SIMTEK CORP
Form SB-2
November 18, 2004

As filed with the Securities and Exchange Commission on November 18, 2004
Registration 333-

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form SB-2
REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933

SIMTEK CORPORATION
(Exact name of registrant as specified in its charter)

Colorado	84-1057605
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

4250 Buckingham Dr. #100
Colorado Springs, Colorado 80907
(719) 531-9444
(Address, including zip code, and telephone number, including area code, of Principal Executive Offices)

Douglas M. Mitchell
Chief Executive Officer, President and Chief Financial Officer (acting)
Simtek Corporation
4250 Buckingham Dr. #100
Colorado Springs, CO 80907
(719) 531-9444
(Name, address, including zip code and telephone number, including area code, of agent for service)

Copies to:
Hendrik F. Jordaan, Esq.
Holme Roberts & Owen LLP
90 S. Cascade Avenue, Suite 1300
Colorado Springs, CO 80903
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Approximate Date of Commencement of Proposed Sale to the Public: From time to time after the effective date of this Registration Statement.

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

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

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

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. [ ]

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

CALCULATION OF REGISTRATION FEE(1)

Title of each class of securities to be registered	Amount to be registered(1)	Proposed maximum offering price per share	Proposed maximum aggregate offering price	reg
Common stock, $.01 par value per share	5,159,959	$0.575(2)	$2,966,976(2)	
Common stock, $.01 par value per share	2,966,977	$0.627(3)	$1,860,295(3)	
Total	8,126,936		$4,827,271	

(1) Comprises 5,159,959 shares of common stock. 2,966,977 shares of common stock issuable upon exercise of warrants with an exercise price of $0.627.

(2) Estimated solely for purpose of calculating the registration fee pursuant to Rule 457(c), based on the average of the bid and the asked prices of our common stock as reported on the Over-the-Counter Bulletin Board on November 10, 2004.

(3) Estimated solely for the purposes of calculating the registration fee pursuant to Rule 457(g).

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8 (A) OF THE SECURITIES ACT OF 1933 OR UNTIL THE REGISTRATION STATEMENT SHALL BECOME EFFECTIVE ON SUCH DATE AS THE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(A), MAY DETERMINE.

The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities nor does it seek an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

PROSPECTUS (SUBJECT TO COMPLETION) DATED NOVEMBER 16, 2004
8,126,936 Shares

SIMTEK CORPORATION

Common stock

This prospectus is being used to register 8,126,936 shares of Simtek Corporation's common stock being offered by the selling security holders, SF Capital Partners Ltd., Bluegrass Growth Fund LP, Bluegrass Growth Fund LTD and Merriman Curhan Ford & Co. 5,159,959 of these shares have been issued to some of the selling security holders in exchange for a $2,500,000 equity financing that some of the selling security holders completed with us on October 12, 2004. In addition to the 5,159,959 shares, the selling security holders received warrants to acquire 2,966,977 shares of our common stock.

Our common stock is traded on the OTC Bulletin Board under the symbol "SRAM." On November 10, 2004, the closing sale price of our common stock was $.058 per share.

See "Risk Factors" beginning on page [5] to read about factors you should consider before buying our stock.

Neither the Securities and Exchange Commission nor state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of the prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is November ____, 2004.

TABLE OF CONTENTS

SUMMARY

This summary highlights selected information from this prospectus and does not contain all of the information that may be important to you. Please carefully read the entire prospectus and the documents incorporated by reference.

OUR COMPANY

We develop, market and subcontract the production of nonvolatile semiconductor memories. Nonvolatility prevents loss of programs and data when electrical power is removed from the semiconductor. Our memory products feature fast data access and programming speeds. Our products are targeted for use in commercial or military electronic equipment markets. These markets are industrial control systems, office automation, medical instrumentation, telecommunication systems, cable television, and numerous military systems, including communications, radar, sonar and smart weapons. Our wholly owned subsidiary, Q-DOT Group, Inc., specializes in advanced technology research and development for data acquisition, signal processing, imaging and data communications.

Our principal executive office is located at 4250 Buckingham Dr. #100; Colorado Springs, Colorado 80907. Our telephone number is 719-531-9444.

THE OFFERING

We are registering 8,126,936 shares of our common stock that may be offered for resale by SF Capital Partners Ltd., Bluegrass Growth Fund LP, Bluegrass Growth Fund LTD and Merriman Curhan Ford & Co. We refer to these companies as the "selling security holders."

On October 12, 2004, we received $2,500,000 from SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD in return for issuing 5,159,959 shares of our common stock and warrants to acquire 2,579,980 shares of our common stock. In connection with the $2,500,000 equity financing, we issued to Merriman Curhan Ford & Co. warrants to acquire 386,997 shares of our common stock. The warrants issued to the selling security holders have 5-year terms with an exercise price of $0.627 per share.

SUMMARY FINANCIAL INFORMATION

In the table below, we provide you with our summary financial information. The summary financial information presented below is not necessarily comparable from period to period and you should read it together with our historical financial statements and related notes.

	Years Ended December 31,		Nine Months Ended September 3	
	2003	2002	2004	200
			(Unaudited)	
Statement of Operations Data:				
Net revenues	$14,503,771	$ 14,326,705	$10,381,210	$ 10,77
Total expenses	16,534,054	15,185,945	13,593,976	12,58
Operating loss	(2,030,283)	(859,240)	(3,212,766)	(1,80
Loss before taxes	(2,272,641)	(962,867)	(3,378,897)	(1,96
Net loss	$(2,272,641)	$ (962,867)	$(3,378,897)	$ (1,96
Net loss per share:				
Basic and diluted	$ (.04)	$ (.02)	$ (.06)	$

	December 31,2003	September 30, 2004
Balance Sheet Data:		(Unaudited)
Cash and cash equivalents	$ 3,431,679	$ 1,705,387
Working capital	5,104,329	2,114,099
Total assets	7,997,787	5,551,184
Shareholders' equity	3,049,688	26,751

RISK FACTORS

You should consider carefully the following risk factors, as well as the other information in this prospectus before buying our shares. The semiconductor industry is changing rapidly. Therefore, the forward-looking statements and statements of expectations, plans and intent in this prospectus are subject to a greater degree of risk than similar statements regarding some other industries.

OUR LIMITED OPERATING CAPITAL AND OUR ABILITY TO RAISE ADDITIONAL MONEY MAY HARM OUR ABILITY TO DEVELOP AND MARKET OUR PRODUCTS

To date, we have required significant capital for product development, subcontracted production and marketing. We have funded this from the sale of products, the sale of product and technology licenses and from royalties as well as from the sale of our convertible debt and equity securities.

We have not seen any significant increase in our product sales in the past year and our gross margins are less than we had anticipated. Therefore, our cash requirements for the development, subcontracted production and marketing of our existing product families have been difficult to maintain. We are not sure whether we will be able to achieve an increase in product sales and gross margins. We may need more capital in the next year and after that to develop new products. We are not sure that we will be able to raise more capital on reasonable terms, if at all. If we cannot, then we may not be able to develop and market new products. The development, subcontracted production and marketing of our existing products may also suffer, causing our financial position and stock price to deteriorate.

WE MAY EXPERIENCE OPERATING LOSSES IN THE NEXT SEVERAL YEARS

We began business in 1987. Through September 30, 2004, we had accumulated losses of approximately $40.0 million. We realized net income for the first time for the year ended December 31, 1997 and continued to realize net income through June 30, 2000. Subsequent to June 30, 2000 and through September 30, 2004, we realized net losses primarily as a result of accounting charges from the purchase of incomplete research and development in September 2000, decreased revenue, decreased gross margins and increased research and development costs related to new product development. We may continue to experience net operating

losses for the foreseeable future. Continuing net operating losses could materially harm our results of operations, increase our need for additional capital in the future, and hurt our stock price. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Net Loss - Semiconductor Devices, Net (Loss) -- Government Contracts."

WE MIGHT NOT BE ABLE TO RE-GAIN COMPLIANCE WITH CERTAIN COVENANTS SET FORTH IN OUR LOAN AGREEMENT WITH RENN CAPITAL GROUP; IF WE ARE UNABLE TO DO SO, RENN CAPITAL GROUP COULD ACCELERATE THE $3 MILLION LOAN AND FORECLOSE ON THE COLLATERAL THAT WE GRANTED TO IT

Our loan agreement with RENN Capital Group (formerly Renaissance Capital Group, Inc.) contains various financial covenants. As of December 31, 2003, we were not in compliance with two of the covenants set forth in the loan agreement which covenants relate to the interest coverage ratio and debt to equity ratio. However, we subsequently received a waiver for one of the covenants and a modification and a waiver to the loan agreement with respect to the other covenant, the waiver and modification were effective through April 1, 2005. During the quarter ended September 30, 2004, we determined it was highly likely we would not meet the revised covenants as of September 30, 2005. On October 28, 2004, we received a waiver for the two covenants through October 1, 2005. However, significant variances in future actual operations from our current estimates could result in the reclassification of this note to a current liability. If the note becomes due and we cannot pay it, RENN Capital Group may foreclose on the assets that we pledged as security for the note. This would significantly harm our business.

BECAUSE OUR COMMON STOCK IS LISTED ONLY ON THE OTC ELECTRONIC BULLETIN BOARD, IT WILL BE MORE DIFFICULT TO SELL OUR COMMON STOCK

Our common stock is listed on the OTC Electronic Bulletin Board under the symbol "SRAM." Our common stock was listed on the Nasdaq Small-Cap Market until July 18, 1995, but, because we no longer met Nasdaq's listing requirements,

our common stock transferred to the OTC Electronic Bulletin Board as mandated by Nasdaq rules. We may not be able to meet the requirements for relisting our common stock on Nasdaq in the near future or in the longer term.

Securities that are not listed on the Nasdaq Small-Cap Market are subject to a Securities and Exchange Commission rule that imposes special requirements on broker-dealers who sell those securities to persons other than their established customers and accredited investors. The broker-dealer must determine that the security is suitable for the purchaser and must obtain the purchaser's written consent prior to the sale. These requirements may make it more difficult for our security holders to sell their securities and may affect our ability to raise more capital. It may also make it harder for you to sell our stock than the stock of some other companies.

