedges; however, they do offset the fluctuations of our intercompany debt due to foreign exchange rate changes. These forward contracts are typically for one month periods. At March 31, 2013 and December 31, 2012 we had outstanding Euro, Swiss Franc, and Canadian Dollar forward contracts.

The notional amount of foreign currency exchange contracts at March 31, 2013 and 2012 was $24.2 million and $41.5 million, respectively, and the fair value of these contracts was not significant at March 31, 2013 and 2012. During the three months ended March 31, 2013 and 2012, we recognized a gain of $0.6 million and a loss of $1.0 million, respectively, on our foreign currency exchange contracts. These gains and losses were offset by corresponding gains and losses on the related intercompany debt and both are included as a component of Other income (expense), net, in our Condensed Consolidated Statements of Operations.

12

Table of Contents

NOTE 7. ASSETS MEASURED AT FAIR VALUE

The following tables present information about our financial assets measured at fair value, on a recurring basis, as of March 31, 2013, and December 31, 2012. The tables indicate the fair value hierarchy of the valuation techniques utilized to determine such fair value. We did not have any financial liabilities measured at fair value, on a recurring basis, as of March 31, 2013, and December 31, 2012.

March 31, 2013	Level 1	Level 2	Level 3	Total
	(In thousands)			
Certificates of deposit	—	12,260	—	12,260
Municipal bonds/notes	—	283	—	283
Total marketable securities	$—	$12,543	$—	$12,543

December 31, 2012	Level 1	Level 2	Level 3	Total
	(In thousands)			
Commercial paper	$—	$749	$—	$749
Certificates of deposit	—	12,498	—	12,498
Corporate bonds/notes	—	11,253	—	11,253
Municipal bonds/notes	—	285	—	285
Agency bonds/notes	898	—	—	898
Total marketable securities	$898	$24,785	$—	$25,683

There were no transfers in or out of Level 1, 2, or 3 fair value measurements during the three months ended March 31, 2013.

NOTE 8. INVENTORIES

Our inventories are valued at the lower of cost or market and computed on a first-in, first-out (FIFO) basis. Components of inventories are as follows (in thousands):

	March 31, 2013	December 31, 2012
Parts and raw materials	$61,570	$59,484
Work in process	6,523	3,728
Finished goods	11,429	18,270
Inventories, net of reserves	$79,522	$81,482

Table of Contents
ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

NOTE 9. PROPERTY AND EQUIPMENT

Details of property and equipment are as follows (in thousands):

	March 31, 2013	December 31, 2012
Buildings and land	$1,715	$1,794
Machinery and equipment	40,241	40,993
Computer and communication equipment	23,017	22,895
Furniture and fixtures	1,835	1,845
Vehicles	384	359
Leasehold improvements	27,972	27,976
Construction in process	3,909	3,362
	99,073	99,224
Less: Accumulated depreciation	(61,934)	(59,701)
Property and equipment, net	$37,139	$39,523

Depreciation expense recorded in continuing operations is as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Depreciation expense	$3,073	$2,841

NOTE 10. GOODWILL

The following summarizes the changes in goodwill during the three months ended March 31, 2013 (in thousands):

Balance as of December 31, 2012	$60,391
Adjustments	(11)
Translation adjustments	(495)
Balance as of March 31, 2013	$59,885

NOTE 11. INTANGIBLE ASSETS

Other intangible assets consisted of the following as of March 31, 2013 (in thousands, except weighted-average useful life):

	Gross Carrying Amount	Effect of Changes in Exchange Rates	Accumulated Amortization	Net Carrying Amount	Weighted-Average Useful Life in Years
Amortizable intangibles:					
Technology-based	$44,668	$(14)	$(12,613)	$32,041	7
Trademarks and other	13,714	(29)	(2,012)	11,673	9
Total amortizable intangibles	$58,382	$(43)	$(14,625)	$43,714	

Table of Contents
ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Other intangible assets consisted of the following as of December 31, 2012 (in thousands, except weighted-average useful life):

	Gross Carrying Amount	Effect of Changes in Exchange Rates	Accumulated Amortization	Net Carrying Amount	Weighted-Average Useful Life in Years
Amortizable intangibles:					
Technology-based	$44,668	$83	$(10,775)	$33,976	7
Trademarks and other	13,703	167	(1,637)	12,233	9
Total amortizable intangibles	$58,371	$250	$(12,412)	$46,209	

Amortization expense relating to other intangible assets included in our income from continuing operations is as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Amortization expense	$2,213	$1,372

Amortization expense related to intangibles for each of the five years 2013 through 2017 and thereafter is as follows (in thousands):

Year Ending December 31,	
2013 (remaining)	$6,689
2014	9,681
2015	9,228
2016	7,031
2017	3,621
Thereafter	7,464
	$43,714

NOTE 12. OTHER ACCRUED EXPENSES

Other accrued expenses consisted of the following (in thousands):

	March 31, 2013	December 31, 2012
Other accrued expenses:		
Current deferred tax liability	$4,137	$4,137
Accrued restructuring costs	655	1,853
Current contingent consideration	2,773	2,773
Accrued sales and use tax	983	1,010
Other*	6,820	5,626
Total Other accrued expenses	$15,368	$15,399

*Other accrued expenses consisted of items that are individually less than 5% of total current liabilities.

NOTE 13. RESTRUCTURING COSTS

In September 2011, we approved and committed to several initiatives to realign our manufacturing and research and development activities in order to foster growth and enhance profitability. These initiatives are designed to align research and development activities with the location of our customers and reduce production costs. Under this plan, we reduced our global

Table of Contents
ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

headcount, consolidated our facilities by terminating or exiting several leases, and recorded impairments for assets no longer in use due to the restructuring of our business. All activities under this restructuring plan were completed prior to December 31, 2012.

The following table summarizes our restructuring liabilities under the plan (in thousands):

	Balances at December 31, 2012	Costs incurred and charged to expense	Cost paid or otherwise settled	Effect of change in exchange rates	Balances at March 31, 2013
Severance and related costs	$1,345	$—	$(1,044)	$(26)	$275
Facility closure costs	508	—	(128)	—	380
Total restructuring liabilities	$1,853	$—	$(1,172)	$(26)	$655

NOTE 14. WARRANTIES

Provisions of our sales agreements include product warranties customary to these types of agreements, ranging from 18 months to 24 months following installation for Thin Films products and 5 years to 10 years following installation for Solar Energy products. Our provision for the estimated cost of warranties is recorded when revenue is recognized. The warranty provision is based on historical experience by product, configuration and geographic region.

