

KEY TECHNOLOGY INC  
Form 10-K/A  
January 23, 2004

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549-1004

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**FORM 10-K/A**

Amendment No. 1

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

**for the fiscal year ended September 30, 2003**

**or**

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

**For the transition period from                      to                      .**

**Commission File No. 0-21820**

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**KEY TECHNOLOGY, INC.**

(Exact name of Registrant as specified in its charter)

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**OREGON**  
(State of Incorporation)

**93-0822509**  
(I.R.S. Employer Identification No.)

**150 Avery Street, Walla Walla, Washington**  
(Address of principal executive offices)

**99362**  
(Zip Code)

**(509) 529-2161**  
(Registrant's telephone number, including area code)

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

**None**

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

**Common Stock, no par value**

**Series B Convertible Preferred Stock, par value \$.01 per share**

**Warrants to purchase Common Stock, dated July 12, 2000**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Sections 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 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 an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes ☐ No ☒

The aggregate market value of the Registrant's common stock held by non-affiliates on March 31, 2003 and December 3, 2003 (based on the last sale price of such shares) was approximately \$21,570,125 and \$58,576,022, respectively.

There were 4,846,486 shares of the Registrant's common stock outstanding on December 3, 2003.

**DOCUMENTS INCORPORATED BY REFERENCE**

Parts of Registrant's Proxy Statement dated on or about January 8, 2004 prepared in connection with the Annual Meeting of Shareholders to be held on February 4, 2004 are incorporated by reference into Part III of this Report.

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**EXPLANATORY NOTE**

Key Technology, Inc. is filing this Amendment to its Annual Report on Form 10-K/A (the "Form 10-K/A") to amend certain items in its Annual Report on Form 10-K for the fiscal year ended September 30, 2003, which was originally filed with the Securities and Exchange Commission on December 19, 2003 (the "Annual Report").

Item 8 is amended to add the conformed signature of the Company's independent auditor, Deloitte & Touche LLP, to the Independent Auditor's Report. As a result, the rules of the Securities and Exchange Commission require that certain exhibits previously provided in Item 15 also be amended. Item 15 is therefore amended to provide the consent of Deloitte & Touche LLP as Exhibit 23.2 and to provide the certifications required by the Sarbanes-Oxley Act of 2002 as Exhibits 31.3, 31.4, 32.3 and 32.4.

This amendment is limited in scope to the portions of the Annual Report set forth above and does not amend, update, or change any other items or disclosures contained in the Annual Report. Accordingly, all other items that remain unaffected are omitted in this filing. None of the amendments to the Annual Report reflected in this Form 10-K/A resulted in a change to or restatement of the financial statements or other financial information included in the Annual Report.

This Form 10-K/A continues to speak as of the date of the original filing of the Annual Report and we have not updated the disclosures contained therein to reflect any events that occurred at any subsequent date. The filing of this Form 10-K/A shall not be deemed an admission that the original filing, when made, included any untrue statement of a material fact or omitted to state a material fact necessary to make a statement therein not misleading.

KEY TECHNOLOGY, INC.

2003 FORM 10-K/A

TABLE OF CONTENTS

Part II

Item 8. Financial Statements and Supplemental Data

Part IV

Item 15. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

Signatures

Exhibit Index

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.**

Title

Independent Auditors' Report

Consolidated Balance Sheets at September 30, 2003 and 2002

Consolidated Statements of Operations for the three years ended September 30, 2003

Consolidated Statements of Shareholders' Equity for the three years ended September 30, 2003

Consolidated Statements of Cash Flows for the three years ended September 30, 2003

Notes to Consolidated Financial Statements

Supplementary Data

**INDEPENDENT AUDITORS' REPORT**

Board of Directors and Shareholders  
Key Technology, Inc.  
Walla Walla, Washington

We have audited the accompanying consolidated balance sheets of Key Technology, Inc. and subsidiaries as of September 30, 2003 and 2002, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended September 30, 2003. The consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Key Technology, Inc. and subsidiaries as of September 30, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 2003 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 145, *Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections*, which resulted in amounts recorded in fiscal year 2002 as an extraordinary item from the early extinguishment of debt to be reclassified as part of net income from continuing operations. As discussed in Notes 1 and 4 to the consolidated financial statements, effective October 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*.

DELOITTE & TOUCHE LLP

Portland, Oregon

December 16, 2003





**KEY TECHNOLOGY, INC. AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

**SEPTEMBER 30, 2003 AND 2002**

(In thousands)

ASSETS	2003	2002
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 6,442	\$ 1,707
Trade accounts receivable, net	9,479	7,556
Inventories	13,968	13,969
Deferred income taxes	1,935	1,730
Prepaid expenses and other assets	1,062	1,477
Total current assets	32,886	26,439
PROPERTY, PLANT, AND EQUIPMENT, Net	5,503	6,407
DEFERRED INCOME TAXES	768	3,472
OTHER ASSETS	819	940
GOODWILL AND OTHER INTANGIBLES, Net	11,239	12,562
TOTAL	\$ 51,215	\$ 49,820

See notes to consolidated financial statements.

**KEY TECHNOLOGY, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****SEPTEMBER 30, 2003 AND 2002**

(In thousands, except shares)

<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>2003</b>	<b>2002</b>
<b>CURRENT LIABILITIES:</b>		
Short-term borrowings	\$	\$ 6,596
Accounts payable	1,587	1,437
Accrued payroll liabilities and commissions	4,547	2,769
Accrued customer support and warranty costs	1,058	999
Income tax payable	185	
Other accrued liabilities	2,419	1,969
Customers' deposits	4,798	3,328
Current portion of long-term debt	1,066	1,668
<b>Total current liabilities</b>	<b>15,660</b>	<b>18,766</b>
<b>LONG-TERM DEBT</b>	<b>3,249</b>	<b>3,747</b>
<b>DEFERRED INCOME TAXES</b>	<b>205</b>	<b>238</b>
<b>MANDATORILY REDEEMABLE PREFERRED STOCK</b>	<b>1,526</b>	<b>2,815</b>
<b>WARRANTS</b>	<b>356</b>	<b>652</b>
<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>SHAREHOLDERS' EQUITY:</b>		
Preferred stock - no par value; 5,000,000 shares authorized; none issued and outstanding		
Common stock - no par value; 15,000,000 shares authorized; 4,785,961 and 4,767,206 issued and outstanding 2003 and 2002, respectively	9,568	9,456
Retained earnings	20,729	14,970
Other accumulated comprehensive income (loss)	(78)	(824)
<b>Total shareholders' equity</b>	<b>30,219</b>	<b>23,602</b>
<b>TOTAL</b>	<b>\$ 51,215</b>	<b>\$ 49,820</b>

See notes to consolidated financial statements.

