

KULICKE & SOFFA INDUSTRIES INC

Form 10-K

December 14, 2006

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended September 30, 2006

OR

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

For the transition period from _____ to _____.

Commission file number 0-121

KULICKE AND SOFFA INDUSTRIES, INC.

(Exact Name of Registrant as Specified in Its Charter)

PENNSYLVANIA
(State or Other Jurisdiction of Incorporation)

23-1498399
(IRS Employer Identification No.)

1005 VIRGINIA DRIVE, FORT WASHINGTON, PENNSYLVANIA 19034

(Address of principal executive offices)

Registrants telephone number including area code (215) 784-6000

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

COMMON STOCK, WITHOUT PAR VALUE

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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 No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

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

The aggregate market value of the registrant's common stock (its only voting stock and common equity) held by non-affiliates of the registrant as of April 1, 2006 was approximately \$532,214,000 based upon the closing sale price of the common stock on the Nasdaq Global Market (Reference is made to Part II, Item 5 herein for a statement of assumptions upon which this calculation is based).

As of December 1, 2006 there were 57,323,065 shares of the registrant's common stock, without par value, outstanding.

Documents Incorporated by Reference

Portions of the registrant's Proxy Statement for the 2007 Annual Shareholders' Meeting to be filed on or about January 3, 2007 are incorporated by reference into Part III, Items 10, 11, 12, 13 and 14 herein of this Report. Such Proxy Statement, except for the parts therein which have been specifically incorporated by reference, shall not be deemed filed for the purposes of this Report on Form 10-K.

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KULICKE AND SOFFA INDUSTRIES, INC.

2006 Annual Report on Form 10-K

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PART I

In addition to historical information, this filing contains statements relating to future events or our future results. These statements are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act) and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), and are subject to the safe harbor provisions created by statute. Such forward-looking statements include, but are not limited to, statements that relate to our future revenue, product development, demand forecasts, competitiveness, operating expenses, cash flows, profitability, gross margins, and benefits expected as a result of (among other factors):

the projected growth rates in the overall semiconductor industry, the semiconductor assembly equipment market, and the market for semiconductor packaging materials; and

the projected continuing demand for wire bonder and die bonder equipment.

Generally, words such as may, will, should, could, anticipate, expect, intend, estimate, plan, continue, goal, and believe, or the negative of or other variations on these and other similar expressions identify forward-looking statements. These forward-looking statements are made only as of the date of this filing. We do not undertake to update or revise the forward-looking statements, whether as a result of new information, future events or otherwise.

Forward-looking statements are based on current expectations and involve risks and uncertainties and our future results could differ significantly from those expressed or implied by our forward-looking statements. These risks and uncertainties include, without limitation, those described under Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations . In light of these and other uncertainties, you should not conclude that we will necessarily achieve any plans or objectives or projected financial results referred to in any forward-looking statements.

Item 1. BUSINESS.

We design, manufacture and market capital equipment and packaging materials as well as service, maintain, repair and upgrade equipment, all used to assemble semiconductor devices. We are currently the world's leading supplier of semiconductor wire bonding assembly equipment, according to VLSI Research, Inc. Our business is currently divided into two product segments:

equipment; and

packaging materials.

Our goal is to be both the technology leader and the lowest cost supplier in each of our major lines of business. We believe we are the only major supplier to the semiconductor assembly industry that provides customers with semiconductor wire bonding and die bonding equipment along with the complementary packaging materials that actually contact the surface of the customer's semiconductor devices. We believe that the ability to control all of these assembly related products provides us with a significant competitive advantage, and should allow us to develop system solutions to the new technology challenges inherent in assembling and packaging next-generation semiconductor devices.

The semiconductor industry has been historically volatile, with periods of rapid growth followed by downturns. In response to recent downturns, we shifted our strategy, focusing on our larger, more established product lines, and divesting or discontinuing smaller or more speculative businesses. Additionally, we continuously seek to further reduce our cost structure by moving operations to lower cost areas, moving a portion of our supply chain to lower cost suppliers and increasing our productivity. We believe the historical volatility of the semiconductor industry both upward and downward will persist.

On November 3, 2006, we completed the acquisition of Alphasem, a leading supplier of die bonder equipment, from Dover Technologies International, Inc., a subsidiary of Dover Corporation. The consideration for the acquisition was approximately \$27.1 million in cash, after a working capital adjustment and subject to further post closing adjustments. Alphasem will be integrated into our equipment segment.

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During the three months ended April 1, 2006, we committed to a plan of disposal and sold our test business in two separate transactions as follows:

1. On March 3, 2006, we completed the sale of substantially all of the assets and certain of the liabilities of our wafer test business to SV Probe, PTE. Ltd. (SV Probe) for initial proceeds of \$10.0 million in cash plus the assumption of accounts payable and certain other liabilities, subject to a post-closing working capital adjustment that was settled in the three months ended July 1, 2006. Certain accounts receivable were excluded from the assets sold.
2. On March 31, 2006, we completed the sale of substantially all of the assets and certain of the liabilities of our package test business to Antares conTech, Inc., an entity formed by Investcorp Technology Ventures II, L.P. and its affiliates (collectively Investcorp) for initial proceeds of \$17.0 million in cash plus the assumption of accounts payable and certain other liabilities, subject to a post-closing working capital adjustment that was settled in the three months ended July 1, 2006.

We recorded a loss of \$0.8 million on the disposal of our test business. We sold the test business to strengthen our focus on our core businesses semiconductor assembly equipment and materials and explore growth opportunities in these markets.

As part of the terms of each sale noted above, the associated China-based assets were not transferred to the buyers on the above referenced closing dates, as neither buyer had a legal entity in China that could accept the transfer of the China-based assets as of the closing date. The China-based assets associated with the sale to SV Probe were transferred to SV Probe in September 2006 and the China-based assets associated with the sale to Antares conTech were transferred to Antares conTech in December 2006, without additional consideration. In addition, we provided manufacturing and other transition services (invoiced at cost) to SV Probe through September 1, 2006 and provided these services to Antares conTech through November 2006.

In accordance with Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the financial results of the test business have been presented as discontinued operations in our Consolidated Financial Statements. See Note 2 to our Consolidated Financial Statements included in Item 8 of this report for further discussion of the divestiture of our test business.

Unless otherwise indicated, amounts provided throughout this Form 10-K relate to continuing operations only.

Kulicke and Soffa Industries, Inc. was incorporated in Pennsylvania in 1956. Our principal offices are located at 1005 Virginia Drive, Fort Washington, Pennsylvania 19034 and our telephone number is (215) 784-6000. We maintain a website with the address www.kns.com. We are not including the information contained on our website as a part of, or incorporating it by reference into, this filing. We make available free of charge (other than an investor's own Internet access charges) on or through our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to these reports, as soon as reasonably practicable after the material is electronically filed with or otherwise furnished to the Securities and Exchange Commission (the SEC). Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports are also available on the SEC website at <http://www.sec.gov>.

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We offer a range of wire bonding and die bonding equipment (and related spare parts) and packaging materials. Set forth below is a table listing the net revenue from continuing operations for each business segment for our fiscal years ended September 30, 2004, 2005, and 2006:

	(in thousands)		
	Fiscal Year Ended September 30,		
	2004	2005	2006
Equipment	\$ 361,244	\$ 201,608	\$ 319,788
Packaging materials	234,690	273,934	376,523
	\$ 595,934	\$ 475,542	\$ 696,311

Our equipment sales have been, and are expected to remain, highly volatile due to the semiconductor industry's need for new capability and capacity. Packaging material unit sales tend to be less volatile, following the trend of total semiconductor unit production; however, fluctuations in gold metal commodity prices can have a significant impact on reported package material net revenues.

See Note 11 to our Consolidated Financial Statements, included in Item 8 of this report, for financial results by business segment and sales by geographic location.

Equipment

We manufacture and market a line of wire bonders and die bonders. Our wire bonders are used to connect very fine wires, typically made of gold, aluminum or copper, between the bond pads of a semiconductor die and the leads on the integrated circuit (IC) package to which the die has been attached. We believe that our wire bonders offer competitive advantages by providing customers with high productivity/throughput and superior package quality/process control. In particular, our machines are capable of performing very fine pitch bonding as well as creating the sophisticated wire loop shapes that are needed in the assembly of advanced semiconductor packages. Our die bonders perform the task of removing a semiconductor die from a previously cut/separated wafer and placing it onto a bed of dispensed epoxy, or tape, which will permanently attach the die to its package substrate. This step precedes the wire bonding process. We believe our die bonders have good position in the market, serving a wide range of applications. Die bonders and wire bonders share many of the same sub-assemblies, software features, and components and we believe joining the engineering and manufacturing expertise of these two products will yield superior equipment platforms. Our principal products are:

Ball Bonders. Automatic IC ball bonders represent a large majority of our semiconductor equipment business. As part of our competitive strategy, we have been introducing new models of IC ball bonders every 15 to 24 months, with each new model designed to increase both productivity and process capability compared to its predecessor. We extended the life of the successful Maxum product line introducing the Maxum Ultra to succeed the Maxum Plus and the Maxum Elite to succeed the Nutek. Each of these machines provides approximately a 10% productivity improvement over its predecessor and offers various other performance improvements.

Specialty Wire Bonders. We also produce other models of wire bonders, targeted at specific market niches, including: the Model 8098, a large area ball bonder designed for wire bonding hybrid, chip on board applications, and other large area applications; and the Model 8090, a large area wedge bonder. We introduced a new model wafer stud bumper in the fourth quarter of fiscal 2005, the AT Premier. The AT Premier is targeted for gold-to-gold interconnect in the flip chip market. With industry-leading speed and technology, the machine lowers the cost of ownership for stud bumping, enabling a wider range of applications than previously served. We also manufacture and market a line of manual wire bonders.

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IC Die Bonders. In November 2006, we acquired the Alphasem die bonder product lines, consisting of the SwissLine and EasyLine models. These products are used by many of the same customers and applications that our wire bonders serve today. We expect to utilize the same competitive strategy as our wire bonders by developing new models that will both improve the productivity of the die bonders and increase the size of the market that the new models will serve.

Specialty Die Bonders. A portion of the Alphasem product line is a series of specialty bonders that consist of several equipment models based on our die bonder platforms. This equipment is used for various assembly processes that include die sorting, power device assembly, MEMS assembly, and others.

We believe that our industry knowledge and technical experience have positioned us to deliver innovative, customer-specific offerings that reduce the cost of owning our equipment over its useful life. In response to customer trends in outsourcing packaging requirements, we provide repair and maintenance services, a variety of equipment upgrades, machine and component rebuild activities and expanded customer training through our customer operations group.

Packaging Materials

We manufacture and market a range of semiconductor packaging materials and expendable tools for the semiconductor assembly market, including gold, aluminum and copper wire, capillaries, wedges, die collets and saw blades, all of which are used in packaging and assembly processes. Our packaging materials are designed for use on both our own and our competitors' assembly equipment. A wire bonder uses a capillary or wedge tool and bonding wire much like a sewing machine uses a needle and thread. Our principal products are:

Bonding Wire. We manufacture gold, aluminum and copper wire used in the wire bonding process. This wire is bonded to the chip surface and package substrate by the wire bonder and becomes a permanent part of the customer's semiconductor package. We produce wire to a wide range of specifications, which can satisfy most wire bonding applications across the spectrum of semiconductor packages.

Expendable Tools. Our expendable tools include a wide variety of capillaries, wedges, die collets and wafer saw blades. The capillaries and wedges attach the wire to the semiconductor chip, allow a precise amount of wire to be fed out to form a permanent wire loop, then attach the wire to the package substrate, and finally cut the wire so that the bonding process can be repeated again. Die collets are used to pick up and place die into packages before the wire bonding process begins. Our wafer saw blades are used to cut silicon wafers into individual semiconductor die.

Customers

Our major customers include large semiconductor manufacturers and their subcontract assemblers and vertically integrated manufacturers of electronic systems. Customers may vary from year-to-year based on their capital investment and operating expense budgets.