IF WE CANNOT ACHIEVE ACCEPTABLE MANUFACTURING YIELDS AND CONTINUE PRODUCTION WITH CHARTERED SEMICONDUCTOR MANUFACTURING OF SOME OF OUR MEMORY PRODUCTS IN ITS WAFER FABRICATION FACILITY #2, OUR REVENUES, EARNINGS AND STOCK PRICE COULD SUFFER

Chartered Semiconductor Manufacturing Plc. ("Chartered') of Singapore

closed its wafer fabrication facility #1 in March 2004. Prior to this closing we had purchased silicon wafers, the raw materials used to produce our nonvolatile semiconductor memory products, from fabrication facility #1. We have been working with Chartered to transfer the manufacturing process of our memory wafers to Chartered's facility #2. Chartered's facility #2 is newer and more modern than its facility #1, processing 8 inch wafers rather than the older 6 inch wafers processed in facility #1. In the third quarter of 2004, we qualified and began shipping our 3 volt 256 kilobit nonvolatile semiconductor memory product built on silicon wafers received from Chartered's facility 2 In the third quarter of 2004, we began shipping our 5 volt 256 kilobit nonvolatile semiconductor memory products, tested to production requirements on a provisional qualification, built on silicon wafers received from Chartered's facility 2. As of September 30, 2004, we received production wafers for our 64 kilobit nonvolatile semiconductor memory products from Chartered's facility #2 suitable for customer shipments. We believe our 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory products will be qualified early in the fourth quarter of 2004. If production yields or wafer availability from Chartered's facility #2 do not meet our production requirements, this may have a material negative impact on our future revenues, earnings and stock price.

We have not had a manufacturing contract with Chartered since 1998. However, we have maintained a good relationship with Chartered for the pricing and delivery of our wafers. Due to our not having a contract with Chartered and the volatility of the semiconductor market, we may have no control over the pricing and availability of the wafers we require in order to build our products. The risk of us not receiving the products and pricing we need from Chartered has escalated, but we are evaluating alternative sources of supply. If we are unable to obtain the products and pricing we need, our business could suffer.

SINCE WE DEPEND GREATLY ON SUBCONTRACTORS, THEIR POOR PERFORMANCE COULD HURT OUR OPERATIONS

We subcontract the silicon wafer processing, product assembly, and product testing portions of our business to independent companies. Our operating results depend on these subcontractors' ability to supply us with silicon wafers that meet our specifications and to assemble and test enough of our products to meet our customers' needs.

We have depended on Chartered to manufacture all of our silicon wafers for our 0.8 micron memory products which accounted for approximately 78% of our total revenue for 2003. These wafers are the raw materials required to manufacture our semiconductor products. Without these wafers, we would be unable to sell our products. If Chartered is unable to meet our silicon wafer needs on time and at a price that we find acceptable, we would have to find another wafer manufacturer. If we cannot find other suppliers, manufacturers or assemblers on acceptable terms, we may not be profitable. In addition, our subcontractors must be audited and recertified by us on a regular basis for us to continue to produce military-qualified products. We cannot assure you that we will be able to complete this recertification successfully or in a timely manner.

THE UNCERTAINTY INVOLVED IN MANUFACTURING SEMICONDUCTORS MAY INCREASE THE COSTS AND DECREASE THE PRODUCTION OF OUR PRODUCTS

In order for us to be profitable, we must keep our manufacturing costs down and secure the production of sufficient product. Semiconductor manufacturing depends on many factors that are very complex and beyond our control and often beyond the control of our subcontractors. These factors include contaminates in

the manufacturing environment, impurities in the raw materials used and equipment malfunctions. Under our arrangements with our subcontractors, our subcontractors pass on to us substantially all of their costs that are unique to the manufacture of our products. Accordingly, these factors could increase the cost of manufacturing our products and decrease our profits. These factors could also reduce the number of semiconductors that our subcontractors are able to make in a production run. If our subcontractors produce fewer of our products, our revenues may decline.

DELAYS IN MANUFACTURING MAY NEGATIVELY IMPACT OUR REVENUE AND NET INCOME

It takes approximately three months for us to manufacture our semiconductors. Any delays in receiving silicon wafers from our subcontractors will delay our ability to deliver our products to customers. This would delay sales revenue and could cause our customers to cancel existing orders or not place future orders. In addition, if we are not able to make all of our planned semiconductors in a production run this could delay delivery of our products. These delays could occur at any time and would affect our net income.

WE DEPEND ON INDEPENDENT SALES REPRESENTATIVES AND DISTRIBUTORS TO SELL OUR PRODUCTS AND THE TERMINATION OF ANY OF THESE RELATIONSHIPS MAY HARM OUR REVENUE

We use independent sales representatives and distributors to sell the majority of our products. The agreements with these sales representatives and distributors can be terminated without cause by either party with only 30 to 90 days written notice. If one or more of our sales representatives or distributors terminates our relationship, we may not be able to find replacement sales representatives and distributors on acceptable terms or at all. This would affect our profitability. In addition, during 2003 approximately 30% of our product sales were to two distributors. We are not sure that we will be able to maintain our relationship with these distributors.

DELAYS IN OR FAILURE OF PRODUCT QUALIFICATION MAY HARM OUR BUSINESS

Prior to selling a product, we must establish that it meets expected performance and reliability standards. As part of this testing process, known as product qualification, we subject representative samples of products to a variety of tests to ensure that performance in accordance with commercial, industrial and military specifications, as applicable. If we are unable to successfully accomplish product qualification for our future products, we will be unable to sell these future products. Even with successful initial product qualifications, we cannot be assured that we will be able to maintain product qualification or achieve sufficient sales to meet our operating requirements.

SINCE THE SEMICONDUCTOR INDUSTRY IS FAST CHANGING, OUR SUCCESS DEPENDS ON OUR ABILITY TO INTRODUCE NEW PRODUCTS

The semiconductor industry is characterized by rapid changes in technology and product obsolescence. Our success in the semiconductor industry depends in part upon our ability to expand our existing product families and to develop and market new products. The technology we currently use may be made obsolete by other competing or newly developed memory or other technologies. The development of new semiconductor designs and technologies typically requires substantial costs for research and development. Even if we are able to develop new products, the success of each new product depends on several factors including whether we selected the proper product and our ability to introduce it at the right time,

whether the product is able to achieve acceptable production yields and whether the market accepts the new product. We cannot guarantee you that we will be successful in developing new products or whether any products that we do develop will satisfy the above factors. In September 2003, we began shipping samples of our 1 megabit 3 volt nonvolatile semiconductor memory product. We cannot assure you that we will not discover technical problems or manufacturing concerns with this new product, that demand will develop for the new product or that we will be able to sell this new product at a profit.

THE CYCLICALITY OF THE SEMICONDUCTOR INDUSTRY MAY PREVENT US FROM MAINTAINING A CONSISTENT REVENUE STREAM AND MAY HARM OUR STOCK PRICE

The semiconductor industry has historically experienced significant peaks and valleys in sales volumes resulting in large variations of revenues and resulting profits or losses. We do not have direct influence on the nature of the broad semiconductor market. Variations in the revenues and profits within the semiconductor industry may cause us significant losses in the future. If the stock prices of many semiconductor companies decrease, our stock price may also

suffer. Recently, the semiconductor industry has experienced increased losses and the stock prices of many semiconductor companies, including us, have fluctuated.

OUR AGREEMENT WITH DONGBUANAM SEMICONDUCTOR TO CO-DEVELOP A SEMICONDUCTOR PROCESS MODULE THAT COMBINES OUR NONVOLATILE TECHNOLOGY WITH ITS ADVANCED 0.25 MICRON DIGITAL COMPLEMENTARY METAL-OXIDE SEMICONDUCTOR FABRICATION WILL RESULT IN SIGNIFICANT EXPENDITURES

We entered into an agreement with Amkor Technology to cooperate to develop a semiconductor process module that combines our nonvolatile technology with Amkor's advanced 0.25 micron digital complementary metal-oxide semiconductor, or "CMOS," fabrication line. The module will incorporate silicon oxide nitride oxide silicon technology, which will be used to manufacture both high density silicon oxide nitride oxide silicon flash and nonvolatile Static Random Access memories, for stand alone and embedded products. During 2003, our research and development team along with Amkor's research and development team worked aggressively on the co-development program. The co-development program is scheduled to yield a qualified 1 megabit 3.0 volt nonvolatile Static Random Access memory as the primary development vehicle. In February 2003, Amkor Technology sold a controlling interest of its wafer fabrication facility to DongbuAnam Semiconductor. All contractual obligations were transferred to Anam U.S.A., a wholly-owned subsidiary of DongbuAnam Semiconductor. Our co-development program has not been affected by the change in ownership and we do not expect any material changes in the support required to complete the program. There could, however, be changes made by the newly combined management team that could postpone or cancel this co-development project.

Since entering into the agreement with DongbuAnam Semiconductor we estimate that we have spent approximately $4,700,000 in development costs. These costs include increases in headcount, contract engineering services, equipment leases, maintenance agreements for software and wafer fabrication costs. If DongbuAnam Semiconductor terminates our agreement there is no guarantee that we could find a suitable replacement. If we cannot find a replacement, a significant delay and cost increase in the introduction of new products could result.

THE INTENSE COMPETITION IN THE SEMICONDUCTOR INDUSTRY MAY CAUSE US TO LOSE SALES REVENUE TO OTHER SUPPLIERS

There is intense competition in the semiconductor industry. We experience competition from a number of domestic and foreign companies, most of which have significantly greater financial, technical, manufacturing and marketing resources than we have. Our competitors include major corporations with worldwide silicon wafer fabrication facilities and circuit production facilities and diverse, established product lines. We also compete with emerging companies, such as Ramtron International Corporation, attempting to obtain a share of the market for our product families. If any of our new products achieve market acceptance, other companies may sell competitive products at prices below ours. This would have an adverse effect on our operating results. We have sold product and technology licenses to Zentrum Mikroelektronik Dresden. We have granted this company unlimited rights to much of our technology through its license agreements with us. Zentrum Mikroelektronik Dresden has entered the market and has become one of our significant competitors

GIVEN THE SCARCITY OF TRAINED PERSONNEL IN THE SEMICONDUCTOR INDUSTRY, THE LOSS OF KEY EMPLOYEES COULD MATERIALLY AFFECT OUR FINANCIAL RESULTS

Our success depends in large part on our ability to attract and retain qualified technical and management personnel. There are limited personnel trained in the semiconductor industry resulting in intense competition for these personnel. If we lose any of our key personnel, this could have a material adverse affect on our ability to conduct our business and on our financial results.

OUR PATENTS MAY NOT PROVIDE US EFFECTIVE INTELLECTUAL PROPERTY PROTECTION; THIS COULD HARM OUR BUSINESS

We have been issued 26 U.S. patents relating to specific aspects of our current products and we have four applications pending. We have also applied outside the United States for patents on our technology. We plan to continue to protect our intellectual property. We are not sure that any of the patents for which we have applied will be issued or, even if they are issued, will provide us with meaningful protection from competition. We may also not have the money required to maintain or enforce our patent rights. Notwithstanding our patents, other companies may obtain patents similar or relating to our patents.

We seek to protect a significant portion of our intellectual property as trade secrets, rather than patents. Unlike patents, trade secrets must remain confidential in order to retain protection as proprietary intellectual property. We cannot assure you that our trade secrets will remain confidential. If we lose trade secret protection, our business could suffer.