**KEY TECHNOLOGY, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****THREE YEARS ENDED SEPTEMBER 30, 2003**

(In thousands, except per share data)

	2003	2002	2001
NET SALES	\$ 82,622	\$ 70,234	\$ 72,954
COST OF SALES	48,626	42,352	47,186
Gross profit	33,996	27,882	25,768
OPERATING EXPENSES:			
Selling	11,695	10,733	13,248
Research and development	4,874	4,467	5,371
General and administrative	7,329	6,963	7,487
Amortization of intangibles	1,323	1,323	2,084
Total operating expenses	25,221	23,486	28,190
GAIN ON SALE OF ASSETS	4	883	76
INCOME (LOSS) FROM OPERATIONS	8,779	5,279	(2,346)
OTHER INCOME (EXPENSE):			
Royalty income	18	9	131
Interest income	59	109	126
Interest expense	(399)	(843)	(1,673)
Other, net	(5)	(1,008)	76
Total other income (expense) net	(327)	(1,733)	(1,340)
Earnings (loss) from continuing operations before income taxes	8,452	3,546	(3,686)
Income tax (benefit) expense	2,693	1,238	(1,343)
Net earnings (loss) from continuing operations	5,759	2,308	(2,343)
Earnings (loss) from discontinued operation net of tax		39	(436)
Loss on sale of discontinued operation, net of tax			(2,145)

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Total earnings (loss) from discontinued operation			39		(2,581)
Net earnings (loss) before change in accounting principle	\$	5,759	\$	2,347	\$ (4,924)
Change in accounting principle, net of tax			(4,302)		
NET EARNINGS (LOSS)		5,759		(1,955)	(4,924)
Accretion of mandatorily redeemable preferred stock			(582)		(939)
Net earnings (loss) available to common shareholders	\$	5,759	\$	(2,537)	\$ (5,863)
Net earnings (loss) from continuing operations per share basic	\$	1.21	\$	0.36	\$ (0.69)
Net earnings (loss) from continuing operations per share diluted	\$	1.15	\$	0.36	\$ (0.69)
Net earnings (loss) from discontinued operation per share basic and diluted	\$		\$	0.01	\$ (0.55)
Net earnings (loss) before change in accounting principle per common share basic	\$	1.21	\$	0.37	\$ (1.24)
Net earnings (loss) before change in accounting principle per common share diluted	\$	1.15	\$	0.37	\$ (1.24)
Net loss from change in accounting principle per common share basic and diluted	\$		\$	(0.90)	\$
EARNINGS (LOSS) PER SHARE Basic	\$	1.21	\$	(0.53)	\$ (1.24)
EARNINGS (LOSS) PER SHARE Diluted	\$	1.15	\$	(0.53)	\$ (1.24)
SHARES USED IN PER SHARE CALCULATION Basic		4,774		4,759	4,740
SHARES USED IN PER SHARE CALCULATION Diluted		4,989		4,759	4,740

See notes to consolidated financial statements.

## KEY TECHNOLOGY, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

## THREE YEARS ENDED SEPTEMBER 30, 2003

(Dollars in thousands)

	Common Stock		Retained Earnings	Other Accumulated Comprehensive Income (Loss)	Total
	Shares	Amount			
Balance at October 1, 2000	4,733,560	\$ 9,329	\$ 23,370	\$ (1,234)	\$ 31,465
Components of comprehensive income (loss):					
Net loss			(4,924)		(4,924)
Comprehensive income foreign currency translation adjustment, net of tax				31	31
Total comprehensive loss					(4,893)
Accretion of mandatorily redeemable preferred stock			(939)		(939)
Issuance of common stock upon exercise of preferred stock and warrants	602	7			7
Issuance of stock for Employee Stock Purchase Plan	17,184	71			71
Balance at September 30, 2001	4,751,346	9,407	17,507	(1,203)	25,711
Components of comprehensive income (loss):					
Net loss			(1,955)		(1,955)
Comprehensive income foreign currency translation adjustment, net of tax				379	379
Total comprehensive loss					(1,576)
Accretion of mandatorily redeemable preferred stock			(582)		(582)
Issuance of stock for Employee Stock Purchase Plan	15,860	49			49
Balance at September 30, 2002	4,767,206	9,456	14,970	(824)	23,602

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Components of comprehensive income (loss):							
Net earnings				5,759			5,759
Comprehensive income foreign currency translation adjustment, net of tax					746		746
Total comprehensive income							6,505
Issuance of common stock upon exercise of stock options	11,837		67				67
Issuance of stock for Employee Stock Purchase Plan	6,918		45				45
Balance at September 30, 2003	4,785,961	\$	9,568	\$	20,729	\$	(78) \$ 30,219

See notes to consolidated financial statements.