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The chart below shows our top ten end-use customers, based on net sales, for each of the last three fiscal years:

Fiscal 2004	Fiscal 2005	Fiscal 2006
1. Advanced Semiconductor Engineering*	1. Advanced Semiconductor Engineering*	1. Advanced Semiconductor Engineering*
2. ST Microelectronics	2. ST Microelectronics*	2. ST Microelectronics*
3. Texas Instruments	3. Siliconware Precision Industries	3. STATS ChipPAC
4. Siliconware Precision Industries	4. Infineon Technologies	4. Siliconware Precision Industries
5. National Semiconductor	5. Intel	5. Texas Instruments
6. STATS ChipPAC	6. STATS ChipPAC	6. Infineon Technologies
7. Infineon Technologies	7. Samsung	7. United Test and Assembly Center
8. Amkor Technologies	8. Advanced Micro Devices	8. Spansion
9. Advanced Micro Devices	9. National Semiconductor	9. Samsung
10. Samsung	10. Amkor Technologies	10. National Semiconductor

* Accounted for more than 10% of total fiscal year net sales.

We believe that developing long-term relationships with our customers is critical to our success. By establishing these relationships with semiconductor manufacturers, semiconductor subcontract assemblers, and vertically integrated manufacturers of electronic systems, we gain insight into our customers' future IC packaging strategies. This insight assists us in our efforts to develop material, equipment, and process solutions that address our customers' future assembly requirements.

International Operations

We sell our products to semiconductor manufacturers, semiconductor subcontract assemblers, and vertically integrated manufacturers of electronic systems, which are primarily located in or have operations in the Asia/Pacific region. Approximately 93% of our fiscal 2006 net sales and 95% of our fiscal 2005 and 2004 net sales were for delivery to customer locations outside of the United States. The majority of these foreign sales were destined for customer locations in the Asia/Pacific region, including Taiwan, Malaysia, Singapore, Korea, Japan, China and the Philippines. We expect sales outside of the United States to continue to represent a majority of our future revenues.

Sales and Customer Support

We believe that providing comprehensive worldwide sales, service, training, and support are important competitive factors in the semiconductor equipment industry, and we manage these functions through our global customer operations group. We rely on a combination of a direct sales force, manufacturers' representatives and distributors for the sale of our various product lines. In order to support our customers whose semiconductor assembly operations are located primarily outside of the United States, we have sales, service, and support personnel based in China, Hong Kong, Japan, Korea, Malaysia, the Philippines, Singapore, Taiwan, Thailand, and Europe, and applications labs in Singapore, Japan, Israel, and Taiwan. We provide timely customer service and support by positioning our service representatives and spare parts near customer facilities, which provides customers with the ability to place orders locally and to deal with service and support personnel who speak the customer's language and are familiar with local country practices.

Backlog

At September 30, 2006, we had a backlog of customer orders totaling \$56.0 million, compared to \$59.0 million at July 1, 2006 and \$91.5 million at September 30, 2005. Our backlog consists of customer orders which are scheduled for shipment within 12 months. Virtually all orders are subject to cancellation, deferral or rescheduling by the customer with limited or no penalties. Because of the possibility of customer changes in delivery schedules or cancellations and potential delays in product shipments, our backlog as of any particular date may not be indicative of revenues for any succeeding quarterly period.

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Manufacturing

We believe excellence in manufacturing can create a competitive advantage, both through lower costs and superior responsiveness. In order to achieve these goals, we manage our manufacturing operations through a single organization and are trending to fewer, larger factories to take advantage of economies of scale and the cost savings available in low labor cost areas.

Equipment. Our equipment manufacturing activities consist primarily of integrating outsourced parts and subassemblies, and testing the finished product to customer specifications. During fiscal 2006, most of our equipment manufacturing took place in Singapore, with a small number of machines built in Pennsylvania. We believe the outsourcing model enables us to minimize our fixed costs and capital expenditures and focus on product differentiation through technology innovations in system design and manufacturing quality control. Just-in-time inventory management has reduced our manufacturing cycle times and reduced our on-hand inventory requirements. We have received ISO 9001 and ISO 14001 certifications for our equipment manufacturing facility in Singapore.

Packaging Materials. We manufacture expendable tools at facilities in Yokneam, Israel and Suzhou, China, and bonding wire at facilities in Singapore and Thalwil, Switzerland. We manufacture blades for wafer sawing in Suzhou, China. Our bonding wire facility in Switzerland has received ISO 9001 certification; our bonding wire facility in Singapore has received QS9000 and ISO 14001 certifications; our bonding tools facility in Yokneam, Israel has received ISO 9001 and ISO 14001 certifications; and our bonding tools and dicing blades facility in Suzhou, China has received ISO 9001 and ISO 14001 certifications.

Research and Product Development

Many of our customers generate technology roadmaps describing the future manufacturing capability requirements needed to support their product development plans. Our research and product development activities are organized so that our products anticipate our customers requirements. This can happen either through continuous improvement of our existing products, including upgrades for products already installed in customers facilities, or through the creation of next-generation products. Examples of our continuous improvement strategy include the Maxum Elite and Maxum Ultra wire bonders both improvements of the Maxum product line and our DuraCap line of bonding tools. Major next-generation development programs are underway for our wire bonders and die bonders. Whether we proceed via continuous improvement, or via next-generation technology development, our goal is technology leadership in each of our major product lines.

Our net expenditures for research and development totaled approximately \$37.7 million, \$28.5 million, and \$28.4 million during our fiscal years ended September 30, 2006, 2005 and 2004, respectively.

Competition

The market for semiconductor equipment and packaging materials products is intensely competitive. Significant competitive factors in the semiconductor equipment market include price, as well as speed/throughput, production yield, process control, and customer support, each of which contribute to lower the overall cost per package being manufactured. Our major equipment competitors include:

Wire bonders: ASM Pacific Technology and Shinkawa

Epoxy Die Bonders: Renesas, ESEC, ASM Pacific Technology and Shinkawa

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Significant competitive factors in the semiconductor packaging materials industry include performance, price, delivery, product life, and quality. Our significant packaging materials competitors include:

Bonding tools: Gaiser Tool Co., Small Precision Tools, Inc. and PECO

Saw blades: Disco Corporation

Bonding wire: Tanaka Electronic Industries, Sumitomo Metal Mining, Heraeus, and Nippon Metal.

In each of the markets we serve, we face competition and the threat of competition from established competitors and potential new entrants, some of which have greater financial, engineering, manufacturing, and marketing resources than we have. Some of our competitors are Asian and European companies that have had and may continue to have an advantage over us in supplying products to local customers because many of these customers appear to prefer to purchase from local suppliers, without regard to other considerations.

Intellectual Property

Where circumstances warrant, we seek to obtain patents on inventions governing new products and processes developed as part of our ongoing research, engineering, and manufacturing activities. We currently hold a number of United States patents, some of which have foreign counterparts. We believe that the duration of our patents generally exceeds the life cycles of the technologies disclosed and claimed in the patents. We believe that our portfolio of patents will have more value in the future but that our success will depend primarily on our engineering, manufacturing, marketing, and service skills.

In addition, we believe that much of our important technology resides in our trade secrets and proprietary software. As long as we rely on trade secrets and unpatented knowledge, including software, to maintain our competitive position, we cannot assure you that competitors may not independently develop similar technologies and possibly obtain patents containing claims applicable to our products and processes. Our ability to defend ourselves against these claims may be limited. In addition, although we execute non-disclosure and non-competition agreements with certain of our employees, customers, consultants, selected vendors and others, there is no assurance that such secrecy agreements will not be breached, or that they can be enforced. Additional disclosures regarding these risks, as well as other risk factors facing the Company are included in Item 7 Management's Discussion and Analysis, included herein.

Environmental Matters

We are subject to various federal, state, local and foreign laws and regulations governing, among other things, the generation, storage, use, emission, discharge, transportation and disposal of hazardous materials and the health and safety of our employees. In addition, we are subject to environmental laws which may require investigation and cleanup of any contamination at facilities we own or operate or at third party waste disposal sites we use or have used. These laws could impose liability upon us even if we did not know of, or were not responsible for, the contamination.

We have in the past and will in the future incur costs to comply with environmental laws. We are not, however, currently aware of any costs or liabilities relating to environmental matters, including any claims or actions under environmental laws or obligations to perform any cleanups at any of our facilities or any third party waste disposal sites, that we expect to have a material adverse effect on our business, financial condition or operating results. It is possible, however, that material environmental costs or liabilities may arise in the future.

Employees

At September 30, 2006, we had 2,454 permanent employees and 197 temporary and contract workers worldwide. The only employees represented by a labor union are the bonding wire employees in Singapore. Generally, we believe our employee relations to be good. Competition in the recruiting of personnel in the semiconductor and semiconductor equipment industry is intense, particularly with respect to engineering. We believe that our future

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success will depend in part on our continued ability to hire and retain qualified management, marketing and technical employees.

Executive Officers of the Company

The following table sets forth certain information regarding the executive officers of the Company as of September 30, 2006. Our executive officers are appointed by and serve at the discretion of the Board of Directors.

Name	Age	First Became an Officer (calendar year)	Position
C. Scott Kulicke	57	1976	Chairman of the Board of Directors and Chief Executive Officer
Charles Salmons	51	1992	Senior Vice President, Acquisition Integration
Jagdish (Jack) G. Belani	53	1999	Senior Vice President of Package Materials and Corporate Marketing
Maurice E. Carson	49	2003	Vice President and Chief Financial Officer
Bruce Griffing	56	2004	Vice President, Engineering
Christian Rheault	41	2005	Vice President, Equipment Segment

C. Scott Kulicke has been the Chief Executive Officer of our Company since 1979 and Chairman of the Board of Directors since 1984. His present term as a director expires in 2007. He first became an officer of the Company in 1976 and has held a number of executive positions with us since that time.

Charles Salmons holds the position of Senior Vice President, Acquisition Integration. He was appointed to this position in September 2006. He held the position of Senior Vice President, Wafer Test from November 2004. Mr. Salmons was Senior Vice President, Product Development from September 2002 to November 2004 and until 2006 Senior Vice President Operations from 1999 to 2004. From 1998 to 1999, he was General Manager, Wire Bonder operations and from 1994 to 1998 he was Vice President of Operations. Mr. Salmons has been an officer of the Company since 1992.

Jagdish (Jack) G. Belani holds the position of Senior Vice President of Package Materials and Corporate Marketing. He was appointed to this position in November 2005. Before this, he was Vice President of Wire Bonding and Corporate Marketing. Mr. Belani has also held the following positions: Vice President of all the Business Units and Marketing, President of the Wire Bonding Division and President of XLAM, which was our high density substrate group. He became an officer of the Company upon joining us in April 1999. Before joining us, he served for more than three years at Cypress Semiconductor Corporation, where he was Vice President of Assembly and Packaging. Before Cypress, he was with National Semiconductor Corporation for approximately 18 years in a variety of technical and managerial positions and one year with Advanced Micro Devices as a Wafer Fabrication Process Development Engineer. Mr. Belani has a B.Tech in Chemical Engineering from IIT, Madras; a M.S. in Metallurgical and Materials Engineering from IIT, Chicago and a J.D. from the Univ. Santa Clara.

Maurice E. Carson holds the position of Vice President, Chief Financial Officer. He was appointed to this position when he joined us in September 2003. From 1996 until he joined us in 2003, Mr. Carson served in various finance positions culminating as the Vice President, Finance and Corporate Controller for Cypress Semiconductor Corporation. Before Cypress he was with Ephigraphx as the Chief Operating Officer.

Bruce Griffing holds the position of Vice President, Engineering. He was appointed to this position when he joined us in September 2004. From 2001 to 2003 Dr. Griffing served as Vice President and Chief Technology Officer of DuPont Photomask, a company that provides microimaging solutions. Before DuPont Photomask, Dr. Griffing worked for General Electric from 1979 to 2001, serving as a Laboratory Manager from 1986 to 2001. Dr. Griffing received his Ph.D in Physics from Purdue University in 1979.

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Christian Rheault holds the position of Vice President, Equipment Segment. He was appointed to this position in 2006. Mr. Rheault manages the overall marketing and business operations for the Company's equipment line, which includes all ball bonders and wafer bumping products, microelectronics products, die bonders, manual wire bonders as well as equipment rebuilds and spares. Previously, he served as Vice President and General Manager of our Ball Bonder Business Unit. An employee since 1998, Mr. Rheault has served in other positions of increasing responsibility including Director of Strategic Marketing and Vice President/General Manager of the Company's Microelectronics Business Unit. Prior to joining the Company, Mr. Rheault held engineering and management positions at IBM Canada. He holds an Electrical Engineering degree at Canada's Laval University and a DSA (Business Administration Diploma) at Sherbrooke University in Canada.