IF OUR PRODUCTS AND TECHNOLOGY INFRINGE ON THIRD PARTY PATENTS, OUR PRODUCT SALES MAY SUFFER

We have not determined whether our products are free from infringement of others' patents. If patent infringement claims are asserted against us and are upheld, we will try to modify our products so that they are non-infringing. If we are unable to do so, we will have to obtain a license to sell those products or stop selling the products for which the claims are asserted. We may not be able to obtain the required licenses. Any successful infringement claim against

us, our failure to obtain any required license or requirement for us to stop selling any of our products, may force us to discontinue production and shipment of these products. This may result in reduced product sales and harm our revenues.

We were notified of possible patent infringement by one company in December 1989. After reviewing the related patents we responded in the same month with a position that our products were still under development, but that the analysis revealed no infringement. There was no further response from this company. In January of 1991 a second company sent us a package of nonvolatile memory and other memory patents for review to evaluate for any possible infringement and to seek licenses as appropriate. Our internal evaluation determined that there were no obvious infringements requiring the pursuit of licenses from this company. In both cases we believe that there are no definitive claims for infringement against our products, so no further actions have been taken, although there has not been direct recognition of this position by the other parties. However, we cannot assure you that these companies will not assert patent infringement claims against us in the future.

In 1998, we received notice of a claim for an unspecified amount from a foundation that owns approximately 180 patents and 70 pending applications. The foundation claimed that some of the machines and processes used in the building of our semiconductor devices infringe on the foundation's patents. In April 1999, we reached an agreement with the foundation for us to purchase a nonexclusive license of the foundation's patents, based on our product offerings and sales forecast at that time. If our products or actual sales revenue vary significantly from the time of the agreement, we may be subject to additional payments.

In late 2002, we received notice of possible patent infringement from a corporation that has acquired a portfolio of patents. We are currently reviewing any potential infringements. If there are any infringements, we believe we will need to enter into a licensing agreement with such company without any material impact on us.

FOREIGN CURRENCY EXCHANGE RATE FLUCTUATIONS MAY INCREASE OUR COSTS, LOWER OUR REVENUES AND CAUSE LOSS OF CUSTOMERS TO OUR COMPETITORS

We purchase materials, including silicon wafers, from outside the United States. In 2003, over 54% of our sales were to customers located outside of the United States. We operate using United States dollars as the functional currency. Changes in foreign currency exchange rates can reduce our revenues and increase our costs. For example, our subcontractors may increase the prices they charge us, on a per purchase order basis, for silicon wafers if the United States dollar weakens. Any large exchange rate fluctuation could affect our ability to compete with manufacturers who operate using foreign currencies. We do not try to reduce our exposure to these exchange rate risks by using hedging transactions. Although we have not had any material losses due to exchange rate fluctuations over the last three years, we cannot assure you that we will not incur significant losses in the future.

IF WE ISSUE SECURITIES AT LOW PRICES IN THE FUTURE, SOME OF OUR SECURITY HOLDERS MAY BE ENTITLED TO ACQUIRE MORE OF OUR SECURITIES WHICH MAY DILUTE AND HARM THE HOLDERS OF OUR COMMON STOCK

We may be obligated under agreements with certain of our security holders to issue to them additional securities in exchange for little or no consideration if we sell our securities in the future at or below certain prices. The issuance of such securities could dilute and harm the holders of our common stock.

BECAUSE WE DO NOT INTEND TO PAY DIVIDENDS IN THE FORESEEABLE FUTURE, YOUR INVESTMENT RETURN MAY BE LIMITED

We have never paid cash dividends on our common stock. We do not expect to pay dividends in the foreseeable future. We intend to use any earnings to finance growth. You should not expect to receive dividends on your shares of common stock.

IF OUR BOARD OF DIRECTORS AUTHORIZES THE ISSUANCE OF PREFERRED STOCK, HOLDERS OF OUR COMMON STOCK COULD BE DILUTED AND HARMED

Our board of directors has the authority to issue up to 2,000,000 shares of preferred stock in one or more series and to establish the preferred stock's voting powers, preferences and other rights and qualifications without any further vote or action by the shareholders. The issuance of preferred stock by our board of directors could dilute and harm the rights of the holders of our common stock. It could potentially be used to discourage attempts by others to obtain control of us through merger, tender offer, proxy contest or otherwise by making such attempts more difficult to achieve or more costly. Given our present capital requirements, it is possible that we may need to raise capital through the sale of preferred stock in the future.

USE OF PROCEEDS

8,126,936 shares are covered by this prospectus. These shares include shares of our common stock issuable upon exercise of warrants issued to the

selling security holders incident to our October 12, 2004 equity financing. We will not receive any proceeds from the resale of these shares by the selling security holders.

CAPITALIZATION

The following table shows our capitalization at September 30, 2004.

Treasury stock, 10,000 shares	$ (12,504)
Preferred stock, $1.00 par value, 2,000,000 shares authorized, none issued and outstanding	0
Common stock, $0.01 par value, 300,000,000 shares authorized, 57,713,387 issued and 57,703,387 shares outstanding	577,034
Additional paid-in capital	39,576,270
Accumulated deficit as of September 30, 2004	(40,114,049)
Shareholders' equity	$ 26,751

MARKET FOR OUR COMMON STOCK AND RELATED SECONDARY HOLDER MATTERS

Our common stock is listed on the OTC Electronic Bulletin Board under the symbol "SRAM." Securities not included in the Nasdaq Small-CAP Market are covered by the Securities and Exchange Commission rule that imposes additional sales practice requirements on broker-dealers who sell such securities to persons other than established customers and accredited investors (generally institutions with assets in excess of $5,000,000 or individuals with net worth in excess of $1,000,000 or annual income exceeding $200,000 or $300,000 jointly with their spouse). For transactions covered by the rule, the broker-dealer must make a special suitability determination for the purchaser and receive the purchaser's written agreement to the transaction prior to the sale. Consequently, the rule may affect the ability of broker-dealers to sell our securities, which will have an adverse effect on the ability of our security holders to sell their securities and our ability to raise additional capital.

Shown below is the closing high bid and the closing low offer for our common stock as reported by the OTC Electronic Bulletin Board on the last day of the quarter.

	Common Stock	
	High Bid	Low Bid
2002		
First Quarter	.41	.33
Second Quarter	.26	.24
Third Quarter	.18	.15
Fourth Quarter	.17	.16
2003		
First Quarter	.16	.14
Second Quarter	.43	.36
Third Quarter	.80	.78
Fourth Quarter	1.26	1.20
2004		
First Quarter	1.64	1.56
Second Quarter	.72	.68
Third Quarter	.62	.60
Fourth Quarter (through November 10, 2004)	.61	.55

The quotations listed above reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not represent actual transactions.

As of November 16, 2004, we had 460 shareholders of record. As of March 23, 2004, we had approximately 7,700 shareholders who beneficially own common stock held in nominee or "street name." We have not paid any dividends on our common stock since inception and we do not intend to pay any dividends on our common stock in the foreseeable future.

Pursuant to a Convertible Loan Agreement, dated as of June 28, 2002, we issued convertible debentures to Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC. We received $3,000,000 in funding. The convertible debentures have 7-year terms at a 7.5% per annum interest rate; each of the funds invested $1,000,000. The holder of the debentures has the right, at any time, to convert all, or in multiples of $100,000, any part of the debenture into fully paid and nonassessable shares of our common stock. The debentures are convertible into our common stock at $0.312 per share, which was in excess of market price on the closing date. There is no public trading market for the debentures. We have agreed to register for resale all of the common stock issuable upon conversion of the debentures. RENN Capital Group is agent for the three investment funds with respect to the Convertible Loan Agreement and the debentures issued thereby.

On November 7, 2003, we closed a $1,500,000 equity financing with Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC. In exchange for the $1,500,000, we issued 550,661 shares of our common stock to each of the three investment funds. The purchase price of $0.908 per share was based on the average closing price of our common stock as reported on the Over-the-Counter

Bulletin Board over the five trading days before closing. In addition to the shares of common stock, each of the three investment funds received warrants to acquire 250,000 shares of our common stock. The warrants have a 5-year term with an exercise price of $1.25 per share for 125,000 shares and $1.50 per share for 125,000 shares.

On October 12, 2004, we closed a $2,500,000 equity financing with SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD. In exchange for the $2,500,000, we issued 4,127,967 shares of our common stock to SF Capital Partners Ltd., 515,996 shares of our common stock to Bluegrass Growth Fund LP and 515,996 shares of our common stock to Bluegrass Growth Fund LTD. The purchase price was based on a 15% discount to the closing price of our common stock as reported on the Over-the-Counter Bulletin Board on October 11, 2004, resulting in a price of $0.4845 per share. In addition to the shares of common stock, SF Capital Partners Ltd., Bluegrass Growth Fund LP, and Bluegrass Growth Fund LTD received warrants to acquire 2,063,984, 257,998, and 257,998 shares of our common stock, respectively. The warrants have a 5-year term with an exercise price of $0.627 per share. Merriman Curhan Ford & Co., the placement agent for the $2,500,000 equity financing, received a cash payment of $187,500 and warrants to acquire 386,997 shares of our common stock. The warrants have a 5-year term with an exercise price of $0.627 per share. In addition, Merriman Curhan Ford & Co. is entitled to receive another cash payment equal to 7.5% of the capital received by us upon the exercise of the warrants issued to SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD pursuant to the $2,500,000 equity financing (provided such exercise is within an applicable tail period).

SELECTED FINANCIAL DATA

The statements of operations for the years ended December 31, 2003 and 2002 and the balance sheet data as of December 31, 2003 have been derived from the financial statements that have been audited by Hein & Associates LLP, Independent Registered Public Accounting Firm. The balance sheet as of September 30, 2004 and the statements of operations for the nine months ended September 30, 2004 and 2003 are unaudited. In our opinion, these financial statements include all adjustments necessary for the fair presentation of the financial position as of September 30, 2004 and statements of operations for the nine

months ended September 30, 2004 and 2003. The balance sheet as of September 30, 2004 and the statements of operations for the nine months ended September 30, 2004 and 2003 were prepared on a consistent basis with our year end financial information. The balance sheet as of December 31, 2003 has been audited by Hein & Associates LLP. This financial data should be read in conjunction with our financial statements and the notes thereto included elsewhere in this prospectus and "Management's Discussion and Analysis of Results of Operations and Financial Condition."