## KEY TECHNOLOGY, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

## THREE YEARS ENDED SEPTEMBER 30, 2003

(In thousands)

	2003	2002	2001
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net earnings (loss)	\$ 5,759	\$ (1,955)	\$ (4,924)
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Loss from sale of discontinued operation, net of tax			2,145
(Earnings) loss from discontinued operation, net of tax		(39)	436
(Gain) loss on sale of assets	(4)	(883)	(76)
Losses on early extinguishment of debt, net of tax		471	
Foreign currency exchange (gain) loss	(242)	(80)	(242)
Depreciation and amortization	3,698	3,791	4,530
Change in accounting principle provision for goodwill, net of tax		4,302	
Deferred income taxes	2,080	1,503	(1,343)
Deferred rent	66	279	26
Bad debt expense	162	39	63
Changes in assets and liabilities:			
Trade accounts receivable	(1,646)	5,956	(4,204)
Inventories	799	816	5,052
Prepaid expenses and other current assets	365	(651)	830
Income taxes receivable	76	831	
Accounts payable	27	(4,063)	2,212
Accrued payroll liabilities and commissions	1,702	210	(1,259)
Accrued customer support and warranty costs	35	(17)	(104)
Income taxes payable	237	(346)	171
Other accrued liabilities	317	612	(735)
Customers deposits	1,275	1,081	(183)
Other	(183)	(696)	323
Cash provided by operating activities	14,523	11,161	2,718
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Proceeds from sale of subsidiary		3,577	
Proceeds from sale of property	12	4,355	478
Purchases of property, plant, and equipment	(836)	(532)	(545)
Cash provided by (used in) investing activities	(824)	7,400	(67)



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CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds from (repayments of) short-term borrowings	\$	(6,650)	\$	4,596	\$	2,000
Payments on long-term debt		(1,740)		(23,535)		(5,591)
Proceeds from issuance of long-term debt		500		10,500		
Prepayment penalty on early extinguishment of debt				(516)		
Redemption of warrants		(296)		(170)		(2,122)
Redemption of mandatorily redeemable preferred stock		(1,289)		(8,559)		(2,382)
Proceeds from issuance of common stock		112		49		71

Cash used in financing activities		(9,363)		(17,635)		(8,024)
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EFFECT OF EXCHANGE RATE CHANGES ON CASH		399		220		(42)
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NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS FROM CONTINUING OPERATIONS		4,735		1,146		(5,415)
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NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS FROM DISCONTINUED OPERATION				(177)		(274)
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CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR		1,707		738		6,427
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CASH AND CASH EQUIVALENTS, END OF YEAR	\$	6,442	\$	1,707	\$	738
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SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid during the year for interest	\$	443	\$	783	\$	1,818
Cash paid (received) during the year for income taxes		306		(472)		(731)

SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:

Equipment obtained through capital leases	\$		\$	110	\$	126
Accounts payable paid through lease financing						856

See notes to consolidated financial statements.

**KEY TECHNOLOGY, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**THREE YEARS ENDED SEPTEMBER 30, 2003**

**1. THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Key Technology, Inc. and its wholly-owned subsidiaries (the Company) design, manufacture, and sell process automation systems, integrating electro-optical inspection and sorting, specialized conveying and product preparation equipment. The consolidated financial statements include the accounts of Key Technology, Inc. and its wholly-owned subsidiaries, Key Technology Holdings U.S.A., LLC, Key Technology AMVC LLC, Key Technology Australia Pty. Ltd., and Key Technology FSC, Inc., a foreign sales corporation (FSC). Suplusco Holding B.V., a wholly-owned European subsidiary of Key Technology Holdings U.S.A., LLC includes the accounts of Key Technology B.V. Key Technology AMVC LLC includes the accounts of Applied Laser Systems, Inc. (inactive). All significant intercompany accounts and transactions have been eliminated.

**Revenue Recognition** Sales revenue net of allowances is recognized at the time equipment is shipped to customers or when title and risk of loss passes, or in the case of trial units, upon the customers' acceptance of the product. Revenue from maintenance and support contracts is recognized over the period the service is provided. Revenue from other service contracts is recognized at the time the service is provided. Upon receipt of an order, the Company generally receives a deposit which is recorded as customers' deposits. The Company makes periodic evaluations of the creditworthiness of its customers and generally does not require collateral. An allowance for credit losses is provided based upon historical experience and anticipated losses.

**Cash and Cash Equivalents** The Company considers all highly liquid investments with original maturities of 90 days or less at date of acquisition to be cash equivalents.

**Inventories** are stated at the lower of cost (first-in, first-out method) or market.

**Property, Plant, and Equipment** are recorded at cost and depreciated over estimated useful lives on the straight-line method. The range in lives for assets is as follows:

**Years**

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Buildings and improvements	7 to 40
Manufacturing equipment	5 to 10
Office equipment, furniture, and fixtures	3 to 7

***Goodwill and Other Intangibles*** Prior to October 1, 2001, goodwill was amortized over the estimated useful lives of the related goodwill or 15 years, whichever was shorter. Beginning October 1, 2001, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, and as a result, ceased amortization of goodwill. Assessment of potential goodwill impairment is performed by the Company on an annual basis or sooner, if necessary.

Other intangibles which consist of patents, developed technologies, trademarks and trade names, and purchased customer development are amortized over the estimated useful lives of the related assets, which is 10 years for the majority of the assets. Management periodically evaluates the

recoverability of other intangibles based upon current and anticipated net income and undiscounted future cash flows. Amortization of other intangibles (including goodwill in fiscal 2001) was \$1,323,000, \$1,323,000, and \$2,084,000 for the years ended September 30, 2003, 2002, and 2001, respectively (see Note 4).

**Accrued Customer Support and Warranty Costs** The Company provides customer support services consisting of installation and training to its customers. The Company also provides a warranty on its products ranging from ninety days to two years following the date of shipment. Management establishes allowances for customer support and warranty costs based upon the types of products shipped, customer support and product warranty experience and estimates such costs for related new products where experience is not available. The provision of customer support and warranty costs is charged to cost of sales at the time such costs are known or estimable.

A reconciliation for the changes in the Company's allowances for warranties is as follows (in thousands):

	2003	2002
Beginning balance	\$ 869	\$ 748
Warranty costs incurred	(1,736)	(2,426)
Warranty expense accrued	1,680	2,545
Translation adjustments	24	2
Ending balance	\$ 837	\$ 869

**Income Taxes** Deferred income taxes are provided for the effects of temporary differences arising from differences in the reporting of revenues and expenses for financial statement and income tax purposes under the asset and liability method using currently enacted tax rates.

**Foreign Currency Translation** Assets and liabilities denominated in a foreign currency are translated to U.S. dollars at the exchange rate on the balance sheet date. Translation adjustments are shown as part of other accumulated comprehensive income (loss). Revenues, costs, and expenses are translated using an average rate. Realized and unrealized foreign currency transaction gains and losses are included in the consolidated statement of operations.