Item 1A. RISK FACTORS

Risks Relating to Our Business

The semiconductor industry is volatile with sharp periodic downturns and slowdowns

Our operating results are significantly affected by the capital expenditures of large semiconductor manufacturers and their subcontract assemblers and vertically integrated manufacturers of electronic systems. Expenditures by semiconductor manufacturers and their subcontract assemblers and vertically integrated manufacturers of electronic systems depend on the current and anticipated market demand for semiconductors and products that use semiconductors, including personal computers, telecommunications equipment, consumer electronics, and automotive goods. Significant downturns in the market for semiconductor devices or in general economic conditions reduce demand for our products and materially and adversely affect our business, financial condition and operating results.

Historically, the semiconductor industry has been volatile, with periods of rapid growth followed by industry-wide retrenchment. These periodic downturns and slowdowns have adversely affected our business, financial condition and operating results. They have been characterized by, among other things, diminished product demand, excess production capacity, and accelerated erosion of selling prices. These downturns historically have severely and negatively affected the industry's demand for capital equipment, including the assembly equipment and the packaging materials that we sell. There can be no assurances regarding levels of demand for our products, and in any case, we believe the historical volatility—both upward and downward—will persist.

We may experience increasing price pressure

Our historical business strategy for many of our products has focused on product performance and customer service rather than on price. The length and severity of the fiscal 2001—fiscal 2003 economic downturn increased cost pressure on our customers and we have observed increasing price sensitivity on their part. In response, we are actively seeking to reduce our cost structure by moving operations to lower cost areas and by reducing other operating costs. If we are unable to realize prices that allow us to continue to compete on the basis of performance and service, our financial condition and operating results may be materially and adversely affected.

Our quarterly operating results fluctuate significantly and may continue to do so in the future

In the past, our quarterly operating results have fluctuated significantly. We expect that they will continue to fluctuate. Although these fluctuations are partly due to the volatile nature of the semiconductor industry, they also reflect other factors, many of which are outside of our control.

Some of the factors that may cause our revenues and/or operating margins to fluctuate significantly from period to period are:

market downturns;

the mix of products that we sell because, for example:

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some lines of equipment within our business segments are more profitable than others; and

some sales arrangements have higher margins than others;

the volume and timing of orders for our products and any order postponements;

virtually all of our orders are subject to cancellation, deferral or rescheduling by the customer without prior notice and with limited or no penalties;

competitive pricing pressures may force us to reduce prices to retain the business;

higher than anticipated costs of development or production of new equipment models;

the availability and cost of the components for our products;

unanticipated delays in the development and manufacture of our new products and upgraded versions of our products and market acceptance of these products when introduced;

customers' delay in purchasing our products due to anticipation that we or our competitors may introduce new or upgraded products; and

our competitors' introduction of new products.

Many of our expenses, such as research and development, selling, general and administrative expenses, and interest expense, do not vary directly with our net sales. Our research and development efforts include long-term projects lasting a year or more, which require significant investments. In order to realize the benefits of these projects, we believe that we must continue to fund them during periods when our net sales have declined. As a result, a decline in our net sales would adversely affect our operating results. In addition, if we were to incur additional expenses in a quarter in which we did not experience comparable increased net sales, our operating results would decline. In a downturn, we may have excess inventory, which is required to be written off. Some of the other factors that may cause our expenses to fluctuate from period-to-period include:

the timing and extent of our research and development efforts;

severance, resizing, and other costs of relocating facilities;

inventory write-offs due to obsolescence; and

inflationary increases in the cost of labor or materials.

Because our revenues and operating results are volatile and difficult to predict, we believe that consecutive period-to-period comparisons of our operating results may not be a good indication of our future performance.

We may not be able to rapidly develop, manufacture and gain market acceptance of new and enhanced products required to maintain or expand our business

We believe that our continued success depends on our ability to continuously develop and manufacture new products and product enhancements on a timely and cost-effective basis. We must introduce these products and product enhancements into the market in a timely manner in response to customers' demands for higher performance assembly equipment, leading-edge materials customized to address rapid technological advances in integrated circuits, and capital equipment designs. Our competitors may develop new products or enhancements to their products that offer

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performance, features and lower prices that may render our products less competitive. The development and commercialization of new products requires significant capital expenditures over an extended period of time, and some products that we seek to develop may never become profitable. In addition, we may not be able to develop and introduce products incorporating new technologies in a timely manner that will satisfy our customers' future needs or achieve market acceptance.

Substantially all of our sales and manufacturing operations are located outside of the United States, and we rely on independent foreign distribution channels for certain product lines; all of which subject us to risks, including risks from changes in trade regulations, currency fluctuations, political instability and war

Approximately 93% of our net sales for fiscal 2006 and 95% of our net sales for fiscal 2005 and 2004 were to customers located outside of the United States, in particular to customers located in the Asia/Pacific region. Our future performance will depend on our ability to continue to compete in foreign markets, particularly in the Asia/Pacific region. These economies have been highly volatile, resulting in significant fluctuation in local currencies, and political and economic instability. These conditions may continue or worsen, which may materially and adversely affect our business, financial condition and operating results.

We also rely on non-United States suppliers for materials and components used in our products, and nearly all of our manufacturing operations are located in countries other than the United States. We manufacture our automatic ball bonders and bonding wire in Singapore, we manufacture capillaries in Israel and China, die bonders in Switzerland and China, bonding wire in Switzerland, and we have sales, service and support personnel in China, Japan, Korea, Malaysia, the Philippines, Singapore, Taiwan and Europe. We also rely on independent foreign distribution channels for certain of our product lines. As a result, a major portion of our business is subject to the risks associated with international, and particularly Asia/Pacific, commerce, such as:

risks of war and civil disturbances or other events that may limit or disrupt manufacturing and markets;

seizure of our foreign assets, including cash;

longer payment cycles in foreign markets;

international exchange restrictions;

restrictions on the repatriation of our assets, including cash;

significant foreign and United States taxes on repatriated cash;

the difficulties of staffing and managing dispersed international operations;

possible disagreements with tax authorities regarding transfer pricing regulations;

episodic events outside our control such as, for example, an outbreak of Severe Acute Respiratory Syndrome or influenza;

tariff and currency fluctuations;

changing political conditions;

labor conditions and costs;

foreign governments' monetary policies and regulatory requirements;

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less protective foreign intellectual property laws; and

legal systems which are less developed and which may be less predictable than those in the United States.

Because most of our foreign sales are denominated in United States dollars, an increase in value of the United States dollar against foreign currencies, particularly the Japanese yen, will make our products more expensive than those offered by some of our foreign competitors. Our ability to compete overseas in the future may be materially and adversely affected by a strengthening of the United States dollar against foreign currencies.

Our international operations also depend upon favorable trade relations between the United States and those foreign countries in which our customers, subcontractors, and materials suppliers have operations. A protectionist trade environment in either the United States or those foreign countries in which we do business, such as a change in the current tariff structures, export compliance or other trade policies, may materially and adversely affect our ability to sell our products in foreign markets.

We are exposed to fluctuations in currency exchange rates that could negatively impact our financial results and cash flows

Because a significant portion of our business is conducted outside the United States, we face exposure to adverse movements in foreign currency exchange rates which could have a material adverse impact on our financial results and cash flows. Historically, our primary exposures have related to (net) receivables denominated in currencies other than a foreign subsidiaries' functional currency, and remeasurement of our foreign subsidiaries' net monetary assets from the subsidiaries' local currency into the subsidiaries' functional currency (the U.S. dollar). In general, an increase in the value of the U.S. dollar could require certain of our foreign subsidiaries to record translation and remeasurement gains. Conversely, a decrease in the value of the U.S. dollar could require certain of our foreign subsidiaries to record losses on translation and remeasurement. An increase in the value of the dollar could increase the cost to our customers of our products in those markets outside the United States where we sell in dollars, and a weakened dollar could increase the cost of local operating expenses and procurement of raw materials. An increase in the value of China's Yuan could increase our material, labor, and other operating expenses in China. Our board has granted management with limited authority to enter into foreign exchange forward contracts and other instruments designed to minimize the short term impact currency fluctuations have on our business. We have entered into foreign exchange forward contracts and expect to enter into additional foreign exchange forward contracts and other instruments in the future. Our attempts to hedge against these risks may not be successful and may result in a material adverse impact on our financial results and cash flows.

We may not be able to consolidate manufacturing facilities without incurring unanticipated costs and disruptions to our business

As part of our ongoing efforts to further reduce our cost structure, we seek to consolidate our manufacturing facilities. We may incur significant and unexpected costs, delays and disruptions to our business during this consolidation process. Because of unanticipated events, including the actions of governments, suppliers, employees or customers, we may not realize the synergies, cost reductions and other benefits of any consolidation to the extent or within the timeframe that we currently expect.

Our business depends on attracting and retaining management, marketing and technical employees

Our future success depends on our ability to hire and retain qualified management, marketing and technical employees. In particular, we periodically experience shortages of technical personnel. If we are unable to continue to attract and retain the managerial, marketing and technical personnel we require, our business, financial condition and operating results could be materially and adversely affected.

Difficulties in forecasting demand for our product lines may lead to periodic inventory shortages or excesses

We typically operate our business with limited visibility of future demand. As a result, we sometimes experience inventory shortages or excesses. We generally order supplies and otherwise plan our production based on internal

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forecasts of demand. We have in the past, and may again in the future, fail to forecast accurately demand for our products, in terms of both volume and configuration for either our current or next-generation wire bonders. This has led to and may in the future lead to delays in product shipments or, alternatively, an increased risk of inventory obsolescence. If we fail to forecast accurately demand for our products, including assembly equipment and packaging materials, our business, financial condition and operating results may be materially and adversely affected.

Advanced packaging technologies other than wire bonding may render some of our products obsolete

Advanced packaging technologies have emerged that may improve device performance or reduce the size of an integrated circuit package, as compared to traditional die and wire bonding. These technologies include flip chip and chip scale packaging. Some of these advanced technologies eliminate the need for wires to establish the electrical connection between a die and its package. The semiconductor industry may, in the future, shift a significant part of its volume into advanced packaging technologies, such as those discussed above, which do not employ our products. If a significant shift to advanced packaging technologies were to occur, demand for our equipment and related packaging materials may be materially and adversely affected.

Because a small number of customers account for most of our sales, our revenues could decline if we lose a significant customer

The semiconductor manufacturing industry is highly concentrated, with a relatively small number of large semiconductor manufacturers and their subcontract assemblers and vertically integrated manufacturers of electronic systems purchasing a substantial portion of our semiconductor assembly equipment and packaging materials. Sales to a relatively small number of customers account for a significant percentage of our net sales. During fiscal 2006, 2005, and 2004, sales to Advanced Semiconductor Engineering, our largest customer accounted for 17%, 15% and 19%, respectively, of our net sales.

We expect that sales of our products to a small number of customers will continue to account for a high percentage of our net sales for the foreseeable future. Thus, our business success depends on our ability to maintain strong relationships with our important customers. Any one of a number of factors could adversely affect these relationships. If, for example, during periods of escalating demand for our equipment, we were unable to add inventory and production capacity quickly enough to meet the needs of our customers, they may turn to other suppliers making it more difficult for us to retain their business. Similarly, if we are unable for any other reason to meet production or delivery schedules, particularly during a period of escalating demand, our relationships with our key customers could be adversely affected. If we lose orders from a significant customer, or if a significant customer reduces its orders substantially, these losses or reductions may materially and adversely affect our business, financial condition and operating results.

We depend on a small number of suppliers for raw materials, components and subassemblies. If our suppliers do not deliver their products to us, we would be unable to deliver our products to our customers

Our products are complex and require raw materials, components and subassemblies having a high degree of reliability, accuracy and performance. We rely on subcontractors to manufacture many of these components and subassemblies and we rely on sole source suppliers for some important components and raw materials, including gold. As a result, we are exposed to a number of significant risks, including:

lack of control over the manufacturing process for components and subassemblies;

Changes in our manufacturing processes, in response to changes in the market, which may delay our shipments;

our inadvertent use of defective or contaminated raw materials;

the relatively small operations and limited manufacturing resources of some of our suppliers, which may limit their ability to manufacture and sell subassemblies, components or parts in the volumes we require and at acceptable quality levels and prices;

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reliability or quality problems with certain key subassemblies provided by single source suppliers as to which we may not have any short term alternative;

shortages caused by disruptions at our suppliers and subcontractors for a variety of reasons, including work stoppage or fire, earthquake, flooding or other natural disasters;

delays in the delivery of raw materials or subassemblies, which, in turn, may delay our shipments; and

the loss of suppliers as a result of consolidation of suppliers in the industry.