We establish accruals for warranty issues that are probable to result in future costs. Changes in product warranty accruals are as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Balances at beginning of period	$14,797	$14,719
Increases to accruals related to sales during the period	2,001	1,835
Warranty expenditures	(3,059)	(2,235)
Balances at end of period	$13,739	$14,319

We also offer our Solar Energy customers the option to purchase additional warranty coverage up to 20 years after the base warranty period expires. Deferred revenue related to such extended warranty contracts was $20.8 million as of March 31, 2013, of which $0.3 million is classified in Customer deposits and $20.5 million is classified in Other long-term liabilities in the Condensed Consolidated Balance Sheet as of March 31, 2013. As of December 31, 2012, deferred revenue related to extended warranty contracts was $20.5 million, of which $0.4 million is classified in Customer deposits and $20.1 million is classified in Other long-term liabilities.

NOTE 15. STOCK-BASED COMPENSATION

We recognize stock-based compensation expense based on the fair value of the awards issued. Stock-based compensation for the three months ended March 31, 2013 and 2012 is as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Stock-based compensation expense	$2,034	$5,009

Stock Options

Stock option awards, other than awards under our 2012-2014 Long Term Incentive Plan ("LTI Plan"), are generally granted with an exercise price equal to the market price of our common stock at the date of grant, a four-year vesting schedule, and a term of 10 years.

Under the LTI Plan, we made grants of performance based options and awards during the first quarter of 2012, which will vest annually over a three-year period based on the Company's achievement of return on net assets targets established by our

Table of Contents

Board of Directors at the beginning of each year. These awards are granted with an exercise price equal to the market price of our common stock at the date of grant and have a term of 10 years. The fair value of each grant was estimated on the date of grant using the Black-Scholes-Merton option pricing model utilizing an expected volatility of 61.5%, a risk-free rate of 1.2%, a dividend yield of zero, and an expected term of 5.9 years. The weighted-average grant date fair value of the options is $6.19 per share. The weighted average grant date fair value of the awards is $11.03 per share.

A summary of our stock option activity for the three months ended March 31, 2013 is as follows (in thousands):

	Shares
Options outstanding at December 31, 2012	5,659
Options granted	—
Options exercised	(1,068)
Options forfeited	(415)
Options expired	(21)
Options outstanding at March 31, 2013	4,155

Restricted Stock Units

Restricted Stock Units ("RSU") are generally granted with a four-year vesting schedule.

A summary of our non-vested RSU activity for the three months ended March 31, 2013 is as follows (in thousands):

	Shares
Balance at December 31, 2012	2,073
RSUs granted	—
RSUs vested	(273)
RSUs forfeited	(22)
Balance at March 31, 2013	1,778

NOTE 16. ACCUMULATED OTHER COMPREHENSIVE INCOME

Accumulated other comprehensive income consisted of the following (in thousands):

	Foreign Currency Adjustments	Unrealized Gains (Losses) on Marketable Securities	Total Accumulated Other Comprehensive Income
Balances at December 31, 2012	$29,730	$(5)	$29,725
Current period other comprehensive income (loss)	(2,834)	(7)	(2,841)
Balances at March 31, 2013	$26,896	$(12)	$26,884

NOTE 17. COMMITMENTS AND CONTINGENCIES

We have firm purchase commitments and agreements with various suppliers to ensure the availability of components. The obligation as of March 31, 2013 is approximately $62.6 million. Our policy with respect to all purchase commitments, is to record losses, if any, when they are probable and reasonably estimable. We continuously monitor these commitments for exposure to potential losses and will record a provision for losses when it is deemed necessary.

Table of Contents
ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

NOTE 18. RELATED PARTY TRANSACTIONS
During the three months ended March 31, 2013 and 2012, we engaged in the following transactions with companies related to members of our Board of Directors, as described below (in thousands):

	Three Months Ended March 31,	
	2013	2012
Sales - related parties	$31	$154
Rent expense - related parties	475	460

Sales - Related Parties
Members of our Board of Directors hold various executive positions and serve as directors at other companies, including companies that are our customers. During the three months ended March 31, 2013, we had sales to two such customers as noted above and accounts receivable from one such customers totaled $23,160 at March 31, 2013. During the three months ended March 31, 2012, we had sales to two such customers as noted above and no aggregate accounts receivable from these customers at December 31, 2012.
Rent Expense - Related Parties
We lease our executive offices, research and development, and manufacturing facilities in Fort Collins, Colorado from a limited liability partnership in which Douglas Schatz, our Chairman of the Board and former Chief Executive Officer, holds an interest. The leases relating to these spaces expire during 2021 and obligate us to total annual payments of approximately $1.5 million, which includes facilities rent and common area maintenance costs.

NOTE 19. SEGMENT INFORMATION
Our Thin Films SBU offers power conversion products for direct current, pulsed DC mid frequency, and radio frequency power supplies, matching networks, and RF instrumentation, as well as thermal instrumentation products. Our power conversion systems refine, modify, and control the raw electrical power from a utility and convert it into power that may be customized and is predictable and repeatable. Our thermal instrumentation products provide temperature measurement solutions for applications in which time-temperature cycles affect material properties, productivity, and yield. These products are used in rapid thermal processing, chemical vapor deposition, and other semiconductor and solar applications requiring non-contact temperature measurement. Our network of global service support centers offer repair services, conversions, upgrades, and refurbishments to companies using our products. Our Thin Films SBU principally serves original equipment manufacturers (“OEMs”) and end customers in the semiconductor, flat panel display, solar panel, and other capital equipment markets.
Our Solar Energy SBU offers both a transformer-based and a transformerless advanced grid-tied PV inverter solution primarily for commercial and utility-scale system installations. Our PV inverters are designed to convert renewable solar power, drawn from large and small scale solar arrays, into high-quality, reliable electrical power. Our Solar Energy SBU focuses on commercial and utility-scale solar projects and installations, selling primarily to distributors, engineering, procurement, and construction contractors, developers, and utility companies. Our Solar Energy revenue has seasonal variations. Installations of inverters are normally lowest during the first quarter as a result of typically poor weather and installation scheduling by our customers.
Our chief operating decision maker, who is our Chief Executive Officer, and other management personnel regularly review our performance and make resource allocation decisions by reviewing the results of our two business segments separately. Revenue and operating profit is reviewed by our chief operating decision maker. We have also divided inventory and property and equipment based on business segment.