	For the Years Ended December 31,		Nine Months En September 3	
	2003	2002	2004	
				(U
Statement of Operations Data:				
Net Sales	$14,503,771	$14,326,705	$10,381,210	$1
Cost of Sales	9,621,249	8,481,262	7,101,323	
Gross Margin	4,882,522	5,845,443	3,279,887	
Operating Expenses:				
Research and development	4,518,528	4,308,499	4,249,136	
General and administrative	847,503	754,676	833,428	
Sales and Marketing	1,546,774	1,641,508	1,410,089	
Total Operating Expenses	6,912,805	6,704,683	6,492,653	
Other income (expense), net	(242,358)	(103,627)	(166,131)	
Net loss before taxes	(2,272,641)	(962,867)	(3,378,897)	(
Provision for income taxes	-	-	-	
Net loss	$(2,272,641)	$ (962,867)	$(3,378,897)	$(
Net loss per common share:				
Basic and diluted EPS	$ (.04)	$ (.02)	$ (.06)	$
Weighted average common shares outstanding:				
Basic and diluted	54,889,008	54,204,525	57,375,272	

	December 31, 2003	September 30, 2004
Balance Sheet Data:		(Unaudited)
Working capital	$5,104,329	$2,114,099
Total assets	7,997,787	5,551,184
Shareholders' equity	$3,049,688	$ 26,751

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

OVERVIEW OF RECENT DEBT AND EQUITY TRANSACTIONS

On October 12, 2004, we closed a $2,500,000 equity financing with SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD. In exchange for the $2,500,000, we issued 4,127,967 shares of our common stock to SF Capital Partners Ltd., 515,996 shares of our common stock to Bluegrass Growth Fund LP and 515,996 shares of our common stock to Bluegrass Growth Fund LTD. The purchase price was based on a 15% discount to the closing price of our common stock as reported on the Over-the-Counter Bulletin Board on October 11, 2004, resulting in a price of $0.4845 per share. In addition to the shares of common stock, SF Capital Partners Ltd., Bluegrass Growth Fund LP, and Bluegrass Growth Fund LTD received warrants to acquire 2,063,984, 257,998, and 257,998 shares of our common stock, respectively. The warrants have a 5-year term with an exercise price of $0.627 per share. Merriman Curhan Ford & Co., the placement agent for the $2,500,000 equity financing, received a cash payment of $187,500 and warrants to acquire 386,997 shares of our common stock. The warrants have a 5-year term with an exercise price of $0.627 per share. In addition, Merriman Curhan Ford & Co. is entitled to receive another cash payment equal to 7.5% of the capital received by us upon the exercise of the warrants issued to SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD pursuant to the $2,500,000 equity financing (provided such exercise is within an applicable tail period).

On November 7, 2003, we closed our $1,500,000 equity financing with Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC and on July 1, 2002, we received $3,000,000 in our financing transaction with Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC. RENN Capital Group is the agent for the three investment funds. One of our directors holds the position of Senior Vice President of RENN Capital Group.

RESULTS OF OPERATIONS

General. We have designed and developed nonvolatile static random access products since we commenced business operations in May 1987. We have concentrated on the design and development of our nonvolatile static random access memory product families and technologies, marketing, distribution channels, and sources of supply, including production at subcontractors. During 2000, we added the capability to design, develop and produce gate array integrated circuits, or our logic products but ceased supporting this product as of December 31, 2003.

Our business was founded on a specialized technology that supports development of nonvolatile static random access memories. We developed our current memory products out of this technology. This single product family does not allow growth into a broad range of applications. Therefore, in an effort to expand our products, we acquired from WebGear, Inc. incomplete research and development of Bluetooth technology. "Bluetooth" is an industry standard, short range wireless communications technology designed to allow a variety of electronic devices, such as wireless telephones, Personal Digital Assistants, notebook computers, desktop computers, peripheral input-output devices, television set-top boxes and Internet appliances to exchange data without the use of physical cabling. During the twelve month period ending December 31, 2002, we spent approximately $123,000 on the development of our Bluetooth technology. Due to a poor semiconductor market and delays related to widespread adoption of Bluetooth technology, we have decided to stop further development of our Bluetooth technology until the semiconductor market recovers and the Bluetooth technology becomes generally accepted.

In September 1991, we began the sale of our commercially qualified 64 kilobit nonvolatile static random access memory products based on a 1.2 micron process technology. A 1 micron process technology is manufactured with spacing between design elements of approximately one millionth of one meter. Generally speaking, the smaller the spacing between design elements, the less expensive the production cost of our memory products. Accordingly, we generally try to design with lower micron technology. Kilobits are a measure of the amount of data that can be stored. More kilobits imply more storage.

Beginning in 1991, after initial qualification of our first product, through 1995, we began expanding the 64 kilobit nonvolatile static random access memory product family. We achieved qualification of the complete product family for commercial, industrial and military markets and had commenced sales of these products. When we say we "qualify" a product, we mean that our internal quality organization confirms the product's performance to the product's data sheet and

accepted industry standards. Commercial products operate from 0 degrees to 70 degrees Centigrade, industrial products from -40 degrees to 85 degrees Centigrade and military products from -55 degrees to 125 degrees Centigrade. Specific customers require operation over different temperatures for their applications. In 1995 through 1997, we developed and qualified our 64 kilobit and 256 kilobit nonvolatile static random access memory products based on a 0.8 micron process technology. We qualified these products for use in the commercial, industrial and military markets. Development and qualification originally occurred in Zentrum Mikroelektronik Dresden's silicon wafer fabrication facility. In 1997, we transferred the process development of these products to Chartered's silicon wafer fabrication facility. Qualification of these products for use in the commercial, industrial and military markets was completed in 1998. In October 2001, we entered into an agreement with Amkor Technology, who later sold controlling interest in its wafer fabrication facility to DongbuAnam Semiconductor. The agreement we entered into includes the development of a module which incorporates silicon-oxide-nitride-oxide- silicon technology, that will be used to manufacture both high density silicon oxide nitride oxide silicon flash and non volatile static random access memories for stand alone embedded products. The primary development product is our 1 megabit 3.0 volt nonvolatile static random access memory. In September 2003, we began shipping samples of the 1 megabit 3.0 volt nonvolatile static random access memory. We are currently shipping 1 megabit products tested to production requirements on a provisional qualification and plan to have qualification complete in the fourth quarter of 2004. During the third quarter of 2004, we began receiving initial production orders.. Sales of our 1 megabit 3 volt products accounted for approximately 3% of our revenue for the three and nine months ended September 30, 2004. In 2002, we developed and qualified for sale, into the commercial and industrial markets, a 3 volt version of our 256 kilobit nonvolatile static random access memory product built on 0.8 micron process technology in Chartered's silicon wafer fabrication facility. During the second quarter of 2004, we qualified our 256 kilobit 3 volt nonvolatile static random access memory, produced on wafers received from Chartered's facility #2, for use in commercial and industrial applications. During the third quarter of 2004, we began shipping our 3 volt 256 kilobit nonvolatile semiconductor memory product built on silicon wafers received from Chartered's facility #2. In the third quarter of 2004, we began shipping our 5 volt 256 kilobit nonvolatile semiconductor memory products, tested to production requirements on a provisional qualification, built on silicon wafers received from Chartered's

facility 2. We anticipate that qualification of the 5 volt 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory products from Chartered's facility #2 will be completed early in the fourth quarter of 2004.

Chartered closed its wafer fabrication facility #1 in March 2004. We have purchased silicon wafers, the raw materials used to produce our nonvolatile semiconductor memory products, from fabrication facility #1. We have been working with Chartered to transfer the manufacturing process of our memory wafers to Chartered's facility #2. Chartered's facility #2 is newer and more modern than its facility #1, processing 8 inch wafers rather than the older 6 inch wafers that were processed in facility #1. Our research and development activities related to the 3 volt 256 kilobit nonvolatile semiconductor memory product have been redirected to yield improvement. As of September 30, 2004, we received production wafers for our 64 kilobit nonvolatile semiconductor memory products from Chartered's facility #2 suitable for customer shipments. We believe our 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory products will be qualified early in the fourth quarter of 2004. If production yields or wafer availability from Chartered's facility #2 do not meet our production requirements, this may have a material negative impact on our future revenues, earnings and stock price. If production yields or wafer availability from Chartered's facility #2 do not meet our production requirements, this may have a material negative impact on our future revenues, earnings and stock price.

We have not had a manufacturing contract with Chartered since 1998. However, we have maintained a good relationship with Chartered for the pricing and delivery of our wafers. Due to our not having a contract with Chartered and the volatility of the semiconductor market, we may have no control over the pricing and availability of the wafers we require in order to build our products. The risk of us not receiving the products and pricing we need from Chartered has escalated, but we are evaluating alternative sources of supply. If we are unable to obtain the products and pricing we need, our business could suffer.

We entered into a Process Transfer Agreement with X-FAB to install our Silicon Nitride Oxide Semiconductor technology into its wafer fabrication facility to provide an additional manufacturing source to material supplied by Chartered. Through the middle of the third quarter of 2004, we were engaged with X-FAB to install our nonvolatile semiconductor memory process. Due to a lack of our and X-FAB's resources required to install our nonvolatile semiconductor memory process into X-FAB and the marginal anticipated return-on-investment, we ceased the installation of our nonvolatile semiconductor memory process into X-FAB's wafer fabrication facility in August 2004.

Our programmed semiconductor logic products were supported with silicon wafers, built on 0.5 micron process technology, purchased from United Microelectronics and silicon wafers purchased from Chartered built on a 0.35 micron process technology. Products manufactured with smaller spacing generally support lower product costs by reducing the amount of raw material required for the product. In February 2003, we received notification from United Microelectronics that it would be unable to supply us with logic wafers after August 2003. We supported customers with 0.5 micron logic wafers manufactured at United Microelectronics through December 2003 by offering opportunities to purchase their life-time requirements for these products with deliveries scheduled by the end of 2003. We do not plan to support sales logic products to

the market in the foreseeable future.

Sales of products built on wafers purchased from Chartered and United Microelectronics accounted for essentially all of our semiconductor product sales revenue for 2002 and 2003.

REVIEW OF OPERATIONS FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 - SEMICONDUCTOR DEVICES

Total product sales of our semiconductor devices for 2003 were approximately $12,300,000. We have seen an increase in units shipments of our commercial products in 2003. The majority of this increase was for large production orders, with competitive bidding, which resulted in a decrease of average selling prices as compared to 2002. Revenues from our 4/16 kilobit, 64 kilobit and 256 kilobit commercial products saw a total increase of approximately 7% in 2003 as compared to 2002. The majority of the increase was for large production orders, with competitive bidding, which resulted in a decrease of average selling prices. Revenues from our high-end industrial and military products saw an approximate decrease of approximately 28% in 2003 as compared to 2002. This decrease was due to a slow-down of production related to military systems. Sales of our logic products saw a decrease of approximately 13% in 2003 as compared to 2002. This decrease was primarily due to our decision to phase-out this product line by December 31, 2003.

Due to a decrease in high-end industrial and military product revenues and decreases average selling prices of our commercial products, we had an approximate 9% decrease in our gross margins for 2003 as compared to 2002.

REVIEW OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 - SEMICONDUCTOR DEVICES

We have seen a slight increase in unit shipments for the nine months ended September 30, 2004 as compared to the nine months ended September 30, 2003. Our net revenue was $9,000,000 for the nine months ended September 30, 2004 as compared to $9,200,000 for the comparable period of 2003. The decrease in revenue was due to the elimination of revenue from our logic products. The loss of revenue from our logic products was offset by an increase in revenue from our high end industrial and military products. The loss of revenue from our logic products was a result of our decision to discontinue this product line at the end of 2003.

Increased operating expenses had an impact on our profitability for the nine months ended September 30, 2004 compared to the nine months ended September 30, 2003.

Review of Operations for the Twelve Months Ended December 31, 2003 - Government Contracts

Total revenue received from our research and development contracts for 2003 was approximately $2,200,000 up from the $1,900,000 in 2002. This was equal to 15% of our total revenue in 2003.

REVIEW OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 - GOVERNMENT CONTRACTS

Total revenue received from our research and development contracts for the

first nine months of 2004 was approximately $1,300,000 down from the $1,600,000 for the same period in 2003. This was equal to approximately 13% of our total revenue for the first nine months of 2004. The decrease of revenue from our research and development contracts was the result of a decrease in billable labor and a decrease in materials billed against certain government contracts and an increase in research and development expenditures committed to internal product developments.

RESULTS OF OPERATIONS - TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 AND NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003

REVENUES FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002- SEMICONDUCTOR DEVICES

The following table sets forth our net revenues for semiconductor devices by product markets for the twelve months ended December 31, 2003 and 2002 (in thousands):

	2003	2002	Variance
Commercial	$ 9,548	$ 8,892	$ 656
High-end industrial and military	$ 1,759	$ 2,433	$(674)
Logic products	$ 956	$ 1,097	$(141)
Total Semiconductor Revenue	$12,263	$12,422	$(159)

Commercial product revenues increased by $656,000 for the twelve month period ending December 31, 2003 as compared to the same period in 2002. The increase was due to an increase in unit demand of our commercial nonvolatile semiconductor memory products.

High-end industrial and military product revenues accounted for a decrease of $674,000 for the twelve month period ending December 31, 2003 as compared with the same period in 2002. The decrease in revenue was due primarily to a slow- down of production related to military contracts.

Revenues from our logic products decreased by $141,000 for the twelve month period ending December 31, 2003 as compared to the same period in 2002. The decrease was due primarily to a reduction in demand for this product and our decision to eliminate this product line effective December 31, 2003.

One distributor and one direct customer accounted for approximately 30% of our semiconductor device product sales for the twelve months ended December 31, 2003. Products sold to distributors are sold without significant recourse. Distributor contracts allow distributors to return up to 5% in value of product inventory in each six month period. This allows them to keep inventory current to market demand. Distributors resell our products to various end customers. If one of these distributors was to terminate its relationship with us, we believe that there would not be a material impact on our semiconductor device product sales.

REVENUES FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - SEMICONDUCTOR DEVICES

The following table sets forth our net revenues by product markets for the nine months ended September 30, 2004 and 2003 (in thousands):

	Nine Months Ended September 30,

	2004	2003	Variance
Commercial	$7,243	$7,344	$ (101)
igh-end industrial and military	$1,824	$1,240	$ 584
Logic products	$ -	$ 607	$ (607)
Total Semiconductor Revenue	$9,067	$9,191	$ (124)

Commercial revenues decreased by $101,000 for the nine months ended September 30, 2004 when compared to the same period in 2003. The decrease for the nine month period was due to a decrease in product availability of our commercial nonvolatile semiconductor memory products.

High-end industrial and military product revenues increased by $584,000 for the nine months ended September 30, 2004 when compared to the comparable period in 2003. The increase was primarily due to completing shipments of our nonvolatile semiconductor memory products against on-going military contracts.

Revenues from our logic products decreased by $607,000 for the nine months ended September 30, 2004 as compared to 2003. The decrease was due to a reduction in demand for this product and our decision to eliminate this product line effective December 31, 2003.

Three distributors accounted for approximately 36% of our semiconductor device product sales for the nine months ended September 30, 2004. Products sold to distributors are re-sold to various end customers.

COST OF SALES AND GROSS MARGINS FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - SEMICONDUCTOR DEVICES

We recorded costs of sales for semiconductor devices of $8,528,000 and $7,578,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively. These costs reflect an approximate 9% decrease in gross margin percentages for twelve months ended December 31, 2003 as compared to the twelve months ended December 31, 2002. Actual gross margin percentages were 30% and 39% for the twelve months ended December 31, 2003 and 2002, respectively. The decreases were due primarily to a decrease in sales of our high-end industrial and military products and to lower average selling prices of our commercial products

Chartered closed its wafer fabrication facility #1 in March 2004. If we cannot successfully complete the transfer of manufacturing into Chartered's facility #2 and achieve acceptable manufacturing yields or if we cannot qualify X-FAB, this will have a material negative impact on our future revenues and earnings. Please see "Risk Factors--If we cannot achieve acceptable manufacturing yields and continue production with Chartered of some of our memory products in its wafer fabrication facility #2, our revenues, earnings and stock price could suffer."

COST OF SALES AND GROSS MARGINS FOR THE NINE MONTHS ENDED SEPTEMBER 30,

2004 AND 2003 - SEMICONDUCTOR DEVICES

We recorded cost of sales for semiconductor devices of $6,441,000 for the nine months ended September 30, 2004 as compared with $6,391,000 for the nine months ended September 30, 2003. These costs reflect an approximate 2% decrease in gross profit margin percentage for the nine months ended September 30, 2004 as compared to the nine months ended September 30, 2003. The actual gross profit margin percentage for the nine month periods ending September 30, 2004 was 29%. The decrease in gross margin percentage for the nine month period was due to an increase in production costs.

We purchased all of our silicon wafers to produce our 0.8 micron nonvolatile static random access memory products from a single supplier, Chartered to support sales of our nonvolatile semiconductor memory products. Sales of products built on these wafers accounted for approximately 97% of our semiconductor product revenue for the nine month period ending September 30, 2004. We purchased our silicon wafers to produce our 1 megabit nonvolatile static random access memory products built on 0.25 micron technology from DongbuAnam Semiconductor. Sales of the 1 megabit semiconductor products built on these wafers accounted for approximately 3% of our semiconductor product revenue for the nine month period ended September 30, 2004.

We had an agreement with Chartered to provide wafers through September 1998. Although Chartered continues to provide us with wafers under the terms defined in this contract we do not have a current signed agreement with Chartered. In March 2004, Chartered closed its wafer fabrication facility #1

where our memory wafers were manufactured. We received our final shipments from Chartered's facility #1 at the end of March 2004. We have been working with Chartered to transfer the process of the manufacturing of our memory wafers to Chartered's facility #2. We began receiving our memory wafers manufactured in Facility #2 in late second quarter of 2004 and through the third quarter of 2004. However, with this process being transferred to an alternative manufacturing facility, we have seen lower than average production yields, which in turn has lowered our gross margins. We are continuing to work with Chartered to improve our production yields. If we cannot improve our production yields, it will have a material negative impact on our future revenues and earnings.

Through the middle of the third quarter of 2004, we were engaged with X-FAB to install our nonvolatile semiconductor memory process. Due to a lack of our and X-FAB's resources required to install our nonvolatile semiconductor memory process into X-FAB and the marginal anticipated return-on-investment, we have ceased the installation of our nonvolatile semiconductor memory process into X-FAB's wafer fabrication facility in August 2004.

RESEARCH AND DEVELOPMENT FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - SEMICONDUCTOR DEVICES

We believe that continued investments in new product development are required for us to remain competitive in the markets we serve. Beginning in the fourth quarter 2001, our research and development department has been focusing its efforts on the installation of our process at Amkor Technology for the development of a 1 megabit 3 volt nonvolatile static random access memory. Development of the 1 megabit 3 volt nonvolatile static random access memory is

continuing and we began shipping samples in September 2003. We are currently shipping 1 megabit products tested to production requirements on a provisional qualification and plan to have qualification complete in the third quarter of 2004.

Total research and development expenses related to the semiconductor portion of our business were $3,987,000 and $3,795,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively.

The $192,000 increase for the twelve month period was related to increases in payroll and payroll overhead costs of $390,000, equipment leases, maintenance agreements for software and depreciation of $195,000 and reductions in contract engineering and professional services of $226,000, new product development costs of $147,000 and other expenses of $20,000. The primary increase in payroll costs is related to an increase in employee headcount. Increased headcount and contract engineering services are required in order to meet production schedules of our new products. New product development costs are primarily due to the purchases of silicon wafers and reticles required to develop new products. Equipment leases, maintenance agreements for software and depreciation are related primarily to software licenses and hardware required to design our new products.

RESEARCH AND DEVELOPMENT FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - SEMICONDUCTOR DEVICES

We believe that continued investments into new product development are required for us to remain competitive in the markets we serve. Beginning in the fourth quarter 2001, our research and development department has been focusing its efforts on developing a 3 volt 256 kilobit nonvolatile semiconductor memory and the installation of our process at DongbuAnam Semiconductor for the development of a 1 megabit 3 volt nonvolatile semiconductor memory. During the first nine months of 2004, we continued to see increased demand for our 3 volt 256 kilobit nonvolatile semiconductor memories. Development of the 1 megabit 3 volt nonvolatile semiconductor memory is continuing and we began shipping samples of our 1 megabit 3 volt nonvolatile semiconductor during the third quarter of 2003. During the third quarter of 2004, we began receiving initial production orders. Sales of our 1 megabit 3 volt products accounted for approximately 3% of our revenue for the three and nine months ended September 30, 2004.

Research and development expenses for the nine month period ending September 30, 2004 have been directly related to the development and qualification of our family of 0.25 micron nonvolatile semiconductor memory products at DongbuAnam Semiconductor, the transfer of our 3 volt 256 kilobit nonvolatile semiconductor memory into Chartered's facility #2, and the transfer of our 5 volt 64 kilobit and 256 kilobit nonvolatile semiconductor memory products into Chartered's facility #2 and into X-FAB. In August 2004, we stopped our transfer of our 5 volt 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory into X-FAB. In the third quarter of 2004, we qualified and began shipping our 3 volt 256 kilobit nonvolatile semiconductor memory product built on silicon wafers received from Chartered's facility 2. In the third

quarter 2004, we began shipping our 5 volt 256 kilobit nonvolatile semiconductor memory products, tested to production requirements on a provisional qualification, built on silicon wafers received from Chartered's facility 2. Our

research and development activities related to the 3 volt 256 kilobit nonvolatile semiconductor memory product have been redirected to yield improvement. We anticipate that qualification of the 0.25 micron nonvolatile semiconductor memory products from DongbuAnam Semiconductor and the 5 volt 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory products from Chartered's facility #2 will be completed early in the fourth quarter of 2004. While the qualification of these products is nearing completion, our research and development activities have begun focusing more on yield improvements of our 0.25 micron product family and 5 volt 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory products, enhancements to the 1 megabit 3 volt product family, and development of our next-generation 0.18 micron nonvolatile memory process.

Total research and development expenses related to the semiconductor portion of our business were $3,999,000 for the nine months ended September 30, 2004 compared to $3,037,000 for the nine months ended September 30, 2003.

The increase of $962,000 for the nine month period was related to the net between increases in payroll and payroll costs of $193,000, product development costs of $908,000, qualification costs of $19,000 and a decrease in contract engineering services of $158,000. The primary increase in payroll costs is related to an increase in employee headcount which is required to meet production schedules of our new products. The primary increase in product development costs was due to an increase in silicon wafer purchases, reticles, assembly and testing of our 1 megabit products from DongbuAnam Semiconductor, 64 kilobit and 256 kilobit products from X-FAB and 64 kilobit and 256 kilobit products from Chartered's wafer fabrication facility #2 and an increase in costs related to the commercial development of datacomm products performed by our Q-DOT subsidiary. The increase in product development costs included a one-time write off of capital purchases, of approximately $61,000, related to the development at X-FAB that ended in August 2004.

SALES AND MARKETING FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - SEMICONDUCTOR DEVICES

Total marketing expenses related to the semiconductor portion of our business were $1,213,000 and $1,336,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively.

The $123,000 decrease for the twelve month period was related to an increase in advertising of $18,000 and reductions in payroll and payroll related costs of $101,000, travel costs of $33,000 and sales commissions of $7,000. The increase in advertising was due to increased advertising for our new 1 megabit product. The decrease in payroll and payroll related costs was a direct result of reduced headcount. The decrease of travel expenses was due to a reduction in travel within the sales organization. The decrease in sales commissions is a direct result of decreased revenue.

SALES AND MARKETING FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - SEMICONDUCTOR DEVICES

Total marketing expenses related to the semiconductor portion of our business were $1,161,000 for the nine months ended September 30, 2004 as compared to $941,000 for the nine months ended September 30, 2003.

The increase of $220,000 for the nine month period ended September 30, 2004 as compared to September 30, 2003 was due to an increase in payroll and payroll related costs of $172,000, advertising expenses of $40,000 and travel and other miscellaneous expenses of $26,000, offset by a decrease in sales commissions of $18,000. The increase in payroll and payroll overhead costs was a result of increased headcount.

ADMINISTRATION FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - SEMICONDUCTOR DEVICES

Total administration expenses related to the semiconductor portion of our business were $706,000 and $639,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively.

The $67,000 increase was due primarily to increased professional fees, payroll and payroll related costs and travel of $62,000, $7,000, and $3,000, respectively and a reduction in bad debt of $5,000. The increase in professional fees was due to costs associated with our shareholder meeting, board fees, increased legal and audit fees. The majority of these increases were implemented to ensure ongoing compliance with newly enacted regulations resulting from the Sarbanes-Oxley Act.

ADMINISTRATION FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - SEMICONDUCTOR DEVICES

Total administration expenses related to the semiconductor portion of our business were $729,000 for the nine months ended September 30, 2004 as compared to $579,000 for the nine months ended September 30, 2003.

The $150,000 increase for the nine month period was due to increases in accounting and legal fees of $45,000, professional fees of $57,000, costs associated with our annual meeting of shareholders of $47,000 and other miscellaneous expenses including travel of $21,000 and a decrease in payroll and payroll overhead costs of $20,000. The increase in legal fees was primarily related to costs incurred in relation to our annual meeting of shareholders and increased legal fees related to our registration statements on Form SB-2 that we are contractually obligated to file with the Securities and Exchange Commission. The increase in professional services was primarily due to an increase in fees paid to our Board of Directors and fees paid for financial consulting. The increase in accounting fees was due to increased audit fees related to our registration statements on Form SB-2.

TOTAL OTHER INCOME (EXPENSE) FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - SEMICONDUCTOR DEVICES

The $115,000 increase in total other income (expense) for the twelve month period ending December 31, 2003 as compared to the twelve month period ending December 31, 2002 was primarily related to an increase of interest expense and an increase in interest income which was a direct result of the $3,000,000 funding we received on July 1, 2002 from RENN Capital Group.

NET LOSS FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - SEMICONDUCTOR DEVICES

We recorded a net loss of $2,389,000 and $1,028,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively. The increase of $1,361,000 in net loss for the twelve month period was due primarily to a decrease in gross margins, and an increase in research and development costs and administration costs.

NET LOSS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 -

SEMICONDUCTOR DEVICES

We recorded a net loss of $3,424,000 for the nine months ended September 30, 2004 as compared to a net loss of $1,913,000 for the nine months ended September 30, 2003. The increase in net loss for the nine month period was due primarily to increased operating expenses which were primarily related to research and development expenses.

REVENUES FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - GOVERNMENT CONTRACTS

The following table sets forth our net revenues from the government contracts portion of our business for the twelve months ended December 31, 2003 and December 31, 2002 (in thousands):

	2003	2002	Variance
Government Contracts	$2,241	$1,905	$336

The increase of revenue for the twelve months ended December 31, 2003 as compared to the twelve months ended December 31, 2002 was the result of increased direct labor costs and increased materials and services that were invoiced against development contracts. Direct labor increased due to the addition of employees.

Costs on contracts with the government (including allocable indirect costs) are subject to audit and adjustment by negotiations between Q-DOT and government representatives. Costs submitted for reimbursement are subject to government audits for compliance with government cost accounting standards, federal acquisitions regulations and other contract terms. Negotiations for all of the

years through March 31, 1999 have been completed without any material adjustments. Management does not believe the results of the March 31, 2000, December 31, 2000, December 31, 2001, December 31, 2002 and December 31, 2003 government audits and subsequent negotiations will have a material effect on the accompanying financial statements.

REVENUES FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - GOVERNMENT CONTRACTS

The following table sets forth our net revenues from our government contracts portion of our business for the nine months ended September 30, 2004 and 2003 (in thousands):

	Nine Months Ended September 30,		
	2004	2003	Variance
Government Contracts	$1,314	$1,586	$(272)

The decrease of revenue for the nine month period ending September 30, 2004 as compared to the same period in 2003 was the result of a decrease in billable labor and a decrease in materials billed against certain government contracts

and an increase in research and development expenditures committed to internal product developments.

COST OF SALES AND GROSS MARGIN FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - GOVERNMENT CONTRACTS

We recorded cost of sales for government contracts of $1,093,000 and $903,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively. These costs reflect an approximate 2% decrease in gross margin percentages for the twelve months ended December 31, 2003 as compared to twelve months ended December 31, 2002. The decrease in gross margin percentages was primarily due to an increase in non-direct labor which could not be billed as revenue. Actual gross margin percentages for the twelve months ending December 31, 2003 and December 31, 2002 were 51% and 53%, respectively.

COST OF SALES AND GROSS MARGIN FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - GOVERNMENT CONTRACTS

The cost of sales for the government contracts portion of our business was $660,000 for the nine months ended September 30, 2004 as compared to $833,000 for the same period in 2003. This was equivalent to a gross margin percentage of 50% for the nine months ended September 30, 2004 as compared to a gross margin percentage of 47% for the same period in 2003. The increase in gross margin percentage for the nine month period was primarily due to a decrease in direct labor, materials and services.

RESEARCH AND DEVELOPMENT FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - GOVERNMENT CONTRACTS

Total research and development expenses related to the government contracts portion of our business were $531,000 and $514,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively.

The $17,000 increase for the twelve month period was related to decreases in payroll and payroll overhead costs of $103,000 and an increase in software maintenance contacts and equipment leases of $120,000. The primary reason for the decrease in payroll and payroll overhead costs was due to decreased recruiting expenses and decreased contract maintenance.

RESEARCH AND DEVELOPMENT FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - GOVERNMENT CONTRACTS

Total research and development expenses related to the government contracts portion of our business were $250,000 for the nine months ended September 30, 2004 compared to $432,000 for the nine months ended September 30, 2003.

The $182,000 decrease for the nine month period ending September 30, 2004 as compared to the same period in 2003 was related to decreases of $15,000 in employment related expenses, $25,000 in software maintenance contracts and equipment leases, $8,000 in miscellaneous expenses and $134,000 of overhead costs that were transferred to the semiconductor portion of the business. The overhead costs that were transferred to the semiconductor portion of the

business were related to the labor associated with the commercial development of

datacomm products.

MARKETING FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - GOVERNMENT CONTRACTS

Total marketing expenses related to the government contracts portion of our business were $334,000 and $306,000 for the twelve months ended December 31, 2003 and December 31, 2002, respectively.

The increase of $28,000 for the twelve months ended December 31, 2003 as compared to December 31, 2002 was primarily due to an increase in bid and proposal activities required to complete small business innovative research proposals requiring engineering and administrative support.

MARKETING FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - GOVERNMENT CONTRACTS

Total marketing expenses related to the government contracts portion of our business were $249,000 for the nine months ended September 30, 2004 as compared to $259,000 for the nine months ended September 30, 2003.

The $10,000 decrease for the nine months ended September 30, 2004 as compared to the same period in 2003 was related to increases in bid and proposal labor of $10,000 and travel expenses of $5,000 which were offset by $25,000 of overhead costs that were transferred to the semiconductor portion of the business. The overhead costs that were transferred to the semiconductor portion of the business were related to the labor associated with the commercial development of datacomm products.

ADMINISTRATION FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - GOVERNMENT CONTRACTS

Total administration expenses related to the government contracts portion of our business were $142,000 and $116,000 for the twelve month period ended December 31, 2003 and December 31, 2002, respectively.

The $26,000 increase for the twelve months ended December 31, 2003 as compared to December 31, 2002 was due to an increase in indirect labor expenses of $40,000 which was offset by decreased legal fees of $14,000.

ADMINISTRATION FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - GOVERNMENT CONTRACTS

Total administration expenses related to the government contracts portion of our business were $104,000 for the nine months ended September 30, 2004 as compared to $114,000 for the nine months ended September 30, 2003.

The $10,000 decrease in administration expenses for the nine month period was due to an increase in employee related expenses of $10,000 and miscellaneous expenses of $5,000 which were offset by a decrease of $25,000 in overhead costs that were transferred to the semiconductor portion of the business. The overhead costs that were transferred to the semiconductor portion of the business were related to the labor associated with the commercial development of datacomm products.

NET INCOME FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2003 AND 2002 - GOVERNMENT CONTRACTS

We recorded a net income of $116,000 for the twelve months ended December 31, 2003 as compared to a net income of $65,000 for the twelve months ended December 31, 2002 for the government contracts portion of our business. The $51,000 increase in net income for the twelve month period was due primarily to

increased revenue.

NET INCOME/LOSS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003 - GOVERNMENT CONTRACTS

We recorded a net income of $45,000 for the nine months ended September 30, 2004 as compared to a net loss of $54,000 for nine months ended September 30, 2003 for the government contracts portion of our business. The increase in net income for the nine month period ending September 30, 2004 was primarily due to a decrease in operating expenses

FUTURE RESULTS OF OPERATIONS

Our ability to be profitable will depend primarily on our ability to continue reducing manufacturing costs and increasing net product sales by increasing the availability of existing products, by the introduction of new products and by expanding our customer base. We are also dependent on the overall state of the semiconductor industry and the demand for semiconductor products by equipment manufacturers.

We are continuing our co-development program with DongbuAnam Semiconductor to develop a semiconductor process module that combines our nonvolatile technology with Anam's advanced 0.25 micron digital CMOS fabrication line. CMOS is the semiconductor technology used in the transistors that are manufactured into most of today's computer microchips. The module incorporates silicon oxide nitride oxide silicon ("SONOS") technology, which will be used to manufacture both high density SONOS flash and nonvolatile static random access memories, for stand alone and embedded products. During 2002 and through September 30, 2004, our research and development team along with the research and development team of Amkor Technology, the predecessor of Anam, worked aggressively on the co-development program. Our 1 megabit 3.0 volt nonvolatile static random access memory was the primary development vehicle. In February 2003, Amkor Technology sold controlling interest of its wafer fabrication facility to DongbuAnam Semiconductor. All contractual obligations were transferred to Anam U.S.A., a wholly owned subsidiary of DongbuAnam Semiconductor. Our co-development program has not been affected by the change in ownership and we do not expect any material changes in the support required to complete the program. In August 2003, we received the first complete processed silicon from this development which yielded working samples of our new 1 megabit 3 volt nonvolatile semiconductor memory product. We began shipping samples of our new 1 megabit 3 volt nonvolatile semiconductor memory product in September 2003. During the third quarter of 2004, we began receiving initial production orders. We are currently shipping 1 megabit products tested to production requirements on a provisional qualification and plan to have qualification complete early in the fourth quarter of 2004. We cannot assure you that we will not discover technical problems or manufacturing concerns with this new product, that demand will develop for the new product or that we will be able to sell this new product at a profit.

As of September 30, 2004, we had a backlog of unshipped customer orders of approximately $3,238,000 expected to be filled by March 31, 2005. Orders are cancelable without penalty at the option of the purchaser prior to 30 days before scheduled shipment and therefore are not necessarily a measure of future product revenue.

Chartered closed its wafer fabrication facility #1 in March 2004. We have purchased silicon wafers, the raw materials used to produce our nonvolatile semiconductor memory products, from fabrication facility #1. We have been working with Chartered to transfer the manufacturing process of our memory wafers to Chartered's facility #2. Chartered's facility #2 is newer and more modern than its facility #1, processing 8 inch wafers rather than the older 6 inch wafers that were processed in facility #1. In the third quarter of 2004, we qualified and began shipping our 3 volt 256 kilobit nonvolatile semiconductor memory product built on silicon wafers received from Chartered's facility 2. In the third quarter 2004, we began shipping our 5 volt 256 kilobit nonvolatile semiconductor memory products, tested to production requirements on a provisional qualification, built on silicon wafers received from Chartered's facility 2. Our research and development activities related to the 3 volt 256 kilobit nonvolatile semiconductor memory product have been redirected to yield improvement. As of September 30, 2004, we received production wafers for our 64 kilobit nonvolatile semiconductor memory products from Chartered's facility #2 suitable for customer shipments. We believe our 64 kilobit and 5 volt 256 kilobit nonvolatile semiconductor memory products will be qualified early in the fourth quarter of 2004. If production yields or wafer availability from Chartered's facility #2 do not meet our production requirements, this may have a material negative impact on our future revenues, earnings and stock price.

We cannot assure you that the growth in demand, or demand for our products, will increase in the future. Through the first nine months ended September 30, 2004, we were dependent on our 0.8 micron products for revenue, for which customer demand has remained substantially flat over the past nine months. We continue to explore alternatives to further reduce our cost to manufacture our existing products built on 0.8 micron technology. However, with our current wafer manufacturer transferring our process to its alternate manufacturing facility we have seen lower average production yields, which in turn has lowered our gross profit margins. We do anticipate that once the transfer is complete and our customer demand transitions to the 0.25 micron product family from DongbuAnam, it will have a positive affect on our gross margins. We are currently reviewing additional cost reduction measures that may have the potential to improve our earnings.

In the first nine months of 2004 and the years ended December 31, 2003 and 2002, we purchased all of our silicon wafers to produce our 0.8 micron nonvolatile static random access memory products from a single supplier, Chartered. Approximately 97% of our semiconductor product sales for the nine months ended September 30, 2004 and approximately 92% and 91% of our semiconductor device sales for 2003 and 2002, respectively, were from finished units produced from these silicon wafers. We had an agreement with Chartered to provide wafers through September 1998. Although Chartered continues to provide us wafers under the terms defined in this contract we do not have a current signed agreement. DongbuAnam Semiconductor provides silicon wafers for our 0.25 micron process to support our 1 megabit product family. Approximately 3 % of our semiconductor product sales for the nine months ended September 30, 2004 were from finished units produced from these silicon wafers.

We entered into a Process Transfer Agreement with X-FAB to install our Silicon Nitride Oxide Semiconductor technology into its wafer fabrication facility to provide an additional manufacturing source to material supplied by Chartered. Due to a lack of our and X-FAB's resources required to install our nonvolatile semiconductor memory process into X-FAB and the marginal anticipated return-on-investment, we have ceased the installation of our nonvolatile

semiconductor memory process into X-FAB's wafer fabrication facility in August 2004.

Zentrum Mikroelektronik Dresden has established production and sales of nonvolatile static random access memory products. We believe that this second source for nonvolatile static random access memory products, may have a positive impact on our business because many large manufacturers require two sources from which to purchase product. We will not be receiving any further license payments from our contract with Zentrum Mikroelektronik Dresden. We also, however, expect increased competition from Zentrum Mikroelektronik Dresden with respect to nonvolatile static random access memory products.

We intend to continue designing, developing and subcontracting the production of our memory products. We also propose to continue to sell to existing and new customers through our normal sales and marketing efforts. We will also begin development of high performance data communications products based on silicon germanium process expertise gained through our acquisition of Q-DOT Group. We believe that the addition of data communication products will allow us to expand our product offering into new applications and additional customers. We anticipate that this will reduce our dependence on any single product line and provide additional potential sources of revenue.

Our ability to achieve profitability will depend primarily on our ability to continue reducing our manufacturing costs and increasing net product sales by improving the availability of existing products, by the introduction of new products and by expanding our customer base. With the positive feedback we have received from the customers who we have sampled our new 1 megabit product with, we expect to ramp production of this product during the fourth quarter of 2004. In order to achieve these goals, we are dependent on the overall state of the semiconductor industry and the demand for semiconductor products by equipment manufacturers. Please see "Risk Factors" for additional risks to which we are exposed.

LIQUIDITY AND CAPITAL RESOURCES

On October 12, 2004, we closed a $2,500,000 equity financing with three separate investment funds, SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD. In exchange for the $2,500,000, we issued 4,127,967 shares of our common stock to SF Capital Partners Ltd., 515,996 shares of our common stock to Bluegrass Growth Fund LP and 515,996 shares of our common stock to Bluegrass Growth Fund LTD. The purchase price was based on a 15% discount to the closing price of our common stock as reported on the Over-the-Counter Bulletin Board on October 11, 2004, resulting in a price of $0.4845 per share. In addition to the shares of common stock, SF Capital Partners Ltd., Bluegrass Growth Fund LP, and Bluegrass Growth Fund LTD received warrants to acquire 2,063,984, 257,998, and 257,998 shares of our common stock, respectively. The warrants have a 5-year term with an exercise price of $0.627

per share. Merriman Curhan Ford & Co., the placement agent for the $2,500,000 equity financing received a cash payment of $187,500 and warrants to acquire 386,997 shares of our common stock. The warrants have a 5-year term with an exercise price of $0.627 per share. In addition, Merriman Curhan Ford & Co. is entitled to receive another cash payment equal to 7.5 % of the capital received by us upon the exercise of the warrants issued to SF Capital Partners Ltd., Bluegrass Growth Fund LP and Bluegrass Growth Fund LTD pursuant to the $2,500,000 equity financing (provided such exercise is within applicable tail

period).

On November 7, 2003, we closed our $1,500,000 equity financing with Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC. On July 1, 2002, we received $3,000,000 in our financing transaction with Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFS US Special Opportunities Trust PLC pursuant to a Convertible Loan Agreement. As of December 31, 2003, we were not in compliance with two of the covenants set forth in the loan agreement which covenants relate to the interest coverage ratio and debt to equity ratio. However, we subsequently received a waiver for one of the covenants and a modification and a waiver to the loan agreement with respect to the other covenant, the waiver and modification were effective through April 1, 2005. During the quarter ended September 30, 2004, we determined it was highly likely we would not meet the revised covenants as of September 30, 2005. On October 28, 2004, we received a waiver for the two covenants through October 1, 2005. However, significant variances in future actual operations from our current estimates could result in the reclassification of this note to current liabilities.

The change in cash flows for the nine months ended September 30, 2004 used in operating activities was primarily a result of a net loss of $3,378,897, which is offset by $356,344 in depreciation and amortization, decreases in accounts receivable, prepaid expenses and accrued expenses of $706,115, $21,994 and $40,151, respectively, and increases in allowance accounts, loss on disposal of assets, inventory and accounts payable of $33,124, $75,110, $103,754 and $865,271, respectively. The decrease of $706,115 in accounts receivable was directly related to the decrease in revenue for the third quarter of 2004. The $865,271 increase in accounts payable was due to the receipt of raw materials at the end of September 2004 that we are not obligated to pay until October 2004. The increase in inventory of $103,754 was primarily due to the timing of receiving raw materials at the end of September 2004 that will be used to support product shipments in the fourth quarter of 2004. The $75,100 loss on disposal of assets, was primarily related to writing off the capital expenditures purchased for the installation of our process at X-FAB. The change in cash flows used in investing activities of $370,831 was primarily due to the purchase of equipment required to test our nonvolatile semiconductor memory products and reticles required to produce our wafers. The change in cash flows provided by financing activities of $96,936 was primarily due to the net effect of payments on a line of credit and capital leases offset by funds received from the exercise of stock options by employees of ours.

The change in cash flows for the year ended December 31, 2003 used in operating activities was primarily a result of a net loss of $2,272,641, which is offset by $497,701 in depreciation and amortization, decreases in allowance accounts, accounts receivable, inventory, prepaid expenses, accounts payable and deferred revenue of $16,376, $402,361, $411,358, $114,542, $49,314 and $40,500, respectively and increases in accrued expenses of $64,626. The decrease of $402,361 in accounts receivable was directly related to certain customers paying invoices within our payment terms. The decrease in inventory was primarily due to an increase in finished goods shipments at the end of 2003. The decrease in prepaid expenses of $114,542 was due primarily to the renegotiation of certain software licenses. The decrease in accounts payable of $49,314 was primarily due to the timing of payments for standard operating expenses. The increase in accrued expenses was due primarily to increased vacation payable. The increase in vacation payable has occurred due to certain employees not using as much vacation time. The change in cash flows used in investing activities of $501,244 was primarily due to the purchase of equipment required to test our nonvolatile semiconductor memory products and software acquired for research and development activities. The cash flows provided by financing activities of $1,640,296 was due to $1,475,515 (after expenses) received from the November 2003 equity financing transaction we did with Renaissance Capital Growth and Income Fund

III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC, net borrowings on a line of credit of $150,000, proceeds of $183,131 for the exercise of stock options by certain employees less payments on a capital lease obligation of $168,350.

The change in cash flows for the year ended December 31, 2002 used in operating activities was primarily a result of a net loss of $962,867, which is offset by $443,146 in depreciation and amortization, a decrease in allowance accounts, inventory, accounts payable and accrued expenses of $71,150, $261,442, $328,848 and $122,594, respectively. These decreases were offset by increase in accounts receivable, prepaid and other and deferred revenue of $618,653,

$123,972 and $25,500, respectively. The $261,442 decrease in inventory and the $618,653 increase in accounts receivable, were due to an increase in customer demand in the late fourth quarter of 2002, this increase allowed us to dispose of inventory on hand. The $328,848 decrease of accounts payable was primarily due to the timing of raw materials received within the period. Materials were received and paid for late in 2001, but due to a soft market demand, had not been fully consumed, resulting in larger inventory levels at December 31, 2001. The $122,594 decrease in accrued expenses was due to our completing payments of accrued salary and vacation payments to our former Chief Financial Officer. The $123,972 increase in prepaid expenses and other was directly related to in increase in software licensing and maintenance agreements that are required to be paid in advance. These software licensing agreements are required for us to design our 1 megabit nonvolatile static random access memory. The change in cash flows used in investing activities of $163,657 was primarily due to the purchase of hardware and software required for research and development activities and equipment required to manufacture our semiconductor devices at Chartered and United Microelectronics Corp. The cash flows provided by financing activities of $2,699,678 were due primarily to the $3,000,000, net of $116,175 in financing fees, received from Renaissance Capital Growth and Income Fund III, Inc., Renaissance US Growth & Investment Trust PLC and BFSUS Special Opportunities Trust PLC, borrowings and payments on notes payable and a capital lease obligation and the exercise of stock options by our employees.

Short-term liquidity.

Our cash balance at September 30, 2004 was $1,705,387.

Our future liquidity will depend on our revenue growth and our ability to sell our products at positive gross margins and control of our operating expenses. Over the coming twelve months, we expect to spend approximately $9,000,000 for operating expenses assuming revenue growth and no significant change in marketing or product development strategies. We expect to meet these capital needs from sales revenues and, to the extent we do not have sufficient revenues, from our existing cash reserves.

Long-term liquidity.

We continue to evaluate our long-term liquidity. Our growth plans may require additional funding from outside sources. We are in ongoing discussions with investment banking organizations and potential lenders to ensure access to funds as required.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Simtek's consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which require us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and the related disclosures. A summary of these significant accounting policies can be found in Simtek's Notes to Consolidated Financial Statements included in this Form SB-2. The estimates used by management are based upon Simtek's historical experiences combined with managements understanding of current facts and circumstances. Certain of our accounting polices are considered critical as they are both important to the portrayal of our financial condition and the results of our operations and require significant or complex judgments on our part. We believe that the following represent the critical accounting policies of Simtek as described in Financial Reporting Release No. 60, Cautionary Advice Regarding Disclosure About Critical Accounting Policies, which was issued by the Securities and Exchange Commission: inventories; deferred income taxes; allowance for doubtful accounts; and, allowance for sales returns.

The valuation of inventories involves complex judgments on our part. Excess finished goods inventories are a natural component of market demand of semiconductor devices. We continually evaluate and balance the levels of inventories based on sales projections, current orders scheduled for future delivery and historical product demand. While certain finished goods items will sell out, quantities of other finished goods items will remain. These finished goods are reserved as excess inventory. We believe we have adequate controls with respect to the amount of finished goods inventories that are anticipated to become excess. While we believe this process produces a fair valuation of inventories, changes in general economic conditions of the semiconductor industry could materially affect valuation of our inventories.

The allowance for doubtful accounts reflects a reserve that reduces customer accounts receivable to the net amount estimated to be collectible. Estimating the credit worthiness of customers and the recoverability of customer accounts requires management to exercise considerable judgment. In estimating uncollectible amounts, we consider factors such as industry specific economic conditions, historical customer performance and anticipated customer performance. While we believe our processes to be adequate to effectively quantify our exposure to doubtful accounts, changes in industry or specific customer conditions may require us to adjust our allowance for doubtful accounts.

We record an allowance for sales returns as a net adjustment to customer accounts receivable. The allowance for sales returns consists of two separate segments, distributor stock rotation and distributor price reductions. When we record the allowance, the net method reduces customer accounts receivables and gross sales. Generally, we calculate the stock rotation portion of the allowance based upon distributor inventory levels. The contracts we have with our distributors allow them to return to us a 5% percent of their inventory in exchange for inventory which better meets their demands. At times, we are required to allow our distributors to lower the selling price of a specific device in order to meet competition. When this occurs, we record an allowance for potential credit that our distributor's will be requesting. This allowance is based on approved pricing changes, inventory affected and historical data. We believe that our processes to adequately predict our allowance for sales returns are effective in quantifying our exposures due to industry or specific customer

conditions.

We record an allowance that directly relates to the warranty of our products for one year. The allowance for warranty return reduces our gross sales. This allowance is calculated by looking at annual revenues and historical rates of our products returned due to warranty issues. While we believe this process adequately predicts our allowance for warranty returns, changes in the manufacturing or design of our product could materially affect valuation of our warranties.

We have various government contracts which are subject to audit by the government. However, audits for the periods ending December 31, 2002 and December 31, 2003 have not been completed. In addition, certain of these contracts are based on our estimate as to their percentage of completion as of the balance sheet date. Our historical experience has not resulted in a material adjustment to prior recorded revenue amounts.

We have recorded a valuation allowance on deferred tax assets. Future operations may change our estimate in connection with potential utilization of these assets.

INFLATION

The impact of inflation on our business has not been material.

OFF BALANCE-SHEET ARRANGEMENTS

We are party to a lease agreement with Baja Properties, LLC as landlord pursuant to which we lease approximately 16,000 square feet of space in Colorado Springs, Colorado. The lease is scheduled to expire on February 28, 2013. Our monthly rental payment obligation is approximately $16,000.

DESCRIPTION OF PROPERTY

We do not own any real estate. We do not have a policy:

1. limiting the percentage of assets which may be invested in any one investment or type of investment

2. regarding whether we acquire assets primarily for possible capital gain or primarily for income, or

3. with respect to investments in real estate, interests in real estate, real estate mortgages, or securities of or interests in persons primarily engaged in real estate activities.

BUSINESS

GENERAL

We provide integrated circuits to the electronics market for use in a variety of systems, such as computers, copiers, factory controllers, electric meters and military systems. We design, market and sell our products, but we

subcontract the majority of our manufacturing requirements. We have designed and developed nonvolatile static random access memory products since we began business operations in May 1987 as a Colorado Corporation. We have concentrated on the design and development of the 4, 16, 64 and 256 kilobit and 1 megabit nonvolatile static random access memory product families and technologies, distribution channels, and sources of supply, including production at subcontractors. Kilobits are a measure of the amount of data that can be stored; more kilobits imply more storage. Megabits are also a measure of the amount of data that can be stored; there are 1,000 kilobits in a megabit. During 2000, we added the capability to design, develop and produce programmed semiconductor logic products. During 2003, due to adverse market conditions, we determined to no longer offer our programmed semiconductor logic products after December 31, 2003.

In March 2001, we acquired Q-DOT Group, Inc. Q-DOT Group specializes in advanced technology research and development for data acquisition, signal processing, imaging and data communications. Their projects are supported by "conventional" government and commercial contracts in addition to government contracts sponsored by the Small Business Innovation Research program. We operate Q-DOT Group's government contract research and development operations as our wholly owned subsidiary. This acquisition was intended to enable us to enter the high speed data communications market, addressing both wired and wireless applications, based on advanced "silicon germanium" process technology.

As of September 30, 2004, our backlog for released purchase orders was approximately $3,238,000, all of which is expected to ship by March 31, 2005. Orders are cancelable without penalty at the option of the purchaser prior to 30 days before scheduled shipment and, therefore, are not necessarily a measure of future product revenue.

We are in production of our family of memory products. Our 256 kilobit nonvolatile static random access memory product was qualified by our internal quality organization to the product's data sheet and in accordance with accepted industry standard practices in 1997 for sales into commercial and industrial markets and in 1998 for shipment into the military market. During 2002, we designed and qualified a 3 volt version of our 256 kilobit nonvolatile static random access memory product for sale into commercial and industrial markets. During the second quarter of 2004, we qualified our 256 kilobit 3 volt nonvolatile static random access memory, produced on wafers received from Chartered's facility #2, for use in commercial and industrial applications. Our 64 kilobit nonvolatile static random access memories have been qualified for sale into commercial, industrial and military markets. Our 16 kilobit and 4 kilobit nonvolatile static random access memory products have been qualified for sales into commercial and industrial markets. During 2003, we designed and began sampling of our 1 megabit nonvolatile static random access memory product for sale into commercial and industrial markets. We are currently shipping production-tested 1 megabit products under a provisional qualification. We anticipate that this qualification will be complete in the fourth quarter of 2004. Our nonvolatile static random access memory products are physically smaller and require less maintenance than static random access memory devices that achieve nonvolatility through the use of internal batteries and are more convenient to use than static random access memory devices that achieve nonvolatility by being combined with additional chips. We have merged our logic design engineers into our memory design group in order to incorporate unique features into our next generation memory products currently under development.

We reduce capital requirements by subcontracting the majority of the manufacturing process. Chartered began providing silicon wafers for our nonvolatile static random access memory products in September 1993 and continues to provide wafers based on our product technology. Chartered closed its wafer fabrication facility #1 in March 2004. We entered into a Process Transfer Agreement with X-FAB to install our Silicon Nitride Oxide Semiconductor

technology into its wafer fabrication facility to provide an additional manufacturing source to material supplied by Chartered. Due to a lack of our and X-FAB's resources required to install our nonvolatile semiconductor memory process into X-FAB and the marginal anticipated return-on-investment, we have ceased the installation of our nonvolatile semiconductor memory process into X-FAB's wafer fabrication facility in August 2004. We began receiving our memory wafers manufactured in Chartered's Facility #2 in late second quarter of 2004 and through the third quarter of 2004. However, with this process being transferred to an alternative manufacturing facility, we have seen lower than average production yields, which in turn has lowered our gross margins. We are continuing to work with Chartered to improve our production yields. If we cannot improve our production yields, it will have a material negative impact on our

future revenues and earnings. Please see "Risk Factors--If we cannot achieve acceptable manufacturing yields and continue production with Chartered of some of our memory products in its wafer fabrication facility #2, our revenues, earnings and stock price could suffer".

DongbuAnam Semiconductor provides silicon wafers for our 0.25 micron process to support our 1 megabit product family.

United Microelectronics and Chartered provided silicon wafers for our programmed semiconductor logic products based on 0.5 micron and 0.35 micron product technology, respectively. In February 2003, we received notification from United Microelectronics that it will be unable to supply us with logic wafers after August 2003. We supported customers with 0.5 micron logic wafers manufactured at United Microele