If we are unable to deliver products to our customers on time for these or any other reasons; if we are unable to meet customer expectations as to cycle time; or if we do not maintain acceptable product quality or reliability, our business, financial condition and operating results may be materially and adversely affected.

Diversification into multiple businesses increases demands on our management and systems

We recently acquired Alphasem, a manufacturer of die bonders, and may from time to time in the future seek to expand through further acquisition. Significant acquisitions increase demands on management, financial resources and information and internal control systems. Our success will depend, in part, on our ability to manage and integrate acquired businesses with our existing businesses and to successfully implement, improve and expand our systems, procedures and controls. If we fail to integrate businesses successfully or to develop the necessary internal procedures to manage diversified businesses, our business, financial condition and operating results may be materially and adversely affected.

We may be unable to continue to compete successfully in the highly competitive semiconductor equipment and packaging materials industries

The semiconductor equipment and packaging materials industries are very competitive. In the semiconductor equipment, significant competitive factors include performance, quality, customer support and price. In the semiconductor packaging materials industry, competitive factors include price, delivery and quality.

In each of our markets, we face competition and the threat of competition from established competitors and potential new entrants. In addition, established competitors may combine to form larger, better capitalized companies. Some of our competitors have or may have significantly greater financial, engineering, manufacturing and marketing resources than we have. Some of these competitors are Asian and European companies that have had and may continue to have an advantage over us in supplying products to local customers who appear to prefer to purchase from local suppliers, without regard to other considerations.

We expect our competitors to improve their current products' performance, and to introduce new products and materials with improved price and performance characteristics. Our competitors may independently develop technology that is similar to or better than ours. New product and materials introductions by our competitors or by new market entrants could hurt our sales. If a particular semiconductor manufacturer or subcontract assembler selects a competitor's product or materials for a particular assembly operation, we may not be able to sell products or materials to that manufacturer or assembler for a significant period of time because manufacturers and assemblers sometimes develop lasting relations with suppliers, and assembly equipment in our industry often goes years without requiring replacement. In addition, we may have to lower our prices in response to price cuts by our competitors, which may materially and adversely affect our business, financial condition and operating results. We cannot assure you that we will be able to continue to compete in these or other areas in the future. If we cannot compete successfully, we could be forced to reduce prices, and could lose customers and market share and experience reduced margins and profitability.

Our success depends in part on our intellectual property, which we may be unable to protect

Our success depends in part on our proprietary technology. To protect this technology, we rely principally on

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contractual restrictions (such as nondisclosure and confidentiality provisions) in our agreements with employees, subcontractors, vendors, consultants and customers and on the common law of trade secrets and proprietary know-how. We also rely, in some cases, on patent and copyright protection. We may not be successful in protecting our technology for a number of reasons, including the following:

employees, subcontractors, vendors, consultants and customers may violate their contractual agreements, and the cost of enforcing those agreements may be prohibitive, or those agreements may be unenforceable or more limited than we anticipate;

foreign intellectual property laws may not adequately protect our intellectual property rights;

our patent and copyright claims may not be sufficiently broad to effectively protect our technology; our patents or copyrights may be challenged, invalidated or circumvented; or we may otherwise be unable to obtain adequate protection for our technology.

In addition, our partners and alliances may also have rights to technology that we develop. We may incur significant expense to protect or enforce our intellectual property rights. If we are unable to protect our intellectual property rights, our competitive position may be weakened.

Third parties may claim we are infringing on their intellectual property, which could cause us to incur significant litigation costs or other expenses, or prevent us from selling some of our products

The semiconductor industry is characterized by rapid technological change, with frequent introductions of new products and technologies. Industry participants often develop products and features similar to those introduced by others, creating a risk that their products and processes may give rise to claims that they infringe on the intellectual property of others. We may unknowingly infringe on the intellectual property rights of others and incur significant liability for that infringement. If we are found to have infringed on the intellectual property rights of others, we could be enjoined from continuing to manufacture, market or use the affected product, or be required to obtain a license to continue manufacturing or using the affected product. A license could be very expensive to obtain or may not be available at all. Similarly, changing or re-engineering our products or processes to avoid infringing the rights of others may be costly, impractical or time consuming.

Occasionally, third parties assert that we are, or may be, infringing on or misappropriating their intellectual property rights. In these cases, we will defend against claims or negotiate licenses where we consider these actions appropriate. Intellectual property cases are uncertain and involve complex legal and factual questions. If we become involved in this type of litigation, it could consume significant resources and divert our attention from our business.

We may be materially and adversely affected by environmental and safety laws and regulations

We are subject to various federal, state, local and foreign laws and regulations governing, among other things, the generation, storage, use, emission, discharge, transportation and disposal of hazardous material, investigation and remediation of contaminated sites and the health and safety of our employees. Increasingly, public attention has focused on the environmental impact of manufacturing operations and the risk to neighbors of chemical releases from such operations.

Proper waste disposal plays an important role in the operation of our manufacturing plants. In many of our facilities we maintain wastewater treatment systems that remove metals and other contaminants from process wastewater. These facilities operate under permits that must be renewed periodically. A violation of those permits may lead to revocation of the permits, fines, penalties or the incurrence of capital or other costs to comply with the permits, including potential shutdown of operations.

In the future, existing or new land use and environmental regulations may: (1) impose upon us the need for additional capital equipment or other process requirements, (2) restrict our ability to expand our operations, (3) subject us to liability for, among other matters, remediation, and/or (4) cause us to curtail our operations. We cannot

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assure you that any costs or liabilities associated with complying with these environmental laws will not materially and adversely affect our business, financial condition and operating results.

Anti-takeover provisions in our articles of incorporation and bylaws, and under Pennsylvania law may discourage other companies from attempting to acquire us

Some provisions of our articles of incorporation and bylaws as well as Pennsylvania law may discourage some transactions where we would otherwise experience a fundamental change. For example, our articles of incorporation and bylaws contain provisions that:

Classify our board of directors into four classes, with one class being elected each year;

permit our board to issue blank check preferred stock without stockholder approval; and

Prohibit us from engaging in some types of business combinations with a holder of 20% or more of our voting securities without super-majority board or stockholder approval.

Further, under the Pennsylvania Business Corporation Law, because our bylaws provide for a classified board of directors, stockholders may remove directors only for cause. These provisions and some other provisions of the Pennsylvania Business Corporation Law could delay, defer or prevent us from experiencing a fundamental change and may adversely affect our common stockholders' voting and other rights.

Terrorist attacks, or other acts of violence or war may affect the markets in which we operate and our profitability

Terrorist attacks may negatively affect our operations. There can be no assurance that there will not be further terrorist attacks against the United States or United States businesses. Terrorist attacks or armed conflicts may directly impact our physical facilities or those of our suppliers or customers. Our primary facilities include administrative, sales and R&D facilities in the United States and manufacturing facilities in the United States, Singapore, Switzerland, China and Israel. Additional terrorist attacks may disrupt the global insurance and reinsurance industries with the result that we may not be able to obtain insurance at historical terms and levels for all of our facilities. Furthermore, additional attacks may make travel and the transportation of our supplies and products more difficult and more expensive and ultimately affect the sales of our products in the United States and overseas. Additional attacks or any broader conflict, could negatively impact on our domestic and international sales, our supply chain, our production capability and our ability to deliver products to our customers. Political and economic instability in some regions of the world could negatively impact our business. The consequences of terrorist attacks or armed conflicts are unpredictable, and we may not be able to foresee events that could have an adverse effect on our business.

We may be unable to generate enough cash to repay our debt

Our ability to make payments on our indebtedness and to fund planned capital expenditures and other activities will depend on our ability to generate cash in the future. If our convertible debt is not converted to our common shares, we will be required to make annual cash interest payments of \$1.3 million in each of fiscal years 2007 and 2008, \$0.8 million in fiscal 2009 and \$0.5 million in fiscal 2010 on our aggregate \$195.0 million of convertible subordinated debt. Principal payments of \$130.0 million and \$65.0 million on the convertible subordinated debt are due in fiscal 2009 and 2010, respectively. Our ability to make payments on our indebtedness is affected by the volatile nature of our business, and general economic, competitive and other factors that are beyond our control. Our indebtedness poses risks to our business, including that:

insufficient cash flow from operations to repay our outstanding indebtedness when it becomes due may force us to sell assets, or seek additional capital, which we may be unable to do at all or on terms favorable to us; and

our level of indebtedness may make us more vulnerable to economic or industry downturns.

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We cannot assure you that our business will generate cash in an amount sufficient to enable us to service interest, principal and other payments on our debt, including the notes, or to fund our other liquidity needs. We are not restricted under the

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agreements governing our existing indebtedness from incurring additional debt in the future. If new debt is added to our current levels, our leverage and our debt service obligations would increase and the related risks described above could intensify.

We have the ability to issue additional equity securities, which would lead to dilution of our issued and outstanding common stock

The issuance of additional equity securities or securities convertible into equity securities will result in dilution of existing stockholders' equity interests in us. Our board of directors has the authority to issue, without vote or action of stockholders, shares of preferred stock in one or more series, and has the ability to fix the rights, preferences, privileges and restrictions of any such series. Any such series of preferred stock could contain dividend rights, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences or other rights superior to the rights of holders of our common stock. In addition, we are authorized to issue, without stockholder approval, up to an aggregate of 200 million shares of common stock, of which approximately 57.2 million shares were outstanding as of September 30, 2006. We are also authorized to issue, without stockholder approval, securities convertible into either shares of common stock or preferred stock.

Weaknesses in our internal controls and procedures could result in material misstatements in our financial statements

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal controls over financial reporting are processes designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with U.S. generally accepted accounting principles. A material weakness is a control deficiency, or combination of control deficiencies, that results in a more than remote likelihood that a material misstatement of annual or interim financial statements will not be prevented or detected.

Management determined that a material weaknesses in our internal control over financial reporting existed as of September 30, 2006. See Item 9A – Controls and Procedures for a description of this material weakness.

We have begun to implement measures designed to remediate the material weakness in our internal controls by September 30, 2007 (See Item 9A – Controls and Procedures). We cannot assure you as to when the remediation measures will be fully implemented, nor can we assure you that additional material weaknesses will not be identified by our management or independent accountants in the future. In addition, even after the remediation measures are fully implemented, our internal controls may not prevent all potential errors or fraud, because any control system, no matter how well designed and implemented, can only provide reasonable and not absolute assurance that the objectives of the control system will be achieved.

Table of Contents**Item 2. PROPERTIES.**

Our major operating facilities are described in the table below:

Facility	Approximate Size	Function	Products Manufactured	Lease
				Expiration Date (4)
Fort Washington, Pennsylvania	88,000 sq. ft. (1)	Corp. headquarters, manufacturing, technology center, sales and service	Wedge, large area bonders	April 2028
Suzhou, China	136,379 sq. ft. (1)	Manufacturing	Capillaries, dicing blades	October 2022
Singapore	77,500 sq.ft. (1)	Manufacturing, technology center, assembly systems	Wire bonders	August 2008
Singapore	38,400 sq. ft. (1)	Manufacturing, technology center, assembly systems	Bonding wire	May 2009
Yokneam, Israel	53,800 sq .ft. (2)	Manufacturing, technology center	Capillaries, wedges, die collets	N/A
Thalwil, Switzerland	15,100 sq .ft. (1)	Manufacturing	Bonding wire	(3)
Berg, Switzerland	69,940 sq.ft. (2)	Manufacturing, technology center	Die bonders	N/A

(1) Leased.

(2) Owned.

(3) Cancelable semi-annually upon six months notice.

(4) Includes lease extension periods at the Company's option.

We also rent space for sales and service offices in: San Jose, California; Chandler, Arizona; China; Germany; Japan; Korea; Malaysia; the Philippines; Taiwan; and Thailand. We believe that our facilities generally are in good condition.

Item 3. LEGAL PROCEEDINGS.