Sales with respect to our operating segments is as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Thin Films	$61,777	$60,390
Solar Energy	50,037	45,397
Total	$111,814	$105,787

Income from continuing operations before income taxes by operating segment is as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Thin Films	$7,511	$3,167
Solar Energy	208	493
Total segment operating income	7,719	3,660
Corporate expenses	—	(462)
Restructuring charges	—	(2,575)
Other income (expense), net	(203)	411
Income from continuing operations before income taxes	$7,516	$1,034

Corporate expenses in 2012 consist of intangible amortization that is now being allocated to the business units.
Segment assets consist of inventories, net and property and equipment, net. A summary of consolidated total assets by segment follows (in thousands):

	March 31, 2013	December 31, 2012
Thin Films	$38,932	$40,965
Solar Energy	73,593	76,393
Total segment assets	112,525	117,358
Unallocated corporate property and equipment	4,136	3,647
Unallocated corporate assets	434,868	417,155
Consolidated total assets	$551,529	$538,160

"Corporate" is a non-operating business segment with the main purpose of supporting operations. Unallocated corporate assets include accounts receivable, deferred income taxes, other current assets and intangible assets.
During the three months ended March 31, 2013, we had two customers accounting for 10% or more of our sales. Sales to Applied Materials, Inc. were $18.7 million or 16.7% of total sales and sales to Fluor Enterprises, Inc. were $13.5 million or 12.1% of total sales. During the three months ended March 31, 2012, we had one customer accounting for 10% or more of our sales. Sales to Applied Materials, Inc. were $17.8 million or 16.9% of total sales. Our sales to Applied Materials, Inc. include thin film products used in semiconductor processing and solar, flat panel display, and architectural glass applications and our sales to Fluor Enterprises include power stations. No other customer accounted for 10% or more of our sales during these periods.

NOTE 20. CREDIT FACILITY

In October 2012, we, along with two of our wholly-owned subsidiaries, AE Solar Energy, Inc. and Sekidenko, Inc., entered into a Credit Agreement (the “Credit Agreement”) with Wells Fargo Bank, National Association (“Wells Fargo”), as agent for and on behalf of certain lenders (each a “Lender”), which provides for a new secured revolving credit facility of up to $50.0 million (the “Credit Facility”). The Credit Facility provides us with the ability to borrow up to $50.0 million, although the amount of the Credit Facility may be increased by an additional $25.0 million up to a total of $75.0 million subject to receipt of lender commitments and other conditions. Borrowings under the Credit Facility are subject to a borrowing base based upon our domestic accounts receivable and inventory and are available for various corporate purposes, including general working capital, capital expenditures, and certain permitted acquisitions. The Credit Agreement also permits us to issue letters of credit. The maturity date of the Credit

Table Of Contents

Facility is October 12, 2017.
At our election, the loans comprising each borrowing will bear interest at a rate per annum equal to either: (a) a “base rate” plus between one-half (0.5%) and one (1.0%) full percentage point depending on the amount available for additional draws under the Credit Facility (“Base Rate Loan”); or (b) the LIBOR rate then in effect plus between one and one-half (1.5%) and two (2%) percentage points depending on the amount available for additional draws under the Credit Facility. The “base rate” for any Base Rate Loan will be the greatest of the federal funds rate plus one-half (0.5%) percentage point; the one-month LIBOR rate plus one (1.0%) percentage point; and Wells Fargo's “prime rate” then in effect. As of March 31, 2013, the rate in effect was 4.25%.
The Credit Agreement requires us to pay certain fees to the Lenders and contains affirmative and negative covenants, which, among other things, require us to deliver to the Lenders specified quarterly and annual financial information, and limit us and our Guarantors (as defined below), subject to various exceptions and thresholds, from, among other things: (i) creating liens on our assets; (ii) merging with other companies or engaging in other extraordinary corporate transactions; (iii) selling certain assets or properties; (iv) entering into transactions with affiliates; (v) making certain types of investments; (vi) changing the nature of our business; and (vii) paying certain distributions or certain other payments to affiliates. Additionally, during any period in which $12.5 million or less is available to us under the Credit Facility and for sixty (60) days thereafter, the Credit Agreement requires the maintenance of a defined consolidated fixed charge coverage ratio.
The Credit Agreement requires us to pay certain fees to the Lenders, including a $2,500 collateral management fee for each month that the Credit Facility is in place, and a fee based on the unused amount of the Credit Facility. In addition, if the Credit Agreement is terminated by us within one (1) year we will be obligated to pay an early termination fee equal to one percent (1%) of the maximum amount that may be drawn or borrowed under the Credit Facility. During the three months ended March 31, 2013, we expensed $0.1 million in interest and fees related to unused line of credit fees and amortization of debt issuance costs. We did not borrow against the Credit Facility in the first quarter of 2013.
Pursuant to a Guaranty and Security Agreement (the “GS Agreement”), borrowings under the Credit Facility are guaranteed by our wholly-owned subsidiaries Aera Corporation and AEI US Subsidiary, Inc., (collectively the “ Guarantors”). Under the GS Agreement, we and the Guarantors granted the Lenders a security interest in certain, but not all, of our and the Guarantors' assets.
NOTE 21. SUBSEQUENT EVENT
On April 8, 2013, Advanced Energy and Blitz S13-103, GmbH, an indirect wholly-owned subsidiary of Advanced Energy (“Purchaser”) entered into a Sale and Purchase Agreement (the “Agreement ”) with Jolaos Verwaltungs GmbH (“Seller”) and Prettl Beteilgungs Holding Gmbh (“Seller's Guarantor”) whereby the Purchaser acquired from Seller, on the same date, all of the shares of RefuSol Holding GmbH (“Refusol Holding”) which owns all of the shares of RefuSol GmbH and its subsidiaries (collectively and together with RefuSol Holding, “RefuSol”). RefuSol develops, manufactures, distributes and services photovoltaic inverters.
Under the terms of the Agreement, Seller received €59.0 million in cash, we assumed €9.0 million of debt and had a working capital reduction of €1.8 million. The preliminary base price is subject to a post-closing adjustment based on confirmation of the financial statements of RefuSol effective as of the closing date. Each party has agreed to pay its own expenses related to the transaction.
Additional earn-out cash and stock consideration, up to a maximum of €10.0 million total, is payable to Seller if certain stretch financial targets are met by Advanced Energy's Solar Energy Business Unit and RefuSol, on a combined basis, at the end of the twelve (12) calendar months following April 1, 2013. Half of the earn-out, or up to €5.0 million, is payable in cash. The other half of the earn-out, up to €5.0 million is payable in Advanced Energy common stock at a price of approximately $18.85 per share. The per share price was determined based on the volume-weighted average price of Advanced Energy's common stock during the fifteen (15) trading days prior to April 5, 2013. No more than 342,105 shares are issuable pursuant to the earn-out.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Special Note on Forward-Looking Statements