**Impairment of Long-Lived Assets** The Company evaluates its long-lived assets for financial impairments based upon undiscounted cash flows and will continue to evaluate them if events or changes in circumstances indicate the carrying amount of such assets may not be fully recoverable.

**Estimates** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make 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 reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Financial Instruments** The carrying value of the Company's cash and cash equivalents, short-term investments, accounts and notes receivable, trade payables, and other accrued liabilities approximates their estimated fair values due to the short maturities of those instruments.

**Earnings Per Share** Basic earnings (loss) per share (EPS) has been computed by dividing net earnings (loss) available to common shareholders by the weighted average number of shares

outstanding during each period. Diluted EPS has been computed by dividing net earnings (loss) available to common shareholders by the weighted average common stock and common stock equivalent shares outstanding during each period using the treasury stock method for employee stock option plans and warrants, and the if-converted method for mandatorily redeemable preferred stock, if the common equivalent shares were not anti-dilutive. In fiscal years 2002 and 2001, all common stock equivalents were anti-dilutive. Net earnings (loss) for the calculation of both basic and diluted EPS is the same for each period presented. The calculation of the weighted average outstanding shares is as follows (in thousands):

	2003	2002	2001
Weighted average shares outstanding basic	4,774	4,759	4,740
Common stock options and warrants	215		
Weighted average shares outstanding diluted	4,989	4,759	4,740

Options to purchase 714,125, 818,933, and 699,433 shares of common stock were outstanding as of September 30, 2003, 2002, and 2001, respectively, but were not included in the computation of diluted EPS for the year then ended because the options were anti-dilutive. These options expire on dates beginning in January 2004 through February 2013. As of September 30, 2003, common equivalent shares of 35,553 from assumed conversion of warrants were not included in the computation of diluted EPS due to anti-dilution. As of September 30, 2002, common equivalent shares of 187,663 and 65,162 from assumed conversion of mandatorily redeemable preferred stock and warrants, respectively, were not included in the computation of diluted EPS due to anti-dilution. As of September 30, 2001, common equivalent shares of 892,756 and 82,200 from assumed conversion of mandatorily redeemable preferred stock and warrants, respectively, were not included in the computation of diluted EPS due to anti-dilution.

**Accounting for Stock-Based Compensation** During 1995, the Financial Accounting Standards Board (FASB) issued SFAS No. 123, *Accounting for Stock-Based Compensation*, which defines a fair value based method of accounting for employee stock options and similar equity instruments and encourages all entities to adopt that method of accounting for all of their employee stock compensation plans. However, it also allows an entity to continue to measure compensation cost for those plans using the method of accounting prescribed by Accounting Principles Board Opinion No. 25 ( APB 25 ). Entities electing to remain with the accounting in APB 25 must make pro forma disclosures of net income and, if presented, earnings per share, as if the fair value based method of accounting defined in SFAS No. 123 has been adopted.

The Company has elected to account for its stock-based compensation plans under APB 25. The Company has computed, for pro forma disclosure purposes, the value of all stock and stock options granted under the Employee Stock Purchase Plan and the Restated Employees Stock Option Plan during 2003, 2002, and 2001 using the Black-Scholes option pricing model as prescribed by SFAS No. 123 using the following weighted average assumptions for the years ended September 30, 2003, 2002, and 2001:

	2003	2002	2001
Risk-free interest rate	2.36%	1.6%	3.7%
Expected dividend yield	0%	0%	0%
Expected lives	4.55 years	6.0 years	5.5 years

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Expected volatility	74%	75%	71%
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Using the Black-Scholes methodology, the total value of stock options granted during 2003, 2002, and 2001 was \$991,000, \$311,000, and \$192,000, respectively, which would be amortized on a pro

forma basis over the vesting period of the options (typically five years). The weighted average fair value of options granted under the Restated Employees' Stock Option Plan during 2003, 2002, and 2001 was \$5.43 per share, \$1.94 per share, and \$5.03 per share, respectively.

The total compensatory value of stock purchased under the Employee Stock Purchase Plan during 2003, 2002, and 2001 was \$8,000, \$9,000, and \$12,000, respectively. The weighted average fair value of the stock purchased during 2003, 2002, and 2001 was \$1.14 per share, \$0.54 per share, and \$0.73 per share, respectively.

If the Company had accounted for the Restated Employees' Stock Option Plan and Employee Stock Purchase Plan in accordance with SFAS No. 123, the Company's net earnings and earnings per share would approximate the pro forma disclosures below (in thousands, except per share amounts):

	Year Ended September 30, 2003		Year Ended September 30, 2002		Year Ended September 30, 2001	
	As Reported	Pro Forma	As Reported	Pro Forma	As Reported	Pro Forma
Net earnings (loss)	\$ 5,759	\$ 5,261	\$ (1,955)	\$ (2,408)	\$ (4,924)	\$ (5,542)
Earnings (loss) per share						
basic	\$ 1.21	\$ 1.11	\$ (0.53)	\$ (0.63)	\$ (1.24)	\$ (1.37)
diluted	\$ 1.15	\$ 1.06	\$ (0.53)	\$ (0.63)	\$ (1.24)	\$ (1.37)

The effects of applying SFAS No. 123 in this pro forma disclosure are not indicative of future amounts. SFAS No. 123 does not apply to awards prior to October 1, 1995, and additional awards may occur in future years.

**Future Accounting Changes** In August 2001, the FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations*, which is effective October 1, 2003. SFAS No. 143 requires, among other things, the accounting and reporting of legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development, or normal operation of a long-lived asset. The Company does not believe this will have a material effect on its financial statements.

In November 2002, the Emerging Issues Task Force (EITF) ratified a consensus on Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*, which is effective for the Company beginning October 1, 2003. Issue No. 00-21 addresses accounting and reporting of a company's delivery or performance of multiple products, services, and/or rights customers might have to use a company's held assets to fulfill its needs, with delivery or performance that may occur at different points in time or over different periods of time. Management believes this will not have a material effect on the Company's consolidated financial statements.

In December 2002, the FASB issued SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure*, which is effective for fiscal years ending after December 31, 2002. SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair



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value method of accounting for stock-based employee compensation. In addition, this statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company has adopted the disclosure requirements. The Company has elected not to implement any transitional method of accounting for stock-based compensation. The Company will defer action until the FASB has issued its final definitive pronouncement on this issue, which is expected sometime in 2004.