From time to time, we are a plaintiff or defendant in various cases arising out of our business. We cannot assure you of the results of any pending or future litigation, but we do not believe that resolution of these matters will materially and adversely affect our business, financial condition or operating results.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

Table of Contents**PART II****Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.**

Our common stock is traded on the Nasdaq Global Market under the symbol KLIC. The following table lists the high and low per share sale prices for our common stock for the periods indicated:

	Common Stock Price	
	High	Low
Fiscal year ended September 30, 2006:		
First Quarter	\$ 9.33	\$ 5.95
Second Quarter	12.50	8.47
Third Quarter	10.23	7.05
Fourth Quarter	9.18	6.50
Fiscal year ended September 30, 2005:		
First Quarter	\$ 9.30	\$ 5.70
Second Quarter	8.68	5.90
Third Quarter	8.44	4.94
Fourth Quarter	10.60	6.74

The payment of dividends on our common stock is within the discretion of our board of directors. We have not historically paid any cash dividends on our common stock, including during the past two fiscal years, and we do not expect to declare cash dividends on our common stock in the near future. We intend to retain earnings to finance the growth of our business and/or pay down debt.

For the purposes of calculating the aggregate market value of the shares of our common stock held by nonaffiliates, as shown on the cover page of this report, we have assumed that all of our outstanding shares were held by nonaffiliates except for the shares held by our directors and executive officers. However, this does not necessarily mean that all directors and executive officers of the Company are, in fact, affiliates of the Company, or that there are not other persons who may be deemed to be affiliates of the Company. Further information concerning the beneficial ownership of our executive officers, directors and principal shareholders will be included in our proxy statement relating to our 2007 Annual Meeting of Shareholders to be filed with the SEC on or about January 3, 2007.

On December 1, 2006, there were 535 holders of record of the shares of outstanding common stock.

Recent Sales of Unregistered Securities:

During the last fiscal year, except as otherwise disclosed on our current reports on Form 8-K, we have not sold any of our securities without registration under the Securities Act, except as described below:

During the quarter ended April 1, 2006, we issued and contributed 200,000 shares of our common stock with a fair value of approximately \$1.8 million (based upon the market price at the time of contribution) to Reliance Trust Company, as Trustee of our defined benefit pension plan, in a private placement under Section 4(2) of the Securities Act. We issued and contributed the shares of our common stock to the trust to fund certain obligations to the pension plan.

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On February 14, 2006, the Company purchased a portion of its outstanding 0.5% Convertible Subordinated Notes having an aggregate principal amount of \$52.2 million for consideration consisting of 2.5 million shares of common stock with an aggregate fair value of \$29.5 million and \$18.7 million in cash. On February 16, 2006, the Company purchased an additional portion of its outstanding 0.5% Convertible Subordinated Notes having an aggregate principal amount of \$22.8 million for consideration consisting of 1.1 million shares of common stock with an aggregate fair value of \$13.2 million and \$8.0 million in cash. In accordance with Accounting Principles Board Opinion No. 26, *Early Extinguishment of Debt*, the Company recorded a net gain on the transactions of \$4.0 million, net of deferred financing cost write-offs of \$1.3 million and transaction costs of \$0.4 million.

Item 6. SELECTED FINANCIAL DATA.

The following selected consolidated financial data should be read in conjunction with our consolidated financial statements, related notes and other financial information included elsewhere in this report or in annual reports filed previously by us in respect of the fiscal years identified in the column headings of the tables below.

	<i>(in thousands, except per share amounts)</i>				
	Fiscal Year Ended September 30,				
	2002	2003	2004	2005	2006
Statement of Operations Data:					
Net Sales:					
Equipment	\$ 169,469	\$ 198,447	\$ 361,244	\$ 201,608	\$ 319,788
Packaging materials	157,398	174,606	234,690	273,934	376,523
Total net sales	326,867	373,053	595,934	475,542	696,311
Cost of sales:					
Equipment	142,965	129,092	208,616	115,558	178,473
Packaging materials	118,094	132,779	182,593	223,903	321,277
Total cost of sales (1)	261,059	261,871	391,209	339,461	499,750
Operating expenses:					
Equipment	141,204	85,609	76,159	65,606	85,445
Packaging materials	53,827	31,896	26,399	30,724	33,674
Gain on sale of assets					(4,544)
Total operating expenses (1)	195,031	117,505	102,558	96,330	114,575
Income (loss) from operations:					
Equipment	(114,700)	(16,254)	76,469	20,444	55,870
Packaging materials	(14,523)	9,931	25,698	19,307	21,572
Gain on sale of assets					4,544
Income (loss) from operations (1)	(129,223)	(6,323)	102,167	39,751	81,986
Interest income (expense), net					
	(14,941)	(16,491)	(9,357)	(1,578)	795
Gain (loss) on early extinguishment of debt					
			(10,510)		4,040
Other income and minority interest					
	2,010				
Income (loss) from continuing operations before taxes	(142,154)	(22,814)	82,300	38,173	86,821
Provision for income taxes from continuing operations (2)	31,719	8,001	7,583	4,836	9,789
Income (loss) from continuing operations	(173,873)	(30,815)	74,717	33,337	77,032
Loss from discontinued operations, net of tax (2)(3)	(100,242)	(45,874)	(18,837)	(137,419)	(24,862)
Net income (loss)	\$ (274,115)	\$ (76,689)	\$ 55,880	\$ (104,082)	\$ 52,170

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	<i>(in thousands, except per share amounts)</i>				
	Fiscal Year Ended September 30,				
	2002	2003	2004	2005	2006(1)
Per Share Data:					
Income (loss) from continuing operations (4)					
Basic	\$ (3.53)	\$ (0.62)	\$ 1.47	\$ 0.65	\$ 1.40
Diluted	\$ (3.53)	\$ (0.62)	\$ 1.17	\$ 0.52	\$ 1.14
Discontinued operations, net of tax per share: (4)					
Basic	\$ (2.04)	\$ (0.92)	\$ (0.37)	\$ (2.67)	\$ (0.45)
Diluted	\$ (2.04)	\$ (0.92)	\$ (0.28)	\$ (2.03)	\$ (0.36)
Net income (loss) per share: (4)					
Basic	\$ (5.57)	\$ (1.54)	\$ 1.10	\$ (2.02)	\$ 0.95
Diluted	\$ (5.57)	\$ (1.54)	\$ 0.89	\$ (1.51)	\$ 0.78
Shares used in per common share calculations: (4)					
Basic	49,217	49,695	50,746	51,619	55,089
Diluted	49,217	49,695	68,582	67,662	68,881
Balance Sheet Data:					
Cash, cash equivalents and short-term investments	\$ 111,300	\$ 73,051	\$ 95,766	\$ 95,369	\$ 157,283
Working capital	159,813	125,829	175,953	186,049	248,978
Total assets	538,682	442,861	476,958	386,496	405,501
Long-term debt (5) (6)	300,000	300,000	270,000	270,000	195,000
Shareholders' equity (deficit)	69,323	97	67,020	(31,748)	79,306

(1) During fiscal 2006, we recorded the following charges in continuing operations: \$3.5 million in cost of sales and \$0.8 million in operating expenses for the cumulative adjustment to correct immaterial errors in the consolidated financial statements; \$0.6 million in cost of sales and \$4.1 million in operating expenses for FAS 123R stock compensation expense; \$9.0 million in operating expenses for incentive compensation and a gain on the sale of assets of \$4.5 million in operating expenses.

During fiscal 2005, we recorded the following charges as operating expenses in continuing operations: severance charges of \$0.9 million; China start-up costs of \$1.2 million; and inventory write-downs of \$1.0 million. We also recorded a gain on the sale of assets of \$1.7 million within fiscal 2005 operating expenses.

During fiscal 2004, we recorded the following charges as operating expenses in continuing operations: severance charges of \$1.9 million; China start-up costs of \$0.1 million; inventory write-downs of \$0.4 million; and a reversal of prior year resizing charges of \$0.1 million. We also recorded a gain on the sale of assets of \$0.9 million within fiscal 2004 operating expenses.

During fiscal 2003, we recorded the following charges as operating expenses in continuing operations: loss on sale of product lines of \$5.3 million and asset impairment of \$0.5 million which resulted from the write-down of assets that were sold and assets that became obsolete, \$3.1 million of severance associated with workforce reductions; and charges for inventory write-downs of \$1.7 million (to costs of sales).

During fiscal 2002, we recorded the following charges as operating expenses: goodwill impairment of \$2.3 million associated with our saw blade business unit; asset impairment of \$30.3 million primarily due to the cancellation of a company-wide integrated information system, the closure of our high density interconnect substrate business and the write-off of development and license costs of certain engineering and manufacturing software; \$14.1 million of resizing charges comprised primarily of severance and contractual commitments associated with reductions in workforce in our continuing businesses. In fiscal 2002, we also recorded charges for inventory write-downs of \$9.2 million (to costs of sales).

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- (2) In fiscal 2006, we reversed \$38.2 million of valuation allowance associated with our U.S. net operating loss carryforward deferred tax asset and provided \$21.5 million for withholding tax liability associated with future repatriation of earnings. In fiscal 2005, we recorded \$15.0 million of valuation allowance associated with our U.S. net operating loss carryforward deferred tax asset. In fiscal 2004, we reversed \$11.2 million of valuation allowance associated with our U.S. net operating loss carryforward deferred tax asset. In fiscal 2003, we recorded a valuation allowance against our deferred tax asset consisting primarily of U.S. net operating loss carryforwards of \$12.1 million. In fiscal 2002 we recorded a valuation allowance against our deferred tax asset consisting primarily of U.S. net operating loss carryforwards of \$65.3 million and a charge of \$25.0 million to provide for tax expense on repatriation of certain foreign earnings.
- (3) Reflects the operations of the Company's former flip chip business unit and test division which were sold in February 2004 and March 2006, respectively.
- (4) For fiscal years 2002 and 2003, only the common shares outstanding have been used to calculate both the basic earnings per common share and diluted earnings per common share because the inclusion of potential common shares would be anti-dilutive due to the net losses from continuing operations reported in those years. The after-tax interest expense recognized in fiscal 2004, 2005 and 2006 associated with our convertible subordinated notes that was added back to net income in order to compute diluted net income per share was \$5.2 million, \$1.7 million and \$1.4 million, respectively.
- (5) Does not include letters of credit.
- (6) In June 2004, we issued \$65.0 million in principal amount of 1% Convertible Subordinated Notes due 2010 and in December 2003, we issued \$205.0 million in principal amount of 0.5% Convertible Subordinated Notes due 2008. In February 2006, we repurchased \$75.0 million of our 0.5% Convertible Subordinated Notes. In August 2001, we issued \$125.0 million in principal amount of 5 1/4 % Convertible Subordinated Notes due 2006, which we redeemed in their entirety in August 2004. In December 1999, we issued \$175.0 million in principal amount of 4.75% Convertible Subordinated Notes due 2006, which we redeemed in their entirety in December 2003.

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Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

In addition to historical information, this filing contains statements relating to future events or our future results. These statements are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act) and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), and are subject to the safe harbor provisions created by statute. Such forward-looking statements include, but are not limited to, statements that relate to our future revenue, product development, demand forecasts, competitiveness, operating expenses, cash flows, profitability, gross margins, and benefits expected as a result of (among other factors):

the projected growth rates in the overall semiconductor industry, the semiconductor assembly equipment market, and the market for semiconductor packaging materials; and

the projected continuing demand for wire bonder and die bonder equipment.

Generally, words such as may, will, should, could, anticipate, expect, intend, estimate, plan, continue, goal and believe, or the negative of or other variations on these and other similar expressions identify forward-looking statements. These forward-looking statements are made only as of the date of this filing. We do not undertake to update or revise the forward-looking statements, whether as a result of new information, future events or otherwise.

Forward-looking statements are based on current expectations and involve risks and uncertainties and our future results could differ significantly from those expressed or implied by our forward-looking statements. These risks and uncertainties include, without limitation, those described below and under the heading Risk Factors within this section and in our other reports and registration statements filed from time to time with the Securities and Exchange Commission (SEC). This discussion should be read in conjunction with the Consolidated Financial Statements and Notes in this report.

Introduction

We design, manufacture and market capital equipment and packaging materials as well as service, maintain, repair and upgrade equipment, all used to assemble semiconductor devices. We are currently the world's leading supplier of semiconductor wire bonding assembly equipment, according to VLSI Research, Inc. Our business is currently divided into two product segments:

equipment; and

packaging materials.