The following discussion contains, in addition to historical information, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Statements in this report that are not historical information are forward-looking statements. For example, statements relating to our beliefs, expectations and plans are forward-looking statements, as are statements that certain actions, conditions or circumstances will continue. The inclusion of words such as "anticipate," "expect," "estimate," "can," "may," "continue," "enables," "plan," "intend," or "believe," as well as statements that events or circumstan occur or continue, indicate forward-looking statements. Forward-looking statements involve risks and uncertainties, which are difficult to predict and many of which are beyond our control. Therefore, actual results could differ materially and adversely from those expressed in any forward-looking statements.

For additional information regarding factors that may affect our actual financial condition, results of operations and accuracy of our forward-looking statements, see the information under the caption "Risk Factors" in Part II Item 1A of this Quarterly Report on Form 10-Q and, in our Annual Report on Form 10-K for the year ended December 31, 2012. We undertake no obligation to revise or update any forward-looking statements for any reason.

BUSINESS OVERVIEW

We design, manufacture, sell and support power conversion products that transform power into various usable forms. Our products enable manufacturing processes that use thin-film and plasma enhanced chemical and physical processing for various products as well as grid-tied power conversion. We also supply thermal instrumentation products for advanced temperature control in the thin-film process for these markets. Our network of global service support centers provides local repair and field service capability in key regions.

- Our power conversion products refine, modify and control the raw electrical power from a utility and convert it into power that is predictable, repeatable and customizable. Our power conversion products are primarily used by semiconductor, solar panel and similar thin-film manufacturers including flat panel display, data storage, and architectural glass manufacturers.
- Our thermal instrumentation products, used primarily in the semiconductor industry, provide temperature measurement and control solutions for applications in which time-temperature cycles affect productivity and yield. These products are used in rapid thermal processing, chemical vapor deposition, and other semiconductor and solar applications requiring non-contact temperature measurement.
- Our grid-tied power conversion products offer advanced transformer-based or transformerless grid-tied PV solutions for commercial and utility-scale system installations and transformer-based solutions for residential installations. Our PV inverters are designed to convert renewable solar power, drawn from large and small scale solar arrays, into high-quality, reliable electrical power. These products are used for residential, commercial and utility-scale solar projects and installations, and are sold primarily to distributors; engineering, procurement, and construction contractors; developers; and utility companies. These product revenues have seasonal variations. Installations of inverters are normally lowest during the first quarter of the year due to less favorable weather conditions and installation scheduling by our customers.
- Our network of global service support centers offer repair services, upgrades and refurbishments to businesses that use our products.

On October 15, 2010, we sold our gas flow control business, which includes the Aera® mass flow control and related product lines, to Hitachi Metals, Ltd. Consequently, the results of operations from our gas flow control business have been excluded from our discussions relating to continuing operations.

On November 8, 2012, we acquired Solvix SA ("Solvix"), a privately held company based in Villaz-Saint-Pierre, Switzerland. The financial results discussed below include the financial results of Solvix for the three months ended March 31, 2013. Note 2. Business Acquisition & Disposition in Part I Item 1 of this Form 10-Q describes the acquisition of Solvix.

As noted in Note 21. Subsequent Event in Part I Item 1 of this Form 10-Q, we acquired Refusol Holdings GmbH ("Refusol") on April 8, 2013, subsequent to the end of the first quarter. As such, the results of Refusol are not included

in the discussion below of financial results for the three months ended March 31, 2013.

Table Of Contents

Our analysis presented below is organized to provide the information we believe will be helpful for understanding our historical performance and relevant trends going forward. This discussion should be read in conjunction with our Condensed Consolidated Financial Statements in Part I, Item 1 of this report, including the notes thereto. Also included in the following analysis are measures that are not in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). A reconciliation of the non-GAAP measures to U.S. GAAP is also provided.

Results of Operations

The following table sets forth, for the periods indicated, certain data derived from our Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended March 31,	
	2013	2012
Sales	$111,814	$105,787
Gross profit	41,839	39,744
Operating expenses	34,120	39,121
Operating income	7,719	623
Other income (expenses), net	(203)	411
Income from continuing operations before income taxes	7,516	1,034
Provision for income taxes	690	268
Income from continuing operations, net of income taxes	$6,826	$766

The following table sets forth, for the periods indicated, the percentage of sales represented by certain items reflected in our Condensed Consolidated Statements of Operations:

	Three Months Ended March 31,	
	2013	2012
Sales	100.0 %	100.0 %
Gross profit	37.4 %	37.6 %
Operating expenses	30.5 %	37.0 %
Operating income	6.9 %	0.6 %
Other income (expenses), net	(0.2)%	0.4 %
Income from continuing operations before income taxes	6.7 %	1.0 %
Provision for income taxes	0.6 %	0.3 %
Income from continuing operations, net of income taxes	6.1 %	0.7 %

SALES

The following tables summarize annual sales, and percentages of sales, by segment for the three months ended March 31, 2013 and 2012 (in thousands):

	Three Months Ended March 31,					
	2013	% of Total Sales	2012	% of Total Sales	Increase/ (Decrease)	Percent Change
Thin Films:						
Semiconductor capital equipment	$32,700	29.2 %	$38,348	36.3 %	$(5,648)	(14.7)%
Non-semiconductor capital equipment	16,610	14.9 %	10,068	9.5 %	6,542	65.0 %
Global support	12,467	11.1 %	11,974	11.3 %	493	4.1 %
Total Thin Films	61,777	55.2 %	60,390	57.1 %	1,387	2.3 %
Solar Energy	50,037	44.8 %	45,397	42.9 %	4,640	10.2 %
Total sales	$111,814	100.0 %	$105,787	100.0 %	$6,027	5.7 %

Table Of Contents

Total Sales

Overall, our sales increased $6.0 million, or 5.7%, to $111.8 million for the three months ended March 31, 2013 from $105.8 million for the three months ended March 31, 2012. The increase in sales is the result of increased solar inverter sales, primarily to the utility markets, in the first quarter of 2013 as compared to the same period in 2012. Although Thin Film sales were relatively flat, we did experience a decline in semiconductor sales during the three months ended March 31, 2013 as compared to 2012 and an offsetting increase in the non-semiconductor markets. The continued decline of capital spending in the semiconductor market throughout 2012 drove the decline in the first quarter of 2013 compared to 2012. The increase in sales in non-semiconductor markets is partially due to the acquisition of Solvix in the fourth quarter of 2012. The first quarter of 2013 included a full quarter of sales of those products. The remaining increase is due to improvements in the flat panel display markets.

Thin Films

Results for our Thin Films SBU for the three months ended March 31, 2013 and 2012 were as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Sales	$61,777	$60,390
Operating Income	7,511	3,167

Thin Films sales increased 2.3% to $61.8 million, or 55.2% of sales, for the three months ended March 31, 2013 versus $60.4 million, or 57.1% of sales, for the three months ended March 31, 2012. The increase reflects the market improvements noted above coupled with a full quarter of sales attributable to our acquisition of Solvix.

In the three months ended March 31, 2013, sales in the thin film semiconductor market decreased 14.7% to $32.7 million, or 29.2% of sales, from $38.3 million, or 36.3% of sales for the three months ended March 31, 2012. The decline in end user capital expansion that began in the third quarter of 2011 continued throughout 2012 resulting in utilization rates at semiconductor foundries that remain reduced compared to previous levels. This drove the decline in sales in the first quarter of 2013 as compared to the same period of 2012. Although sales are still down compared to the first quarter of 2012, markets began to improve during the first quarter of 2013 resulting in sequential growth in sales from the fourth quarter of 2012. Utilization rates are increasing and capital spending is expected to remain stronger into the second quarter of 2013.

Sales in the thin film non-semiconductor capital equipment markets increased 65.0% to $16.6 million, or 14.9% of sales, for the three months ended March 31, 2013 compared to $10.1 million, or 9.5% of sales, for the three months ended March 31, 2012. The markets that comprise the thin-film non-semiconductor capital equipment markets include solar panel, flat panel display, data storage, architectural glass and other industrial thin-film manufacturing equipment markets. Our customers in these markets are primarily global OEMs. The increase in these markets for the three months ended March 31, 2013, as compared to the same period a year ago, was driven by investment in the flat panel display market.

Sales to customers in the thin film solar panel market decreased to $0.3 million, or 0.3% of total sales, for the three months ended March 31, 2013 as compared to $2.0 million, or 1.9% of total sales, for the three months ended March 31, 2012. Capacity in the solar panel market continues to exceed demand. We currently do not anticipate new investment in the foreseeable future as consolidation of manufacturers continues. As a result, we expect sales to the solar panel market to remain at historically low levels through the first half of 2013.

The flat panel market experienced significant growth in the first quarter of 2013, increasing 548.3% compared to the same quarter in 2012. This increase was driven by investments in the transition to active-matrix light-emitting diode ("AMOLED") technology. We expect continued investment in this new technology keeping sales stronger through the first half of 2013.

Our global support revenue increased to $12.5 million, or 11.1% of total sales, for the three months ended March 31, 2013, compared to $12.0 million, representing 11.3% of sales, for the three months ended March 31, 2012. Fab utilization rates have stabilized and preventive maintenance has increased resulting in the increase in sales this quarter. We expect to see continued improvements in utilization rates through 2013 resulting in stable revenues for our global support business.

Operating income for Thin Films was $7.5 million for the three months ended March 31, 2013, an increase of $4.3 million from the same period of 2012. The increase is the result of improved gross margins coupled with declines in operating expenses as a result of the restructuring efforts completed in 2012.

Table Of Contents

Solar Energy

Results for our Solar Energy SBU for the three months March 31, 2013 and 2012 are as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Sales	$50,037	$45,397
Operating income	208	493

Solar Energy sales were $50.0 million, or 44.8% of sales, for the three months ended March 31, 2013 as compared to $45.4 million, or 42.9% of sales, for the three months ended March 31, 2012.

Sales for the first quarter of 2013 were up from the comparable quarter a year ago due to an increased presence in Canada. Sales to the Canadian market grew significantly in the second half of 2012 and have continued to grow, although at a slower pace. We expect Solar Energy sales to increase in the second quarter of 2013 due to the acquisition discussed in "Note 21. Subsequent Event" in Part I Item I of this Form 10-Q.

Operating income for Solar Energy was $0.2 million for the three months ended March 31, 2013 as compared to $0.5 million for the three months ended March 31, 2012. The decrease in operating income for the three months ended March 31, 2013 as compared to the same periods in 2012 is due to lower gross margins resulting from changes in the mix of products sold.

Backlog

Our overall backlog was $86.9 million at March 31, 2013 as compared to $92.7 million at December 31, 2012. The decrease from the prior year-end is due primarily to lower orders in our Solar Energy SBU resulting from the push out of projects due to permit and financing delays.

GROSS PROFIT

Our gross profit was $41.8 million, or 37.4% of sales, for the three months ended March 31, 2013, as compared to $39.7 million, or 37.6% of sales for the three months ended March 31, 2012. The year-over-year increase in terms of absolute dollars was due to the overall increase in sales in our Solar Energy business. Gross profit as a percentage of sales was relatively flat in the first quarter of 2013 as compared to the same period of 2012.

OPERATING EXPENSE

The following table summarizes our operating expenses as a percentage of sales for the three months ended March 31, 2013 and 2012 (in thousands):

	Three Months Ended March 31,					
	2013			2012		
Research and development	$14,253	12.7	%	$15,115	14.3	%
Selling, general, and administrative	17,654	15.8	%	20,059	19.0	%
Amortization of intangible assets	2,213	2.0	%	1,372	1.3	%
Restructuring charges	—	—	%	2,575	2.4	%
Total operating expenses	$34,120	30.5	%	$39,121	37.0	%

As a result of declines in certain markets that we serve, we initiated a plan in September 2011 to re-align our manufacturing and research and development activities to be closer to our customers and reduce production costs. These initiatives included headcount reductions, facilities closures, and asset impairments and were completed in the fourth quarter of 2012.

In connection with our acquisition of Refusol Holdings GmbH ("Refusol") described in Note 21. Subsequent Event in Part I Item I of this Form 10-Q, we committed to a restructuring plan to take advantage of additional cost saving opportunities. Over the next nine months, we will consolidate several facilities including moving the remaining manufacturing in Bend, Oregon to our Fort Collins, Colorado facility; transfer the remaining supply chain activities of our Thin Films business unit to the Shenzhen, China manufacturing facility; and rationalize the inverter product line. As a result, we anticipate total charges in the amount of $30.0 to $35.0 million, of which approximately $7.0 million to $15.0 million are expected to be cash expenditures. The charges

Table Of Contents

are expected to include approximately $4.0 million to $6.0 million of severance costs, $5.5 million to $6.0 million for space consolidation, and $20.5 million to $23.0 million for product rationalization and impairments of the intangible assets associated with the technology around those products. The actions taken under this restructuring plan as well those underway and already taken are expected to deliver annual savings of approximately $70.0 to $75.0 million.

Research and Development

The markets we serve constantly present opportunities to develop products for new or emerging applications and require technological changes driving for higher performance, lower cost, and other attributes that we expect may advance our customers' products. We believe that continued and timely development of new and differentiated products, as well as enhancements to existing products to support customer requirements, are critical for us to compete in the markets we serve. Accordingly, we devote significant personnel and financial resources to the development of new products and the enhancement of existing products, and we expect these investments to continue. All of our research and development costs have been expensed as incurred, except those incurred as a result of a business acquisition.

Research and development expenses for the three months ended March 31, 2013 were $14.3 million, or 12.7% of sales, as compared to $15.1 million, or 14.3% of sales, for the three months ended March 31, 2012. Research and development costs declined in the three months ended March 31, 2013 as compared to the same period in 2012 primarily due to lower costs of materials and supplies.

Selling, General and Administrative

Our selling expenses support domestic and international sales and marketing activities that include personnel, trade shows, advertising, third-party sales representative commissions, and other selling and marketing activities. Our general and administrative expenses support our worldwide corporate, legal, tax, financial, governance, administrative, information systems, and human resource functions in addition to our general management.

Selling, general and administrative ("SG&A") expenses decreased $2.4 million in the three months ended March 31, 2013 as compared to the same period in 2012. The decrease for the three months ended March 31, 2013 as compared to the same period in 2012 is due to lower incentive compensation accruals in the current period based on company performance as compared to plan targets partially offset by increased purchased services for due diligence related to the business acquisition discussed in Note 21. Subsequent Event in Part I Item I of this Form 10-Q.

Amortization Expense

Amortization of intangible assets expense was $2.2 million for the three months ended March 31, 2013, compared to $1.4 million for the same period ending March 31, 2012. The increase in amortization is due to in process research and development projects that were placed in service the first quarter of 2012 and therefore began amortization in the second quarter of 2012. This project was in process at the acquisition date of PV Powered and was recorded as a non-amortizing intangible asset at the acquisition date. As the projects acquired were completed they began amortizing over their estimated useful lives.

Other Income (expenses), net

Other income (expenses), net consists primarily of interest income and expense, foreign exchange gains and losses, gains and losses on sales of fixed assets, and other miscellaneous items. Other income (expenses), net was a $0.2 million loss for the three months ended March 31, 2013 as compared to a $0.4 million gain in the same period of 2012. The loss in the current year is primarily due to foreign exchange losses while the prior year gain resulted from the sale of fixed assets.

Provision for Income Taxes

We recorded an income tax provision from continuing operations for the three months ended March 31, 2013 of $0.7 million compared to $0.3 million for the three months ended March 31, 2012, resulting in effective tax rates of 9.2% and 25.9%, respectively. Our tax rate is lower than the U.S. federal income tax rate primarily due to the benefit of earnings in foreign jurisdictions which are subject to lower tax rates. In addition, during the three months ended March 31, 2013, we recognized a discrete tax benefit of $1.4 million related to the January 2, 2013 reinstatement of the 2012 U.S. research and development tax credit.

Our future effective income tax rate depends on various factors, such as changes in tax laws, regulations, accounting principles, or interpretations thereof and the geographic composition of our pre-tax income. We carefully monitor

these factors and adjust our effective income tax rate accordingly.
Discontinued Operations

25

Table Of Contents

On October 15, 2010, we completed the sale of our gas flow control business, which includes the Aera® mass flow control and related product lines to Hitachi, for $43.3 million. Assets and liabilities sold include, without limitation, inventory, real property in Hachioji, Japan, equipment, certain contracts, intellectual property rights related to the gas flow control business, and certain warranty liability obligations. Results of continuing operations for 2012 were reduced by the revenue and costs associated with the gas flow control business which are included in Income from discontinued operations, net of income taxes, in our Condensed Consolidated Statements of Operations.

Non-GAAP Results

To evaluate business performance against business objectives and for planning purposes, management uses non-GAAP results. We believe these measures will enhance investors' ability to review our business from the same perspective as management and facilitate comparisons of this period's results with prior periods. These non-GAAP measures are not in accordance with U.S. GAAP and may differ from non-GAAP methods of accounting and reporting used by other companies. The presentation of this additional information should not be considered a substitute for results prepared in accordance with U.S. GAAP.

The non-GAAP results presented below exclude the impact of restructuring charges, stock-based compensation, amortization of intangible assets, and acquisition-related costs (in thousands):

	Three Months Ended March 31,	
	2013	2012
Income from continuing operations, net of tax, as reported	$6,826	$766
Adjustments, net of tax		
Restructuring charges	—	1,651
Acquisition-related costs	993	—
Stock-based compensation	1,847	3,191
Amortization of intangible assets	2,010	874
Non-GAAP income from continuing operations, net of tax	$11,676	$6,482
Diluted weighted-average common shares outstanding	39,598	41,292
Non-GAAP Earnings Per Share	$0.29	$0.16

Impact of Inflation

In recent years, inflation has not had a significant impact on our operations. However, we continuously monitor operating price increases, particularly in connection with the supply of component parts used in our manufacturing process. To the extent permitted by competition, we pass increased costs on to our customers by increasing sales prices over time. From time to time, we may also receive pressure from customers to decrease sales prices due to reductions in the cost structure of our products from cost improvement initiatives and decreases in component part prices. Sales price increases and decreases, however, were not significant in any of the periods presented herein.

Table Of Contents

Liquidity and Capital Resources

LIQUIDITY

We believe that adequate liquidity and cash generation is important to the execution of our strategic initiatives. Our ability to fund our operations, acquisitions, capital expenditures, and product development efforts may depend on our ability to generate cash from operating activities which is subject to future operating performance, as well as general economic, financial, competitive, legislative, regulatory, and other conditions, some of which may be beyond our control. Our primary sources of liquidity are our available cash, investments, and cash generated from current operations as well as our credit facility discussed in Note 20. Credit Facility in Part I Item 1 of this Form 10-Q.

At March 31, 2013, we had $182.3 million in cash, cash equivalents, and marketable securities. We believe that our current cash levels and our cash flows from future operations will be adequate to meet anticipated working capital needs, anticipated levels of capital expenditures, and contractual obligations for the next twelve months. We may seek additional financing from time to time.

On October 12, 2012, we entered into an agreement with Wells Fargo Bank, National Association which provides for a secured revolving credit facility ("Credit Facility") of up to $50.0 million. Borrowings under the Credit Facility are subject to a borrowing base based upon our accounts receivable and inventory and are available for various corporate purposes. The Credit Facility provides us further flexibility for execution of our strategic plans including acquisitions. For more information on the Credit Facility see Note 20 - Credit Facility of our Consolidated Financial Statements.

On October 30, 2012, we announced a $25.0 million share repurchase program authorized by our Board of Directors. The repurchase program is authorized through October 2013, requires no minimum number of shares to be repurchased, and may be discontinued at any time. No repurchases have been made under this program.

CASH FLOWS

A summary of our cash provided by and used in operating, investing and financing, activities is as follows (in thousands):

	Three Months Ended March 31,	
	2013	2012
Net cash provided by (used in) operating activities	$(549)	$34,691
Net cash provided by (used in) investing activities	11,675	(2,892)
Net cash provided by (used in) financing activities	12,138	(22,110)
Effect of currency translation on cash	(100)	(1,910)
Increase in cash and cash equivalents	23,164	7,779
Cash and cash equivalents, beginning of the period	146,564	117,639
Cash and cash equivalents, end of the period	$169,728	$125,418

2013 CASH FLOWS COMPARED TO 2012

Net cash provided by (used in) operating activities

Net cash used in operating activities for the three months ended March 31, 2013 was $0.5 million, compared to cash provided by operating activities of $34.7 million for the same period ended March 31, 2012. The decrease of $35.2 million in net cash flows from operating activities is primarily due to significant collections of accounts receivable in the first quarter of 2013 driving overall receivables balances down from previous levels.

Net cash provided by (used in) investing activities

Net cash provided by investing activities for the three months ended March 31, 2013 was $11.7 million, an increase of $14.6 million from the same period ended March 31, 2012. The increase in cash provided by investing activities in 2013 is due to proceeds from the liquidation of a portion of our marketable securities. Movement of cash between marketable securities and cash and cash equivalents is related to our cash needs at a point in time and may fluctuate from one period to the next. Capital expenditures for the three months ended March 31, 2013 were down $1.7 million compared to the same period in 2012. We expect to fund future capital expenditures with cash generated from operations.

Table Of Contents

Net cash provided by (used in) financing activities

Net cash provided by financing activities in the three months ended March 31, 2013 was $12.1 million, a $34.2 million change from the cash used in financing activities of $22.1 million in the same period of 2012. The exercise of stock options provided $13.1 million of cash in 2013 as compared to $0.1 million in 2012. The first quarter of 2012 included stock repurchases of $21.9 million while no repurchases have been made in 2013.

Effect of currency translation on cash

During the three months ended March 31, 2013, currency translation had a negative $0.1 million impact on cash compared to a negative impact of $1.9 million in the same period of 2012. The functional currencies of our worldwide operations primarily include U.S. dollar ("USD"), Japanese Yen ("JPY"), Chinese Yuan ("CNY"), New Taiwan Dollar ("NTD"), South Korean Won ("KRW"), British Pound ("GBP"), Swiss Franc ("CHF"), Canadian Dollar ("CAD") and Euro ("EUR"). Our purchasing and sales activities are primarily denominated in USD, JPY, CNY, and EUR. The change in these key currency rates during the three months ended March 31, 2013 and 2012 are as follows:

		Three Months Ended March 31,			
From	To	2013		2012	
CNY	USD	0.3	%	0.2	%
EUR	USD	(2.8	)%	3.2	%
JPY	USD	(7.9	)%	(5.6	)%
KRW	USD	(4.4	)%	2.6	%
NTD	USD	(2.8	)%	2.9	%
GBP	USD	(6.4	)%	3.4	%
CAD	USD	(2.5	)%	2.5	%
CHF	USD	(3.6	)%	4.2	%

Off Balance Sheet Arrangements

We have no off-balance sheet arrangements or variable interest entities.

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires us to make judgments, assumptions and estimates that affect the amounts reported in the Condensed Consolidated Financial Statements and accompanying notes. Note 1 to the Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2012 describes the significant accounting policies and methods used in the preparation of our Consolidated Financial Statements. Our critical accounting estimates, discussed in the Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2012, include estimates for allowances for doubtful accounts, determining useful lives for depreciation and amortization, the valuation of assets and liabilities acquired in business combinations, assessing the need for impairment charges for identifiable intangible assets and goodwill, establishing warranty reserves, accounting for income taxes, and assessing excess and obsolete inventories. Such accounting policies and estimates require significant judgments and assumptions to be used in the preparation of the Condensed Consolidated Financial Statements and actual results could differ materially from the amounts reported based on variability in factors affecting these estimates.

Our management discusses the development and selection of our critical accounting policies and estimates with the Audit Committee of our Board of Directors at least annually. Our management also internally discusses the adoption of new accounting policies or changes to existing policies at interim dates, as it deems necessary or appropriate.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

Our market risk exposure relates to changes in interest rates in our investment portfolio and credit facility. We generally place our investments with high-credit quality issuers and by policy are averse to principal loss and seek to protect and preserve our invested funds by limiting default risk, market risk, and reinvestment risk.

Table Of Contents

As of March 31, 2013, our investments consisted primarily of certificates of deposit, municipal bonds, and institutional money markets, all with maturity of less than 2 years. As a measurement of the sensitivity of our portfolio and assuming that our investment portfolio balances remain constant, a hypothetical decrease of 100 basis points (1%) in interest rates would decrease annual pre-tax earnings by approximately $0.1 million.

We had no debt outstanding as of March 31, 2013. Our only debt instrument at March 31, 2013 was the Credit Facility, which would be subject to variable interest rates and principal payments should we decide to borrow against it. However, assuming a full drawdown on the revolving credit facility, and holding other variables constant, a hypothetical immediate one percentage point change in interest rates would be expected to have an impact on pre-tax earnings and cash flows of approximately $0.5 million over the course of 12 months.

Foreign Currency Exchange Rate Risk

We are impacted by changes in foreign currency exchange rates through sales and purchasing transactions when we sell products and purchase materials in currencies different from the currency in which product and manufacturing costs were incurred. Our purchasing and sales activities are primarily denominated in the USD, JPY, CNY and EUR. As these currencies fluctuate against each other, and other currencies, we are exposed to foreign currency exchange rate risk on sales, purchasing transactions and labor.

Our reported financial results of operations, including the reported value of our assets and liabilities, are also impacted by changes in foreign currency exchange rates. Assets and liabilities of many of our subsidiaries outside the U.S. are translated at period end rates of exchange for each reporting period. Operating results and cash flow statements are translated at weighted-average rates of exchange during each reporting period. Although these translation changes have no immediate cash impact, the translation changes may impact future borrowing capacity, and overall value of our net assets.

From time to time, we enter into foreign currency exchange rate contracts to hedge against changes in foreign currency exchange rates on assets and liabilities expected to be settled at a future date. Market risk arises from the potential adverse effects on the value of derivative instruments that result from a change in foreign currency exchange rates. We minimize our market risk applicable to foreign currency exchange rate contracts by establishing and monitoring parameters that limit the types and degree of our derivative contract instruments. We enter into derivative contract instruments for risk management purposes only. We do not enter into or issue derivatives for trading or speculative purposes.

Currency exchange rates vary daily and often one currency strengthens against the USD while another currency weakens. Because of the complex interrelationship of the worldwide supply chains and distribution channels, it is difficult to quantify the impact of a change in one or more particular exchange rates.

See the “Risk Factors” set forth in Part I, Item 1A of our Annual Report on Form 10-K for more information about the market risks to which we are exposed. There have been no material changes in our exposure to market risk from December 31, 2012.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We have established disclosure controls and procedures, which are designed to ensure that information required to be disclosed in reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. These disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Act is accumulated and communicated to management, including our Principal Executive Officer (Garry Rogerson, Chief Executive Officer) and Principal Financial Officer (Danny C. Herron, Executive Vice President & Chief Financial Officer), as appropriate, to allow timely decisions regarding required disclosures.

As of the end of the period covered by this report, we conducted an evaluation, with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the disclosure controls and procedures pursuant to the Exchange Act Rule 13a-15(b). Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2013. The conclusions of the Chief Executive Officer and Chief Financial Officer from this

evaluation were communicated to the Audit Committee. We intend to continue to review and document our disclosure controls and procedures, including our internal controls and procedures for financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our business.

Table Of Contents

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the fiscal quarter covered by this Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table Of Contents

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are involved in disputes and legal actions arising in the normal course of our business.
There have been no material developments in legal proceedings in which we are involved during the quarter ended March 31, 2013. For a description of previously reported legal proceedings refer to Part I, Item 3, “Legal Proceedings” of our Annual Report on Form 10-K for the year ended December 31, 2012.

ITEM 1A. RISK FACTORS

Item 1A, “Risk Factors,” of our Annual Report on Form 10-K for the year ended December 31, 2012 describes some of the risks and uncertainties associated with our business. The risk factors set forth below update such disclosures. Other factors may also exist that we cannot anticipate or that we currently do not consider to be significant based on information that is currently available. These risks and uncertainties have the potential to materially affect our business, financial condition, results of operations, cash flows and future results. Such risks and uncertainties also may impact the accuracy of forward-looking statements included in this Form 10-Q and other reports we file with the Securities and Exchange Commission.

Activities necessary to integrate acquisitions may result in costs in excess of current expectations or be less successful than anticipated.

As noted in Note 21. Subsequent Event in Part I Item 1 of this Form 10-Q, we recently acquired Refusol Holding GmbH, and we may acquire other businesses in the future. The success of such transactions will depend on, among other things, our ability to integrate assets and personnel acquired in these transactions and to apply our internal controls process to these acquired businesses. The integration of acquisitions may require significant attention from our management, and the diversion of management's attention and resources could have a material adverse effect on our ability to manage our business. Furthermore, we may not realize the degree or timing of benefits we anticipated when we first enter into the acquisition transaction, or the acquired business may cause us to incur unanticipated costs or liabilities. If actual integration costs are higher than amounts originally anticipated, if we are unable to integrate the assets and personnel acquired in an acquisition as anticipated, if we are unable to benefit from anticipated sales, or if we are unable to fully benefit from anticipated synergies, our business, financial condition, results of operations and cash flows could be materially adversely affected.

ITEM 2.UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

None.

Table Of Contents

ITEM 6. EXHIBITS

3.1	Restated Bylaws, as amended
31.1	Certification of the Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Table Of Contents

SIGNATURES

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

ADVANCED ENERGY INDUSTRIES, INC.

Dated: May 8, 2013

/s/ Danny C. Herron
Danny C. Herron
Executive Vice President and Chief Financial Officer

Table Of Contents

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