In November 2002, the FASB issued Financial Interpretation No. ( FIN ) 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, on the accounting and disclosure guidance for guarantors. The standard

requires guarantors to recognize at inception the fair value of all its obligations it has undertaken to issue a guarantee and requires additional disclosures related to such. This statement, as it relates to the recognition and measurement of the liability, if any, would be effective in fiscal 2004 and the Company does not believe this will have a material effect on its financial statements.

**Reclassifications** Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

In April 2002, the FASB issued SFAS No. 145, *Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections*, which was effective October 1, 2002. SFAS No. 145, among other things, rescinds the requirement of SFAS No. 4 to treat gains and losses on the early extinguishment of debt as extraordinary items. Reclassification of prior periods is required. As a result of the adoption of this statement, amounts recorded in fiscal year 2002 as extraordinary items from the early extinguishment of debt have been reclassified to part of net income from continuing operations.

## **2. DISCONTINUED OPERATION**

Prior to September 30, 2001, management, with Board of Directors approval, committed to a plan to sell Ventek, Inc. ( Ventek ), a wholly-owned subsidiary that supplied machine vision systems to the forest products industry. Ventek was acquired by the Company as part of its acquisition of Advanced Machine Vision Corporation ( AMVC ) in July 2000. In October 2001, the Company signed a definitive agreement to sell Ventek to Veneer Technology, Inc., a company owned by four current managers of Ventek. The terms of the sale include a cash payment of approximately \$3.6 million, a note for \$0.9 million and the cashless tender of Veneer Technology's holdings of Key Technology Series B convertible preferred stock having a stated redemption value of \$2.0 million. As a result of the sale of Ventek, the Company recorded a one-time charge of approximately \$2.1 million, with no tax effect, in its fiscal 2001 results.

Accordingly, the financial statements for fiscal years 2001 and 2002 reflect Ventek as a discontinued operation.

For the one month of fiscal year 2002 prior to the sale, Ventek revenues were \$577,000 with pre-tax earnings of \$61,000. In fiscal year 2001, Ventek revenues were \$4,992,000 with a pre-tax loss of \$678,000.

## **3. SALE OF BUILDING**

In April 2002, the Company completed the sale of its Medford facility, which had a net book value of approximately \$3.5 million, for \$4.6 million and moved its remaining Medford operations into a small leased portion of the facility. The proceeds of the sale were used to retire the mortgage on the building totaling \$2.8 million, requiring an early payment penalty of \$516,000, resulting in net cash proceeds from the sale of \$972,000 after paying the costs associated with the sale. The lease is for a five-year term at approximately \$9,600 per month, plus shared occupancy costs. The base lease is being accounted for as an operating lease.

**4. GOODWILL AND OTHER INTANGIBLE ASSETS**

In July 2001, the FASB issued SFAS No. 142, *Goodwill and Other Intangible Assets*, which was effective October 1, 2002 and may be adopted early. The Company elected to adopt SFAS No. 142 prior to its filing of its first quarter financial statements on Form 10-Q for the quarter ended December 31, 2001. SFAS No. 142 requires, among other things, the discontinuance of goodwill amortization. In addition, the standard includes provisions for the reclassification of certain existing recognized intangibles, reclassification of certain intangibles out of previously reported

goodwill, and the identification of reporting units for purposes of assessing potential future impairments of goodwill. SFAS No. 142 also required the Company to complete a transitional goodwill impairment test within six months from the date of adoption. As a result of the implementation of this change in accounting principle, the Company recorded an impairment of goodwill associated with the automated inspection systems reporting unit, based on a discontinued cash flow analysis, effective at the beginning of fiscal 2002, of \$4.4 million, and related income tax benefits of \$71,000. The Company determined there was no impairment of the \$2.5 million of goodwill associated with the process systems reporting unit.

As of September 30, 2001, the Company had approximately \$6.9 million of intangible assets which are no longer being amortized. Amortization of these assets was \$749,000 in the year ended September 30, 2001. In addition, amortization of goodwill and other indefinite life intangible assets included in discontinued operations was \$197,000 in the year ended September 30, 2001. In compliance with SFAS No. 142, the results for the year ended September 30, 2001 have not been restated. A reconciliation of net loss and loss per share as if SFAS No. 142, exclusive of the charges for the impairment of goodwill, had been adopted in the prior period is shown below.

	September 30, 2001		
	As Previously Reported	Adjustments	Pro Forma
Net earnings (loss) from continuing operations net of tax	\$ (2,343)	\$ 601	\$ (1,742)
Net earnings (loss) from discontinued operation net of tax	(2,581)	126	(2,455)
Net earnings (loss)	(4,924)	727	(4,197)
Net earnings (loss) from continuing operations per share basic and diluted	(0.69)	0.13	(0.56)
Net earnings (loss) from discontinued operation per share basic and diluted	(0.55)	0.03	(0.52)
Net earnings (loss) per share basic and diluted	(1.24)	0.16	(1.08)

As of September 30, 2003, the Company has approximately \$10.9 million of intangible assets related to patents and developed technologies with a net book value of approximately \$7.0 million; \$1.7 million of intangible assets related to purchased trademarks and trade names with a net book value of approximately \$1.1 million; and \$900,000 of intangible assets related to purchased customer development with a net book value of approximately \$600,000. The significant majority of these assets are being amortized over 10 years. Amortization expense for the next five fiscal years is expected to be approximately \$1.3 million per year.

As of September 30, 2003, the Company had \$2.5 million of goodwill associated with the process systems reporting unit which is not being amortized.

**5. TRADE ACCOUNTS RECEIVABLE**

Trade accounts receivable consist of the following (in thousands):

	September 30,	
	2003	2002
Trade accounts receivable	\$ 10,021	\$ 7,942
Allowance for doubtful accounts	(542)	(386)
Total trade accounts receivable, net	\$ 9,479	\$ 7,556

**6. INVENTORIES**

Inventories consist of the following (in thousands):

	September 30,	
	2003	2002
Purchased components and raw materials	\$ 6,746	\$ 6,416
Sub-assemblies	1,476	1,770
Work-in-process	3,907	3,550
Finished goods	1,839	2,233
Total inventories	\$ 13,968	\$ 13,969

**7. PROPERTY, PLANT, AND EQUIPMENT**

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

	September 30,	
	2003	2002
Land	\$ 434	\$ 394
Buildings and improvements	3,855	3,547

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Manufacturing equipment	12,192	11,872
Office equipment, furniture, and fixtures	11,128	10,686
	27,609	26,499
Accumulated depreciation	(22,106)	(20,092)
Total property, plant, and equipment, net	\$ 5,503	\$ 6,407

**8. FINANCING AGREEMENTS**

The Company's domestic credit facility provides a credit accommodation totaling \$13.2 million in the United States consisting of a term loan of \$3.2 million and a revolving credit facility of up to the lesser of \$10.0 million or the available borrowing base, which is based on varying percentages of eligible accounts receivable and inventories. The revolving credit facility matures on July 31, 2004. The term loan requires quarterly payments of principal of \$200,000 and matures on July 31, 2007.

The term loan and operating line bear interest at the Wall Street Journal prime rate, which was 4.00% at September 30, 2003. The credit facility is secured by all of the U.S. personal property, including patents and other intangibles of the Company and its subsidiaries, and contains covenants which require the maintenance of a defined debt service ratio, a defined debt ratio, minimum working capital and current ratio, and minimum profitability. At September 30, 2003, the Company was in compliance with all loan covenants and had an available borrowing base of approximately \$6.9 million under the revolving credit facility. At September 30, 2003, borrowings under the term loan were \$3.2 million. There were no borrowings under the revolving credit facility. At September 30, 2002, borrowings were \$6.6 million under the revolving credit facility, and borrowings under the term loan and under a standby line of credit were \$4.0 million and \$500,000, respectfully.

Additionally, the Company's credit accommodation with a commercial bank in The Netherlands provides a credit facility for its European subsidiary. This credit accommodation totals \$3.7 million and includes a term loan facility of \$814,000, an operating line of the lesser of \$1.7 million or the available borrowing base, which is based on varying percentages of eligible accounts receivable and inventories, and a bank guarantee facility of \$1.2 million. The term loan facility requires quarterly principal payments of \$36,000 and matures in August 2012. It is secured by real property of the Company's European subsidiary, while the operating line and bank guarantee facility are secured by all of the subsidiary's personal property. The credit facility bears interest at the bank's prime rate plus 1.75%, which at September 30, 2003 was 4.5%. At September 30, 2003, the Company had borrowings under this facility of approximately \$814,000 in term loans. Additionally, the Company had received bank guarantees of \$882,000 under this agreement.

Long-term debt consists of the following (in thousands):

	September 30,	
	2003	2002
Term loan dated August 2002, variable interest payable quarterly at the bank's prime rate (4.0% at September 30, 2003), due in quarterly principal payments of \$200,000 through July 2007. Secured by business property.	\$ 3,200	\$ 4,000
Reducing non-revolving \$4 million note dated August 2002, fully maturing in July 2003. Secured by business property.		500
Note payable, interest of 5.25%, due in quarterly principal and interest installments through August 2012, secured by certain land and buildings.	539	
Note payable, interest rate of 5.25%, due in quarterly principal and interest installments through October 2006, secured by certain land and buildings.	275	302
Capital leases, interest rates between 6% and 11%, due in principal and interest installments through September 2005, secured by certain office and manufacturing equipment.	301	613
	4,315	5,415
Current portion	(1,066)	(1,668)
Total long-term debt	\$ 3,249	\$ 3,747





Principal payments on long-term debt are as follows (in thousands):

**Year Ending  
September 30**

2004	\$	1,066
2005		1,088
2006		974
2007		881
2008		58
Thereafter		248
Total	\$	4,315

Based on the borrowing rates currently available to the Company for loans with similar terms and average maturities, the fair value of long-term debt at September 30, 2003 approximates carrying value.

## 9. LEASES

The Company has agreements with the Port of Walla Walla to lease two operating facilities one of which expires in 2010 and the other in 2015. The Company currently has the option to purchase the land and plant under both of the agreements. The purchase price of one facility is determined by reducing the original plant construction costs of approximately \$8,800,000 by one thirty-fifth for each lease year prior to the exercise of the option and adding \$600,000 for the land, subject to further reductions if exercised after the fifteenth year of the lease. The other facility may be purchased at the appraised fair market value. The Company also has two leased operating facilities in Oregon. Both leases expire in 2007. The Company has leased an operating facility in The Netherlands. This lease expires in 2008.

Rent expense is recognized on a straight-line basis over the term of the lease. Rental expense for the Company's operating leases referred to above was \$1,367,000 for the year ended September 30, 2003, \$1,368,000 for the year ended September 30, 2002, and \$1,322,000 for the year ended September 30, 2001.

The following is a schedule of future minimum rental payments required under operating leases and future rental expense (in thousands):

<b>Year Ending September 30</b>	<b>Rental Payments</b>	<b>Rental Expense</b>
2004	\$ 1,429	\$ 1,376
2005	1,456	1,376
2006	1,482	1,376
2007	1,393	1,278

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2008	1,156	1,082
Thereafter	5,469	5,046
Total	\$ 12,385	\$ 11,534

**10. MANDATORILY REDEEMABLE PREFERRED STOCK AND WARRANTS**

The Company issued 1,340,366 shares of Series B convertible preferred stock ( Series B ) at a price of \$8.60 per share in conjunction with the acquisition of AMVC. Each share of Series B, par value of \$0.01 per share, may be converted into 2/3 of a share of common stock. The Series B is convertible at the option of the holder at any time, unless previously redeemed, or by the Company upon a merger, consolidation, share exchange or sale of substantially all of its assets. The holders of Series B may require the Company to repurchase any or all of their shares at any time after July 12, 2002 at the redemption price of \$10.00. If not converted to common stock or redeemed at the option of the Series B holder after July 12, 2002, the Company must redeem the Series B for \$10.00 per share on July 12, 2005. The redemption date may be accelerated if the average closing price of Key Technology common stock, as listed on the Nasdaq National Market, is \$15.00 or more for thirty consecutive trading days. The Series B was accreted from its issue price to its scheduled redemption price using the effective interest method. In connection with the sale of Ventek (see Note 2), 200,595 shares of Series B were redeemed in a cash-less tender of Veneer Technology's holdings.

The holders of Series B are entitled to vote on all matters based on the number of whole shares of common stock into which the holder's stock could be converted. The holders of Series B are not entitled to any dividends. In the event of any liquidation, dissolution, or winding up of the company's business, the holders of Series B would be entitled to a payment of \$10.00 per share before any amount is distributed to holders of common stock. If assets were insufficient to permit this payment to the holders of Series B, the entire assets available for distribution to holders of capital stock would be distributed ratably among the holders of Series B.

The Company also issued 119,106 shares of Series C convertible preferred stock ( Series C ) at a price of \$20.00 per share in conjunction with the acquisition of AMVC. In fiscal year 2001, the Series C shareholder redeemed the entire outstanding amount of its shares and warrants.

The Company issued 365,222 warrants at a fair market value of \$10.00 per warrant in conjunction with the issuance of the convertible preferred stock. Each warrant entitles its holder to purchase at any time for a period of five years from July 12, 2000 one share of common stock at \$15.00 per share, subject to certain adjustments. The warrants permit the holder to engage in a net exercise of the warrants if the fair market value of one share of common stock is greater than \$15.00 per share on the date of exercise. Prior to the expiration date of the warrant, the holder may require the Company to redeem the warrant for cash at a price equal to \$10.00 for each whole share of common stock that may be purchased under the warrant. The warrant holders do not have the right to vote or participate in any matters as shareholders.

As of September 30, 2003, there were 152,630 shares of Series B convertible preferred stock outstanding and 35,553 warrants which had not been redeemed or converted.

**11. INCOME TAXES**

The provision (benefit) for income taxes from continuing operations consists of the following (in thousands):

	Year Ended September 30,		
	2003	2002	2001
Current:			
Federal	\$ 352	\$	\$
State	261		
	613		
Deferred:			
Federal	2,133	1,127	(1,247)
State	(53)	111	(96)
	2,080	1,238	(1,343)
Total income tax expense (benefit)	\$ 2,693	\$ 1,238	\$ (1,343)

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities are as follows (in thousands):

	September 30,	
	2003	2002
Deferred tax asset:		
Reserves and accruals	\$ 2,014	\$ 2,126
NOL and other tax credit carryforwards	3,391	5,756
Translation adjustment to equity	40	425
Deferred tax liability:		
Accumulated depreciation	(224)	(259)
Intangible assets	(2,723)	(3,084)
Net deferred tax asset	\$ 2,498	\$ 4,964
Deferred tax:		
Current asset	\$ 1,935	\$ 1,730
Long-term asset	768	3,472
Long-term liability	(205)	(238)
Net deferred tax asset	\$ 2,498	\$ 4,964

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Income tax expense (benefit) is computed at rates different than statutory rates. The reconciliation between effective and statutory rates is as follows:

	Year Ended September 30,		
	2003	2002	2001
Statutory rates	34.0%	34.0%	(34.0)%
Increase (reduction) in income taxes resulting from:			
ETI deductions	(2.3)	(2.0)	(3.5)
R&D credit	(0.3)	(0.6)	(1.6)
State income taxes, net of federal benefit	1.6	2.0	(1.7)
Change in tax laws	(1.8)		
Other permanent differences	0.7	1.5	4.3
Income tax combined effective rate	31.9%	34.9%	(36.5)%

At September 30, 2003, there were \$8.5 million of net operating loss carryforwards which expire between 2007 and 2019, \$110,000 of research and development credit carryforwards which expire between 2020 and 2022, \$335,000 of foreign tax credit carryforwards which expire between 2005 and 2007, and \$74,000 of AMT credit carryforwards which do not expire.

## 12. SHAREHOLDERS EQUITY

**Employee Stock Purchase Plan** Most employees are eligible to participate in the Company's Employee Stock Purchase Plan (the "Purchase Plan"). Shares are not available to employees who already own 5% or more of the Company's stock. Employees can withhold, by payroll deductions, up to 5% of their regular compensation to purchase shares at a purchase price of 85% of the fair market value of the common stock on the purchase date. There were 500,000 shares reserved for purchase under the Purchase Plan. During the years ended September 30, 2003, 2002, and 2001, the Company issued shares totaling 6,918, 15,860, and 17,184, respectively, under the Purchase Plan.

**Employees' Stock Option Plan** Under the Restated Employees' Stock Option Plan (the "Option Plan"), eligible employees may receive either incentive stock options or nonstatutory stock options and such options may be exercised only after an employee has remained in continuous employment for one year after the date of grant. Thereafter, the options become exercisable as stipulated by the individual option agreements, generally 25% per year on the anniversary date of the grant. The option price is fair market value determined at date of grant. The following table summarizes activity under this Option Plan:

	Number of Shares	Outstanding Options Weighted Average Price Per Share
Balance at October 1, 2000	724,833	\$ 12.20
Options granted	40,000	\$ 7.89
Options forfeited	(65,400)	\$ 13.21
Balance at September 30, 2001	699,433	\$ 11.86
Options granted	169,100	\$ 2.96
Options forfeited	(49,600)	\$ 9.85
Balance at September 30, 2002	818,933	\$ 10.14
Options granted	182,500	\$ 8.98
Options exercised	(11,837)	\$ 5.71
Options forfeited	(52,033)	\$ 9.32

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Balance at September 30, 2003	937,563	\$	10.02
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At September 30, 2003, the total number of shares reserved for option exercises was 1,187,483, of which 238,083 were available for grant. At that date, options for 565,046 shares were exercisable at prices from \$2.51 to \$23.25 per share. At September 30, 2002, the total number of shares reserved for option exercises was 1,187,483, of which 368,550 were available for grant. At that date, options for 493,958 shares were exercisable at prices from \$7.00 to \$23.25 per share. At September 30, 2001, the total number of shares reserved for option exercises was 1,187,483, of

which 488,050 were available for grant. At that date, options for 410,066 shares were exercisable at prices from \$7.00 to \$23.25 per share.

The following table summarizes information about stock options outstanding at September 30, 2003:

Range of Exercise Prices	Number Outstanding	Options Outstanding		Weighted Average Exercise Price	Options Exercisable	
		Weighted Average Remaining Contractual Life (years)			Number of Shares Exercisable	Weighted Average Exercise Price
\$2.51 - 5.00	149,538	4.1	\$	2.95	33,585	\$ 2.95
\$5.00 - 10.00	496,825	3.3		8.63	260,261	8.52
\$10.01 - 15.00	129,700	4.3		11.46	109,700	11.69
\$15.01 - 20.00	88,700	3.4		17.25	88,700	17.25
\$20.01 - 23.25	72,800	2.6		22.58	72,800	22.58
\$2.51 - 23.25	937,563	3.5	\$	10.02	565,046	\$ 11.99

### 13. EMPLOYEE BENEFIT PLANS

The Company has a 401(k) profit sharing plan which covers substantially all employees. The Company is required to match 50% of employee contributions up to 2% of each participating employee's compensation. The Company contributed \$285,000, \$250,000, and \$331,000 in matching funds to the plan for the years ended September 30, 2003, 2002, and 2001, respectively.

The 401(k) plan also permits the Company to make discretionary profit sharing contributions to all employees. Discretionary profit sharing contributions are determined annually by the Board of Directors. Profit sharing plan expense was \$860,000, \$238,000, and zero for the years ended September 30, 2003, 2002, and 2001, respectively.

### 14. SEGMENT INFORMATION

The Company's business units serve customers in its primary market—the food processing and agricultural products industry—through common sales and distribution channels. Therefore, the Company reports on one segment. The following table summarizes information about products and services (in thousands).

Year Ended September 30,		
2003	2002	2001



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Net sales by product category:					
Automated inspection systems	\$	30,230	\$	24,965	\$ 26,884
Process systems		31,759		25,767	27,050
Parts and service/contracts		20,633		19,502	19,020
Total net sales by product category	\$	82,622	\$	70,234	\$ 72,954

Net sales for service/contracts were less than 10% of total net sales for the years ended September 30, 2003, 2002, and 2001, respectively, and are therefore summarized with parts.

The following table summarizes information about geographic areas:

	Year Ended September 30,		
	2003	2002	2001
Net sales:			
Domestic	\$ 41,538	\$ 40,590	\$ 37,496
International	41,084	29,644	35,458
Total net sales	\$ 82,622	\$ 70,234	\$ 72,954
Long-lived assets:			
Domestic	\$ 14,067	\$ 16,286	\$ 26,995
International	2,677	2,683	3,031
Total long-lived assets	\$ 16,744	\$ 18,969	\$ 30,026

There was no customer that accounted for greater than 10% of net sales during fiscal 2003. During fiscal 2002 and 2001, net sales to one major customer amounted to approximately 16% and 17% of total net sales, respectively.

During 2003, net sales to various customers in Canada accounted for approximately 11% of total net sales. During 2001, net sales to various customers in France accounted for approximately 10% of total net sales. No single international geographic location accounted for more than 10% of net sales during 2002. Location of the customer is the basis for the categorization of net sales.

## 15. ROYALTY INCOME

As part of a settlement agreement entered into during 1997, the Company received royalty payments through 2001 related to the sale of certain equipment to a selected market. The payment may be reduced by a percentage of the purchases of equipment from the Company by the other party. The Company recognized royalty income from this agreement of zero, zero, and \$122,000 during the years ended September 30, 2003, 2002, and 2001, respectively.

\* \* \* \* \*

**SUPPLEMENTARY DATA****QUARTERLY FINANCIAL INFORMATION** (*Unaudited*)

The following is a summary of operating results by quarter for the years ended September 30, 2003 and 2002 (in thousands, except per share data):

<b>2003 Quarter Ended</b>	<b>December 31,</b>	<b>March 31,</b>	<b>June 30,</b>	<b>September 30,</b>	<b>Total</b>
Net sales	\$ 15,395	\$ 20,927	\$ 25,013	\$ 21,287	\$ 82,622
Gross profit	6,305	8,115	10,983	8,593	33,996
Net earnings	221	1,153	3,002	1,383	5,759
Net earnings per share basic	0.05	0.24	0.63	0.29	1.21
Net earnings per share diluted	0.04	0.23	0.60	0.27	1.15

<b>2002 Quarter Ended</b>	<b>December 31,</b>	<b>March 31,</b>	<b>June 30,</b>	<b>September 30,</b>	<b>Total</b>
Net sales	\$ 13,945	\$ 18,849	\$ 19,890	\$ 17,550	\$ 70,234
Gross profit	5,445	7,512	8,283	6,642	27,882
Net earnings (loss) from continuing operations	(323)	823	1,390	418	2,308
Net earnings from discontinued operation	39				39
Net loss from change in accounting principle	(4,302)				(4,302)
Net earnings (loss)	(4,586)	823	1,390	418	(1,955)
Net earnings (loss) from continuing operations per share basic	(0.11)	0.13	0.25	0.09	0.36
Net earnings (loss) from continuing operations per share diluted	(0.11)	0.13	0.25	0.08	0.36
Net earnings from discontinued operations per share basic and diluted	0.01				0.01
Net loss from change in accounting principle per share basic and diluted	(0.90)				(0.90)
Net earnings (loss) per share basic	(1.00)	0.13	0.25	0.09	(0.53)
Net earnings (loss) per share diluted	(1.00)	0.13	0.25	0.08	(0.53)

\* \* \* \* \*



**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K.**

(a) The following documents are filed as part of this Form 10-K/A:

1. Exhibits:

(23.2) Consent of Deloitte & Touche LLP

(31.3) Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

(31.4) Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

(32.3) Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(32.4) Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

***SIGNATURES***

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Amendment No. 1 to its Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized.

KEY TECHNOLOGY, INC.

By:                   /s/ Kirk W. Morton  
Kirk W. Morton  
President and Chief Executive Officer

January 23, 2004

KEY TECHNOLOGY, INC.

**FORM 10-K/A**

**Amendment No. 1**

**EXHIBIT INDEX**

**EXHIBIT  
NUMBER**

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