We believe we are the only major supplier to the semiconductor assembly industry that provides customers with semiconductor die bonding and wire bonding equipment along with the complementary packaging materials that actually contact the surface of the customer's semiconductor devices. We believe that the ability to control these assembly related products provides us with a significant competitive advantage and should allow us to develop system solutions to the new technology challenges inherent in assembling and packaging next-generation semiconductor devices.

The semiconductor industry has been historically volatile, with periods of rapid growth followed by downturns. Compared to the first quarter of fiscal 2006, revenues for the second, third and fourth fiscal quarters were lower, as industry wide demand for automatic ball bonders decreased. As we look ahead to the first fiscal quarter of 2007, we expect net revenue to be in the \$140 to \$150 million range, including approximately \$7 million in revenue from die bonders and excluding any impact of fluctuations in gold pricing. There can be no assurances regarding levels of demand for our products, and in any case, we believe the historical volatility both upward and downward will persist.

We have continued to lower our cost structure by consolidating operations, moving certain of our manufacturing capacity to China, moving a portion of our supply chain to lower cost suppliers and designing higher-performing, lower cost equipment. Cost reduction efforts have become, and will continue to be, an important part of our normal

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ongoing operations and we expect to continue to further drive down our cost structure below current levels, while not diminishing our product quality. Our goal is to be both the technology leader and the lowest cost supplier in each of our major lines of business.

On November 3, 2006, we completed the acquisition of Alphasem, a leading supplier of die bonder equipment, from Dover Technologies International, Inc., a subsidiary of Dover Corporation. The business acquired is a leading supplier of die bonders. The consideration for the acquisition was approximately \$27.1 million in cash, after a working capital adjustment and subject to further post closing adjustments. We will integrate Alphasem into our equipment segment.

Beginning in fiscal year 2006, to align our external reporting with management's internal reporting, we no longer include Corporate and Other as a business segment. Costs previously presented separately for this segment, which primarily consisted of general corporate expenses, have been allocated to our two remaining business segments. The business segment information for fiscal 2004 and 2005 have been restated to reflect this change.

Discontinued Operations

During the three months ended April 1, 2006, we committed to a plan of disposal and sold our test business in two separate transactions as follows:

On March 3, 2006, we completed the sale of substantially all of the assets and certain of the liabilities of our wafer test business to SV Probe, PTE. Ltd. (SV Probe) for initial proceeds of \$10.0 million in cash plus the assumption of accounts payable and certain other liabilities, subject to a post-closing working capital adjustment that was settled in the three months ended July 1, 2006. Certain accounts receivable were excluded from the assets sold.

On March 31, 2006, we completed the sale of substantially all of the assets and certain of the liabilities of our package test business to Antares conTech, Inc., an entity formed by Investcorp Technology Ventures II, L.P. and its affiliates (collectively Investcorp) for initial proceeds of \$17.0 million in cash plus the assumption of accounts payable and certain other liabilities, subject to a post-closing working capital adjustment that was settled in the three months ended July 1, 2006.

We recorded a loss of \$0.8 million on the disposal of our test business. We sold the test business to allow management to strengthen its focus on our core businesses—semiconductor assembly equipment and materials—and explore growth opportunities in these markets.

As part of the terms of each sale noted above, the associated China-based assets were not transferred to the buyers on the above referenced closing dates, as neither buyer had a legal entity in China that could accept the transfer of the China-based assets as of the closing date. The China-based assets associated with the sale to SV Probe were transferred to SV Probe in September 2006 and the China-based assets associated with the sale to Antares conTech were transferred to Antares conTech in December 2006, without additional consideration. In addition, we provided manufacturing and other transition services (invoiced at cost) to SV Probe through September 1, 2006 and provided these services to Antares conTech through November 2006.

In accordance with Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144), the financial results of the test business have been presented as discontinued operations in our Consolidated Financial Statements. See Note 2 to our Consolidated Financial Statements included in Item 8 of this report for further discussion of the divestiture of our test business.

Unless otherwise indicated, amounts provided throughout this report relate to continuing operations only.

Table of Contents**Products and Services**

We offer a range of wire bonding and die bonding equipment (and related spare parts) and packaging materials. Set forth below is a table listing the percentage of our total net revenues from continuing operations for each business segment:

	<i>(in thousands)</i>					
	2004		Fiscal Year Ended September 30, 2005		2006	
	% of Total		% of Total		% of Total	
	Net		Net		Net	
	Net Revenues	Revenues	Net Revenues	Revenues	Net Revenues	Revenues
Equipment	\$ 361,244	61%	\$ 201,608	42%	\$ 319,788	46%
Packaging Materials	234,690	39%	273,934	58%	376,523	54%
	\$ 595,934	100%	\$ 475,542	100%	\$ 696,311	100%

Our equipment sales have been, and are expected to remain, highly volatile due to the semiconductor industry's need for new capability and capacity. Packaging materials unit sales tend to be less volatile, following the trend of total semiconductor unit production, however, fluctuations in gold metal commodity prices can have a significant impact on reported packaging materials net revenues.

See Note 11 to our Consolidated Financial Statements included in Item 8 of this report for financial results by business segment.

Equipment

We manufacture and market a line of wire bonders and die bonders. Our wire bonders are used to connect very fine wires, typically made of gold, aluminum or copper, between the bond pads of a semiconductor die and the leads on the integrated circuit (IC) package to which the die has been attached. We believe that our wire bonders offer competitive advantages by providing customers with high productivity/throughput and superior package quality/process control. In particular, our machines are capable of performing very fine pitch bonding as well as creating the sophisticated wire loop shapes that are needed in the assembly of advanced semiconductor packages. Our die bonders perform the task of removing a semiconductor die from a previously cut/separated wafer and placing it onto a bed of dispensed epoxy, or tape, which will permanently attach the die to its package substrate. This step precedes the wire bonding process. We believe our die bonders have good position in the market, serving a wide range of applications. Die bonders and wire bonders share many of the same sub-assemblies, software features, and components and we believe joining the engineering and manufacturing expertise of these two products will yield superior equipment platforms. Our principal products are:

Ball Bonders. Automatic IC ball bonders represent a large majority of our semiconductor equipment business. As part of our competitive strategy, we have been introducing new models of IC ball bonders every 15 to 24 months, with each new model designed to increase both productivity and process capability compared to its predecessor. We extended the life of the successful Maxum product line introducing the Maxum Ultra to succeed the Maxum Plus and the Maxum Elite to succeed the Nutek. Each of these machines provides approximately a 10% productivity improvement over its predecessor and offers various other performance improvements.

Specialty Wire Bonders. We also produce other models of wire bonders, targeted at specific market niches, including: the Model 8098, a large area ball bonder designed for wire bonding hybrid, chip on board applications, and other large area applications; and the Model 8090, a large area wedge bonder. We introduced a new model wafer stud bumper in the fourth quarter of fiscal 2005, the AT Premier. The AT Premier is targeted for gold-to-gold interconnect in the flip chip market. With industry-leading speed and technology, the machine lowers the cost of ownership for stud bumping,

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enabling a wider range of applications than previously served. We also manufacture and market a line of manual wire bonders.

IC Die Bonders. In November 2006, we acquired the Alphasem die bonder product lines, consisting of the SwissLine and EasyLine models. These products are used by many of the same customers and applications that our wire bonders serve today. We expect to utilize the same competitive strategy as our wire bonders by developing new models that will both improve the productivity of the die bonders and increase the size of the market that the new models will serve.

Specialty Die Bonders. A portion of the Alphasem product line is a series of specialty bonders that consist of several equipment models based on the die bonder platform. This equipment is used for various assembly processes that include die sorting, power device assembly, MEMS assembly, and others.

We believe that our industry knowledge and technical experience have positioned us to deliver innovative, customer-specific offerings that reduce the cost of owning our equipment over its useful life. In response to customer trends in outsourcing packaging requirements, we provide repair and maintenance services, a variety of equipment upgrades, machine and component rebuild activities and expanded customer training through our customer operations group.

Packaging Materials

We manufacture and market a range of semiconductor packaging materials and expendable tools for the semiconductor assembly market, including gold, aluminum and copper wire, capillaries, wedges, die collets, and saw blades, all of which are used in packaging and assembly processes. Our packaging materials are designed for use on both our own and our competitors' assembly equipment. A wire bonder uses a capillary or wedge tool and bonding wire much like a sewing machine uses a needle and thread. Our principal products are:

Bonding Wire. We manufacture gold, aluminum and copper wire used in the wire bonding process. This wire is bonded to the chip surface and package substrate by the wire bonder and becomes a permanent part of the customer's semiconductor package. We produce wire to a wide range of specifications, which can satisfy most wire bonding applications across the spectrum of semiconductor packages.

Expendable Tools. Our expendable tools include a wide variety of capillaries, wedges, die collets and wafer saw blades. The capillaries and wedges attach the wire to the semiconductor chip, allow a precise amount of wire to be fed out to form a permanent wire loop, then attach the wire to the package substrate, and finally cut the wire so that the bonding process can be repeated again. Die collets are used to pick up and place die into packages before the wire bonding process begins. Our hub blades are used to cut silicon wafers into individual semiconductor die.

Accounting Policies and Estimates

We believe the following accounting policy is critical to the preparation of our financial statements:

Revenue Recognition. Our revenue recognition policy is in accordance with Staff Accounting Bulletin (SAB) No. 104 (SAB 104), *Revenue Recognition*. We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable, the collectibility is reasonably assured, and we have satisfied equipment installation obligations and received customer acceptance, or are otherwise released from our installation or customer acceptance obligations. In the event terms of the sale provide for a lapsing customer acceptance period, we recognize revenue based upon the expiration of the lapsing acceptance period or customer acceptance, whichever occurs first. Our standard terms are Ex Works (Kulicke & Soffa factory), with title transferring to our customer at our loading dock or upon embarkation. We do have a small percentage of sales with other terms, and revenue is recognized in accordance with the terms of the related customer purchase order. Revenue related to services is generally recognized upon performance of the services requested by a

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customer. Revenue for extended maintenance service contracts with a term more than one month is recognized on a prorated straight-line basis over the term of the contract. Revenue from royalty arrangements and license agreements is recognized in accordance with the contract terms, generally prorated over the life of the contract or based upon specific deliverables.

Our business is subject to contingencies related to customer orders as follows:

Right of Return: A large portion of our revenue comes from the sale of machines that are used in the semiconductor assembly process. Other product sales relate to consumable products, which are sold in high-volume quantities, and are generally maintained at low stock levels at our customer's facility. Customer returns have historically represented a very small percentage of customer sales on an annual basis. Our policy is to provide an allowance for customer returns based upon our historical experience and management assumptions.

Warranties: Our products are generally shipped with a one-year warranty against manufacturer's defects and we generally do not offer extended warranties in the normal course of our business. We recognize a liability for estimated warranty expense when revenue for the related product is recognized. The estimated liability for warranty is based upon historical experience and our estimates of future expenses.

Conditions of Acceptance: Sales of our consumable products and bonding wire generally do not have customer acceptance terms. In certain cases, sales of our equipment products do have customer acceptance clauses which generally require that the equipment perform in accordance with specifications during an on-site factory inspection by the customer, as well as when installed at the customer's facility. In such cases, if the terms of acceptance are satisfied at our facility prior to shipment, the revenue for the equipment will be recognized upon shipment. If the terms of acceptance are satisfied at our customer's facility, the revenue for the equipment will be not be recognized until acceptance, which typically consists of installation and testing, is received from the customer.

Price Protection: We do not provide price protection to our customers.

Critical Estimates and Assumptions:

Generally accepted accounting principles require the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The more significant areas involving the use of estimates in our financial statements include allowances for uncollectible accounts receivable, reserves for excess and obsolete inventory, carrying value and lives of fixed assets, goodwill and intangible assets, valuation allowances for deferred tax assets and deferred tax liabilities, repatriation of unremitted foreign subsidiary earnings, self-insurance reserves, pension benefit liabilities, equity-based compensation expense, resizing, warranties, and litigation. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which are the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following accounting policies require significant judgments and estimates:

Allowance for Doubtful Accounts. We maintain allowances for doubtful accounts for estimated losses resulting from our customers failure to make required payments. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. We are also subject to concentrations of customers and sales to a few geographic locations, which would also impact the collectibility of certain receivables. If economic or political conditions were to change in some of the countries where we do business, it could have a significant impact on the results of our operations, and our ability to realize

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the full value of our accounts receivable.

Inventory Reserves. We generally provide reserves for obsolete inventory and for inventory considered to be in excess of 12 or 18 months of forecasted future demand. The forecasted demand is based upon internal projections, historical sales volumes, customer order activity, and a review of consumable inventory levels at our customers' facilities. We communicate forecasts of our future demand to our suppliers and adjust commitments to those suppliers accordingly. If required, we record additional reserves for the difference between the carrying value of our inventory and the lower of cost or market value, based upon assumptions about future demand, market conditions and the next cyclical market upturn. If actual market conditions are less favorable than our projections, additional inventory reserves may be required. We review and physically dispose of excess and obsolete inventory on a regular basis.

Valuation of Long-lived Assets. Our long-lived assets include property, plant and equipment, and goodwill and intangible assets. Our property, plant and equipment and intangible assets are depreciated over their estimated useful lives, and are reviewed for impairment whenever changes in circumstances indicate the carrying amount of these assets may not be recoverable. The fair value of our goodwill and intangible assets is based upon our estimates of future cash flows and other factors to determine the fair value of the respective assets. We manage and value our intangible technology assets in the aggregate, as one asset group, not by individual technology. We perform our annual goodwill and intangible assets impairment tests in the fourth quarter of each fiscal year, which coincides with our annual planning process. We also test for impairment whenever a triggering event occurs. Our impairment testing resulted in an impairment charge related to our discontinued test segment business of \$100.6 million in fiscal 2005, and an impairment charge of \$3.2 million in fiscal 2004 (recorded in Discontinued Operations) related to our PC board fabrication business. No impairment charge was recorded in fiscal 2006, as a result of our annual impairment test. If our actual results are less favorable than the estimates or assumptions used to determine the fair value of the respective assets, we may be required to record additional impairment charges in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*.

Income Taxes. We record a valuation allowance to reduce our deferred tax assets to the amount that we expect is more likely than not to be realized. While we have considered future taxable income and our ongoing tax planning strategies in assessing the need for the valuation allowance, if we were to determine that we would be able to realize our deferred tax assets in the future in excess of our net recorded amount, an adjustment to the deferred tax asset would increase income in the period such determination was made. Likewise, should we determine that we would not be able to realize all or part of our net deferred tax assets in the future, an adjustment to the deferred tax asset would decrease income in the period such determination was made. In fiscal 2002 and 2003 we established a valuation allowance against our deferred tax assets generated from our U.S. net operating losses. In fiscal 2004 and 2006 we reversed the portion of the valuation allowance that was equal to the U.S. federal income tax expense on our U.S. income for that fiscal year or related to our plans to repatriate certain unremitted foreign earnings. In fiscal 2005, we generated additional U.S. net operating loss carryforwards and established additional valuation allowances against these deferred tax assets. Also in fiscal 2005, we reduced the valuation allowance against U.S. net operating loss carryforwards for the repatriation of certain foreign earnings in fiscal 2006.

Significant judgment is required in determining our annual tax rate and in evaluating our tax positions. We establish reserves when, despite our belief that our tax return positions are fully supportable, we believe that certain positions are subject to challenge and that we may not succeed. We are currently subject to multiple tax audits and we believe that it is unlikely that the result of any of these audits would result in expense greater than our reserves. An adverse finding could result in a significant cash outlay.

Equity-based Compensation. Beginning on October 1, 2005 we account for our employee stock option grants under the provisions of SFAS No. 123R, *Share-Based Payments* (SFAS 123R). SFAS 123R requires the recognition of the fair value of equity-based compensation in net income. The fair value of our stock option awards was estimated using a Black-Scholes option valuation model. This model requires the input of highly subjective assumptions and elections in adopting and implementing SFAS 123R, including expected stock price volatility and the estimated life of each award. The fair value of equity-based awards is amortized over the vesting period of the award and we have elected to use the straight-line method for awards granted after the adoption of SFAS 123R and continue to use a graded vesting method for awards granted prior to the adoption of SFAS 123R. Prior to the adoption of SFAS 123R,

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we accounted for our stock option grants under the provisions of Accounting Principles Board (APB) Opinion No. 25 *Accounting For Stock Issued to Employees* (APB 25) and made pro forma footnote disclosures as required by SFAS No. 148, *Accounting For Stock-Based Compensation - Transition and Disclosure*, which amends SFAS No. 123, *Accounting For Stock-Based Compensation*. Pro forma net income and pro forma net income per share disclosed in the footnotes to our consolidated financial statements were estimated using a Black-Scholes option valuation model. As a result of the adoption of SFAS 123R, we will only recognize a benefit from stock-based compensation in paid-in-capital if an incremental tax benefit is realized after all other tax attributes currently available to us have been utilized.

Correction of Error

As part of our fiscal 2006 annual financial closing process, it was determined that certain balance sheet accounts had not been properly reconciled during prior annual or interim periods. Specifically, the general ledger balance was either not agreed to supporting sub-ledger activity or the supporting documentation was inaccurate. As a result, we have determined that prior to correction, accrued liabilities were overstated by \$4.3 million. We reviewed the impact of these errors on prior annual and interim periods and concluded that the cumulative impact of these errors in fiscal 2006 does not have a material impact on 2006. In accordance with APB No. 28, *Interim Financial Reporting* (APB 28), paragraph 29, in determining materiality for the purpose of reporting the cumulative effect of an error, amounts should be related to the estimated income for the full fiscal year and also the effect on the trend of earnings. Changes that are material with respect to an interim period but not material with respect to the estimated income for the full fiscal year or to the trend of earnings should be separately disclosed in the interim period. As the impact of correcting the error in fiscal 2006 was not material to the full year results, we have recorded the full amount in the fourth quarter of fiscal 2006. See Note 15 to our consolidated financial statements for discussion of the impact of this correction on the fourth quarter of fiscal 2006 results. The correction increased fiscal 2006 income from continuing operations by \$4.3 million and increased the loss from discontinued operations by \$0.5 million.

Overview of Statement of Operations

Net revenues. Our equipment sales depend on the capital expenditures of semiconductor manufacturers and subcontract assemblers worldwide, which in turn, depend on the current and anticipated market demand for semiconductors and technology driven advancements in semiconductor design.

Our packaging materials sales depend on manufacturing expenditures of semiconductor manufacturers and subcontract assemblers worldwide, many of which also purchase our equipment products. However, the volatility in unit demand for our packaging materials is less than that of our equipment sales due to the consumable nature of these products. Our gold bonding wire is generally priced based on a fabrication charge per 1,000 feet of wire, plus the value of the gold, which generally matches the price we pay for the gold from our gold supplier. Accordingly, we do not absorb fluctuations in the price of gold, but they may have a significant impact on our reported net revenue.

Cost of sales. Equipment cost of sales consists mainly of subassemblies, materials, direct and indirect labor costs, and other overhead. We rely on subcontractors to manufacture many of the components and subassemblies for our products and we rely on sole source suppliers for some material components.

Packaging materials cost of sales consists primarily of gold and aluminum, direct labor, and other materials used in the manufacture of bonding wire, capillaries, wedges, and other company products, with the cost of gold metal making up the majority of the cost. To minimize our exposure to gold price fluctuations, we obtain gold for fabrication under a contract with our gold supplier, which generally matches the price we pay for the gold with the price we invoice our customers. Accordingly, fluctuations in the price of gold are generally absorbed by our gold supplier. Since gold makes up a significant portion of the cost of sales and net revenues of our bonding wire business unit, the gross profit as a percentage of sales of that business unit and therefore of the packaging materials segment is lower than can be expected in the equipment business.

Selling, general and administrative expense. Our selling, general and administrative expense is comprised primarily of personnel and related costs, professional fees, and depreciation expense.

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Research and development expense. Our research and development expense consists primarily of labor, prototype material and other costs associated with our development efforts to strengthen our product lines and develop new products and depreciation expense. Included in research and development expense is the cost to develop the software that operates our semiconductor assembly equipment, which is expensed as incurred. We expect to continue to incur significant research and development costs.

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (the FASB) issued SFAS 123R which requires measurement of all employee stock-based compensation awards using a fair-value method and the recording of such expense in the consolidated financial statements. In addition, the adoption of SFAS 123R requires additional accounting changes related to the income tax effects and disclosure regarding the cash flow effects resulting from share-based payment arrangements. In January 2005, the SEC issued SAB No. 107, which provides supplemental implementation guidance for SFAS 123R. We selected the Black-Scholes option pricing model as the method to estimate the fair value for awards and will recognize compensation expense on a straight-line basis over the requisite service period. The Company adopted SFAS 123R in the first quarter of fiscal 2006. (See Note 8 to our consolidated financial statements).

In February 2006, the FASB issued FASB Staff Position No. FAS 123(R)-4, *Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event*. This position amends SFAS 123R to incorporate that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee's control does not meet certain conditions in SFAS 123R until it becomes probable that the event will occur. The guidance in this FASB Staff Position shall be applied upon the initial adoption of SFAS 123R. The Company adopted SFAS 123R in the first quarter of fiscal 2006. (See Note 8 to our consolidated financial statements).

The Company also adopted the following accounting pronouncements in fiscal 2006:

SFAS No. 151, *Inventory Costs – An Amendment of ARB No. 43, Chapter 4* (SFAS 151);

SFAS No. 153, *Exchanges of Non-Monetary Assets – An Amendment of APB Opinion No. 29* (SFAS 153); and

FASB Interpretation No. 47 (FIN 47), *Accounting for Conditional Asset Retirement Obligations, an Interpretation of FASB Statement No. 143*.

The adoption of SFAS 151, SFAS 153 and FIN 47 did not have a material impact on our results of operations and financial condition.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections* (SFAS 154), which replaces APB Opinion No. 20, *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements – An Amendment of APB Opinion No. 28*. SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application, or the earliest practicable date, as the required method for reporting a change in accounting principle and restatement with respect to the reporting of a correction of an error. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. We are required to adopt SFAS 154 in the first quarter of fiscal 2007. We do not expect the adoption of SFAS 154 to have a material impact on our results of operations and financial condition.

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments – an amendment of FASB Statements No. 133 and 140* (SFAS 155). SFAS 155 simplifies the accounting for certain hybrid financial instruments that contain an embedded derivative that otherwise would have required bifurcation. SFAS 155 also eliminates the interim guidance in SFAS 133, which provides that beneficial interests in securitized financial assets are not subject to the provisions of SFAS 133. SFAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. SFAS 155 is required to be adopted by the Company in the first quarter of fiscal 2007. We do not expect the adoption of SFAS

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155 to have a material impact on our results of operations and financial condition.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets – an amendment of FASB Statement No. 140* (SFAS 156). SFAS 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. The statement permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. SFAS 156 is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. We are required to adopt SFAS 156 in the first quarter of fiscal 2007. We do not expect the adoption of SFAS 156 to have a material impact on our results of operations and financial condition.

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48), an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS 109. FIN 48 prescribes a two-step process to determine the amount of tax benefit to be recognized. First, the tax position must be evaluated to determine the likelihood that it will be sustained upon examination. If the tax position is deemed more-likely-than-not to be sustained, the tax position is then measured to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. FIN 48 is required to be adopted by the Company in fiscal 2008. We are currently evaluating the potential impact of FIN 48 on our financial position and results of operations

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. This Statement clarifies the definition of fair value, establishes a framework for measuring fair value and expands disclosures on fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of the adoption of SFAS No. 157 on our consolidated results of operations or financial position.

In September 2006, the SEC issued SAB No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Current Year Misstatements* (SAB 108). SAB 108 requires analysis of misstatements using both an income statement (rollover) approach and a balance sheet (iron curtain) approach in assessing materiality and provides for a one-time cumulative effect transition adjustment. SAB 108 is effective for annual financial statements issued for fiscal years ending after November 15, 2006. We do not expect the adoption of SAB 108 to have a material impact on our consolidated results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – An Amendment of FASB Statements No. 87, 88, 106, and 132R* (SFAS 158). SFAS 158 requires an employer to: (i) recognize in its statement of financial position an asset for a plan's overfunded status or a liability for a plan's underfunded status; (ii) measure a plan's assets and its obligations that determine its funded status as of the end of the employer's fiscal year; and (iii) recognize changes in the funded status of a defined benefit postretirement plan in the year in which the changes occur. Those changes will be reported in comprehensive income similar to the additional minimum pension liability adjustment required under SFAS No. 87, *Employers Accounting for Pensions*. The requirements listed under (i) and (iii) above are effective for fiscal years ending after December 15, 2006, and the requirement listed under (ii) above is effective as of December 31, 2008. We are currently evaluating the impact of the adoption of SFAS 158 on our financial position and results of operations.

Table of Contents**Results of Operations*****Fiscal Years Ended September 30, 2004, 2005, and 2006***

The table below shows the principal line items from continuing operations of our consolidated statements of operations, as a percentage of our net sales:

	Fiscal Year Ended		
	September 30,		
	2004	2005	2006
Net revenue	100.0%	100.0%	100.0%
Cost of sales	65.6	71.4	71.8
Gross margin	34.4	28.6	28.2
Selling, general and administrative	12.6	14.6	11.7
Research and development	4.8	6.0	5.4
Gain on sale of assets	(0.1)	(0.4)	(0.7)
Income from operations	17.1%	8.4%	11.8%

Fiscal Years Ended September 30, 2005 and September 30, 2006

Bookings and Backlog. During the fiscal year ended September 30, 2006, we recorded bookings of \$660.9 million compared to \$516.2 million in fiscal 2005. A booking is recorded when a customer order is reviewed and a determination is made that all specifications can be met, production (or service) can be scheduled, a delivery date can be set, and the customer meets the Company's credit requirements. At September 30, 2006, the backlog of customer orders totaled \$56.0 million, compared to \$91.5 million at September 30, 2005. Since the timing of deliveries may vary and orders are generally subject to cancellation, our backlog as of any date may not be indicative of net sales for any succeeding period.

Net Revenues

Business segment net revenues:

	<i>(dollar amounts in thousands)</i>		
	Fiscal year ended September 30,		
	2005	2006	% Change
Equipment	\$ 201,608	\$ 319,788	58.6%
Packaging materials	273,934	376,523	37.5%
	\$ 475,542	\$ 696,311	46.4%

Net Revenue. Overall, net revenue for fiscal 2006 increased \$220.8 million or 46.4% to \$696.3 million from \$475.5 million in fiscal 2005. Included in the revenue for the package material segment is gold metal value that is generally passed through to the customer. The total amount of gold metal value included in our packaging materials revenue in fiscal 2006 is \$278.8 million compared to \$183.8 million in fiscal 2005. These same amounts are included in the cost of sales. Following is a review of net revenue for each of our two business segments.

For fiscal 2006, net revenue for the equipment segment increased \$118.2 million or 58.6% to \$319.8 million from \$201.6 million in fiscal 2005. The increase in revenue was due to a 75.1% increase in unit sales of our automatic ball bonders, caused by increased industry-wide demand for backend semiconductor equipment. Average selling

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prices (ASP) decreased 1.5% compared to fiscal year 2005. Fiscal year 2005 included significant volume of a customized product to a customer with a much higher ASP than a traditional ball bonder.

For fiscal 2006, net revenue for the packaging materials segment increased \$102.6 million, or 37.5% to \$376.5 million from \$273.9 million in fiscal 2005. This increase in revenue primarily resulted from a \$100.5 million increase in wire revenue. Of the \$100.5 million increase in wire revenue, \$34.9 million was due to increased volumes of wire sold (measured in Kft) and \$65.6 million was due to an increase in gold wire average selling prices primarily caused by an increase in the price of gold. Gold wire selling prices are heavily dependent upon the price of gold and can fluctuate significantly from period to period.

The majority of our sales are to customers that are located outside of the United States or that have manufacturing facilities outside of the United States. Shipments of our products with ultimate foreign destinations comprised 95% of our total sales in fiscal 2005 and 93% in 2006. The majority of these foreign sales were to customer locations in the Asia/Pacific region, including Taiwan, Malaysia, Korea, Singapore, and Japan. Taiwan accounted for the largest single destination for our product shipments with 25% of our shipments in fiscal 2006 compared to 27% of our shipments in the prior fiscal year.

Gross Profit

Business segment gross profit:

	<i>(dollar amounts in thousands)</i>			
	Fiscal year ended September 30,		Fiscal year ended September 30,	
	2005	% Sales	2006	% Sales
Equipment	\$ 86,050	42.7%	\$ 141,315	44.2%
Packaging materials	50,031	18.3%	55,246	14.7%
	\$ 136,081	28.6%	\$ 196,561	28.2%

Gross profit. Overall, gross profit for fiscal 2006 increased \$60.5 million to \$196.6 million from \$136.1 million in fiscal 2005. This higher gross profit is primarily due to increased industry-wide demand, particularly for automatic ball bonders sold within our equipment segment.

For fiscal 2006, our equipment segment gross profit increased \$55.3 million, compared to fiscal year 2005, as industry-wide demand for automatic ball bonders increased sharply. Gross margin increased to 44.2% in fiscal year 2006 from 42.7% in fiscal year 2005. The increase in gross margin was mainly due to a 0.3% reduction in material cost. Approximately \$3.5 million of our equipment segment's fiscal 2006 gross profit included a cumulative adjustment to correct an immaterial error (See Note 1 and Note 15 to our consolidated financial statements).

For fiscal 2006, our packaging materials segment gross profit increased \$5.2 million to \$55.2 million from \$50.0 million in fiscal 2005. This increase was primarily due to increased sales of gold wire and expendable tools. Our packaging materials gross margin declined to 14.7% from 18.3% for the year ago period. This decline in gross margin was primarily due to a 31.5% increase in the cost of gold during fiscal 2006, compared to the same period a year ago. The 46.6% increase in wire sales also contributed to the decline in gross margins during the twelve months ended September 30, 2006, compared to the same period a year ago.

Table of Contents**Operating Expenses**

	<i>(dollar amounts in thousands)</i>			
	Fiscal year ended September 30,			
	2005	% Sales	2006	% Sales
Selling, general and administrative	\$ 69,525	14.6%	\$ 81,462	11.7%
Research and development	28,495	6.0%	37,657	5.4%
Gain on sale of assets	(1,690)	-0.4%	(4,544)	-0.7%
	\$ 96,330	20.3%	\$ 114,575	16.5%

Selling, General and Administrative Expenses

Selling, General and Administrative (SG&A) expenses of \$81.5 million for the fiscal year ended September 30, 2006 increased \$11.9 million compared to the SG&A expenses of \$69.5 million in fiscal 2005. This increase was primarily due to an increase in incentive compensation of \$9.0 million, and the recording of \$3.0 million of stock-based compensation expense associated with the adoption of SFAS 123R in fiscal 2006. Incentive compensation expense is recorded when net income and certain other performance targets are achieved.

Research and Development

Research and Development expenses for fiscal 2006 increased by \$9.2 million to \$37.7 million from \$28.5 million in fiscal 2005. The increase was primarily due to costs associated with the development of the next generation ball bonder and stock based compensation associated with the adoption of SFAS 123R.

Gain on sale of assets

For the fiscal year ended September 30, 2006, the \$4.5 million net gain on sale of assets represents the gain recognized on the sale of the land and building of our former corporate headquarters location in Willow Grove, Pennsylvania. For the fiscal year ended September 30, 2005, the \$1.7 million net gain on sale of assets primarily consists of the gain on the sale of our wedge bonding technology of \$1.6 million.

Income from Operations

Income from operations by business segment appears below:

	<i>(dollar amounts in thousands)</i>			
	Fiscal year ended September 30,			
	2005	% Sales	2006	% Sales
Equipment	\$ 20,444	10.1%	\$ 55,870	17.5%
Packaging materials	19,307	7.0%	21,572	5.7%
Gain on sale of assets			4,544	0.7%
	\$ 39,751	8.4%	\$ 81,986	11.8%

For fiscal 2006, we had income from operations of \$82.0 million, compared to income from operations of \$39.8 million in fiscal 2005. This change was primarily due to a \$220.8 million increase in sales caused by increased industry-wide demand for automatic ball bonders.

For fiscal 2006, income from operations for our equipment business segment increased \$35.4 million due to increased industry-wide demand for our automatic ball bonders. Income from operations for our packaging materials business segment increased \$2.3 million primarily due to higher volumes of wire sold and an increase in gold wire average selling price caused by an increase in the price of gold.

Table of Contents***Interest Income and Expense***

Interest income during fiscal 2006 was \$1.7 million higher than in fiscal 2005 due to higher rates of return on invested cash balances and higher invested cash balances. Interest expense in fiscal 2006 was \$0.7 million lower than fiscal 2005. Interest expense in both the current and prior fiscal year primarily reflects interest on our Convertible Subordinated Notes. The reduction in interest expense in fiscal 2006 was primarily due to the repurchase of a portion of our outstanding 0.5% Convertible Subordinated Notes having an aggregate principal outstanding amount of \$75.0 million.

Gain (loss) on Early Extinguishment of Debt

In fiscal 2006, we exchanged a total of 3.6 million shares of our common stock and \$26.4 million of cash for \$75.0 million (face value) of our Convertible Subordinated Notes outstanding. In accordance with APB No. 26, *Early Extinguishment of Debt*, we recorded a gain on early extinguishment of debt of \$4.0 million, net of deferred amortization costs written off of \$1.3 million and transaction costs of \$0.4 million, as the exchanges included a number of shares that was less than the number of shares issuable under the original conversion terms.

Provision for Income Taxes

Our provision for income taxes from continuing operations for fiscal 2006 reflects income tax expense of \$9.8 million, which primarily consists of \$1.3 million for federal alternative minimum taxes, \$2.0 million for state income taxes, \$2.0 million for income taxes on income earned in foreign jurisdictions, \$3.6 million of income tax expense for additional foreign income tax exposures, \$0.6 million for potential repatriation of foreign earnings, and \$0.3 for foreign withholding taxes. Our tax expense in fiscal 2005 reflects income tax expense on income in foreign jurisdictions, foreign income tax exposures and potential repatriation of foreign earnings.

Our future effective tax rate would be affected if earnings are lower than anticipated in countries where we have lower statutory rates and higher than anticipated in countries where we have higher statutory rates by changes in the valuation of our deferred tax assets and liabilities, or by changes in tax laws, regulations, accounting principles, or interpretations thereof. We regularly assess the effects resulting from these factors to determine the adequacy of our provision for income taxes.

Loss from Discontinued Operations, net of tax

In fiscal 2005 and 2006, our discontinued operations consist of our former test interconnect business unit (see the description of the sale of this business in the introduction to this Management's Discussion Analysis of Financial Condition and Results of Operations).

The test segment was sold in fiscal 2006, but had net revenue of \$42.7 million through the date of sale. This former segment reported net revenue of \$85.7 million in fiscal 2005. The loss from the test segment's operations for fiscal 2006 was \$24.9 million, including a loss on disposal of \$0.8 million, net of a benefit from income taxes of \$1.4 million. Included in the loss from discontinued operations are operating losses of \$10.6 million, and accrued severance and facilities costs of approximately \$6.4 million and \$6.1 million, respectively. The facilities costs of \$6.1 million are net of estimated sublease income from the affected facilities. These estimates of sublease income are subject to change, and such changes could result in an increase or decrease to the estimated facilities charges previously recorded. These payments are expected to be paid out through September 2012. The loss from the test segment's operations for fiscal 2005 was \$137.4 million. The major classes of test assets and liabilities sold included: \$12.3 million in accounts receivable; \$9.8 million in inventory; \$12.7 million in property, plant and equipment; and \$5.2 million in accounts payable.

Accruals recorded in fiscal 2006 for obligations associated with the discontinuation of the test business are presented below:

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	<i>(in thousands)</i>		
	Severance and		
	related benefits	Facilities	Total
Provisions recorded in fiscal 2006	\$ 6,355	\$ 6,138	\$ 12,493
Payment of obligations	(4,817)	(684)	(5,501)
Balance, September 30, 2006	\$ 1,538	\$ 5,454	\$ 6,992

Fiscal Years Ended September 30, 2004 and September 30, 2005

Bookings and Backlog. During the fiscal year ended September 30, 2005, we recorded bookings of \$516.2 million compared to \$594.7 million in fiscal 2004. A booking is recorded when a customer order is reviewed and a determination is made that all specifications can be met, production (or service) can be scheduled, a delivery date can be set, and the customer meets the Company's credit requirements. At September 30, 2005, the backlog of customer orders totaled \$91.5 million, compared to \$50.8 million at September 30, 2004. Since the timing of deliveries may vary and orders are generally subject to cancellation, our backlog as of any date may not be indicative of net sales for any succeeding period.

Net Revenues

Business segment net revenues: