

LIQUIDMETAL TECHNOLOGIES INC
Form 10-K/A
July 20, 2006

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-K/A

Amendment No. 3

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

For the fiscal year ended December 31, 2004

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

For the transition period from _____ to _____

Commission File No. 000-31332

LIQUIDMETAL TECHNOLOGIES, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or
organization)

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

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25800 Commercentre Drive, Suite 100
Lake Forest, California 92630

(address of principal executive office, zip code)

Registrant's telephone number, including area code: (949) 206-8000

Securities registered pursuant to Section 12(b) of the Act: **None**

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

Title of each Class
Common Stock, \$.001 par value

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes No

The aggregate market value of the registrant's Common Stock held by non-affiliates of the registrant as of June 30, 2004 was approximately \$34,793,699. For purposes of this calculation only, (i) shares of Common Stock are deemed to have a market value of \$1.42 per share, the closing price of the Common Stock as reported on the Nasdaq National Market on June 30, 2004, and (ii) each of the executive officers, directors and persons holding more than 10% of the outstanding Common Stock as of June 30, 2004 is deemed to be an affiliate.

LIQUIDMETAL TECHNOLOGIES, INC.

Amendment No. 3 to the Annual Report on Form 10-K

For the Fiscal Year ended December 31, 2004

EXPLANATORY NOTE

We are filing this Amendment No. 3 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2004, as filed with the U.S. Securities and Exchange Commission (SEC) on March 30, 2005, as amended on May 10, 2005 and on March 16, 2006, to restate our financial statements to properly account for the conversion feature of the senior convertible notes. Additionally, reclassifications to our financial statements have been made for consistent presentation of our warrant liabilities, settlement payable, and change in value of warrant liabilities.

Other than the changes referred to above, all other information included in the above described Form 10-K, as amended, remains unchanged. This amendment does not reflect events occurring after the filing of such Form 10-K, as amended, and does not modify or update the disclosures therein in any way other than as required to reflect the amendment as described above and set forth below.

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PART I

Forward-Looking Statements

This annual report on Form 10-K of Liquidmetal Technologies, Inc. contains forward-looking statements that may state our management's current expectations, estimates, forecasts, and projections about the company and its business. Any statement in this report that is not a statement of historical fact is a forward-looking statement, and in some cases, words such as believe, estimate, project, expect, intend, may, anticipate, plans, seeks, and similar expressions identify forward-looking statements. Forward-looking statements involve risks and uncertainties that could cause actual outcomes and results to differ materially from the anticipated outcomes or result. These statements are not guarantees of future performance, and undue reliance should not be placed on these statements. It is important to note that Liquidmetal Technologies, Inc.'s actual results could differ materially from what is expressed in our forward-looking statements due to the risk factors described in the section of this report entitled "Factors Affecting Future Results," as well as the following risks and uncertainties:

- Our history of losses and uncertainty surrounding our ability to achieve profitability;
- Our limited history of manufacturing products from bulk amorphous alloys;
- Lengthy customer adoption cycles and unpredictable customer adoption practices;
- Our ability to identify, develop, and commercialize new product applications;
- Competition from other materials;
- Our ability to consummate strategic partnerships in the future;
- The potential for manufacturing problems or delays;
- Potential difficulties associated with protecting or expanding our intellectual property position; and
- Pending shareholder litigation against our company

Liquidmetal Technologies, Inc. undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Item 1. Business

Overview

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

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

General Corporate Information

We were originally incorporated in California in 1987, and we reincorporated in Delaware in May 2003. Our principal executive offices are located at 25800 Commercentre Dr., Suite 100, Lake Forest, California 92630. Our telephone number at that address is (949) 206-8000. Previously, our principal executive offices were located in Tampa, Florida. In December 2003, we consolidated all corporate functions into our Lake Forest facility, which had previously served as our principal research and development office. Our Internet website address is www.liquidmetal.com and all of our filings with the Securities and Exchange Commission are available free of charge on our website.

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Our Technology

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

Unique Atomic Structure

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

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

Proprietary Material Composition

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

Advantages of Liquidmetal Alloys

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

Performance Advantages

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

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

Processing Advantages

The processing of a material generally refers to how a material is shaped, formed, or combined with other materials to create a finished product. Bulk Liquidmetal alloys possess processing characteristics that we believe make them preferable to other materials in a wide variety of applications. In particular, our alloys are amenable to processing options that are similar in many respects to those associated with plastics. For example, we believe that bulk Liquidmetal alloys have superior net-shape casting capabilities as compared to high-strength crystalline metals and alloys. Net-shape casting is a type of casting that permits the creation of near-to-net shaped products that do not require much costly post-cast processing or machining. Additionally, unlike most metals and alloys, our bulk Liquidmetal alloys are capable of being thermoplastically molded in bulk form. Thermoplastic molding consists of heating a solid piece of material until it is transformed into a moldable state, although at temperatures much lower than the melting temperature, and then introducing it into a mold to form near-to-net shaped products. Accordingly, thermoplastic molding can be beneficial and economical for net shape fabrication of high-strength products.

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

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

Cost Advantages

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

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

Our Strategy

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

- *Identifying and Developing New Applications for Our Liquidmetal Alloy Technology.* We intend to continue to identify and develop new applications that will benefit from the performance, processing, and cost advantages of Liquidmetal alloys.
- *Focusing Our Marketing and Internal Manufacturing Activities on Select Products with Expected Higher Gross-Margins.* We intend to focus our marketing and internal manufacturing activities on select products with anticipated higher gross margins. This strategy is designed to align our product development initiatives with our manufacturing processes and manufacturing cost structure, and to reduce our exposure to more commodity-type product applications that are prone to unpredictable demand and fluctuating pricing. Our focus is primarily on higher-margin products that possess design features that take optimal advantage of our existing and developing manufacturing technology and that command a price commensurate with the performance advantages of our alloys. In addition to our focus on products with higher gross margins, we will continue to engage in prototype manufacturing, both for internally manufactured products and for products that will ultimately be licensed to or manufactured by third parties.
- *Further Developing Our Manufacturing Processes, Capabilities, and Efficiencies for Bulk Liquidmetal Alloys.* We intend to improve and enhance our internal manufacturing processes, capabilities, and efficiencies in order to maintain quality control over products made from bulk Liquidmetal alloys, to focus on improvements to the processing of our alloys, and to protect our intellectual property. As our alloys become more pervasive, however, we expect to enter into additional strategic relationships that would involve the licensing of Liquidmetal technology to third parties for certain market segments.
- *Pursuing Strategic Partnerships In Order to More Rapidly Develop and Commercialize Products.* We intend to actively pursue and support strategic partnerships that will enable us to leverage the resources, strength, and technologies of other companies in order to more rapidly develop and commercialize products. These partnerships may include licensing transactions in which we license full commercial rights to our technology in a specific application area, or they may include transactions of a more limited scope in which, for example, we outsource manufacturing activities or grant distribution rights. We believe that utilizing such a partnering strategy will enable us to reduce our working capital burden, better fund product development efforts, better understand customer adoption practices, leverage the technical and financial resources of our partners, and more effectively handle product design and process challenges. As this partnering strategy evolves, a growing portion of our revenue mix may be comprised of revenue from the provision of product development services, technical support, and engineering services, as well as revenues from royalties on the sale of Liquidmetal alloy products by our partners.
- *Advancing the Liquidmetal® Brand.* We believe that building our corporate brand will foster continued adoption of our technology. Our goal is to position Liquidmetal alloys as a superior substitute for materials currently used in a variety of products across a range of industries. Furthermore, we seek to establish Liquidmetal alloys as an enabling technology that will facilitate the creation of a broad range of commercially viable new products. To enhance industry awareness of our company and increase demand for Liquidmetal alloys, we are reviewing various brand development strategies that could include collaborative advertising and promotional campaigns with select customers, industry conference and trade show appearances, public relations, and other means.

Initial Applications

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

Casings for Electronic Products

We produce casing components for electronic devices using our bulk Liquidmetal alloys and believe that our alloys offer enhanced performance and design benefits for these casings in certain applications. Bulk Liquidmetal alloys can be used for various structural components of a cellular phone, including the shield, faceplate, hinge, hinge housings, back plate, side plates, brackets, and the cover on the phones. We initially targeted the electronic casings market because of its potential for high product volumes and branding opportunities; however, unpredictable customer adoption practices, short product model lives, processing limitations, and intense pricing pressures make it very challenging to compete in this high-volume market. Accordingly, we are currently limiting our focus in this market to higher-margin applications that have the potential to benefit from the unique performance characteristics of bulk Liquidmetal alloys. We continue to believe that the high strength-to-weight ratio and elastic limit of bulk Liquidmetal alloys enable the production of stronger and thinner electronic devices as compared to plastic, zinc, and magnesium, and we intend to focus on products that require these design and performance benefits.

Through our shipments to date, we have demonstrated that bulk Liquidmetal alloys can be used for structural components of cellular phones and other electronic devices. During 2003 and 2004, we shipped production quantities of cell phone components to Samsung Electronics Company and Vertu Limited, the luxury communication products subsidiary of Nokia, for inclusion in various cellular phone models.

Sporting Goods and Leisure Products

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

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

In the leisure products category, we believe that bulk Liquidmetal alloys can be used to efficiently produce intricately engineered designs with high-quality finishes, such as premium watchcases, and we further believe that Liquidmetal alloy technology can be used to make high-quality, high-strength jewelry from precious metals. We have successfully produced prototype rings made from an amorphous Liquidmetal platinum alloy that is harder (and hence more scratch resistant) than conventional platinum jewelry. In 2003, a special-edition concept chronograph timepiece featuring our titanium-zirconium Liquidmetal alloy was showcased by luxury watchmaker TAG Heuer at the renowned Basel Watch and Jewelry Show in Basel, Switzerland. In 2004, we have begun prototyping various watch pieces with TAG Heuer and we expect to be ready to move into production in 2005.

In order to accelerate the commercialization of Liquidmetal alloys in the jewelry and high-end luxury products market, in June 2003 we entered into a strategic licensing transaction with LLPG, Inc., a corporation headed by a former director of our company with ties to the Swiss jewelry and luxury goods market. Under this agreement, LLPG was granted a 10-year exclusive worldwide license to manufacture and sell a variety of luxury goods, including watchcases and precious-metal jewelry, utilizing Liquidmetal alloys. Under the agreement, we are entitled to royalties over the life of the contract on all products produced and sold by LLPG.

Medical Devices

We are engaged in product development efforts relating to various medical devices that could be made from Liquidmetal alloys. We believe that the unique properties of bulk Liquidmetal alloys provide a combination of performance and cost benefits that could make them a desirable replacement to incumbent materials, such as stainless steel and titanium, currently used in various medical device applications. Our greatest emphasis in 2003 and ongoing in 2004 has been on surgical instrument applications for Liquidmetal alloys. These include, but are not limited to, specialized blades, orthopedic instruments utilized for implant surgery procedures, ultrasonic devices, dental devices, external fixation devices and general surgery devices. The potential value offered by our alloys is high performance in some cases and cost reduction in others, the latter stemming from the ability of Liquidmetal alloys to be net shape cast into components, thus reducing costs of secondary processing. The status of most components in the prototyping phase is subject to non-disclosure agreements with our customers.

We believe that our future success in the medical device market will be driven largely by strategically aligning ourselves with well-established companies that are uniquely positioned to facilitate the introduction of Liquidmetal alloys into this market, especially as it relates to the unique processing challenges and stringent material qualification requirements that are prevalent in this industry. We also believe that our prospects for success in this market will be enhanced through our focus on optimizing existing alloy compositions and developing new alloy compositions to satisfy the industry's rigorous material qualification standards. For example, we have been working with DePuy Orthopaedics, Inc., a Johnson & Johnson company, to develop an alloy for orthopedic implants and instruments in the knee replacement device market. Our agreement with DePuy gives them the exclusive worldwide right and license to market and sell knee replacement devices that incorporate Liquidmetal alloys. We are also in the early stages of working with other orthopedic companies to identify surgical instrument or device applications that would benefit from utilizing Liquidmetal alloys.

Industrial Coatings and Powders

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

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

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

Defense Applications

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

In addition to funding the Army KEP program in 2005, the Department of Defense Spending Bill for 2005 contains money to support the development of an advanced Liquidmetal alloy for use in aerospace applications. Lockheed Martin has joined Liquidmetal Technologies for this new program that will be managed by the U.S. Navy.

Liquidmetal is also working with NASA to conduct an experiment to use Liquidmetal alloys as the optical surface for spaced-based telescopes.

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

Liquidmetal Golf

From 1997 until September 2001, we engaged in the retail marketing and sale of golf clubs through a majority owned subsidiary, Liquidmetal Golf. The retail business of Liquidmetal Golf was discontinued in September 2001 and is now treated as a discontinued operation in our consolidated financial statements. Although the retail golf club business has been discontinued, Liquidmetal Golf will be engaged in the business of manufacturing and selling golf club components to golf original equipment manufacturers that will integrate these components into their own clubs and then sell them under their respective brand names. Liquidmetal Technologies owns 79% of the outstanding common stock in Liquidmetal Golf.

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

Our Intellectual Property

Our intellectual property consists of patents, trade secrets, know-how, and trademarks. Protection of our intellectual property is a strategic priority for our business, and we intend to vigorously protect our patents and other intellectual property. Our intellectual property portfolio includes 24 owned or licensed U.S. patents and numerous patent applications relating to the composition, processing, and application of our alloys, as well as various foreign counterpart patents and patent applications.

Our initial bulk amorphous alloy technology was developed by researchers at the California Institute of Technology (Caltech). We have purchased patent rights that provide us with the exclusive right to commercialize the amorphous alloy and other amorphous alloy technology acquired from Caltech through a license agreement (Caltech License Agreement) with Caltech. Under the Caltech license agreement, we have the exclusive worldwide right to make, use, and sell products from all of Caltech's inventions, proprietary information, know-how, and other technology relating to amorphous alloys existing as of September 1, 2001. We also have an exclusive worldwide license to nine issued patents and four patent applications held by Caltech relating to amorphous alloy technology, as well as all related foreign counterpart patents and patent applications. Of the patents currently issued to Caltech and licensed by us, the earliest expiration date is 2013 and the latest expiration date is 2021. Furthermore, the license agreement gives us the exclusive right to make, use, and sell products from substantially all amorphous alloy technology that is developed in Professor William Johnson's Caltech laboratory during the period September 1, 2001 through August 31, 2005.

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All fees and other amounts payable by us for these rights and licenses have been paid in full, and no further royalties, license fees, or other amounts will be payable in the future under this license agreement.

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

Under the license agreement, we have the right to sublicense any of the licensed technology or patents. The license agreement also provides that Caltech reserves the right to use the licensed technology and patents for noncommercial educational and research purposes. The patents and patent applications that we license from Caltech relate primarily to the composition and processing of our alloys. The currently issued U.S. patents covered by the license agreement will expire between 2013 and 2021.

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

In addition to the patents and patent applications that we license from Caltech, we are building a portfolio of our own patents to expand and enhance our technology position. These patents and patent applications primarily relate to various applications of our bulk amorphous alloys, the composition of our coatings and powders, and the processing of our alloys. The patents relating to our coatings expire on various dates between 2005 and 2017, and the patents relating to our bulk amorphous alloys expire on various dates between 2013 and 2021. Our policy is to seek patent protection for all technology, inventions, and improvements that are of commercial importance to the development of our business, except to the extent that we believe it is advisable to maintain such technology or invention as a trade secret.

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

Research and Development

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

- *Enhance Material Processing and Manufacturing Efficiencies.* We plan to continue research and development of processes and compositions that will decrease our cost of making products from Liquidmetal alloys.
- *Optimize Existing Alloys and Develop New Compositions.* We believe that the primary technology driver of our business will continue to be our proprietary alloy compositions. We plan to continue research and development on new alloy compositions to generate a broader class of amorphous alloys with a wider range of specialized performance characteristics. During 2003 and continuing into 2004, we have successfully expanded our portfolio of bulk amorphous alloys to include additional zirconium-titanium alloys, as well as alloys based on other metals, such as iron and platinum. Although these various compositions are at different stages of development and only a few are currently suitable for commercial use, we believe that a larger alloy portfolio will enable us to increase the attractiveness of our alloys as an alternative to incumbent materials and, in certain cases, drive down product costs. We also believe that our ability to optimize our existing alloy compositions will enable us to better tailor our alloys to our customers' specific application requirements.
- *Develop New Applications.* We will continue research and development of new applications for Liquidmetal alloys. We believe the range of potential applications will broaden by expanding the forms, compositions, and methods of processing of our alloys.

We conduct our research and development programs internally and also through strategic relationships that we enter into with third parties. Our internal research and development efforts are currently focused on product and process development. Our internal research and development efforts are conducted by a team of 21 scientists, engineers and researchers whom we either employ directly or engage as consultants. Included

among this team are Professor William Johnson, who discovered our initial bulk amorphous alloy at Caltech in 1993, and his graduate student at the time, Atakan Peker, who is employed as our Vice President of Technology. Professor Johnson was an employee of our company from October 2001 through December 2003 and then became a consultant to the Company. Professor Johnson continues to be a member of our board of directors.

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In addition to our internal research and development efforts, we enter into cooperative research and development relationships with leading academic institutions. Professor Johnson continues to supervise a laboratory at Caltech, and through our license agreement with Caltech, we have a continuing relationship with the other researchers in Professor Johnson's Caltech laboratory. We have also entered into research relationships with several other academic institutions for the conduct of research relating to the properties and characteristics of our alloys.

We have entered into development relationships with other companies for the purpose of identifying new applications for our alloys and establishing customer relationships with such companies. Some of our product development programs are partially funded by our customers. We are also engaged in negotiations with other potential customers regarding possible product development relationships. Our research and development expenses for the years ended December 31, 2004, 2003, and 2002 were \$1.5 million, \$8.8 million, and \$11.8 million, respectively.

Manufacturing

We currently own and operate a 166,000 square feet manufacturing facility in Pyongtaek, South Korea, which became operational in the third quarter of 2002. We opened a 14,400 square feet facility in Weihai, China in August 2004 to facilitate our bulk alloy manufacturing business. We believe that these facilities will meet our anticipated manufacturing needs for the foreseeable future, although these needs may change depending upon the actual and forecasted orders we receive for our products. We currently intend to develop supplemental research and development, prototyping and manufacturing capabilities elsewhere, including the United States, for purposes of meeting our long-term manufacturing needs and our customers' requirements. In December 2003, we entered into a license agreement with Florida Custom Mold, Inc., a Clearwater, Florida-based company that specializes in high-quality mold design and injection molding services, under which Florida Custom Mold is currently acting as a contract manufacturer to our company for purposes of producing prototypes of certain defense and medical products in the US.

Raw Materials

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

Customers

During 2004, four customers accounted for 10% or more of our revenue from continuing operations. Revenues from Charm Tech and Pntel, both of which are direct suppliers to Samsung, represented 62% of revenue from continuing operations for the year ended 2004. Also, revenues from defense related contracts with the United States of America represented 10% and Growell Metal represented 12% of revenue from continuing operations for the year ended 2004. During 2003, three customers accounted for 10% or more of our revenue from continuing operations. Revenue from Samsung represented 10% of revenue, revenue from LLPG, Inc. represented 12% and defense-related contracts with three departments of the United States of America represented 16% of revenue from continuing operations for the year ended December 31, 2003. During the year ended December 31, 2002, revenue from Samsung represented 15% of revenue while revenue earned on contracts with the government represented 16% of revenue from continuing operations. We expect that a significant portion of our revenue may continue to be concentrated in a limited number of customers, even as our bulk Liquidmetal alloy business grows.

Competition

We are not aware of any other company or business that manufactures, markets, distributes, or sells bulk amorphous alloys or products made from bulk amorphous alloys. We believe it would be difficult to develop a competitive bulk amorphous alloy without infringing our patents. However, we expect that our bulk Liquidmetal alloys will face competition from other materials, including metals, alloys, plastics and composites, which are currently used in the commercial applications that we pursue. Our alloys could also face competition from new materials that may be developed in the future, including new materials that could render our alloys obsolete.

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

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

Backlog

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

Sales and Marketing

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

Employees

As of December 31, 2004, we had 158 full-time employees. As of December 31, 2004, 55 of our Korean operation employees were represented by a labor union. We have not experienced any work stoppages and we consider our employee relations to be favorable.

Governmental Regulation

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

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

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

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

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

Factors Affecting Future Results

This report contains forward-looking statements (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on management's current expectations, estimates, forecasts, and projections about the Company and its business. In addition, other written or oral statements which constitute forward-looking statements may be made from time to time by or on behalf of Liquidmetal Technologies, Inc. Any statement in this report that is not a statement of historical fact is a forward-looking statement, and in some cases, words such as "believe," "estimate," "project," "expect," "intend," "may," "anticipate," "plans," "seeks," and similar expressions identify forward-looking statements. Forward-looking statements involve risks and uncertainties that could cause actual outcomes and results to differ materially from the anticipated outcomes or result. These statements are not guarantees of future performance, and undue reliance should not be placed on these statements. Liquidmetal Technologies, Inc. undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Factors that could cause actual results to differ materially from what is expressed or forecasted in our forward-looking statements include, but are not limited to, the following:

We have not sustained profitability and may incur losses in the future.

We had an accumulated deficit of approximately \$127.5 million at December 31, 2004. Of this accumulated deficit, \$44.5 million was attributable to losses generated by our discontinued equipment manufacturing and retail golf businesses through December 31, 2004. We may incur additional operating losses in the future. Consequently, it is possible that we may not achieve positive earnings and, if we do achieve positive earnings, we may not be able to achieve them on a sustainable basis.

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

We have marketed and sold industrial coatings to distributors in the coatings industry since 1987. Prior to the third quarter of 2002, our experience selling products made from bulk amorphous alloys has been limited to our discontinued retail golf business, which had a different marketing strategy than the one we are currently employing. Therefore, we have a relatively limited history of producing bulk amorphous alloy components and products on a mass-production basis. Many of our relationships with potential customers for bulk alloy products are at an early stage, and there can be no assurance that these customers will enter into purchase commitments with us.

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

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

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

To increase our revenue, we must establish and maintain relationships with customers that will incorporate our components and products into their finished goods. We expect to rely on the marketing, distribution, and, in some cases, the manufacturing, research, and development abilities of our customers to assist us in developing, commercializing, and marketing our products in different markets. Our future growth and success will depend in large part on our ability to enter into these relationships and the subsequent success of these relationships. If our products are selected for use in a customer's products, we still may not realize significant revenue from that customer if that customer's products are not commercially successful.

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

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

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

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

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

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

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

For the near future, we expect that a significant portion of our revenue will be concentrated in a limited number of customers. For example, for the year ended December 31, 2004, revenue from two customers represented approximately 62% of total revenue from continuing operations and for the year ended December 31, 2003, revenue from two customers represented approximately 26% of total revenue from continuing operations. A reduction, delay, or cancellation of orders from one or more of these customers or the loss of one or more customer relationships could significantly reduce our revenue. Unless we establish long-term sales arrangements with these customers, they will have the ability to reduce or discontinue their purchases of our products on short notice.

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

Our future revenue growth and ultimate profitability will depend in part on the ability of our customers to successfully market and sell their finished goods that incorporate our products. We will have little control over our customers' marketing and sales efforts. These marketing and sales efforts may be unsuccessful for various reasons, any of which could hinder our ability to increase revenue or achieve profitability. For example, our customers may not have or devote sufficient resources to develop, market, and sell their finished goods that incorporate our

products. Because we typically will not have exclusive sales arrangements with our customers, they will not be precluded from exploring and adopting competing technologies. Also, products incorporating competing technologies may be more successful for reasons unrelated to the performance of our customers' products or the marketing efforts of our customers.

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

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

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

The future growth and success of our bulk amorphous alloy business will depend in part on our ability to establish and retain a technological advantage over other materials for our targeted applications. For many of our targeted applications, we will compete with manufacturers of similar products that use different materials. For example, we have targeted the cellular phone casing market as an application for bulk Liquidmetal alloys. In this market, we believe we will compete with other manufacturers of cellular phone casings who use plastics or metal to construct their casings. In other markets, we will compete directly with suppliers of the incumbent material. In addition, in each of our targeted markets, our success will depend in part on the ability of our customers to compete successfully in their respective markets. Thus, even if we are successful in replacing an incumbent material in a finished product, we will remain subject to the risk that our customer will not compete successfully in its own market.

Future advances in materials science could render Liquidmetal alloys obsolete.

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

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

Our future growth and success will depend in part on our ability to retain key members of our management and scientific staff, particularly John Kang, our Chairman of the board of directors, Professor William Johnson, a member of our board of directors and a professor at Caltech, and Dr. Atakan Peker, our Vice President of Technology. We do not have key man or similar insurance on any of these individuals. If we lose their services or the services of other key personnel, our financial results or business prospects may be harmed. Additionally, our future growth and success will depend in part on our ability to attract, train, and retain scientific engineering, manufacturing, sales, marketing, and management personnel. We cannot be certain that we will be able to attract and retain the personnel necessary to manage our operations effectively. Competition for experienced executives and scientists from numerous companies and academic and other research institutions may limit our ability to hire or retain personnel on acceptable terms. In addition, many of the companies with which we compete for experienced personnel have greater financial and other resources than we do. Moreover, the employment of non-citizens may be restricted by applicable immigration laws.

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

As a part of our business strategy, we intend to pursue strategic partnering transactions that provide access to new technologies, products, markets, and manufacturing capabilities. These transactions could include licensing agreements, joint ventures, or even business combinations. For example, we may pursue transactions that will give us access to new technologies that are useful in connection with the composition, processing, or application of Liquidmetal alloys. We may not be able to successfully identify any potential strategic partnerships. Even if we do identify one or more potentially beneficial strategic partnering, we may not be able to consummate these transactions on favorable terms or obtain the benefits we anticipate from such a transaction.

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

We have relatively limited experience in manufacturing our products and may be required to manufacture a range of products in high volumes while ensuring high quality and consistency. Although we currently own and operate a 166,000 square feet and a 14,400 square feet manufacturing facilities in South Korea and China, respectively, we cannot guarantee that these facilities will be able to produce the intended products with production yields, quality controls, and production costs that provide us with acceptable margins or profitability or satisfy the requirements of our customers.

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

We expect that we will continue to manufacture a substantial portion of our initial bulk Liquidmetal alloy products in our South Korean facility. As a result, our manufacturing operations are subject to risks of political instability, including the risk of conflict between North Korea and South Korea and tensions between the United States and North Korea. In addition, we anticipate that sales to customers located outside of the United States will account for a significant portion of our revenue in future periods and that the trend of foreign customers accounting for an increasing portion of our total sales may continue. Specifically, we expect to continue to derive a significant amount of revenue from sales to customers located in Asia. A downturn in the economies of Asian countries where our products will be sold, particularly South Korea's economy, could materially harm our business.

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

- staffing and managing our manufacturing facility located in South Korea and post-processing facility located in China;
- product or material transportation delays or disruption, including the availability and costs of air and other transportation between our South Korean and Chinese facilities and the United States;
- political and economic instability, including instability involving North Korea;
- potentially adverse tax consequences;
- burden of complying with complex foreign laws and treaties; and
- trade protection laws, policies, and measures and other regulatory requirements affecting trade and investment, including loss or modification of exemptions for taxes and tariffs. Moreover, customers may sell finished goods that incorporate our components and products outside of the United States, which exposes us indirectly to additional foreign commerce risks.

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

We expect to conduct business in various foreign currencies and will be exposed to market risk from changes in foreign currency exchange rates and interest rates. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material adverse effect on our business, results of operations, and financial condition and could specifically result in foreign exchange gains and losses. The impact of future exchange rate fluctuations on our operations cannot be accurately predicted. To the extent that the percentage of our non-U.S. dollar revenue derived from international sales increases in the future, our exposure to risks associated with fluctuations in foreign exchange rates will increase further. Moreover, as a result of operating a manufacturing facility in South Korea, a substantial portion of our costs are and will continue to be denominated in the South Korean won. Adverse changes in the exchange rates of the South Korean won to the U.S. dollar will affect our costs of goods sold and operating margins and could result in exchange losses.

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

We have an exclusive license from Caltech to several patents and patent applications relating to amorphous alloy technology, and we have obtained several of our own patents. We also have the exclusive right to Caltech's inventions, proprietary information, know-how, and other technology relating to bulk amorphous alloys existing as of September 1, 2001. Our success depends in part on our ability to obtain and maintain patent and other proprietary right protection for our technologies and products in the United States and other countries. If we are unable to obtain or maintain these protections, we may not be able to prevent third parties from using our proprietary rights. Specifically, we must:

- protect and enforce our license agreement with Caltech and our own patents and intellectual property;
- exploit our license of the patented technology under our license agreement with Caltech as well as our own patents; and
- operate our business without infringing on the intellectual property rights of third parties.

Caltech owns several issued United States patents covering the composition and method of manufacturing of the family of Liquidmetal alloys. We also hold several United States and corresponding foreign patents covering the manufacturing processes of Liquidmetal alloys and their use. The patents relating to our coatings expire on various dates between 2005 and 2017, and those relating to our bulk amorphous alloys between 2013 and 2021. If we are unable to protect our proprietary rights prior to the expiration of these patents, we may lose the advantage we have established as being the first to market bulk amorphous alloy products. In addition, the laws of some foreign countries do not protect proprietary rights to the same extent as the laws of the United States, and we may encounter significant problems and costs in protecting our proprietary rights in these foreign countries.

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

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

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

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

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

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

In addition, the processing of beryllium, a minor constituent element of some of our alloys, can result in the release of beryllium into the workplace and the environment and in the creation of beryllium oxide as a by-product. Beryllium is classified as a hazardous air pollutant, a toxic substance, a hazardous substance, and a probable human carcinogen under environmental, safety, and health laws, and various acute and chronic health effects may result from exposure to beryllium. We are required to comply with certain regulatory requirements and to obtain a permit from the U.S. Environmental Protection Agency or other government agencies to process beryllium. Our failure to comply with present or future governmental regulations related to the processing of beryllium could result in suspension of manufacturing operations and substantial fines or criminal penalties.

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

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

Our future capital requirements will depend on the amount of cash generated by our operations. Our projections of cash flows from operations and, consequently, future cash needs are subject to substantial uncertainty. If our available funds and cash generated from operations are insufficient to satisfy our liquidity requirements, we may need additional funds in the future to support our working capital requirements and for other purposes, and we may seek to raise additional funds through public or private equity financing, bank debt financing, or from other sources. Adequate funds may not be available when needed or may not be available on favorable terms. If we raise additional funds by issuing equity securities, existing shareholders may be diluted. If funding is insufficient at any time in the future, we may not be able to develop or enhance our products or services, take advantage of business opportunities, or respond to competitive pressures, any of which could harm our business.

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

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

- authorize our board of directors, without shareholder approval, to issue up to 10,000,000 shares of blank check preferred stock that could be issued by our board of directors to increase the number of outstanding shares and prevent a takeover attempt;
- limit shareholders' ability to call a special meeting of our shareholders;
- provide for a classified board of directors; and

- establish advance notice requirements to nominate directors for election to our board of directors or to propose matters that can be acted on by shareholders at shareholder meetings.

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

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

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

Our stock price may experience volatility.

The trading price of our common stock could fluctuate widely due to:

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

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

Item 2. Properties

Our principal executive offices and principal research and development offices are located in Lake Forest, California and consist of approximately 30,000 square feet. This facility is occupied pursuant to a lease agreement that expires in June 2007. Prior to December 31, 2003, our principal executive offices were located in Tampa, Florida; however, as an outgrowth of various cost reduction measures in the fourth quarter of 2003, activities of the Tampa office were transferred to and consolidated with the Lake Forest office. In Conroe, Texas, we lease an office and warehouse for our coatings business segment. This facility, which is approximately 10,000 square feet, is leased through September 2006.

Our principal prototyping and manufacturing facility is in Pyongtaek, South Korea, and consists of approximately 166,000 square feet. We lease the land on which this facility is located, although we own the buildings, fixtures, and all personal property located on the land. The parcel of land consists of approximately four acres and is leased through 2022. We currently expect that this facility will meet our anticipated internal manufacturing needs for the foreseeable future. Until June 2004 we also leased a facility in Incheon, South Korea, where an equipment manufacturing division of the Company assembled die casting equipment. This facility is approximately 22,430 square feet, and its lease expired in February 2005; however, that die casting equipment division was divested as of June 14, 2004 and the lease was terminated. On August 2004, we entered into a 3 year lease for a post-processing facility located in Wehai, China, which consists of approximately 14,400 square feet, to facilitate our bulk alloy manufacturing.

Item 3. Legal Proceedings

Liquidmetal Technologies and certain of its present and former officers and directors were named as defendants in nine purported class action complaints filed in the United States District Courts for the Middle District of Florida, Tampa Division, and the Central District of California, Southern Division, alleging violations of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. In August 2004, four complaints were consolidated in the United States District Court for the Middle District of Florida under the caption *Primavera Investors v. Liquidmetal Technologies, Inc., et al.*, Case No. 8:04-CV-919-T-23EAJ. John Lee, Chris Cowley, Dwight Mamanteo, Scott Purcell and Mark Rabold, were appointed co-lead plaintiffs (the Lead Plaintiffs). In September 2004, the other five complaints filed in the Central District of California were transferred to the Middle District of Florida for consolidation with the *Primavera Investors* action. The Lead Plaintiffs served their Consolidated Amended Class Action Complaint on January 12, 2005. The Amended Complaint alleges that the Prospectus issued in connection with the Company's initial public offering in May 2002 contained material misrepresentations and omissions regarding the Company's historical financial condition and regarding a personal stock transaction by the Company's chief executive officer. The Lead Plaintiffs further generally allege that during the proposed Class Period of May 21, 2002, through May 13, 2004, the defendants engaged in improper revenue recognition with respect to certain of the Company's business transactions, failed to maintain adequate internal controls, and knowingly disclosed unrealistic but favorable information about market demand for and commercial viability of the Company's products to artificially inflate the value of the Company's stock. The Amended Complaint seeks unspecified compensatory damages and other relief. Defendants' motion to dismiss will be due on March 28, 2005. We intend to vigorously defend against the class action. We cannot currently predict the impact or resolution of this litigation or reasonably estimate a range of possible loss, which could be material. The resolution of this lawsuit may harm our business and have a material adverse impact on our financial condition.

In addition to the above, certain present and former officers and directors of Liquidmetal Technologies, as well as Liquidmetal Technologies as a nominal defendant, have been named in three shareholder derivative actions. Two shareholder derivative complaints were filed in California state court styled *Brian Clair, Derivatively on Behalf of Liquidmetal Technologies, Inc. v. John Kang, et al.*, Case No. 04CC00551, and *Joseph Durgin Derivatively on Behalf of Liquidmetal Technologies, Inc. v. John Kang, et al.*, Case No. 04CC00553, both commenced in the Superior Court of Orange County, California. A third shareholder derivative complaint was filed in Florida federal court styled *Robert Story v. John Kang, et al.*, Case No. 8:04-CV-1587-T23TBM, commenced in the Middle District of Florida, Tampa Division. These shareholder derivative lawsuits allege that the defendants breached various fiduciary duties and otherwise violated state law based primarily upon the same underlying facts and circumstances as alleged in the federal shareholder class action. The plaintiffs seek unspecified compensatory damages, restitution and disgorgement of profits, equitable and/or injunctive relief as permitted by law and other relief. The two shareholder derivative complaints in California state court have been consolidated. Plaintiffs served a Consolidated Shareholder Derivative Complaint on October 12, 2004. The defendants served a Demurrer to the Consolidated Shareholder Derivative Complaint on November 22, 2004, seeking dismissal of that complaint. At a hearing on February 10, 2005, the court sustained the demurrer, dismissing the Consolidated Shareholder Derivative Complaint but giving the plaintiffs 45 days within which to amend the complaint. The amended complaint is due on March 28, 2005. In the Florida derivative action, the Plaintiff filed a First Amended Shareholder Derivative Complaint on November 22, 2004. The Company's Motion to Dismiss was filed on December 20, 2004. Plaintiff's Response and Objection to the Motion to Dismiss was filed on February 4, 2005. We cannot anticipate when the Court will rule on the Motion to Dismiss. We intend to vigorously defend against the derivative actions. We cannot currently predict the impact or resolution of this litigation or reasonably estimate a range of possible loss, which could be material. The resolution of these lawsuits may harm our business and have a material adverse impact on our financial condition.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of our security holders during the fourth quarter of 2004.

PART II**Item 5. Market For Registrant's Common Equity and Related Stockholder Matters**

Prior to July 16, 2004, our common stock was quoted on the Nasdaq National Market under the symbol LQMT. On July 14, 2004, the Company was notified by the Nasdaq Listing Qualifications Panel that the Company's common stock would be delisted from the Nasdaq National Market effective with the open of business on Friday, July 16, 2004. The Company was delisted for its failure to comply with Marketplace Rule 4310(c)(14) due to the Company's inability to file its Form 10-K for the fiscal year 2003 and Form 10-Q for the first quarter of 2004. As of July 19, 2004, the shares of Liquidmetal Technologies, Inc. common stock commenced trading in the Over the Counter (OTC) Pink Sheets Market under the symbol LQMT.PK. On January 13, 2005, the Company filed its Form 10-Q for the third quarter of 2004 and thus, became current on its filings. Subsequently, the Company filed the necessary forms with Nasdaq and is currently working with them to be listed on the Nasdaq (OTC) bulletin boards.

The following table sets forth, for the periods indicated, the high and low sale prices for our common stock as reported by The Nasdaq National Market:

| | Fiscal 2004 | |
|----------------|--------------------|------------|
| | High | Low |
| Fourth Quarter | \$ 4.00 | \$ 1.75 |
| Third Quarter | \$ 2.33 | \$ 0.71 |
| Second Quarter | \$ 3.68 | \$ 0.55 |
| First Quarter | \$ 4.52 | \$ 2.50 |

The closing price of our common stock as reported on The OTC Pink Sheets Market on February 1, 2005 was \$1.55 per share. As of February 1, 2005, there were 238 holders of record of our common stock.

We have never paid a cash dividend on our common stock. We do not anticipate paying any cash dividends on our common stock in the foreseeable future, and we plan to retain our earnings to finance future growth.

Item 6. Selected Consolidated Financial Data

We derived the selected consolidated financial data below as of and for each of the three years in the period ended December 31, 2004 from our audited consolidated financial statements and related notes thereto included elsewhere in this annual report on Form 10-K. The following selected consolidated financial data should be read in conjunction with Liquidmetal Technologies, Inc.'s consolidated financial statements and the related notes thereto, and Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this annual report on Form 10-K. In addition, readers should note the following information regarding the selected historical consolidated financial data presented below.

We have restated our previously reported consolidated financial statements for the fiscal year ended December 31, 2004 to properly account for the conversion feature of the senior convertible notes. The restatement adjustments resulted in a cumulative net reduction of shareholders' equity by \$4.7 million as of December 31, 2004 and an increase in previously reported net loss by \$2.2 million for the year ended December 31, 2004 (see Note 15). We have restated our previously reported consolidated financial statements for the fiscal years ended December 31, 2002 and 2001. The restatement adjustments resulted in a cumulative net reduction to shareholders' equity of \$2.0 million as of December 31, 2002 and an increase in previously reported net loss of \$1.1 million and \$0.9 million for the years ended December 31, 2002 and 2001, respectively. Further, the 2003, 2002, and 2001 balances from our 10-K filed on November 10, 2004 have been restated in order to conform with the presentation of 2004 financial statements as a result of application of SFAS 144 over discontinued operations of our equipment manufacturing business (see Note 18). The selected consolidated financial data presented below includes all such restatements.

See Note 2 in the notes to consolidated financial statements included in this annual report on Form 10-K and in the fiscal 2003 annual report on Form 10-K filed on November 10, 2004, which reflects the restatements of prior year transactions.

| | For the Years Ended December 31, | | | | |
|---|---------------------------------------|--------------|--------------|--------------|-------------|
| | 2004 | 2003 | 2002 | 2001 | 2000 |
| | (Restated) | | (Restated) | (Restated) | (Unaudited) |
| | (In thousands, except per share data) | | | | |
| Consolidated Statement of Operations Data: | | | | | |
| Revenue | \$ 17,429 | \$ 13,658 | \$ 9,138 | \$ 3,882 | \$ 4,200 |
| Cost of sales | 12,168 | 18,162 | 5,656 | 1,924 | 1,983 |
| Gross profit (loss) | 5,261 | (4,504) | 3,482 | 1,958 | 2,217 |
| Operating expenses: | | | | | |
| Selling, general and administrative | 11,591 | 17,729 | 13,099 | 5,239 | 1,449 |
| Research and development | 1,467 | 8,780 | 11,825 | 1,726 | 455 |
| Impairment of goodwill | | 184 | | | |
| Impairment of long lived assets | | 2,684 | | | |
| Total operating expenses | 13,058 | 29,377 | 24,924 | 6,965 | 1,904 |
| (Loss) income before interest, other income, income taxes, minority interest and discontinued operations | (7,797) | (33,881) | (21,442) | (5,007) | 313 |
| Loss from extinguishments of debt | (2,941) | | | | |
| Change in value of warrants, gain | 747 | | | | |
| Change in value of conversion feature, gain | 2,093 | | | | |
| Other income | 302 | | | | |
| Interest expense, net | (6,540) | (86) | (603) | (1,095) | (188) |
| Gain on sale of marketable securities held-for-sale | | 1,178 | 832 | | |
| (Loss) before income taxes, minority interest and discontinued operations | (14,136) | (32,789) | (21,213) | (6,102) | 125 |
| Income taxes | | | | | |
| Minority interest in loss of consolidated subsidiary | | 21 | 118 | | |
| (Loss) income from continuing operations | (14,136) | (32,768) | (21,095) | (6,102) | 125 |
| (Loss) income from operations of discontinued operations, net | (749) | (964) | 83 | (5,973) | (8,938) |
| Gain (loss) from disposal of discontinued operations, net | | 127 | 1,556 | (11,949) | |
| Net (loss) | \$ (14,885) | \$ (33,605) | \$ (19,456) | \$ (24,024) | \$ (8,813) |
| (Loss) income per share from continuing operations basic and diluted | \$ (0.34) | \$ (0.79) | \$ (0.54) | \$ (0.18) | \$ 0.00 |
| Weighted average common shares used to compute income (loss) per share from continuing operations basic and diluted | 41,610 | 41,505 | 38,714 | 33,323 | 30,884 |

| | As of December 31, | | 2002 | 2001 | 2000 |
|--|---------------------------------------|----------|------------|------------|-------------|
| | 2004 | 2003 | (Restated) | (Restated) | (Unaudited) |
| | (in thousands, except per share data) | | | | |
| Consolidated Balance Sheet Data: | | | | | |
| Cash and cash equivalents | \$ 742 | \$ 3,127 | \$ 25,058 | \$ 2,230 | \$ 124 |
| Restricted cash | 754 | | | | |
| Marketable securities held-for-sale | | | 3,068 | | |
| Working capital (deficiency) | (14,910) | (698) | 24,845 | (9,573) | (1,960) |
| Total assets | 28,508 | 30,852 | 27,772 | 6,680 | 1,945 |
| Long-term debt and capital leases, including current portion | 9,672 | 4,360 | 93 | 2,988 | 2,506 |
| Shareholders' equity (deficiency) | 4,191 | 16,163 | (50,599) | (7,504) | (3,680) |

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

This management's discussion and analysis should be read in the conjunction with the condensed consolidated financial statements and notes included elsewhere in this report on Form 10-K.

This management's discussion and analysis, as well as other sections of this report on Form 10-K, may contain forward-looking statements that involve risks and uncertainties, including statements regarding our plans, future events, objectives, expectations, forecasts, or assumptions. Any statement that is not a statement of historical fact is a forward-looking statement, and in some cases, words such as believe, estimate, project, expect, intend, may, anticipate, plans, seeks, and similar expressions identify forward-looking statements. These statements involve risks and uncertainties that could cause actual outcomes and results to differ materially from the anticipated outcomes or results, and undue reliance should not be placed on these statements. These risks and uncertainties include, but are not limited to, the matters discussed under the caption Factors Affecting Future Results in Item 1 of this report and other risks and uncertainties discussed in filings made with the Securities and Exchange Commission (including risks described in subsequent reports on Form 10-Q, Form 10-K, Form 8-K, and other filings). Liquidmetal Technologies, Inc. disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

OVERVIEW

We are a materials technology company that develops and commercializes products made from amorphous alloys. Our Liquidmetal® family of alloys consists of a variety of coatings, powders, bulk alloys, and composites that utilize the advantages offered by amorphous alloy technology. We develop, manufacture, and sell products and components from bulk amorphous alloys that are incorporated into the finished goods of our customers, and we also market and sell amorphous alloy industrial coatings. We also partner with third-party licensees and distributors to develop and commercialize Liquidmetal alloy products. We have the exclusive right to develop, manufacture, and sell what we believe are the only commercially viable bulk amorphous alloys.

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

Our revenues are derived from two principal operating segments: Liquidmetal alloy industrial coatings and bulk Liquidmetal alloy products. Liquidmetal alloy industrial coatings are used primarily as a protective coating for industrial machinery and equipment, such as drill pipe used by the oil drilling industry and boiler tubes used in coal-burning power plants. The historical operating information for fiscal year 2001 is based substantially on sales of Liquidmetal alloy coatings. In the second half of 2002, we began producing bulk Liquidmetal alloy components and products for incorporation into our customers' finished goods. Bulk Liquidmetal alloy segment revenue includes sales of parts or components of electronic devices, medical products, and sports and leisure goods; tooling and prototype parts (including demonstration parts and test samples) for customers with products in development; metal processing equipment (see Note 18 for disclosure regarding the disposal of our equipment manufacturing business); and research and development revenue relating primarily to defense and medical applications. We expect that these sources of revenue will continue to significantly change the character of our revenue mix.

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

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

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

Impairment of goodwill represents the write-down of the goodwill balance of Dongyang Yudoro (Dongyang), our 51% owned subsidiary in South Korea. During 2003, Dongyang experienced net losses as a result of a continuing economic downturn in markets for its machinery products. These events, along with Dongyang's operating cash flow losses and uncertainty surrounding its future cash flows, led us to evaluate our investment for recoverability as of December 31, 2003. As a result, we determined that the carrying value of our investment in Dongyang exceeded its fair value as of December 31, 2003 in the amount of \$184. In March 2004, we sold our 51% investment in Dongyang to the 49% minority shareholder.

Impairment of Long-Lived Assets consists of a write-down of the building of our manufacturing facility in South Korea on the basis that the fair value of this building was determined to be less than the book value as of December 31, 2003. Our significant operational difficulties in 2003 along with our history of operating or cash flow losses and uncertainty surrounding our future cash flows, led us to evaluate our long-lived assets for recoverability as of December 31, 2003. As a result, we determined that the carrying value of our manufacturing plant in Pyongtaek, South Korea exceeded its fair value as of December 31, 2003 in the amount of \$2,684. The fair value of the building was based on the average of two independent appraisals of the building obtained in the first quarter of 2004.

In conjunction with the divestiture of our Dongyang and Taesung subsidiaries in March and June 2004, respectively, the Company decided to discontinue our equipment manufacturing business in order to conform our operations to our broader corporate business strategy (see Note 18). Pursuant to Accounting Principles Board Opinion No. 30, *Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*, we reclassified our consolidated financial statements to reflect the discontinuation of our equipment manufacturing operations. The revenue, costs and expenses, assets and liabilities, and cash flows of the equipment manufacturing business were segregated in our accompanying Consolidated Balance Sheets, Consolidated Statements of Operations and Comprehensive Loss, and Consolidated Statements of Cash Flows.

We have restated our previously issued financial statements for the fiscal year ended December 31, 2004 due to an error related to our accounting for the embedded convertible feature of the senior convertible notes issued in March 2004, which were exchanged in August 2004, in accordance with Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities*, (SFAS 133).

The correction of the error to properly state the fair value of the embedded conversion feature of the senior convertible notes in accordance with SFAS 133 resulted in recognition of \$7.6 million as a conversion feature liability as of the issuance of the senior convertible notes in March 2004 as the convertible notes are considered a non-conventional convertible debt instrument. The correction resulted in recognition of the change in fair value of the embedded conversion feature in the our earnings as a gain of \$2.1 million for the year ended December 31, 2004, as well as adjustments to amortization of debt discount as interest expense of \$3.0 million for the year ended December 31, 2004, and an additional loss on extinguishment of debt of \$1.9 million for the year ended December 31, 2004. Additionally, we recognized \$0.9 million in additional paid in capital from redemption and conversion of convertible notes as of December 31, 2004, respectively.

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

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

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

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On August 4, 2004, the Company established a sub-assembly plant in the city of Weihai in Shandong province of China under Weihai Liquidmetal Company Limited, which is 100 percent owned by Liquidmetal Korea, to facilitate our bulk alloy manufacturing business. Weihai Liquidmetal is consolidated into Liquidmetal Technologies with all intercompany transactions eliminated.

The following discussion and analysis of our financial condition and results of operations focuses on the historical results of our continuing operations and reflects the effect of restating our 2002 and 2003 (2003 quarterly filings) financial statements for proper revenue recognition as disclosed in Note 2 in the notes to the consolidated financial statements in the fiscal 2003 annual report on Form 10-K filed on November 10, 2004.

Results of Operations

Comparison of the years ended December 31, 2004 and 2003

Revenue. Revenue increased to \$17.4 million in the twelve months ended December 31, 2004 from \$13.7 million in the twelve months ended December 31, 2003. The increase was due to increases in revenue earned by our bulk Liquidmetal alloy and coatings segments in the twelve months ended December 31, 2004. This increase in revenue consisted of \$3.8 million from the sale and prototyping of parts manufactured from bulk Liquidmetal alloys, offset by a decrease of \$1.9 million from research and development services related primarily from reduced activity from defense and medical applications. Our coatings business contributed \$1.0 million to the increase in revenues as compared to the twelve months ended December 31, 2003 from increased demand for drill pipe coatings.

Cost of Sales. Cost of sales decreased to \$12.2 million, or 70% of revenue, during the twelve months ended December 31, 2004 from \$18.2 million, or 133% of revenue, in the twelve months ended December 31, 2003. This decrease was a result of the continued maturing of our manufacturing process and represents the Company's efforts to manage costs and focus on our core business while continuing to build production pipeline and manufacturing infrastructure required to prepare for and support the anticipated growth of our bulk Liquidmetal alloy business. The cost of sales for the products sold by the coatings business segment is generally consistent from year to year because the Liquidmetal coatings products are produced by third parties and sold wholesale to various industries.

Selling, General, and Administrative Expenses. Selling, general, and administrative expenses decreased to \$11.6 million, or 66% of revenue, in the twelve months ended December 31, 2004 from \$17.7 million, or 130% of revenue, in the twelve months ended December 31, 2003. This decrease was primarily a result of decrease in wages and related expense by \$5.0 million, decreases in travel and communication expenses by \$0.8 million, decreases in rent by \$0.8 million, decrease in relocation expenses by \$0.7 million, offset by an increase in professional fees, consultant fees, and contract services by \$0.8 million, and an increase in insurance costs by \$0.4 million. These and other decreases in selling, general and administrative expenses represent the Company's efforts to manage costs and focus on our core business while continuing to build our corporate infrastructure required to prepare for and support the anticipated growth of our bulk Liquidmetal alloy business.

Research and Development Expenses. Research and development expenses decreased to \$1.5 million, or 8% of revenue, in the twelve months ended December 31, 2004 from \$8.8 million, or 64% of revenue, in the twelve months ended December 31, 2003. The decrease was primarily a result of decreases in salaries, wages and the related expenses by \$3.0 million, decrease in laboratory and prototyping expenses by \$2.0 million, decrease in depreciation expense by \$0.7 million, decrease in professional fees, consultant fees, and contract services by \$0.6, decrease in research grants by \$0.3 million, and decrease in travel related expenses by \$0.2 million. The decreases were a result of the Company focusing primarily on our core business associated with our bulk Liquidmetal alloy business while managing our costs. The Company continues to perform research and development efforts on new Liquidmetal alloys and related processing capabilities, develop new manufacturing techniques, and contract with consultants and provide research grants to various institutions to advance the development of Liquidmetal alloys.

Impairment of Goodwill. Impairment of goodwill was \$184, or 1% of revenue, in the twelve months ended December 31, 2003. Impairment of goodwill represents the write-down of the goodwill balance of Dongyang Yudoro (Dongyang), our 51% owned subsidiary in South Korea. During 2003, Dongyang experienced net losses as a result of a continuing economic downturn in the market for its machinery products. These events along with Dongyang s operating, and cash flow losses, and uncertainty surrounding its future cash flows, led us to evaluate our investment for recoverability as of December 31, 2003. As a result, we determined that the carrying value of our investment in Dongyang exceeded its fair value as of December 31, 2003 in the amount of \$184. In March 2004, we sold our 51% investment in Dongyang to the 49% minority shareholder (see Note 18). There was no impairment charge to goodwill in the twelve months ended December 31, 2004.

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Impairment of Long Lived Assets. Impairment of long lived assets was \$2.7 million, or 20% of revenue, in the twelve months ended December 31, 2003. Impairment expense represents a write-down of the building of our manufacturing facility in South Korea. Due to the decreased production and usage of our Pyongtaek manufacturing operation, we decided to obtain independent appraisals as to the fair value of this building. Accordingly, the fair value of the building as determined by the average of the two independent appraisals was less than the carrying value of the building as of December 31, 2003. There was no impairment charge to long lived assets in the twelve months ended December 31, 2004.

Loss from Extinguishment of Debt. Loss from extinguishment of debt was \$2.9 million, or 17% of revenue, during the twelve months ended December 31, 2004 due to the extinguishment of our March Notes as it relates to the exchange in August 2004. There was no such loss recorded during twelve months ended December 31, 2003.

Change in Value of Warrants. Change in value of warrants was a net gain of \$0.7 million, or 4% of revenue, during the twelve months ended December 31, 2004 from the change in valuation of warrant payable issued related to the senior convertible debt funded in March 2004, which was exchanged in August 2004 (see Note 15). There were no such amounts recorded for the twelve months ended December 31, 2003.

Change in Value of Conversion Feature. Change in the value of our conversion feature liability from our senior convertible debt funded in March 2004 and exchanged in August 2004 resulted in a Change in value of conversion feature gain of \$2.1 million, or 12% of revenue, during the twelve months ended December 31, 2004, primarily due to fluctuations in our stock price (See Note 15). There were no such amounts recorded for the twelve months ended December 31, 2003.

Other Income. Other income was \$0.3 million, or 2% of revenue, during the twelve months ended December 31, 2004 from certain stock transactions with John Kang, our Chairman, President, and Chief Executive Officer during 2002 (see Note 24). There were no amounts recorded as other income for the twelve months ended December 31, 2003.

Interest Expense. Interest expense was \$6.6 million, or 38% of revenue, in the twelve months ended December 31, 2004 and was \$0.4 million, or 3% of revenue, in the twelve months ended December 31, 2003. During the twelve months ended December 31, 2004, the interest expense was primarily due to the interest accrued, amortization of debt discount and deferred issuance costs on new senior convertible debt originally sold on March 3, 2004 and exchanged in August 2004, and interest accrued on Kookmin Bank loan funded on February 4, 2003. During the twelve months ended December 31, 2003, interest expense was primarily due to interest accrued on the Kookmin Bank loan to our South Korean subsidiary made on February 4, 2003.

Interest Income. Interest income was \$37 for the twelve months ended December 31, 2004 for interest earned on certificate of deposits. Interest income was \$0.3 million or 2% of revenue for the twelve months ended December 31, 2003 for interest earned on short-term, investment grade, interest-bearing securities.

Gain from Sale of Investment. In April 2003 we sold our remaining shares of Growell Metal Co., Ltd. that were purchased in July 2002. We recognized a \$1.2 million gain on the sale of these shares during the twelve months ended December 31, 2003. There were no such gains in the twelve months ended December 31, 2004.

Comparison of the years ended December 31, 2003 and 2002

Revenue. Revenue increased to \$13.7 million in the twelve months ended December 31, 2003 from \$9.1 million in the twelve months ended December 31, 2002. The increase was due to increases in revenue earned by our bulk Liquidmetal alloy segment in the twelve months ended December 31, 2003. This increase in our bulk Liquidmetal alloy segment revenue consisted of a revenue increase of \$1.8 million from the sale of metal processing equipment in the US, an increase of \$0.1 million from the sale and prototyping of parts manufactured from bulk Liquidmetal alloys, and an increase of \$2.2 million from research and development services related primarily to defense and medical applications. The increase in revenue earned by our bulk Liquidmetal alloy segment was offset by a decrease of \$1.6 million in the revenue earned by our coatings business as compared to the twelve months ended December 31, 2002 due to a slowdown in demand for drill pipe coatings.

Cost of Sales. Cost of sales increased to \$18.2 million, or 133% of revenue, during the twelve months ended December 31, 2003 from \$5.7 million, or 62% of revenue, in the twelve months ended December 31, 2002. The cost of sales as a percentage of revenue increased due to three primary factors: first, a higher percentage of plant operating costs allocated to manufacturing in the current period, as opposed to the same twelve month period in 2002 when our manufacturing facility was in the final stages of construction and significant in-plant spending was directed to research and development to support the ramp-up of manufacturing operations; second, the impact of unprofitable electronic casing components and prototypes moving through our manufacturing mix; and third, the impact of the write-down of excess raw material in the amount of \$1.0 million and the write-down of raw material and equipment inventory in the amount of \$2.8 million in connection with a settlement of a dispute with Growell which was finalized in January 2004.

Although the cost to manufacture parts from our bulk Liquidmetal alloys is variable and differs based on the unique design of each product, we expect gross margin to improve as we limit production and prototyping to select products that require the high-performance qualities of Liquidmetal alloys and can be priced accordingly. Furthermore, we believe that strategic licensing agreements and other relationships to advance the development of our technology and processes that we will pursue could also contribute to improved gross margins. The cost of sales for the products sold by the coatings business is expected to remain generally consistent because Liquidmetal coatings products are produced by third parties and sold wholesale to various industries.

Selling, General, and Administrative Expenses. Selling, general, and administrative expenses increased to \$17.7 million, or 130% of revenue, in the twelve months ended December 31, 2003 from \$13.1 million, or 143% of revenue, in the twelve months ended December 31, 2002. This increase was primarily a result of costs incurred for closing our Tampa, Florida offices, which included: an increase in severance costs of \$2.2 million for releasing a substantial number of these employees as well as our expense and accrual of \$0.8 million for terminating our office lease, due to the determination that we will be unable to sublease this space over the remaining term; an increase in professional fees, consultant fees, and contract services of \$0.8 million; an increase in insurance expense of \$0.5 million; an increase in data communications expense of \$0.2 million; an increase in depreciation expense of \$0.3 million; an increase of warranty expense of \$0.5 million; and a \$0.3 million increase in expenses associated with the disposition of certain assets in the twelve months ended December 31, 2003. The increase in selling, general and administrative expenses are associated with the aforementioned cost reduction measures, including the consolidation of offices, the staff reductions, and a corresponding shift in strategy for the continued development of our bulk Liquidmetal alloy business. This was partially offset by a decrease in advertising expense of \$0.1 million; a decrease in bad debt expense of \$0.9 million; and a \$0.7 million decrease in stock compensation expense.

Research and Development Expenses. Research and development expenses decreased to \$8.8 million, or 64% of revenue, in the twelve months ended December 31, 2003 from \$11.8 million, or 129% of revenue, in the twelve months ended December 31, 2002. This decrease was partially a result of the maturing of our manufacturing process and related processing capabilities, the consolidation of our facilities into our California Technology Center, and the discontinuation of certain prototyping and developmental activities that occurred extensively while the Company was identifying our current technology capabilities and limitations. These decreases were partially offset by increases in providing research grants to various institutions to advance the development of Liquidmetal alloys. In the category of research and development expenses: travel decreased by \$0.2 million; professional fees, consultant fees, and contract services decreased by \$1.6 million; laboratory and prototyping expenses decreased by \$0.9 million; and stock compensation expense decreased by \$1.4 million. These expenses were partially offset by increases in depreciation of research equipment of \$0.4 million, increased research grants to educational institutions of \$0.1 million, and increase to salaries, wages and severance net of \$0.5 million.

Impairment of Goodwill. Impairment of goodwill represents the write-down of the goodwill balance of Dongyang Yudoro (Dongyang), our 51% owned subsidiary in South Korea. During 2003, Dongyang experienced net losses as a result of a continuing economic downturn in the market for its machinery products. These events along with Dongyang's operating, and cash flow losses, and uncertainty surrounding its future cash flows, led us to evaluate our investment for recoverability as of December 31, 2003. As a result, we determined that the carrying value of our investment in Dongyang exceeded its fair value as of December 31, 2003 in the amount of \$184. In March 2004, we sold our 51% investment in Dongyang to the 49% minority shareholder.

Impairment of Long Lived Assets. Impairment expense represents a write-down of the building of our manufacturing facility in South Korea. Due to the decreased production and usage of our Pyongtaek manufacturing operation, we decided to obtain independent appraisals as to the fair value of this building. Accordingly, the fair value of the building as determined by the average of the two independent appraisal was less than the carrying value of the building as of December 31, 2003.

Interest Expense. Interest expense was \$0.4 million, or 3% of revenue, in the twelve months ended December 31, 2003 and was \$1.1 million, or 12% of revenue, in the twelve months ended December 31, 2002. During the twelve months ended December 31, 2003, interest expense was primarily due to interest accrued on the Kookmin Bank loan to our South Korean subsidiary made on February 4, 2003. During the twelve months ended December 31, 2002, interest expense was primarily due to the amortization of the fair value of warrants granted in connection with subordinated promissory notes we issued in February 2001.

Interest Income. Interest income was \$0.3 million, or 2% of revenue, in the twelve months ended December 31, 2003 due to interest earned on short-term, investment grade, interest-bearing securities. During the twelve months ended December 31, 2002, interest income was \$0.5 million, or 6% of revenue, which was interest earned from the proceeds of our May 22, 2002 initial public offering.

Gain from Sale of Investment. In April 2003 we sold our remaining shares of Growell Metal Co., Ltd. that were purchased in July 2002. We recognized a \$1.2 million gain on the sale of these shares.

QUARTERLY RESULTS

The following information presents our unaudited quarterly operating results for 2004 and 2003. The data has been prepared by Liquidmetal Technologies, Inc. on a basis consistent with the Consolidated Financial Statements included elsewhere in this Form 10-K, and includes all adjustments, consisting of normal recurring accruals, that we consider necessary for a fair presentation thereof. Included in our 2003 fourth quarter results are costs charged to our cost of sales for the write-down of raw materials of \$1.0 million and a \$2.8 million write-down of inventory and equipment recorded in connection with a dispute settlement with Growell. In addition, as a result of the Company's cost reduction measures taken in the fourth quarter, our selling, general, and administrative expenses include severance costs of \$2.4 million and office relocation costs of \$0.8 million. These operating results are not necessarily indicative of our future performance.

During the fourth quarter of 2004, although our revenues were comparable to prior year, we had a decrease in revenue of \$2.1 million compared to the third quarter due to an unanticipated and temporary decrease in orders from one of our customers, Samsung. In addition, included in our fourth quarter cost of sales is a \$0.4 million charge related to certain hinge finished goods used in Samsung's cell phone models which were nearing its end of life. The Company experienced a gross loss of \$0.4 million for the fourth quarter due to the one time charge of cost of sales and also due to the fact that our cost of sales from our Liquidmetal bulk alloy segment includes primarily fixed costs from our labor and equipment expenses.

These statements should be read in conjunction with Note 2 in the notes to the consolidated financial statements hereto and Note 2 in the notes to consolidated financial statements in the fiscal 2003 annual report on Form 10-K filed on November 10, 2004, which reflects the restatements of prior year transactions.

Pursuant to Accounting Principles Board Opinion No. 30, *Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*, we reclassified our consolidated financial statements to reflect the discontinuation of our equipment manufacturing operations and retail golf business. The revenue, costs and expenses, assets and liabilities, and cash flows of the equipment manufacturing and our retail golf businesses were segregated in our accompanying Consolidated Balance Sheets, Consolidated Statements of Operations and Comprehensive Loss, and Consolidated Statements of Cash Flows. The net operating results, net assets, and net cash flows of the equipment manufacturing and retail golf businesses were reported as discontinued operations in our annual consolidated financial statements and in the condensed consolidated financial statements included in this report on Form 10-K. (see Note 18)

Consolidated Statements of Operations Data:

| | For the Three Months Ended | | | |
|---|--|-------------------|-------------------|-------------------|
| | 12/31/04 | 9/30/04 | 6/30/04 | 3/31/04 |
| | (Restated) | (Restated) | (Restated) | (Restated) |
| | (In thousands, except per share data) | | | |
| | (Unaudited) | | | |
| Revenue | \$ 2,471 | \$ 4,615 | \$ 4,055 | \$ 6,288 |
| Cost of sales | 2,895 | 3,241 | 2,475 | 3,557 |
| Gross profit (loss) | (424) | 1,374 | 1,580 | 2,731 |
| Operating expense: | | | | |
| Selling, general, and administrative | 2,413 | 3,569 | 2,544 | 3,065 |
| Research and development | 407 | 374 | 345 | 341 |
| Total operating expenses | 2,820 | 3,943 | 2,889 | 3,406 |
| Loss from operations | (3,244) | (2,569) | (1,309) | (675) |
| Loss on extinguishments of debt | | (2,941) | | |
| Change in value of warrants, (loss) gain | (99) | (434) | 694 | 586 |
| Change in value of conversion feature, (loss) gain | (1,183) | (2,338) | 3,904 | 1,710 |
| Other income (expense), net | | 302 | | |
| Interest income (expense), net | (640) | (3,283) | (2,233) | (384) |
| Income (loss) from operation before income taxes and discontinued operations | (5,166) | (11,263) | 1,056 | 1,237 |
| Income taxes | | | | |
| Income (loss) from continuing operations | (5,166) | (11,263) | 1,056 | 1,237 |
| Loss from discontinued operations, net of tax | | | (356) | (393) |
| Net income (loss) | \$ (5,166) | \$ (11,263) | \$ 700 | \$ 844 |
| Income (loss) per share from continuing operations basic and diluted | \$ (0.12) | \$ (0.27) | \$ 0.03 | \$ 0.03 |
| Weighted average common shares used to compute income / loss per share from continuing operations basic and diluted | 41,610 | 41,610 | 41,610 | 41,610 |

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| | For the Three Months Ended | | | |
|--|--|-------------|-----------------------|-----------------------|
| | 12/31/03 | 9/30/03 | 6/30/03 (Restated) | 3/31/03 (Restated) |
| | (In thousands, except per share data) (Unaudited) | | | |
| Revenue | \$ 2,645 | \$ 3,281 | \$ 4,533 | \$ 3,199 |
| Cost of sales | 6,761 | 4,595 | 4,146 | 2,660 |
| Gross profit (loss) | (4,116) | (1,314) | 387 | 539 |
| Operating expense: | | | | |
| Selling, general, and administrative | 5,435 | 3,661 | 4,571 | 4,062 |
| Research and development | 1,025 | 981 | 2,736 | 4,038 |
| Impairment of goodwill | 184 | | | |
| Impairment of long-lived assets | 2,684 | | | |
| Total operating expenses | 9,328 | 4,642 | 7,307 | 8,100 |
| Loss from operations | (13,444) | (5,956) | (6,920) | (7,561) |
| Interest income (expense), net | (86) | (53) | (12) | 65 |
| Gain on sale of marketable securities held-for-sale | | | 1,178 | |
| Loss from operations before income taxes, minority interest and discontinued operations | (13,530) | (6,009) | (5,754) | (7,496) |
| Income taxes | | | | |
| Minority interest in loss (income) of consolidated subsidiary | (5) | 23 | 10 | (7) |
| Loss from continuing operations | (13,535) | (5,986) | (5,744) | (7,503) |
| Income (loss) from discontinued operations | (412) | (115) | (317) | 7 |
| Net loss | \$ (13,947) | \$ (6,101) | \$ (6,061) | \$ (7,496) |
| Loss per share from continuing operations basic and diluted | \$ (0.33) | \$ (0.14) | \$ (0.14) | \$ (0.18) |
| Weighted average common shares used to compute loss per share from continuing operations basic and diluted | 41,610 | 41,610 | 41,597 | 41,390 |

LIQUIDITY AND CAPITAL RESOURCES

Our operating activities, including our discontinued equipment manufacturing operations, used cash of \$6.3 million for the year ended December 31, 2004. Our operating activities, including our discontinued equipment manufacturing and retail golf operations, used cash of \$26.5 million for the year ended December 31, 2003. Cash used in operating activities for the year ended December 31, 2004 resulted from net cash used by continuing operations of \$6.4 million offset by net cash provided by discontinued operations of \$0.1 million. Cash used in operating activities for the year ended December 31, 2003 resulted from net cash used by discontinued operations of \$2.4 million and net cash used by continuing operations of \$24.1 million. Our working capital (deficit) was \$(14.9) million as of December 31, 2004.

Our investing activities used cash of \$0.3 million for the year ended December 31, 2004 for the acquisition of property and equipment of \$0.1 million and investment in patents and trademarks of \$0.3 million. These expenditures were offset by proceeds from sale of property and equipment of \$0.1 million.

Our cash provided by financing activities was \$3.9 million for the year ended December 31, 2004, which consists of \$9.9 million in proceeds from borrowings from our senior convertible debt offset by \$5.2 million on repayment of borrowings, \$0.1 million of repayment of other liabilities, and increase in restricted cash of \$0.8 million.

We anticipate that our capital expenditures will be approximately less than \$0.5 million for the full year 2005 for the acquisition of furniture, fixtures, and other business equipment. This amount is subject to change, however, depending upon the nature and the amount of the product orders that we actually receive from customers.

Our capital requirements during the next twelve months will depend on numerous factors, including the success of existing products either in manufacturing or development, the development of new applications for Liquidmetal alloys, the resources we devote to develop and support our Liquidmetal alloy products, and the success of pursuing strategic licensing and funded product development relationships with external partners. During the next twelve months, based on our current business plan, we expect to have sufficient resources to continue to devote limited capital to our research and development activities, to further develop and strengthen our manufacturing technology, and to provide for working capital and other general corporate purposes. However, based on our historical operating results and the continued development of our manufacturing capabilities and alloy compositions, there exists the possibility that these resources will not be adequate to operate at the proposed business plan levels. These expenses and capital expenditures could consume a material amount of our cash resources, but the amount of these requirements will depend on the nature and amount of orders we receive for the purchase of our bulk Liquidmetal alloy products.

Our business is based on commercializing an entirely new and unique technology, and our current business plan contains a variety of assumptions and expectations that are subject to uncertainty, including assumptions and expectations about order flow, unit volumes, manufacturing efficiencies, product cost and pricing, continuing technology improvements, customer adoption practices, strategic licensing relationships and other relevant matters. These assumptions take into account recent significant cost reductions, as well as recent improvements to our manufacturing processes. We have experienced losses from continuing operations during the last two fiscal years and have an accumulated deficit of \$127.5 million as of December 31, 2004. Cash used in continuing operations for the years ended December 31, 2004 and December 31, 2003 was \$6.4 million and \$24.1 million, respectively. At December 31, 2004, our principal source of liquidity was \$0.7 million of cash and cash equivalents and trade accounts receivables of \$1.7 million. Such conditions raise substantial doubt that our Company will be able to continue as a going concern for a reasonable period of time without receiving additional funding. These operating results occurred while we were developing and attempting to commercialize and manufacture products from an entirely new and unique technology. This business plan required significant spending related to start-up costs and capital expenditures. These factors have placed a significant strain on our financial resources. The ultimate success of the Company depends on our ability to continue to reduce operating costs, generate higher revenue, achieve positive cash flow from continuing operations and achieve profitability.

On March 3, 2004, we sold \$9.9 million of 6.0% senior convertible notes due 2007 (the March Notes) to investor groups in a transaction led by Michigan Venture Capital Co., Ltd, a South Korea-based institutional investment firm, and IndiGo Ventures LLC, a New York-based investment firm that served as a financial advisor to the Company for the transaction. The notes were convertible at any time into our common stock at a price of \$3.00 per share. Investors in the private placement received warrants to purchase an aggregate amount of up to approximately 1.2 million shares of common stock, exercisable at \$3.00 per share for varying periods but no later than 100 days following the effectiveness of a registration statement covering the resale of shares issuable upon exercise of the warrants. In addition, the investors had the right to call for repayment of the notes prior to maturity at any time after the second anniversary of the closing of the transaction. (see Note 15 to the Consolidated Financial Statements)

On August 19, 2004, the Company completed a private exchange offer for its March Notes. Under terms of the exchange offer, approximately \$5.5 million in aggregate principal amount of the March Notes have been exchanged for an aggregate of (i) \$2.75 million of 6% Senior Secured Notes Due 2007 (the Long-Term Notes) and (ii) \$2.75 million of 10% Senior Secured Notes Due 2005 (the Short-Term Notes), collectively referred to as Exchange Notes . In addition, the Company redeemed approximately \$4.5 million of the March Notes in cash. The Exchange Notes are collateralized by certain patents owned by the Company and second priority mortgage interest in plant facilities and certain equipment at our plant in South Korea. The Short-Term Notes have a maturity date of July 29, 2005, and a conversion price of \$2.00 per share (compared to a conversion price of \$3.00 per share under the March Notes). The Long-Term Notes have a maturity date of July 29, 2007, and a conversion price of \$1.00 per share. Further, the exchange notes are convertible into Common Stock, at the option of the Company, if at any time after the issuance of the notes, the closing per share price of the Common Stock exceeds \$4.00 (as adjusted for stock splits, reverse splits, stock dividends, and recapitalizations) for 30 consecutive trading days, and further provided that there has been effective registration during such period. Holders of the Long-Term Notes also have the right to call for repayment of the Long-Term Notes prior to maturity at any time after the second anniversary of the completion of the exchange offer. A total of 563,151 warrants to purchase our common stock at an exercise price of \$3.00 per share all of which were previously issued in connection with the purchase of the March Notes have been amended to provide for an extended expiration date of March 1, 2006. As of December 31, 2004, we were in breach of a covenant in the Note Exchange Agreement requiring us to become current in our SEC filings, as well as file a registration statement with the SEC for the shares into which the notes are convertible, within 90 days of the issue date of the new notes. If written notice of default is delivered to us for breach of this covenant, then we will have a period of 30 days to cure the breach before it becomes an event of default under the notes, and if the breach is not cured during such time period, the holders of the notes will become entitled to accelerate the remaining balance of their respective notes and declare them immediately due and payable. As of the date of the filing of this Form 10-K, we have not received a notice for demand for payment as a result of not meeting the registration and listing requirements.

Our future success depends on our ability to continue reducing operating costs and ultimately to generate higher revenue and attain profitability. We cannot be certain that additional capital, whether through selling additional debt or equity securities or obtaining a line of credit or other loan, will be available to us or, if available, will be on terms acceptable to us. If we issue additional securities to raise funds, these securities may have rights, preferences, or privileges senior to those of our common stock, and our current stockholders may experience dilution.

In March 1996, we entered into a distribution agreement whereby we granted to a third party exclusive rights to market and sell golf products incorporating Liquidmetal technology to certain Japanese sporting equipment companies. The third party paid us a \$1.0 million distribution fee as part of this agreement, of which a portion was refundable according to a formula based on the gross profit earned by the third party. The remaining unearned distribution fee of \$0.8 million has not been refunded as of December 31, 2004, and we do not believe the third party is entitled to a refund. On March 28, 2003, the distribution agreement was terminated and we entered into a new agreement to pay to the same third party a commission on the net sales price of all Liquidmetal golf equipment that is shipped by our Company or its affiliates to Japanese golf companies for sale into the Japanese end-market. This commission will apply to golf equipment shipped by our Company or its affiliates during the period beginning on March 28, 2003 and ending on March 28, 2006. If, by March 28, 2006, we have not paid \$0.4 million in commission payments, the balance between commissions paid and \$0.4 million will be paid by April 30, 2006, thereby guaranteeing the third party a \$0.4 million minimum payment during the term of the agreement. We will recognize the unearned distribution fee of \$0.8 million as revenue proportionately with the payment of commissions under the letter agreement.

USE OF PROCEEDS

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

As of December 31, 2003, we have used the \$70.7 million of net proceeds from the Offering. In 2002, we used approximately \$7.8 million of the net proceeds from the Offering to repay all outstanding promissory notes and accrued interest, \$11.1 million to fund the construction of our manufacturing facility in South Korea, \$14.3 million to purchase equipment used to manufacture Liquidmetal parts, \$0.4 million to purchase assets related to production and sale of equipment used in the production process of Liquidmetal alloy products, and \$0.3 million to purchase the 51% interest in our majority owned Dongyang subsidiary. During the third quarter of 2002, we used \$2.0 million to invest in the common stock

of Growell Metal, which supplied a portion of the Liquidmetal alloy ingots used in our manufacturing operations in Korea. We have since sold such stock, realizing a gain on the sale. We used the remaining proceeds of \$32.7 million for working capital in 2002 and 2003, excluding \$2.1 million paid to Paul Azinger in 2002 and 2003 for amounts due under the terms of his terminated endorsement agreement with our discontinued retail golf operations.

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On March 3, 2004, the Company issued \$9.9 million of 6.0% senior convertible notes due 2007, which was exchanged in August 2004, to investor groups in a transaction led by Michigan Venture Capital Co., Ltd, a South Korea-based institutional investment firm, and IndiGo Ventures LLC, a New York-based investment firm (the Placement Agents) that served as a financial advisor to the Company for the transaction (see Note 15). The Company used \$0.6 million of the proceeds to pay various agents as issuance costs of the notes in March 2004. From June through August 2004, the Company redeemed \$4.5 million of the outstanding note balance in cash. We used the remaining proceeds of \$3.3 million for working capital needs and used \$0.8 million as collateral held in certificate of deposit to finance a certain insurance policy. As of December 31, 2004, \$0.7 million of the proceeds are held as cash and cash equivalents. The remaining proceeds of \$0.7 million will be used for working capital needs.

OFF-BALANCE SHEET ARRANGEMENTS

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

We have made no arrangements of the types described in any of the categories that may have a material current or future effect on our financial condition, liquidity or results of operations. See Note 13 to the Consolidated Financial Statements contained in this Annual Report on Form 10-K.

CONTRACTUAL OBLIGATIONS

The following table of material debt and lease commitments at December 31, 2004, summarizes the effect these obligations are expected to have on our cash flow in the future periods set forth below (in thousands):

| | Payments due by period | | | | |
|--------------------------------|------------------------|---------------------|-----------|-----------|----------------------|
| | Total | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
| Contractual Obligations | | | | | |
| Long-term debt | \$ 9,460 | \$ 6,842 | \$ 2,618 | \$ | \$ |
| Capital lease obligation | 212 | 134 | 78 | | |
| Operating leases and rents | 2,240 | 1,215 | 952 | 73 | |
| Growell settlement payable | 3,246 | 3,246 | | | |
| Consulting services payable | 172 | 172 | | | |
| Dongyang payable | 28 | 28 | | | |
| Total | \$ 15,358 | \$ 11,637 | \$ 3,648 | \$ 73 | \$ |

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates and assumptions

are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results could differ materially from these estimates under different assumptions or conditions.

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

- Our earnings and cash flows are subject to fluctuations due to changes in non-U.S. currency exchange rates. We are exposed to non-U.S. exchange rate fluctuations as the financial results of non-U.S. subsidiaries are translated into U.S. dollars. As exchange rates vary, those results, when translated, may vary from expectations and adversely impact overall expected profitability. The cumulative translation effects for subsidiaries using functional currencies other than the U.S. dollar are included in accumulated foreign exchange translation in shareholders' equity. Movements in non-U.S. currency exchange rates may affect our competitive position, as exchange rate changes may affect business practices and/or pricing strategies of non-U.S. based competitors.

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- We record an accrual for potential product warranty costs. Due to the lack of historical information for warranty expense related to bulk alloy products, management estimates product warranties as a percentage of bulk alloy product sales earned during the period. In the event in future periods the actual product warranty costs consistently exceed the estimate for product warranty costs, an adjustment would be made and income would decrease in the period of such determination. Likewise, in the event we determine that actual product warranty costs are consistently lower than the estimate for product warranty costs, an adjustment would be made and income would increase in the period of such determination.
- We record an allowance for doubtful accounts as a contra-asset to our trade receivables for estimated uncollectible accounts. Management estimates the amount of potentially uncollectible accounts by reviewing significantly past due customer balances relative to historical information available for those customers. In the event, in future periods, actual uncollectible accounts exceed the estimate for uncollectible accounts, an adjustment would be made and income would decrease in the period of such determination. Likewise, in the event, in future periods, actual uncollectible accounts are lower than the estimate for uncollectible accounts, an adjustment would be made and income would increase in the period of such determination.
- We value inventories at lower of cost or net realizable value. Management has determined net realizable value to be equal to the selling price of the products to be produced and sold less the cost of disposal. In the event, in future periods, the actual selling prices exceed the estimate for selling prices less cost to sell, an adjustment would be made and income would increase in the period of such determination. Likewise, in the event, in future periods, actual selling prices are lower than the estimate for selling prices, an adjustment would be made and income would decrease in the period of such determination. During 2003 we reduced the carrying value of raw materials held by our subsidiary, Liquidmetal Korea, by the amounts considered to be obsolete. During 2003 we reduced the carrying value of our inventories by \$1.0 million as we determined that certain raw material and inventories exceeded their net realizable value as of December 31, 2003. Additionally, we recorded a write-down of \$2.8 million of raw material and machine inventory associated with the settlement of a dispute with a customer, Growell, in December 2003. Such write-down adjustments are included within Cost of Sales. (see Note 7)
- We record valuation allowances to reduce the deferred tax assets to the amounts estimated to be realized. While we consider taxable income in assessing the need for a valuation allowance, in the event we determine we would be able to realize our deferred tax assets in the future in excess of the net recorded amount, an adjustment would be made and income increased in the period of such determination. Likewise, in the event we determine we would not be able to realize all or part of our deferred tax assets in the future, an adjustment would be made and charged to income in the period of such determination.
- We account for the warrants and embedded conversion feature of our senior convertible notes as derivatives in accordance with Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, and Emerging Issues Task Force Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock. Fair values of warrants and embedded conversion features are measured at each period end using Black-Scholes models and changes in fair value during the

period are reported in our earnings.

RECENT ACCOUNTING PRONOUNCEMENTS

In December 2003, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition. SAB 104 supersedes SAB 101, Revenue Recognition in Financial Statements. SAB 104's primary purpose is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superseded as a result of the issuance of EITF 00-21, Accounting for Revenue Arrangements with Multiple Deliverables. Additionally, SAB 104 rescinds the SEC's Revenue Recognition in Financial Statements Frequently Asked Questions and Answers (the FAQ) issued with SAB 101 that had been codified in SEC Topic 13, Revenue Recognition. Selected portions of the FAQ have been incorporated into SAB 104. While the wording of SAB 104 has changed to reflect the issuance of EITF 00-21, the revenue recognition principles of SAB 101 remain largely unchanged by the issuance of SAB 104, which was effective upon issuance. The adoption of SAB 104 did not impact the consolidated financial statements.

In March 2004, the FASB approved the consensus reached on the Emerging Issues Task Force (EITF) Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. The objective of this Issue is to provide guidance for identifying impaired investments. EITF 03-1 also provides new disclosure requirements for investments that are deemed to be temporarily impaired. In September 2004, the FASB issued a FASB Staff Position (FSP) EITF 03-1-1 that delays the effective date of the measurement and recognition guidance in EITF 03-1 until after further deliberations by the FASB. The disclosure requirements are effective only for annual periods ending after June 15, 2004. The Company has evaluated the impact of the adoption of the disclosure requirements of EITF 03-1 and does not believe the impact will be significant to the Company's overall results of operations or financial position. Once the FASB reaches a final decision on the measurement and recognition provisions, the company will evaluate the impact of the adoption of EITF 03-1.

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In November 2004, the FASB issued SFAS No. 151 *Inventory Costs*, an amendment of ARB No. 43, Chapter 4. The amendments made by Statement 151 clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The guidance is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 23, 2004. The Company has evaluated the impact of the adoption of SFAS 151, and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In December 2004, the FASB issued SFAS No. 153, *Exchanges of Nonmonetary Assets*, an amendment of APB Opinion No. 29, *Accounting for Nonmonetary Transactions*. The amendments made by Statement 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. Opinion 29 provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. The Board believes that exception required that some nonmonetary exchanges, although commercially substantive, be recorded on a carryover basis. By focusing the exception on exchanges that lack commercial substance, the Board believes this Statement produces financial reporting that more faithfully represents the economics of the transactions. The Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of this Statement shall be applied prospectively. The Company has evaluated the impact of the adoption of SFAS 153, and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), *Share-Based Payment*. Statement 123(R) will provide investors and other users of financial statements with more complete and neutral financial information by requiring that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. Statement 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. Statement 123(R) replaces FASB Statement No. 123, *Accounting for Stock-Based Compensation*, and supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*. Statement 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that Statement permitted entities the option of continuing to apply the guidance in Opinion 25, as long as the footnotes to financial statements disclosed what net income would have been had the preferable fair-value-based method been used. Public entities (other than those filing as small business issuers) will be required to apply Statement 123(R) as of the first interim or annual reporting period that begins after June 15, 2005. The Company has evaluated the impact of the adoption of SFAS 123(R), and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In December 2004 the Financial Accounting Standards Board issued two FASB Staff Positions: FSP FAS 109-1, *Application of FASB Statement 109 Accounting for Income Taxes to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*, and FSP FAS 109-2 *Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004*. Neither of these affected the Company as it does not participate in the related activities.

Item 7A. Quantitative and Qualitative Disclosures About Market Risks

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

Interest Rates. We are exposed to market risks relating to changes in interest rates. Although we do not currently have any borrowings with variable interest rates, fluctuations in interest rates may have a negative impact to any future borrowings.

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

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Foreign Exchange Rates. As a result of our manufacturing presence in South Korea, a substantial portion of our costs will be denominated in South Korean won. Consequently, fluctuations in the exchange rates of the South Korean won to the U.S. dollar will affect our costs of goods sold and operating margins and could result in exchange losses. Although we do not currently enter into foreign exchange hedge transactions, we may do so in the future as our business grows.

Item 8. Financial Statements and Supplementary Data

The financial statements required by this item are located beginning on page 30 of this report. The supplementary financial information required by this item is located under the caption "QUARTERLY RESULTS" in Item 7 of this report.

Item 9. Changes in and Disagreements with Accountants on Accounting and financial Disclosures

Information required by this Item may be found in our Form 8-K filed May 6, 2004 in connection with the resignation of Deloitte & Touche LLP as our independent auditors and our Form 8-K filed on May 21, 2004, in connection with our appointment of Stonefield Josephson Inc. as our independent auditors. Following is Item 4 of the respective Form 8-Ks:

May 6, 2004

On May 6, 2004, Deloitte & Touche LLP ("Deloitte"), the Registrant's independent auditors, notified the Registrant that they were resigning from the client-auditor relationship with the Registrant effective as of that date.

Deloitte was engaged by Registrant to serve as the Registrant's independent auditors for the fiscal year ended December 31, 2003, although Deloitte has not issued a report on the financial statements of the Registrant and its subsidiaries for the 2003 fiscal year. The reports of Deloitte with respect to the Registrant's financial statements for the fiscal years ended December 31, 2002 and 2001 contained no adverse opinion or disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope or accounting principles. During the fiscal years ended December 31, 2003 and 2002 and the period from December 31, 2003 through the date of Deloitte's resignation, there were no disagreements between the Registrant and Deloitte on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Deloitte, would have caused Deloitte to make reference to the subject matter of the disagreements in connection with its report on the Registrant's financial statements for such year.

The Registrant previously announced that it expects to restate revenues and results of operations for the third and fourth quarters of 2002 and the first quarter of 2003 in connection with the Registrant's sales of alloy melting and casting equipment during such quarters to Growell Metal Co., Ltd., a South Korea metals processing company ("Growell"). The Registrant's Audit Committee conducted an internal inquiry at the request of Deloitte into the Registrant's transactions with Growell and found that the original revenue recognition on the Growell equipment sales did not take into account all relevant documentation relating to the transactions. The Registrant announced in January 2004 that it entered into a dispute settlement agreement with Growell to resolve various outstanding claims between the parties relating to the Registrant's transactions with Growell.

In connection with the Audit Committee's inquiry into the Growell equipment sales and dispute settlement, the Audit Committee also reviewed the facts and circumstances relating to a personal stock transaction between the Registrant's CEO and Growell. In this transaction, as reported by the CEO, the CEO undertook a private sale of personal shares of Registrant common stock to Growell in February 2002, prior to the Registrant's initial public offering. As part of the inquiry, the CEO reported that this sale included a previously undisclosed personal agreement to ensure that the purchase price of the stock purchased by Growell would be at a thirty percent discount to the Registrant's initial public offering price, and he also provided information regarding his fulfillment of this personal agreement.

As of May 6, 2004, certain details of the foregoing transactions had not been resolved to Deloitte's satisfaction, and the audit for the 2003 fiscal year has therefore not been completed. As a result of the expected restatements and these unresolved issues, the Registrant's previously issued financial statements for the year ended December 31, 2002 and Deloitte's audit report thereon, as well as the Registrant's quarterly financial statements for the third quarter of 2002 and the first, second, and third quarters of 2003 (and Deloitte's related review reports thereon), should no longer be relied upon.

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Deloitte has communicated to the Registrant that it is unwilling to continue to rely on the representations of the Registrant's CEO. Deloitte has also previously communicated to the Registrant that, in light of the facts and circumstances surrounding the expected restatement, there were material weaknesses in the Registrant's internal accounting controls relating to the execution, administration, and accounting for contracts, particularly in the Registrant's South Korean operations. The Registrant has taken and is continuing to take steps to improve these internal controls.

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Other than the foregoing, none of the reportable events described under Item 304(a)(1)(v) of Regulation S-K occurred within the two most recent fiscal years of the Registrant ended December 31, 2003 and 2002 or within the subsequent interim period through the date of Deloitte's resignation.

The Registrant's Audit Committee has discussed with Deloitte the matters disclosed above. The Registrant has authorized Deloitte to respond fully to the inquiries of the Registrant's successor accountant concerning the matters disclosed above.

The Registrant has provided Deloitte with a copy of the foregoing disclosure and has requested that Deloitte furnish it with a letter addressed to the SEC stating whether or not it agrees with the above statements. A copy of that letter will be filed with the SEC promptly upon receipt. The Registrant's Audit Committee has begun the process of selecting new independent certified public accountants and will file a Form 8-K upon the engagement of a new auditing firm.

May 21, 2004

On May 21, 2004, the Audit Committee of Liquidmetal Technologies, Inc. (the Registrant) appointed Stonefield Josephson, Inc. (Stonefield Josephson) as the Registrant's independent auditors. A copy of the press release announcing the engagement of Stonefield Josephson is filed as Exhibit 99.1 to this Current Report on Form 8-K.

During the two most recent fiscal years and through the date of this Current Report on Form 8-K, the Registrant did not consult Stonefield Josephson regarding (i) the application of accounting principles to a specific transaction, either completed or proposed, or the type of audit opinion that may be rendered on the Registrant's financial statements, and neither a written report nor oral advice was provided to the Registrant that Stonefield Josephson concluded was an important factor considered by the Registrant in reaching a decision as to any accounting, auditing or financial reporting issue; or (ii) any matter that was either the subject of a disagreement (as defined in Item 304(a)(1)(iv) of Regulation S-K and the related instructions thereto) or a reportable event (as defined in Item 304(a)(1)(v) of Regulation S-K).

Item 9A. Controls and Procedures

Evaluation of disclosure controls and procedures. During the course of the audit of the financial statements of Liquidmetal Technologies, Inc. (the Company) for the fiscal years ended December 31, 2001, 2002, and 2003, it was determined that revenues from certain equipment sales made by the Company to Growell Metal Co., Ltd. in the third and fourth quarters of 2002 and the first quarter of 2003 should not have been recognized in those periods. **It was also determined that certain amounts relating to sales made to Samsung in December 2002, to JS Technologies in September 2002, and AM Corporation in December 2002 should not have been recognized. It also was determined that compensation expense related to certain stock options granted in 2001 and 2002 were not calculated in accordance with generally accepted accounting principles under APB Opinion No. 25, SFAS No. 123, and EITF 00-23.** These determinations and the associated restatement of previously issued financial statements, as described more fully elsewhere in the Form 10-K for the year ended December 31, 2003, filed on November 10, 2004, suggest that, at the time of the subject transactions and the preparation of the Company's financial statements for the relevant periods, the Company's disclosure controls and procedures (as defined in Rule 13a-15 under the Securities Exchange Act of 1934) were not effective as of the end of the period covered by such Form 10-K.

Liquidmetal Technologies, Inc. (the Company) carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Vice President of Finance, of the effectiveness as of December 31, 2004 of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, as amended. Based on that evaluation, the Chief Executive Officer and Vice President of Finance have concluded that these disclosure controls and procedures, as of December 31, 2004, were not effective. This determination was based primarily on the restatement described above and the material weaknesses in internal controls over financial reporting identified below.

Management's Report on Internal Control Over Financial Reporting. The time and resources committed to the restatement of prior periods' financial statements (as aforementioned) delayed the Company's internal timetable with respect to its

documentation, assessment and evaluation of internal control over financial reporting, which are required to be undertaken to comply with Section 404 of the Sarbanes-Oxley Act of 2002 (SOX 404). Due in part to the issues described in the foregoing paragraph, management s assessment of the effectiveness of the Company s internal control over financial reporting has been substantially delayed and is not complete, which in turn has prevented the Company s independent registered public accounting firm, Stonefield Josephson, Inc. (Stonefield) from being able to satisfactorily complete an audit of the Company s internal control over financial reporting pursuant to SOX 404. Based on the foregoing, Stonefield has disclaimed an opinion on the Company s internal control over financial reporting.

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In attempting to complete its assessment of internal control over financial reporting, management used the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Although management has not yet completed its review and assessment of all of the Company's internal controls over financial reporting, based on the review and assessment efforts that have actually been completed, management has identified several control deficiencies that existed during and as of the year ended December 31, 2004, some of which have been determined to be material weaknesses in internal control over financial reporting. As a result of the following material weaknesses, management has concluded that it did not maintain effective internal control over financial reporting as of December 31, 2004, based on the criteria established in COSO (and the following paragraphs also describe the specific steps that the Company has taken to remediate these material weaknesses):

1. Lack of adequate segregation of duties in accounts payable and accounts receivable involving cash receipts and deposits, bank reconciliations, cash disbursements, purchasing, and accounts receivable reconciliations:

After the Company completely moved its accounting function from Tampa, Florida to Lake Forest, California in July 2004 and reduced the size of its accounting staff, duties such as booking of cash receipts, bank reconciliations and journal entries for corporate accounting were primarily being done by two accountants. During the course of the Company's audit for its 2004 fiscal year (which audit occurred during the first three months of 2005) and in the course of the Company's efforts to complete the assessment required by SOX 404 at the same time, it was determined that this lack of segregation could contribute to preventing detection of potential fraud or misstatements of financial information. Accordingly, beginning in the second quarter of 2005, the Company started taking steps to evaluate its overall accounting duties and segregate these functions for better internal control structure. For example, the Company began segregating the cash receipts booking and bank reconciliation among the two accountants, as well as segregating invoice entry and check run function. Additionally, as discussed below, beginning in the second quarter of 2005, the Company augmented its supervisory review process to mitigate the potential for fraud and misstatements. The Company has not identified any adjustments as a result of this lack of segregation of duties.

2. Lack of adequate controls and monitoring of payroll processing, currently outsourced to a third party provider:

This material weakness existed throughout 2004 as the Company utilized the services of a third party payroll processor that was not certified under SAS 70 (Type II). During the course of the Company's audit for its 2004 fiscal year, it was determined that the risk of using a third party payroll provider that is not SAS 70 certified may contribute to misstatements of payroll and related financial information. The Company intends to remediate this weakness by retaining the services of ADP for payroll processing. ADP is certified under SAS 70 (Type II).

3. Lack of documentation to evidence reviews of certain reconciliations:

During the course of the Company's audit for the 2004 fiscal year, which audit occurred in January 2005, the Company discovered that certain reconciliations, including bank statements and general ledger accounts, were not fully documented because the supervisors performing the review on such reconciliations occasionally omitted their signature evidencing their review. It was determined at the time that this lack of documentation may result in certain accounting documents not being properly reviewed or there being no evidence of review. Beginning in the second quarter of 2005, the Company began taking steps to require that all reviews of reconciliations by supervisors are evidenced by a supervisor signature and that that all accounting documents are subject to proper review. For example, the Company started utilizing a Prepared by, Reviewed by, Checked by stamp and required all reconciliations to have evidence of the review prior to closing month end.

4. Lack of documentation of authorization of transactions:

During the course of the Company's audit for the 2004 fiscal year, the Company discovered that, although accounting transactions may have been authorized by the appropriate persons, the authorizing person occasionally omitted his signature on the relevant documents or approval forms to evidence his authorization. This lack of documentation on invoices, purchase requisitions and expense reports may result in certain transactions not being properly approved, so in the second quarter of 2005, the Company began implementing additional procedures for ensuring that all accounting documents are subject to proper approval as well as indication of the approval. For example, the Company began utilizing a Prepared by, Reviewed by, Checked by stamp and required that all documents have evidence of the approval prior to entry into the Company's accounting system.

5. Manual performance of numerous procedures that could be automated using current reporting systems:

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The Company uses the SAP system for financial reporting. During the course of the audit for the 2004 fiscal year, it was determined that the Company was manually performing numerous procedures that could be automated by using the current SAP system. For example, a sales order module in SAP could be utilized to automate the entire order fulfillment process. While SAP contains many modules and features which would allow the Company to automate certain operational and accounting procedures and thereby minimize the potential for human error, utilization of such modules would require significant investment in upgrading and maintaining the SAP system. Considering the Company's current size and limited resources, management has determined that it is not prudent to make this investment at the current time. Nevertheless, beginning in the second quarter of 2005 and continuing thereafter, the Company has been taking various steps to minimize the potential for human error caused by manual procedures. For example, the Company has established specific procedures for proper review and approval of transactions as outlined in paragraphs 3 and 4 above and expanded utilization of other software tools such as programmed spreadsheets.

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6. Material adjustments to the accounting records and financial statements as of and for the year ended December 31, 2004 that were not initially identified by the Company's internal control over financial reporting:

During the course of the Company's SOX 404 assessment efforts during the first several months of 2005, the Company and its auditors identified a number of necessary material adjustments to the Company's accounting records for 2004. For example, certain adjustments were booked to properly value complex debt instruments associated with the refinancing of the Company's debt. In addition, certain adjustments were booked to impair the Company's assets which are based on Management forecasts and overall assessment of the Company's business. The Company believes that these adjustments were a result of the Company's focus during 2004 on completing the Company's three-year re-audit of its 2001, 2002, and 2003 fiscal years. As a result of the Company's SOX 404 assessment efforts, the Company has identified these adjustments and has implemented additional controls to timely review and assess accounting issues and prevent the need for such adjustments. While there can be no assurance that adjustments to financial statements will not occur in the future, with the completion of the three-year re-audit, the Company believes that it will be able to devote its resources to completing its accounting assessments and entries timely and effectively.

7. Management's documentation of the evaluation of the significance of numerous control deficiencies and significant deficiencies identified, which could rise to the level of a material weakness, has not been completed:

The Company is continuing to diligently work to document and evaluate its internal controls under the requirements of SOX 404 during 2005.

8. The company had inadequate controls related to timely performance of its assessment of internal control over financial reporting:

The Company is diligently working to complete its assessment of its internal controls over financial reporting under the requirements of SOX 404 during 2005.

9. Assurance Consulting 3, the independent third party engaged to help document and assess the Company's internal controls, has identified numerous and significant deficiencies, including those identified above, which management has not completed evaluating whether they would rise to the level of a material weakness in accordance to the PCAOB Audit Standard No. 2.

The Company will review these deficiencies during its assessment of internal controls under the requirements of SOX 404 during 2005.

Management believes that it is taking appropriate steps to address these material deficiencies subsequent to December 31, 2004, including hiring an independent consulting firm, Assurance Consulting 3, who has helped to identify the material weaknesses disclosed above and to propose remedial actions to address and mitigate the deficiencies. We cannot assure you that we will not discover additional material weaknesses in the future; however, management will continue to work with the independent consulting firm and to work towards compliance with SOX 404 as of December 31, 2005.

Changes in Internal Control over Financial Reporting. During the quarter ended December 31, 2004, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting (although various changes made after December 31, 2004 are described above).

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We were engaged to audit management's assessment included in the accompanying Management's Report on Internal Control Over Financial Reporting, that Liquidmetal Technologies, Inc. (the Company) maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Liquidmetal Technologies, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Management has not completed its assessment of internal control over financial reporting, which has prevented us from being able to satisfactorily complete an audit of the Company's internal control over financial reporting. However, management has identified the following material weaknesses during their assessment: lack of adequate segregation of duties in accounts payable and accounts receivable involving cash receipts and deposits, bank reconciliations, cash disbursements, purchasing, and accounts receivable reconciliations; lack of adequate controls and monitoring of payroll processing, currently outsourced to a third party provider; lack of documentation to evidence reviews of certain reconciliations; lack of documentation of authorization of transactions; manual performance of numerous procedures that could be automated using current reporting systems; material adjustments to the accounting records and financial statements as of and for the year ended December 31, 2004 that were not initially identified by the Company's internal control over financial reporting; management's documentation of the evaluation of the significance of numerous control deficiencies and significant deficiencies identified, which could rise to the level of a material weakness, has not been completed; and the Company had inadequate controls related to timely performance of its assessment of internal control over financial reporting. The existence of one or more material weaknesses as of December 31, 2004 would preclude a conclusion that the Company's internal control over financial reporting was effective as of that date. These material weaknesses were considered in determining the nature, timing and extent of audit tests applied in our audit of the 2004 consolidated financial statements, and our disclaimer of opinion regarding the effectiveness of the Company's internal control over financial reporting does not affect our opinion on those consolidated financial statements.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Since management has not completed all the steps necessary to enable us to satisfactorily complete an audit of their internal control over financial reporting, and we were unable to apply other procedures to satisfy ourselves as to the effectiveness of the company's internal control over financial reporting, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion either on management's assessment or on the effectiveness of the company's internal control over financial reporting.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of Liquidmetal Technologies, Inc. and our report dated March 3, 2005 expressed an unqualified opinion including an explanatory paragraph on the Company's ability to continue as a going concern.

We do not express an opinion or any other form of assurance on management's statement referring to steps taken to address material weaknesses subsequent to December 31, 2004 or compliance with SOX 404 as of December 31, 2005.

/s/ Stonefield Josephson, Inc.
Irvine, California
May 9, 2005

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PART III**Item 10. Directors and Executive Officers of the Registrant**

Set forth below is a table identifying our current directors and executive officers:

| Name | Age | Position |
|------------------------|-----|---|
| John Kang | 42 | Chairman of the Board |
| John Thorne | 64 | President and Chief Executive Officer |
| James Kang | 44 | Director and Founder |
| William Johnson, Ph.D. | 56 | Director |
| Dean Tanella | 44 | Director |
| Vincent Addonisio | 49 | Director (Audit Committee Chairman) |
| Robert Biehl | 61 | Director |
| CK Cho | 49 | Director |
| David Binnie | 55 | Senior Vice President of Administration and Secretary |
| Tony Chung | 35 | Vice President of Finance |

John Kang was re-elected as Chairman of our Board of Directors in August 2003. He has been a director of our Company since 1994. From December 1994 to December 2000, he served as Chairman of our Board of Directors in a non-employee capacity, and from December 2000 to June 2001 he served as Chairman of our Board of Directors in an employee capacity. From June 2001 to December 2004, he served as our Chief Executive Officer and President. From July 1996 to September 2000, Mr. Kang served variously as Chief Executive Officer, President, and a director of Medical Manager Corporation, a public company traded on the Nasdaq National Market until its sale in September 2000 to WebMD Corporation. From 1988 to 1995, he was Chairman of the board of directors of Clayton Group, Inc., a private company engaged in the distribution of waterworks equipment. Mr. Kang received a B.A. degree in Economics from Harvard College in 1985. Mr. Kang is the brother of James Kang, the former Chairman of our board of directors.

John Thorne joined Liquidmetal in November 2004 and began serving as our President and Chief Executive Officer in January 2005. Mr. Thorne has more than 35 years of leadership and management experience in fabrication, casting, product development, technical management and P&L responsibility with high-performance alloy and specialty metals companies, including Ruger Investment Casting Division of Sturm, Ruger & Co., Inc., IMI Titanium, Inc., Precision Castparts Corporation and Howmet Corporation. Currently, he is President and CEO of Thorne Technologies, LLC, an Arizona-based metallurgical engineering and management consulting firm serving high technology metals industries. He holds a bachelor degree in Metallurgical Engineering and an MBA in Business Administration from Cornell University, and an MSE and Ph.D. in Metallurgical Engineering from the University of Michigan.

James Kang has served as a director since December 1994 and as executive Founder of our company since August 2003. From December 1994 to June 2001, he served variously as our Chief Executive Officer, President, and

Chairman. Mr. Kang received a B.A. degree in Marketing from the University of Illinois in 1983, and an M.B.A. degree from the Kellogg School of Management at Northwestern University in 1985. Mr. Kang is the brother of John Kang, our Chairman of the Board of Directors, who was also our Chief Executive Officer and President during 2004.

William Johnson, Ph.D., has served as a director since June 2000. From October 2001 to September 2003, he was employed as our executive Vice Chairman of Technology. Since 1997, Professor Johnson has been the Mettler Professor of Engineering and Applied Physics at Caltech. He held a Visiting Professor appointment at the Metal Physics Institute in Gottingen, Germany (1983) and received a Von Humbolt Distinguished Scientist Fellowship in Gottingen (1988). He is the 1995 recipient of the TMS/AIME Hume Rothery Award for his experimental work. He received a B.A. degree in Physics from Hamilton College and a Ph.D. degree in Applied Physics from Caltech. He spent two years at IBM's Research Center (1975-1977). At Caltech, Professor Johnson directed the research that led to the discovery of our bulk Liquidmetal alloy. Professor Johnson is currently a consultant to the Company.

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Dean G. Tanella was elected as a director in February 2004. Mr. Tanella is a 20-year veteran of the institutional investment business and has worked for such leading firms as Raymond James & Associates, CS First Boston Corp., Adams Harkness & Hill, Drexel Burnham Lambert, Inc., Kidder Peabody & Co. and the Vanguard Group. Since 1999, Mr. Tanella has served as President of Safe Harbor Capital, LLC and HarborLight Capital, LLC, both of which are private investment firms. Mr. Tanella received his bachelors degree from Princeton University and his MBA from the Harvard Graduate School of Business Administration.

Vincent Addonisio was elected as a director in May 2004. Mr. Addonisio is President and CEO of Regency Strategic Advisors, Inc., a firm he founded to advise select corporate clients on strategy, business development, and mergers and acquisitions. Previously, he served as a director, executive vice president and chief administrative officer for IMRglobal Corp., a public company that was subsequently acquired in 2001. Prior to joining IMRglobal, he was a director, executive vice president and chief financial officer for ABR Information Services, Inc., a public company which he also helped lead through initial and secondary public offerings and strategic acquisitions. A CPA, Addonisio began his career with an international accounting firm and subsequently joined W.R. Grace, where he held positions of progressive management responsibility. He holds a BS degree in accounting from Binghamton University and earned an MSM from Georgia Institute of Technology in Atlanta.

Robert Biehl has served as a director since January 2005. Mr. Biehl founded the Masterplanning Group International and as President, personally consulted over 400 clients and mentored over 2,500 executives and world leaders. Prior to starting Masterplanning Group, Mr. Biehl was an executive staff of World Vision International where he designed and developed the Love Loaf Program, which has raised millions of dollars worldwide. He has also published many books in the area of personal and organizational development. Mr. Biehl received his B.A. degree in psychology and a Masters Degree in Counseling from Michigan State University.

CK Cho was elected as a director in January 2005. Mr. Cho has over 18 years of experience with Samsung Electronics and managed over \$700 million annual procurement budget responsible for semi-conductor and telecommunication equipment and other electronic components. He is also the CEO of Winvest Venture Partners Inc. Mr. Cho received his bachelors degree majoring in Business Administration and Material Sciences from the Korea University of Seoul.

David Binnie has been Senior Vice President-Administration and Corporate Secretary since December 2003. Previously, he served as Senior Vice President for Human Resources, a position he had held since October 2001. Prior to joining Liquidmetal Technologies, Binnie was a senior official with the School District of Hillsborough County, Florida, where he served as the Assistant Superintendent for Human Resources. Hillsborough County is currently the 10th largest school system in the United States with over 191,000 students and over 32,000 employees. Mr. Binnie earned degrees at the Bachelors (Education 1971), Masters (Education, 1973) and Doctorate (Education Leadership, 1985) levels at the University of South Florida.

Tony Chung has been our Vice President of Finance since October 2004, prior to which he served as our Director of Finance upon joining the Company in May 2004. From September 1992 to May 2004, Mr. Chung served in a variety of senior finance capacities at various companies including Everdream Corporation, a startup venture specializing in IT outsourcing, and MAI Systems Corporation, a publicly traded company that develops and licenses hotel management software. Mr. Chung is a Certified Public Accountant and served eight years at KPMG as an Audit and Consulting Manager for several large multinational companies. He received his B.S. degree specializing in accounting and finance from the University of California at Berkeley in 1992 at The Haas School of Business. Mr. Chung is currently pursuing a Juris Doctorate Degree with Pacific Coast University School of Law and expects to receive his degree in June 2006.

Change in Principal Financial Officer

On November 3, 2004, David Nail resigned as our Vice President of Finance and ceased to be our principal financial officer. On the same day, our board elected Tony Chung to serve as our Vice President of Finance and become our company's principal financial officer. Additional information regarding Mr. Chung is set forth above in this Item 10.

BOARD OF DIRECTORS

Terms of Directors

Our board of directors is divided into three classes (designated CLASS I, CLASS II, and CLASS III), as nearly equal in number as possible, with each class serving three-year terms expiring at the third annual meeting of stockholders after their elections or until their respective successors have been elected and qualified. CLASS I currently consist of the following directors whose term is scheduled to expire at the 2005 annual meeting of stockholders: John Kang, William Johnson, and Robert Biehl. CLASS II currently consists of the following directors whose term is scheduled to expire at the 2006 annual meeting of stockholders: Dean Tanella and CK Cho. CLASS III currently consists of the following directors whose term will expire at the 2007 annual meeting of stockholders: James Kang and Vincent Addoniso.

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Audit Committee

Our board of directors has an Audit Committee that is currently comprised of Mr. Addonisio and Mr. Tanella. The Audit Committee is responsible for reviewing the independence, qualifications, and activities of our independent certified accountants and our financial policies, control procedures, and accounting staff. The Audit Committee is also responsible for the review of transactions between us and any officer, director, or entity in which an officer or director of Liquidmetal has a material interest. Our board of directors has determined that Mr. Addonisio and Mr. Tanella each qualify as audit committee financial experts as defined by the regulations of the Securities and Exchange Commission. The Audit Committee is governed by a written charter approved by the board of directors.

Compensation Committee

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

Corporate Governance and Nominating Committee

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

The Corporate Governance Committee's principal functions include:

- developing and maintaining our corporate governance policy guidelines;
- developing and maintaining our codes of conduct and ethics;
- overseeing the interpretation and enforcement of our Code of Conduct and our Code of Ethics for Chief Executive Officer and Senior Financial and Accounting Officers; and
- evaluating the performance of our board, its committees, and committee chairmen and our directors.
- selecting and recommending a slate of director nominees for election at each of the Company's annual meeting of the shareholders and recommending to the Board director nominees to fill vacancies or new positions on the Board or its committees that may occur from time to time.

Code of Ethics

Our board of directors has adopted a Code of Ethics that is applicable to its principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. The Code of Ethics is attached as Exhibit 14 to the Annual Report on Form 10-K filed on November 10, 2004.

BENEFICIAL OWNERSHIP REPORTING REQUIREMENTS

During the year ended December 31, 2004, our executive officers and directors filed with the Securities and Exchange Commission on a timely basis all required reports relating to transactions involving shares of our common stock beneficially owned by them, except that John Kang, Chairman, disposed of 188,700 shares during various dates in 2004 as gifts to various individuals and organizations and James Kang, Director and Founder, disposed of 67,320 shares on January 5, 2004 as gifts to various individuals and organization. These disposals were reported in John Kang's Form 5 filed on February 17, 2005 and James Kang's Form 4 filed on January 28, 2005.

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Item 11. Executive Compensation

The following table sets forth certain information regarding compensation paid by us for each of our last three years to our Chief Executive Officer and each of our other executive officers during 2004 (collectively, the named executive officers).

| Name and Positions | Year | Annual Compensation | | Other Annual Compensation | Long-Term Compensation Shares Underlying Options Granted | All Other Compensation |
|---|------|---------------------|-------|---------------------------|--|------------------------|
| | | Salary | Bonus | | | |
| John Kang (1) Chairman of the Board | 2004 | \$ 208,586 | | | | |
| | 2003 | \$ 300,007 | | | | |
| | 2002 | \$ 116,671 | | | | |
| John Thorne (2) Chief Executive Officer and President | 2004 | \$ 37,500 | | | | |
| | 2003 | | | | | |
| | 2002 | | | | | |
| James Kang (3) Founder and Director | 2004 | \$ 300,004 | | | | |
| | 2003 | \$ 280,011 | | | | |
| | 2002 | \$ 373,334 | | | 2,877,420 | |
| David Binnie (4) Senior VP of Administration and Secretary | 2004 | \$ 142,506 | | | | |
| | 2003 | \$ 140,005 | | | 150,000 | |
| | 2002 | \$ 150,005 | | | | |
| Tony Chung (5) VP of Finance | 2004 | \$ 73,544 | | | 80,000 | |
| | 2003 | | | | | |
| | 2002 | | | | | |

(1) As of August 22, 2003, John Kang was named Chairman of our board of directors, in addition to already serving as Chief Executive Officer and President. Mr. Kang ceased to be our Chief Executive Officer as of January 14, 2005

(2) As of January 14, 2005, John Thorne was named Chief Executive Officer and President of the Company. Previously during 2004, Mr. Thorne served as a consultant.

(3) As of August 22, 2003, James Kang became the executive Founder of the Company and ceased to be the Chairman of our board of directors.

(4) Mr. Binnie joined Liquidmetal in October 2001 as Vice President of Human Resources and assumed the position of Senior Vice President of Administration and Secretary effective December 2003.

(5) Mr. Chung joined Liquidmetal in May 2004 as Director of Finance and assumed the position of Vice President of Finance effective November 2004.

The following table sets forth information with respect to the aggregate stock option exercises by the executive officers named in the Summary Compensation Table during 2004 and the year-end value of unexercised options held by such executive officers.

Aggregate Option Exercises in Last Year and Year-End Values

| | Shares Acquired on Exercise | Value Realized (1) | Number of Unexercised Options at Year End Exercisable | Unexercisable |
|--------------|--------------------------------------|-----------------------|---|---------------|
| John Kang | | | 1,612,904 | |
| John Thorne | | | | |
| James Kang | | | 2,845,162 | 32,258 |
| David Binnie | | | 69,355 | 112,904 |
| Tony Chung | | | | 80,000 |

(1) Represents the difference between the fair market value of the underlying shares at the time of exercise and the exercise price of the options exercised.

EMPLOYMENT AGREEMENTS

We have entered into employment agreements with the executive officers identified in Item 11 above, as follows:

John Kang. On December 31, 2000, we entered into an employment agreement with John Kang that, as amended, provides for his employment as our Chief Executive Officer and President, and on August 22, 2003, Mr. Kang was named Chairman of our Board of Directors. Mr. Kang's employment agreement expires on December 31, 2005. Mr. Kang receives an annual base salary equal to \$200,000 per year, and his employment will terminate upon the earlier of his death, resignation, disability, or termination by the board of directors for any reason. If we terminate Mr. Kang's employment without cause, or if Mr. Kang terminates his own employment upon a change of control of our company or for other good reason, as defined in the agreement, we are responsible for paying Mr. Kang a lump-sum cash payment equal to 200% of Mr. Kang's annual base salary plus the average cash bonus during the two full fiscal years immediately preceding the termination. Pursuant to the agreement, Mr. Kang was issued options to purchase 1,612,904 shares of our common stock at an exercise price of \$4.65 per share. The options expire on December 31, 2010 and vested immediately upon grant. In addition, Mr. Kang is prohibited, during his employment with us and for one year after he is no longer employed by us, from soliciting any of our employees or competing with us in any manner. Starting in May 2003, Mr. Kang and other members of senior management took a 10% voluntary decrease in their base salary and returned to full salary in June 2004. Mr. Kang ceased to be our President and Chief Executive Officer as of January 14, 2005.

John Thorne. On January 14, 2005, we entered into an employment agreement with John Thorne, which provides for his employment as the named Chief Executive Officer and President of our company. Mr. Thorne's employment expires April 30, 2005, and his term may continue subsequent to the expiration date on a month-to-month basis at the same salary if mutually agreed in writing at least 2 weeks prior to each extension. His monthly salary is \$20,834, and will receive 10,000 stock options on April 30, 2005, contingent on remaining as an employee until that time.

James Kang. On May 1, 2001, we entered into an employment agreement with James Kang that, as amended, provides for his employment as the named executive Founder of our company. Mr. Kang's employment agreement expires on May 1, 2006. Mr. Kang receives an annual base salary equal to \$300,000 per year, and his employment will terminate upon the earlier of his death, resignation, disability, or termination by the board of directors for any reason. If we terminate Mr. Kang's employment without cause, or if Mr. Kang terminates his own employment upon a change of control of our company or for other good reason, as defined in the agreement, we are responsible for paying Mr. Kang

a severance benefit equal to a lump-sum cash payment equal to 200% of Mr. Kang's annual base salary plus the average cash bonus during the two full fiscal years immediately preceding the termination. Pursuant to the agreement, Mr. Kang was issued options to purchase 2,580,646 shares of our common stock at an exercise price of \$6.20 per share. The options expire on April 30, 2011 and vest at a rate of 33% per year for three years, with the first 33% vesting on May 21, 2002 and an additional 33% on May 21, 2003 and 2004. In addition, Mr. Kang is prohibited, during his employment with us and for two years after he is no longer employed by us, from soliciting any of our employees or customers. Starting in May 2003, Mr. Kang and other members of senior management took a 10% voluntary decrease in their base salary and returned to full salary in June 2004.

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David Binnie. On October 1, 2001, we entered into an employment agreement with David Binnie, which provides for his employment as the named Senior Vice President for Human Resources. Mr. Binnie's employment expires September 30, 2006, and his term may continue subsequent to the expiration date on a month-to-month basis at the same salary. His annual salary is \$150,000, and he received 100,000 stock options as part of the employment agreement. In December 2003, Mr. Binnie was named as our Senior Vice President of Administration and Secretary.

Tony Chung. On November 3, 2004, we entered into an employment agreement with Tony Chung, which provides for his employment as the named Vice President of Finance. Mr. Chung's employment expires November 2, 2007, and his term may continue subsequent to the expiration date on a month-to-month basis at the same salary. His annual salary is \$125,000, and he received 20,000 stock options as part of the employment agreement.

REPORT ON EXECUTIVE COMPENSATION

General

The Compensation Committee of our Board of Directors was established in 2002 and currently consists of CK Cho and Robert Biehl. The Compensation Committee is comprised entirely of non-employee directors and is responsible for establishing the compensation of our senior management, including salaries, bonuses, termination arrangements, and other executive officer benefits. The Compensation Committee also administers our equity incentive plans. The Compensation Committee also annually reviews and approves the compensation of John Thorne, our Chief Executive Officer and President.

Compensation Philosophy

The Compensation Committee's goal is to establish and maintain compensation policies that will enable us to attract, motivate, and retain high-quality executives and to ensure that their individual interests are aligned with our long-term interests and our stockholders. The committee places heavy emphasis on paying for performance and believes that a significant portion of an executive's total compensation opportunity should be at risk and tied to company performance. Our compensation package consists of three principal components:

- Base salaries, subject to minimums set forth in individual employment agreements;
- Annual incentive bonus eligibility; and
- Stock option grants and other forms of equity-based compensation.

Base Salary. Base salary is the largest portion of the cash compensation package received by each of our executive officers. The base salary of each of our executive officers is governed by employment agreements that were entered into during 2000 through 2005. Subject to the minimum amounts set forth in their respective employment agreements, we generally establish the base salary of each executive officer based, among other factors, on the Compensation Committee's assessment of that executive officer's position, responsibilities, experience, and performance. Our philosophy is to pay base salaries sufficient to attract and retain highly qualified executives. An executive officer's level of responsibility is the primary factor used in determining base salary. Individual performance also is considered in determining any salary adjustment.

The Compensation Committee reviews and approves all executive officer salary adjustments as recommended by the Chief Executive Officer and determines whether to increase the base salary above the amount set forth in their employment agreements. The Compensation Committee reviews annually the performance of the Chief Executive Officer and establishes his base salary, subject to the minimum \$250,000 annual base salary set forth in his employment agreement. In 2004 and 2003, the Compensation Committee did not increase the base salary of any of the executive officers.

Annual Bonus. Our executive officers are eligible for an annual cash bonus under our Performance Bonus Plan. The plan is designed to:

- put a significant portion of an executive officer's total cash compensation opportunity at risk based on the performance of the Company;
- be aligned with our mission, values and culture;

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- be cost-effective and appropriately budgeted to allow for growth of our revenue as well as growth of individual compensation plans;
- be externally competitive by matching or leading competitors; and
- be internally equitable through alignment with level of contribution, performance-based rewards, and administrative capabilities.

Awards of incentive bonuses generally are based on achieving corporate goals and a subjective evaluation of the contributions of individual executives toward the achievement of our business goals. Eligibility for the bonus will be contingent upon the Company meeting or exceeding company-wide financial goals and successful attainment of individual goals for the position. Both elements must be successfully met in order to be eligible for the bonus. None of our executive officers received bonuses for 2003 and 2004 because the company-wide financial goals were not satisfied.

Equity-Based Compensation.

Our equity-based awards to our executive officers consist principally of stock options granted from time to time under our 2002 Equity Incentive Plan and our 1996 Stock Option Plan. Stock option grants are based on various factors, including the executive officer's position, responsibility and tenure, each executive officer's ability to contribute to our future success, and the other elements of such executive officer's compensation. Generally, we use equity-based compensation to better align the interests of our executive officers with those of our stockholders. For 2004, the Compensation Committee approved awards of options to executive officers and certain members of senior management, with the sizes of the awards determined with reference to the scope of the position and the employees' relative contributions to the Company. In addition, three of our executive officers, John Kang, our Chief Executive Officer, James Kang, our executive Founder, and William Johnson, our Vice Chairman, own a significant amount of our common stock.

CEO Compensation

John Kang's base salary for 2003, as our President and Chief Executive Officer, was originally set at \$200,000, although Mr. Kang and other members of senior management took a 10% voluntary decrease in their base salary starting in May 2003, at which time Mr. Kang's base salary was reduced to \$180,000 per year. This represents a decrease over Mr. Kang's 2002 salary of \$200,000. Mr. Kang's compensation reflects his status as a significant stockholder of the Company. Accordingly, his base salary is lower than the base salary of CEOs of comparable companies. Mr. Kang voluntarily waived his base salary from January 2004 through May 2004 in support of the Company's strategic cash objectives. In June 2004, Mr. Kang returned to his base salary of \$200,000 and received his differential retroactive pay in equal installments over the remaining months of 2004. As a significant stockholder in the Company, his overall compensation is tied directly to sustained increases in the Company's value.

No bonus payments were made to Mr. Kang for 2003 and 2004 because the Compensation Committee determined not to pay any bonuses to any of our executive officers due to the Company missing its financial goals. In addition, no options were granted to Mr. Kang in 2003 and 2004. As of December 31, 2004, Mr. Kang held options and warrants to purchase 1,935,485 shares of our common stock, all of which were fully vested.

John Thorne's base salary, as our President and Chief Executive Officer, effective January 14, 2005, is \$250,008. As of December 31, 2004, Mr. Thorne did not hold any options to purchase our common stock.

The Internal Revenue Code imposes a limitation on the deduction under Section 162(m) for certain executive officers' compensation unless certain requirements are met. Our policy is to have all compensation fully deductible; however, we reserve the right to pay compensation that is not deductible if it is in our best interests.

Compensation Committee of the Board of Directors

CK Cho
Robert Biehl

December 31, 2004

The report of the Compensation Committee shall not be deemed incorporated by reference by any general statement incorporating by reference this Annual Report on Form 10-K into any filing under the Securities Act of 1933 or under the Securities Exchange Act of 1934, except to the extent that we specifically incorporate this information by reference, and shall not otherwise be deemed filed under such acts.

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DIRECTOR COMPENSATION

Our non-employee directors receive an annual fee of \$10,000 for their service to our board and are reimbursed for expenses incurred in attending board and committee meetings. Non-employee directors are also entitled to receive a \$10,000 annual cash stipend for each standing board committee (excluding the Audit Committee) on which the director serves. For Audit Committee service, the Audit Committee chairman is entitled to a \$35,000 annual stipend, and the other members of the Audit Committee are entitled to a \$27,500 annual stipend. In addition to the annual stipends, each non-employee director is entitled to receive a per-meeting fee of \$1,000 for each meeting of the board of directors or any board committee attended in person. Effective May 2004, Vincent Addonisio was elected as the lead independent director of the Company. The lead independent director is entitled to a \$30,000 annual stipend.

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

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

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The following table sets forth certain information regarding the beneficial ownership of our common stock as of December 31, 2004 by:

- each of our directors and the executive officers identified in Item 10 above;
- all directors and executive officers as a group, and
- each person known by us to own beneficially more than 5% of the common stock.

Beneficial ownership is determined under the rules of the Securities and Exchange Commission and generally includes voting or investment power with respect to securities. Unless otherwise indicated, each of the stockholders has sole voting and investment power with respect to the shares beneficially owned, subject to applicable community property laws. As of December 31, 2004, there were 238 holders of record of our common stock. For purposes of calculating amounts beneficially owned by a stockholder, the number of shares deemed outstanding includes 41,609,652 shares of common stock outstanding as of December 31, 2004. In addition, shares of common stock subject to options or warrants that are currently exercisable or exercisable within 60 days of December 31, 2004 are deemed to be outstanding and to be beneficially owned by the person holding the options or warrants for the purpose of computing the beneficial ownership of that person but are not treated as outstanding for the purpose of computing the beneficial ownership of any other person.

| Name | Beneficially Owned Shares | Percent |
|--|---------------------------|---------|
| John Kang (1) | 5,600,474 | 13 % |
| James Kang (2) | 7,003,904 | 17 % |
| William Johnson | 1,195,650 | 3 % |
| David Binnie (3) | 75,115 | * |
| Dean Tanella (4) | 26,120 | * |
| Vincent Addonisio (5) | | * |
| Robert Biehl | 25,000 | * |
| CK Cho (6) | 185,102 | * |
| John Thorne | | * |
| Tony Chung (7) | 47,250 | * |
| All directors and executive officers as a group 10 persons | | 34 % |

* Less than one percent.

(1) As of August 22, 2003, John Kang was named Chairman of our board of directors, in addition to already serving as Chief Executive Officer and President. As of January 14, 2005, John Kang ceased to be our Chief Executive Officer and President. The beneficial shares include:

(a) 1,612,904 shares that are issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of December 31, 2004.

(b) 322,581 shares issuable pursuant to a warrant held jointly by John Kang and Ricardo Salas (a former director of the company) that is currently exercisable; and

(c) 127,800 shares held by Mr. Kang's minor children.

(2) Includes 2,845,162 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of December 31, 2004. Also includes 969 shares held by James Kang's minor children. Does not include 32,258 shares issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of December 31, 2004.

(3) Includes 69,355 shares issuable pursuant to outstanding stock options that are exercisable currently or within 60 days of December 31, 2004. Also includes 760 shares held by Mr. Binnie's family. Does not include 112,904 shares issuable pursuant to outstanding stock options that are not exercisable currently or within 60 days of December 31, 2004.

(4) Includes 16,130 shares held by Mr. Tanella's investment firm, HarborLight Diversified Fund, LP. Also, includes 1,390 shares held by Mr. Tanella's family. Does not include 50,000 shares that are issuable pursuant to outstanding stock options that are not exercisable within 60 days.

- (5) Does not include 70,000 shares that are issuable pursuant to outstanding stock options that are not exercisable within 60 days.
- (6) Includes 109,678 shares held by Mr. Cho's Investment firm, Winvest.
- (7) Does not include 80,000 shares that are issuable pursuant to outstanding stock options that are not exercisable within 60 days.

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Equity Compensation Plan Information

The following table sets forth certain information regarding the securities authorized for issuance under our equity compensation plans as of December 31, 2004.

| Plan Category | Number of Securities To be Issued upon Exercise of Outstanding Options, Warrants, and Rights | Weighted Average Exercise Price of Outstanding Options, Warrants, and Rights | | Number of Securities Remaining Available for Future Issuance |
|---|--|--|-------------|--|
| Equity compensation plans approved by security holders: | 6,899,164 | \$ | 4.95 | 10,232,001 |
| Equity compensation plans not approved by security holders: | | | | |
| Total | 6,899,164 | \$ | 4.95 | 10,232,001 |

Item 13. Certain Relationships and Related Transactions

In June 2003, the Company entered into an exclusive, ten-year license agreement with LLPG, Inc. (LLPG), a corporation headed by a former director of the Company. Under the terms of the agreement, LLPG has the right to commercialize Liquidmetal alloys, particularly precious-metal based compositions, in jewelry and high-end luxury product markets. The Company, in turn, will receive royalty payments over the life of the contract on all Liquidmetal products produced and sold by LLPG. In conjunction with its technology licensing contract, LLPG purchased two proprietary Liquidmetal alloy melting machines and three proprietary Liquidmetal alloy casting machines for a total purchase price of \$2,000,000. At December 31, 2003, the Company had a remaining receivable balance of approximately \$500,000 due from LLPG, which was paid in full in March 2004.

The Company is a party to a license agreement with California Institute of Technology (Caltech) under which the Company exclusively licenses from Caltech certain inventions and technology relating to amorphous alloys. Professor William Johnson, a member of the Company's Board of Directors, is a professor at Caltech, and substantially all of the amorphous alloy technology licensed to the Company under the Caltech license agreement was developed in Professor Johnson's Caltech laboratory. During 2003, the Company paid approximately \$50,000 to Caltech representing the second and final installments on the approximately \$150,000 aggregate fees related to this agreement. Additionally, the Company reimburses Caltech for laboratory expenses incurred by Professor Johnson's Caltech laboratory, which during the years ended December 31, 2004 and 2003, amounted to \$0 and approximately \$22,000, respectively.

A company managed and partially owned by one of the Company's former directors provides technical support services and computer equipment to the Company. During the year ended December 31, 2003, the Company incurred approximately \$20,000 of expenses and equipment purchases related to this arrangement. There were no expenses and payables to this Company as of December 31, 2004.

We are a party to a consulting agreement with Chitnis Consulting, Inc., which is owned 100% by Shekhar Chitnis, a former director and executive officer of our company. Under this agreement, we have engaged Chitnis Consulting to provide consulting services on an as-needed basis through December 31, 2005. During 2003, we incurred approximately \$50,000 in consulting fees from Chitnis Consulting and incurred approximately \$54,000 as of December 31, 2004.

Soo Buchanan, the sister of John Kang and James Kang, was employed by our company and was paid aggregate compensation of approximately \$76,000 and \$43,000 as of December 31, 2003 and 2004. Additionally, Otis Buchanan, the husband of Ms. Buchanan, was employed by the Company and was paid aggregate compensation of approximately \$90,000 and \$54,000 as of December 31, 2003 and 2004, respectively.

In November 2004, we entered into an agreement with John Kang, our Chairman, President, and Chief Executive Officer, in which Mr. Kang agreed that certain stock transactions by him in 2002 involving our common stock should have resulted in a liability under Section 16(b) of the Securities Exchange Act of 1934, as amended (Section 16(b)). These transactions include Mr. Kang's private sale of 285,715 shares of his personal Liquidmetal Technologies common stock to Growell Metal Co., Ltd. in February 2002, prior to our initial public offering. They also

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include Mr. Kang's subsequent indirect purchase and disposition of Liquidmetal Technologies common stock in order to satisfy a personal agreement Mr. Kang made to Growell Metal in February 2002 regarding the guaranteed minimum value of the stock purchased by Growell Metal in February 2002 (the purchases and dispositions incident to this agreement occurred in August and November 2002, respectively). Lastly, the transactions include open-market purchases of an aggregate of 89,300 shares of our common stock made by Mr. Kang in August 2002.

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The Audit Committee of our Board of Directors conducted an independent inquiry into the above-described transactions with the aid of independent legal counsel and, as a result of such inquiry, the Audit Committee concluded that the transactions should have resulted in a liability to the Company under Section 16(b) in the amount of approximately \$302,000. Mr. Kang has acknowledged this liability, and in an agreement negotiated between Mr. Kang and the Audit Committee and approved by the full Board, Mr. Kang will pay this liability through periodic installments in 2005 and 2006. . As a result, the Company accrued the \$302,000 receivable in other assets and other income as of December 31, 2004. The above-described transactions involving Growell Metal were reported on a new Form 4 filed by Mr. Kang on November 15, 2004, and the open-market purchases were previously reported on a timely basis in August 2002.

Item 14. Principal Accounting Fees and Services

Prior to May 2004, Deloitte & Touche LLP was our independent public accountant; however, effective May 2004, Deloitte & Touche LLP resigned as our independent accountant. Liquidmetal Technologies subsequently engaged Stonefield Josephson, Inc. Item 14 includes the principal accounting fees and services for both Deloitte & Touche LLP and Stonefield Josephson, Inc.

Stonefield Josephson, Inc.

Stonefield Josephson, Inc. was engaged in May 2004 and has served as our independent public accountants during the year ended December 31, 2003 and 2004.

The following table summarizes the aggregate fees billed to the Company by Stonefield for professional services:

| Fees | 2003, 2002, and 2001 | 2004 |
|----------------|----------------------|------------|
| Audit Fees (1) | \$ 760,000 | \$ 150,000 |

(1) *Audit Fees.* Fees for audit services billed in 2004 consisted of:

- Audit of the Company's annual financial statements for 2003, 2002, and 2001;
- Review and audit of the Company's quarterly and annual financial statements for 2004, respectively.

Deloitte & Touche LLP

The following table summarizes the aggregate fees billed to the Company by Deloitte & Touche LLP for professional services performed in 2003:

| Fees | 2003 |
|----------------|------------|
| Audit Fees (1) | \$ 296,021 |
| Tax Fees (2) | 68,435 |
| Total | \$ 364,456 |

(1) *Audit Fees.* Fees for audit services billed in 2003 consisted of:

- Audit of the Company's annual financial statements;
- Reviews of the Company's quarterly financial statements;
- Comfort letters, statutory and regulatory audits, consents and other services related to Securities and Exchange Commission matters;
- Consultations about accounting for settlement and fund raising; and

- Reviews of Securities and Exchange Commission documents associated with financing and restructuring.
- (2) Tax Fees. Fees for tax services billed in 2003 and 2002 consisted of tax compliance and tax planning/advice

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The Audit Committee pre-approves all audit and permissible non-audit services provided by the independent directors on a case-by-case basis. The Audit Committee approved 100% of the services performed by Deloitte & Touche LLP and Stonefield Josephson, Inc. in 2004, 2003, and 2002 as identified above.

PART IV

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

(a) The following documents are filed as a part of this report:

1. *Financial Statements*. The Index to our Consolidated Financial Statements is set forth on page 60 of this report.
2. *Financial Statement Schedules*. See the last page of Consolidated Financial Statements.
3. *Exhibits*. See Item 15(c) below.

(b) *Reports on Form 8-K*. The following reports on Form 8-K were filed during the quarter ended December 31, 2004:

| Date Filed | Date of Report | Item |
|-------------------|-------------------|---|
| October 19, 2004 | October 18, 2004 | The Company filed a news release under Item 7.01 of Form 8-K announcing the status of the company's external audit and Form 10-K filing. |
| November 10, 2004 | November 10, 2004 | The Company filed a news release under Item 7.01 of Form 8-K announcing the status of the company's external audit and Form 10-K filing. |
| November 23, 2004 | November 22, 2004 | The Company announced under Item 8.01 of Form 8-K that in a letter and decision dated November 18, 2004, the Listing Council notified the Company that it affirms the Panel's decision to delist the Company's securities from The Nasdaq National Market. |
| December 17, 2004 | December 17, 2004 | The Company filed a news release under Item 5.02 of Form 8-K announcing the appointment of John K. Thorne as Interim President and Chief Executive Officer. Also included in the press release is the stepping down of Thian-Song Tjoa as a member of our Board of Directors, and the elections of Robert J. Biehl and C.K. Cho to the Board. The appointment and elections will become effective on January 1, 2005. |
| December 23, 2004 | December 23, 2004 | The Company filed a news release under Item 2.02 of Form 8-K announcing the results of operations for the quarter ended March 31, 2004. |

(c) *Exhibits*. The exhibits listed on the Exhibit Index, which appears at the end of this Item 15, are filed as part of, or incorporated by reference into, this report.

(d) *Financial Statement Schedules*. See Item 15(a)(2) above.

EXHIBIT INDEX

| Exhibit Number | Description of Document |
|---------------------------|---|
| 2.1 | Agreement and Plan of Merger, dated May 21, 2003, between Liquidmetal Technologies, Inc. and Liquidmetal Technologies (incorporated by reference to Exhibit 2.1 to the Form 10-Q filed on August 14, 2003). |
| 3.1 | Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to the Form 10-Q filed on August 14, 2003) |
| 3.2 | Bylaws (incorporated by reference to Exhibit 3.2 to the Form 10-Q filed on August 14, 2003) |
| 4.1 | Reference is made to Exhibits 3.1 and 3.2. |
| 4.2 | Form of Common Stock Certificate (incorporated by reference to Exhibit 4.2 to the Form 10-Q filed on August 14, 2003) |
| 10.1 | Amended and Restated License Agreement, dated September 1, 2001, between Liquidmetal Technologies, Inc. and California Institute of Technology (incorporated by reference to Exhibit 10.1 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)). |
| 10.2 | Improved Property Commercial Lease, dated September 11, 2002, between Liquidmetal Technologies, Inc. and P & S Properties (incorporated by reference to Exhibit 10.2 of Form 10-K filed on March 31, 2003). |
| 10.3 | Lease, dated October 4, 2001, between Plaza IV Associates, Ltd. and Liquidmetal Technologies, Inc. (incorporated by reference to Exhibit 10.1 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)). |
| 10.4 | Second Amendment of Lease, dated October 3, 2003, between Liquidmetal Technologies, Inc. and Plaza Associates IV, Ltd. (incorporated by reference to Exhibit 10.1 of Form 10-Q filed on November 14, 2003). |
| 10.5 | Standard Lease, dated May 27, 2001, between Investors Equity Fund, Inc. and Amorphous Technologies International (now known as Liquidmetal Technologies, Inc.) (incorporated by reference to Exhibit 10.1 to the Registration Statement on Form S-1 on November 20, 2001 (Registration No. 333-73716)). |
| 10.6* | 1996 Stock Option Plan, as amended, together with form of Stock Option Agreement (incorporated by reference to Exhibit 10.7 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)). |
| 10.7* | 2002 Equity Incentive Plan (incorporated by reference to Exhibit 10.23 to the Registration Statement on Form S-1 (Amendment No. 2) filed on April 5, 2002 (Registration No. 333-73716)). |
| 10.8* | 2002 Non-Employee Director Stock Option Plan (incorporated by reference to Exhibit 10.24 to the Registration Statement on Form S-1 (Amendment No. 2) filed on April 5, 2002 (Registration No. 333-73716)). |
| 10.9* | Employment Agreement, dated December 31, 2000, between Liquidmetal Technologies, Inc. and John Kang, as amended by Amendment No. 1 to Employment Agreement, dated June 28, 2001 (incorporated by reference to Exhibit 10.8 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)). |
| 10.10* | Employment Agreement, dated May 1, 2001, between Liquidmetal Technologies, Inc. and James Kang, as amended by Amendment No. 1 to Employment Agreement, dated June 28, 2001 (incorporated by reference to Exhibit 10.9 to the Registration Statement on Form S-1 (Amendment No. 2) filed on April 5, 2002 (Registration No. 333-73716)). |
| 10.11* | Amendment No. 2 to Employment Agreement, dated September 1, 2003, between James Kang and Liquidmetal Technologies, Inc. (incorporated by reference to Exhibit 10.2 of Form 10-Q filed on November 14, 2003). |
| 10.12* | Employment Agreement, dated October 1, 2001, between Liquidmetal Technologies, Inc. and William Johnson, Ph.D. (incorporated by reference to Exhibit 10.10 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)) |
| 10.13* | Employment Agreement, dated October 1, 2001, between Liquidmetal Technologies, Inc., and David Binnie. (incorporated by reference to Exhibit 10.13 to the Form 10-K filed on November 10, 2004) |
| 10.14* | Employment Agreement, dated November 3, 2004, between Liquidmetal Technologies, Inc. and Tony Chung. (incorporated by reference to Exhibit 10.14 to the Form 10-K filed on November 10, 2004) |

- 10.15* Employment Agreement, dated December 31, 2000, between Liquidmetal Technologies, Inc. and T. Scott Wiggins (incorporated by reference to Exhibit 10.11 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)).
- 10.16* Employment Agreement, dated May 21, 2001, between Liquidmetal Technologies, Inc. and Brian McDougall (incorporated by reference to Exhibit 10.12 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)).
- 10.17* Employment Separation Agreement, dated December 31, 2003, between Liquidmetal Technologies, Inc. and Brian McDougall. (incorporated by reference to Exhibit 10.17 to the Form 10-K filed on November 10, 2004)
- 10.18* Letter Agreement, dated February 26, 2004, between Brian McDougall and Liquidmetal Technologies, Inc. (incorporated by reference to Exhibit 10.18 to the Form 10-K filed on November 10, 2004)
- 10.19* Employment Agreement, December 1, 2002, between Liquidmetal Technologies, Inc. and Thomas Trotter. (incorporated by reference to Exhibit 10.19 to the Form 10-K filed on November 10, 2004)
- 10.20* Employment Separation Agreement, dated November 6, 2003, between Liquidmetal Technologies, Inc. and Thomas Trotter. (incorporated by reference to Exhibit 10.20 to the Form 10-K filed on November 10, 2004)
- 10.21* Separation and Consulting Agreement, dated November 15, 2001, between Liquidmetal Technologies, Inc. and Shekhar Chitnis, together with Consulting Agreement attached as Exhibit A (incorporated by reference to Exhibit 10.14 to the Registration Statement on Form S-1 (Amendment No. 2) filed on April 5, 2002 (Registration No. 333-73716)).
- 10.22 Warrant for Purchase of Shares of Common Stock, dated February 21, 2001, granted by Liquidmetal Technologies, Inc. to John Kang and Ricardo Salas (incorporated by reference to Exhibit 10.18 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)).
- 10.23 Warrant for Purchase of Shares of Common Stock, dated February 21, 2001, granted by Liquidmetal Technologies, Inc. to Tjoa Thian Song (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)).
- 10.24 Non-Qualified Stock Option Agreement, dated January 1, 2001, between Liquidmetal Technologies, Inc. and Paul Azinger (incorporated by reference to Exhibit 10.19 to the Registration Statement on Form S-1 filed on November 20, 2001 (Registration No. 333-73716)).
- 10.25 Foreign Corporation Lease Zone Occupancy (Lease) Agreement, dated March 5, 2002, between Kyonggi Local Corporation and Liquidmetal Korea Co., Ltd. (incorporated by reference to Exhibit 10.22 to the Registration Statement on Form S-1 (Amendment No. 2) filed by Liquidmetal Technologies on April 5, 2002 (Registration No. 333-73716)).
- 10.26 Credit Service Agreement, dated February 2003, between Liquidmetal Korea Co., Ltd. and Kookmin Bank (incorporated by reference to Exhibit 10.20 to the Form 10-K filed on March 31, 2003).
- 10.27 Agreement for Rent dated February, 2003, between Liquidmetal Korea Co., Ltd. and Dong Myung Seo Bank (incorporated by reference to Exhibit 10.21 to the Form 10-K filed on March 31, 2003).
- 10.28 Share Transfer Agreement, dated February 28, 2004, among Liquidmetal Korea Co. Ltd., Sun Joo Ho, and Dongyang Induction Co. Ltd. (incorporated by reference to Exhibit 10.28 to the Form 10-K filed on November 10, 2004)
- 10.29 Settlement Agreement, dated January 10, 2004, between Liquidmetal Korea Co., Ltd. and Growell Metal Co., Ltd. (incorporated by reference to Exhibit 10.29 to the Form 10-K filed on November 10, 2004)
- 10.30 Amended and Restated Securities Purchase Agreement, dated March 1, 2004, among Liquidmetal Technologies, Inc., Michigan Venture Capital Co., Ltd., and the investors identified as Purchasers therein (incorporated by reference to Exhibit 10.1 to the Form 8-K filed on July 2, 2004).
- 10.31 Form of 6% Senior Convertible Note issued under Amended and Restated Securities Purchase Agreement (incorporated by reference to Exhibit 10.2 to the Form 8-K filed on July 2, 2004).
- 10.32 Registration Rights Agreement, dated March 1, 2004, among Liquidmetal Technologies, Inc. and the purchasers under Amended and Restated Securities Purchase Agreement (incorporated by reference to Exhibit 10.3 to the Form 8-K filed on July 2, 2004).
- 10.33 Common Stock Purchase Warrant, dated March 1, 2004, granted by Liquidmetal Technologies, Inc. to Michigan Venture Capital Co., Ltd. (incorporated by reference to Exhibit 10.4 to the Form 8-K filed on July 2, 2004).
- 10.34 Factory Mortgage Agreement, dated March 1, 2004, among Liquidmetal Korea Co., Ltd., Michigan Venture Capital Co., Ltd., and the other parties identified therein (incorporated by reference to Exhibit 10.5 to the Form 8-K filed on July 2, 2004).

| | |
|-----------|---|
| 10.35 | Securities Purchase Agreement, dated March 1, 2004, among Liquidmetal Technologies, Inc. and the investors identified as Purchasers therein (incorporated by reference to Exhibit 10.6 to the Form 8-K filed on July 2, 2004). |
| 10.36 | Form of 6% Senior Convertible Note issued under Securities Purchase Agreement (incorporated by reference to Exhibit 10.7 to the Form 8-K filed on July 2, 2004). |
| 10.37 | Registration Rights Agreement, dated March 1, 2004, among Liquidmetal Technologies, Inc. and the purchasers under Securities Purchase Agreement (incorporated by reference to Exhibit 10.8 to the Form 8-K filed on July 2, 2004). |
| 10.38 | Form of Common Stock Purchase Warrant granted to purchasers under Securities Purchase Agreement (incorporated by reference to Exhibit 10.9 to the Form 8-K filed on July 2, 2004). |
| 10.39 | Form of Placement Agent Common Stock Purchase Warrant, dated March 1, 2004 (incorporated by reference to Exhibit 10.10 to the Form 8-K filed on July 2, 2004). |
| 10.40 | Security Agreement, dated March 1, 2004, between Liquidmetal Technologies, Inc. and Middlebury Capital LLC, as agent (incorporated by reference to Exhibit 10.11 to the Form 8-K filed on July 2, 2004). |
| 10.41 | Note Exchange Agreement, dated July 29, 2004, among Liquidmetal Technologies, Inc. and certain individuals identified as Noteholders therein (incorporated by reference to Exhibit 10.1 to the Form 8-K filed on August 20, 2004). |
| 10.42 | Form of 10% Senior Secured Notes Due 2005 of Liquidmetal Technologies, Inc. issued pursuant to Note Exchange Agreement filed as Exhibit 10.2 hereto (incorporated by reference to Exhibit 10.2 to the Form 8-K filed on August 20, 2004). |
| 10.43 | Form of 6% Senior Security Note Due 2007 of Liquidmetal Technologies, Inc. issued pursuant to Note Exchange Agreement filed as Exhibit 10.3 hereto (incorporated by reference to Exhibit 10.3 to the Form 8-K filed on August 20, 2004). |
| 10.44 | Note Exchange Agreement, dated July 29, 2004, among Liquidmetal Technologies, Inc and Winvest Venture Partners Inc. (incorporated by reference to Exhibit 10.4 to the Form 8-K filed on August 20, 2004). |
| 10.45 | 10% Senior Secured Notes Due 2005 of Liquidmetal Technologies, Inc. issued to Winvest Venture Partners Inc. (incorporated by reference to Exhibit 10.5 to the Form 8-K filed on August 20, 2004). |
| 10.46 | Form of 6% Senior Security Note Due 2007 of Liquidmetal Technologies, Inc. issued to Winvest Venture Partners Inc. (incorporated by reference to Exhibit 10.6 to the Form 8-K filed on August 20, 2004). |
| 10.47 (1) | Employment Agreement, dated January 14, 2005, between Liquidmetal Technologies, Inc. and John Thorne. |
| 14 | Code of Ethics for Chief Executive Officer and Senior Financial and Accounting Officers. (incorporated by reference to Exhibit 14 to the Form 10-K filed on November 10, 2004) |
| 21 | Subsidiaries of the Registrant. (incorporated by reference to Exhibit 21 to the Form 10-K filed on November 10, 2004) |
| 23.1 | Consent of Stonefield Josephson |
| 23.2 | Consent of Choi, Kim, & Park, LLP |
| 24.1 | Power of Attorney relating to subsequent amendments (included on the signature page(s) of this report). |
| 31.1 | Certification of Principal Executive Officer pursuant to Rule 13a-15(e) or 15d-15(e) of the Securities Exchange Act of 1934, as amended. |
| 31.2 | Certification of Principal Financial Officer pursuant to Rule 13a-15(e) or 15d-15(e) of the Securities Exchange Act of 1934, as amended. |
| 32.1 | Certification of Pursuant to 18 U.S.C. Section 1350 |

* Denotes a management contract or compensatory plan or arrangement required to be filed as an exhibit this Form 10-K.

(1) Previously filed

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Liquidmetal Technologies, Inc.

By: /s/ Ricardo A. Salas
Ricardo A. Salas
President and Chief Executive Officer

Date: July 20, 2006

By: /s/ Young Ham
Young Ham
Chief Financial Officer

Date: July 20, 2006

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POWER OF ATTORNEY

KNOW ALL THESE PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Ricardo A. Salas and Young Ham and each of them, jointly and severally, his attorneys-in-fact, each with full power of substitution, for him in any and all capacities, to sign any and all amendments to this Report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each said attorneys-in-fact or his substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K/A has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated:

| Signature | Title | Date |
|--|--|---------------|
| /s/ John Kang John Kang | Chairman of the Board and Director | July 20, 2006 |
| /s/ Ricardo A. Salas Ricardo A. Salas | Chief Executive Officer and President (Principal Executive Officer) | July 20, 2006 |
| /s/ James Kang James Kang | Founder and Director | July 20, 2006 |
| /s/ William Johnson William Johnson | Director | July 20, 2006 |
| /s/ Robert Biehl Robert Biehl | Director | July 20, 2006 |
| /s/ Dean Tanella Dean Tanella | Director | July 20, 2006 |
| /s/ CK Cho CK Cho | Director | July 20, 2006 |

Certifications provided as Exhibits.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited, before the effects of the adjustments for the correction of the error described in Note 2, the accompanying consolidated balance sheets of Liquidmetal Technologies, Inc. and subsidiaries (the Company) as of December 31, 2004 and 2003, and the related consolidated statements of operations and comprehensive loss, shareholders' equity (deficiency), and cash flows for each of the three years in the period ended December 31, 2004 (the 2004 financial statements before the effects of the adjustments discussed in Note 2 are not presented herein). Our audit also included the financial statement schedule listed at index in Item 15(a), except for the correction of the error described in Note 2, as of and for the years ended December 31, 2004. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

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

In our opinion, except for the error described in Note 2, such consolidated financial statements present fairly, in all material respects, the financial position of Liquidmetal Technologies, Inc. and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, except for the error described in Note 2, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

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

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

/s/ Stonefield Josephson, Inc.

Irvine, California
Certified Public Accountants

March 3, 2005

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited the effects of the adjustments for the correction of the error described in Note 2 as of and for the year ended December 31, 2004. We were not engaged to audit, review, or apply any procedures to the 2004 financial statements of the Company other than with respect to the adjustments and, accordingly, we do not express an opinion or any other form of assurance on the 2004 financial statements taken as a whole.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the effects of the adjustments for the correction of the error described in Note 2 as of and for the year ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

/s/ Choi, Kim & Park LLP.

Los Angeles, California
Certified Public Accountants

July 17, 2006

LIQUIDMETAL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

| | December 31, | 2003 |
|---|---------------------|---------------|
| | 2004 | |
| | (Restated) | |
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | \$ 742 | \$ 3,127 |
| Restricted cash | 754 | |
| Trade accounts receivable, net of allowance for doubtful accounts of \$108 and \$127 | 1,668 | 3,748 |
| Inventories | 2,353 | 2,060 |
| Prepaid expenses and other current assets | 930 | 395 |
| Assets available for sale, net | | 827 |
| Total current assets | 6,447 | 10,157 |
| PROPERTY, PLANT AND EQUIPMENT, NET | 16,434 | 17,743 |
| IDLE EQUIPMENT | 1,906 | 1,671 |
| LONG-TERM INVENTORY | 1,810 | |
| OTHER INTANGIBLE ASSETS, NET | 1,143 | 984 |
| OTHER ASSETS | 768 | 297 |
| Total assets | \$ 28,508 | \$ 30,852 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| CURRENT LIABILITIES: | | |
| Accounts payable and accrued expenses | \$ 4,969 | \$ 3,683 |
| Settlement payable | 3,246 | 2,765 |
| Deferred revenue | 900 | 1,435 |
| Long-term debt, current portion | 4,010 | 1,032 |
| Warrant liabilities | 550 | |
| Conversion feature liabilities | 6,650 | |
| Other current liabilities | 1,032 | 1,940 |
| Total current liabilities | 21,357 | 10,855 |
| LONG-TERM DEBT, NET OF CURRENT PORTION | 2,618 | 3,015 |
| OTHER LIABILITIES | 342 | 814 |
| Total liabilities | 24,317 | 14,684 |
| COMMITMENTS AND CONTINGENCIES | | |
| MINORITY INTEREST | | 5 |
| SHAREHOLDERS EQUITY: | | |
| Common stock, \$0.001 par value per share, 100,000,000 shares authorized; 41,609,652 shares issued and outstanding at December 31, 2004 and December 31, 2003 | 42 | 42 |
| Additional paid in capital | 129,650 | 128,581 |
| Unamortized stock-based compensation | | (128) |
| Accumulated deficit | (127,472) | (112,587) |
| Accumulated other comprehensive income | 1,971 | 255 |
| Total shareholders equity | 4,191 | 16,163 |

| | | |
|--|-----------|-----------|
| Total liabilities and shareholders' equity | \$ 28,508 | \$ 30,852 |
|--|-----------|-----------|

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

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LIQUIDMETAL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(in thousands, except per share data)

| | Years Ended December 31, | | |
|---|--------------------------|--------------|--------------|
| | 2004 | 2003 | 2002 |
| | (Restated) | | (Restated) |
| REVENUE, Net | \$ 17,429 | \$ 13,658 | \$ 9,138 |
| COST OF SALES | 12,168 | 18,162 | 5,656 |
| Gross profit (loss) | 5,261 | (4,504) | 3,482 |
| OPERATING EXPENSES: | | | |
| Selling, general and administrative | 11,591 | 17,729 | 13,099 |
| Research and development | 1,467 | 8,780 | 11,825 |
| Impairment of goodwill | | 184 | |
| Impairment of long lived assets | | 2,684 | |
| Total operating expenses | 13,058 | 29,377 | 24,924 |
| LOSS BEFORE INTEREST, OTHER INCOME, INCOME TAXES | | | |
| MINORITY INTEREST AND DISCONTINUED OPERATIONS | (7,797) | (33,881) | (21,442) |
| Loss from extinguishments of debt | (2,941) | | |
| Change in value of warrants, gain | 747 | | |
| Change in value of conversion feature, gain | 2,093 | | |
| Other income | 302 | | |
| Interest expense | (6,577) | (390) | (1,109) |
| Interest income | 37 | 304 | 506 |
| Gain on sale of marketable securities held-for-sale | | 1,178 | 832 |
| LOSS BEFORE INCOME TAXES, MINORITY INTEREST AND DISCONTINUED OPERATIONS | (14,136) | (32,789) | (21,213) |
| Income taxes | | | |
| LOSS BEFORE MINORITY INTEREST AND DISCONTINUED OPERATIONS | (14,136) | (32,789) | (21,213) |
| Minority interest in loss of consolidated subsidiary | | 21 | 118 |
| LOSS FROM CONTINUING OPERATIONS | (14,136) | (32,768) | (21,095) |
| DISCONTINUED OPERATIONS: | | | |
| (Loss) income from operations of discontinued operations, net | (749) | (964) | 83 |
| Gain from disposal of discontinued operations, net | | 127 | 1,556 |
| NET LOSS | (14,885) | (33,605) | (19,456) |
| OTHER COMPREHENSIVE GAIN (LOSS): | | | |
| Foreign exchange translation gain (loss) during the period | 1,716 | 211 | (28) |
| Net unrealized (loss) gain on marketable securities available-for-sale | | (1,668) | 1,668 |
| COMPREHENSIVE LOSS | \$ (13,139) | \$ (35,062) | \$ (17,816) |
| PER COMMON SHARE BASIC and DILUTED: | | | |
| (Loss) from continuing operations | \$ (0.34) | \$ (0.79) | \$ (0.54) |
| (Loss) from discontinued operations | \$ (0.02) | \$ (0.02) | \$ 0.04 |
| Net (loss) | \$ (0.36) | \$ (0.81) | \$ (0.50) |
| Number of weighted average shares basic and diluted | 41,610 | 41,505 | 38,714 |

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

LIQUIDMETAL TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY (DEFICIENCY)

(in thousands, except share data)

| | Preferred Shares | Preferred Stock | Common Shares | Common Stock | Additional Paid in Capital (Restated) | Unamortized Stock-based Compen- sation (Restated) | Accumu- lated Deficit (Restated) | Accumulated Other Comprehensive Income (Loss) Total | |
|--|---------------------|--------------------|------------------|-----------------|--|---|---|--|-------------|
| Balance, December 31, 2001 (As Restated) | 456,857 | \$ 5,577 | 35,023,515 | \$ 29,752 | \$ 23,915 | \$ (7,294) | \$ (59,526) | \$ 72 | \$ (7,504) |
| Common stock issued | | | 5,229,000 | 78,435 | | | | | 78,435 |
| Transaction expenses of initial public offering including commissions | | | | (7,714) | | | | | (7,714) |
| Stock options exercised | | | 299,873 | 504 | | | | | 504 |
| Conversion of preferred stock to common stock | (456,857) | (5,577) | 456,857 | 5,577 | | | | | |
| Stock-based compensation | | | | | | 4,694 | | | 4,694 |
| Unamortized stock option based compensation | | | | | (2,340) | 2,340 | | | |
| Foreign exchange translation loss | | | | | | | (28) | | (28) |
| Net unrealized gain on marketable securities | | | | | | | | 1,668 | 1,668 |
| Net loss (as restated) | | | | | | | (19,456) | | (19,456) |
| Balance, December 31, 2002 (As Restated) | | \$ | 41,009,245 | \$ 106,554 | \$ 21,575 | \$ (260) | \$ (78,982) | \$ 1,712 | \$ 50,599 |
| Stock options exercised | | | 684,165 | 1,149 | | | | | 1,149 |
| Repurchase of shares | | | (93,758) | (653) | | | | | (653) |
| Change in par value due to Reincorporation | | | | (107,008) | 107,008 | | | | |
| Stock-based compensation | | | 10,000 | | 100 | 25 | | | 125 |
| Unamortized stock option based compensation | | | | | (107) | 107 | | | |
| Purchase of common stock of subsidiaries | | | | | 5 | | | | 5 |
| Foreign exchange translation gain | | | | | | | | 211 | 211 |
| Reclassification for net realized gain | | | | | | | | (1,668) | (1,668) |
| Net loss | | | | | | | (33,605) | | (33,605) |
| Balance, December 31, 2003 | | \$ | 41,609,652 | \$ 42 | \$ 128,581 | \$ (128) | \$ (112,587) | \$ 255 | \$ 16,163 |

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| | | | |
|--|------|------------|-----------|
| Stock-based compensation | 261 | 15 | 276 |
| Unamortized stock-based compensation | (113 |) 113 | |
| Redemption of convertible notes payable | 914 | | 914 |
| Warrants cancelled | 7 | | 7 |
| Foreign exchange translation gain | | | 1,716 |
| Net loss | | (14,885 |) 1,716 |
| | | | (14,885 |
| | | |) |
| Balance, December 31, 2004 (As Restated) | \$ | 41,609,652 | \$ 42 |
| | \$ | 129,650 | \$ |
| | \$ | (127,472 |)\$ 1,971 |
| | \$ | 4,191 | |

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

LIQUIDMETAL TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands, except share data)

| | Years Ended December 31, | | |
|--|--------------------------|--------------|--------------|
| | 2004 | 2003 | 2002 |
| | (Restated) | | (Restated) |
| OPERATING ACTIVITIES: | | | |
| Net (loss) | \$ (14,885) | \$ (33,605) | \$ (19,456) |
| Add (gain) loss from operations and loss on disposition of discontinued operations | 749 | 837 | (1,639) |
| Loss from continuing operations | (14,136) | (32,768) | (21,095) |
| Adjustments to reconcile net loss to net cash used by operating activities: | | | |
| Impairment of long lived assets | | 2,684 | |
| Impairment of goodwill | | 184 | |
| Loss from Growell settlement | | 2,765 | |
| Gain on sale of marketable securities held-for-sale | | (1,178) | (832) |
| Gain on disposal of property and equipment | 4 | | |
| Minority interest | | (21) | (118) |
| Bad debt expense | 84 | (28) | 921 |
| Warranty expense | 288 | (297) | 237 |
| Depreciation and amortization | 3,444 | 4,354 | 1,513 |
| Loss on extinguishments of debt | 2,941 | | |
| Amortization of debt discount | 5,834 | | 912 |
| Stock-based compensation | 276 | 123 | 2,203 |
| Gain from change in value of warrants | (747) | | |
| Loss (gain) from change in value of conversion feature | (2,093) | | |
| Changes in operating assets and liabilities: | | | |
| Trade accounts receivable | 1,996 | 1,660 | (5,319) |
| Inventories | (2,103) | (100) | (1,432) |
| Prepaid expenses and other current assets | (535) | 1,689 | (990) |
| Other assets | (869) | 83 | (189) |
| Accounts payable and accrued expenses | 998 | (5,969) | 5,990 |
| Deferred revenue | (535) | 38 | 567 |
| Other liabilities | (1,244) | 2,661 | |
| Net cash used by continuing operations | (6,397) | (24,120) | (17,632) |
| Net cash provided (used) by discontinued operations | 73 | (2,429) | (2,756) |
| Net cash used by operating activities | (6,324) | (26,549) | (20,388) |
| INVESTING ACTIVITIES: | | | |
| Purchases of property and equipment | (73) | (2,329) | (23,527) |
| Proceeds from sale of property and equipment | 38 | | |
| Purchase of marketable securities held-for-sale | | | (2,000) |
| Proceeds from sale of marketable securities held-for-sale | | 2,578 | 1,432 |
| Acquisition of subsidiary, net of cash received | | | 74 |
| Investment in patents and trademarks | (273) | (298) | (144) |
| Net cash used by investing activities | (308) | (49) | (24,165) |
| FINANCING ACTIVITIES: | | | |
| Proceeds from borrowings | 9,924 | 5,488 | 3,500 |
| Repayment of borrowings | (5,184) | (1,441) | (7,400) |
| Repayment of other liabilities | (135) | (72) | (14) |
| Restricted cash | (754) | | |
| Proceeds from issuance of common stock, net of offering costs | | | 70,721 |
| Stock options exercised | | 899 | 504 |
| Proceeds from issuance (repurchase) of common stock by subsidiaries, net | | 5 | |

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| | | | |
|--|----------|-----------|-----------|
| Net cash provided by financing activities | 3,851 | 4,879 | 67,311 |
| EFFECT OF FOREIGN EXCHANGE TRANSLATION | 396 | (212) | 70 |
| NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS | (2,385) | (21,931) | 22,828 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD | 3,127 | 25,058 | 2,230 |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | \$ 742 | \$ 3,127 | \$ 25,058 |
| SUPPLEMENTAL CASH FLOW INFORMATION | | | |
| Interest paid | \$ 640 | \$ 443 | \$ 52 |
| Taxes paid | \$ | \$ | \$ |

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

In 2004, the Company sold its 51% ownership interest in Dongyang to the 49% minority shareholder, which resulted in a loss of \$46 from disposal of discontinued operations.

In 2004, the Company sold assets and liability of its Taesung equipment manufacturing division in Korea to a third party which resulted in a loss of approximately \$184.

In 2003, an option holder surrendered 93,758 shares of the Company's common stock in lieu of cash payment for the option exercise price of \$250 and income taxes payable by the option holder of \$403. The Company immediately canceled the common shares received in lieu of cash payment upon receipt of the shares.

In 2003 the Company reclassified \$1,477 of machines from property, plant and equipment to machines held by customer.

In 2003, the Company entered into a lease agreement for \$291 of laboratory equipment that was recorded as a capital lease obligation.

In 2002, \$2,570 in notes payable and accrued interest were converted to the Company's common stock.

In 2002, the Company recorded a net addition to shareholders' equity of \$2,492 comprised of stock compensation and discounts on convertible notes payable in the discontinued retail golf operations. In 2002, there was a \$98 foreign exchange loss effect in the discontinued retail golf operations.

In 2002, the Company entered into a lease agreement for \$107 of office furniture that was recorded as a capital lease obligation.

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

LIQUIDMETAL TECHNOLOGIES, INC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the Years Ended December 31, 2004, 2003, and 2002

(in thousands, except share data)

1. Description of Business

Liquidmetal Technologies, Inc. (Liquidmetal Technologies) and its subsidiaries (collectively the Company) are in the business of developing, manufacturing, and marketing products made from amorphous alloys. Liquidmetal Technologies markets and sells Liquidmetal® alloy industrial coatings and also manufactures, markets and sells products and components from bulk Liquidmetal alloys that can be incorporated into the finished goods of its customers across a variety of industries. The Company also partners with third-party licensees and distributors to develop and commercialize Liquidmetal alloy products.

The Company classifies operations into two reportable segments: Liquidmetal alloy industrial coatings and bulk Liquidmetal alloys. Liquidmetal alloy industrial coatings are used primarily as a protective coating for industrial machinery and equipment, such as drill pipe used by the oil drilling industry and boiler tubes used by coal-burning power plants. Bulk Liquidmetal alloys include potential market opportunities to manufacture and sell products and components for electronic devices, medical devices, defense applications, and sporting goods. In addition, the bulk Liquidmetal alloys segment includes tooling and prototype sampling, and the manufacture and sale of die casting and VIM equipment (see Note 4 for disclosure regarding the disposal of this segment). In addition, such alloys are used to generate research and development services revenue for developing uses related primarily to defense and medical applications as well as potential license fees, royalties, and other compensation from strategic partnering transactions.

On August 4, 2004, the Company established a post-processing plant in the city of Weihai in Shandong province of China under Weihai Liquidmetal Company Limited, which is 100 percent owned by Liquidmetal Korea, to facilitate our bulk alloy manufacturing business. Weihai Liquidmetal is consolidated into Liquidmetal Technologies with all intercompany transactions eliminated.

2. Restatement

As a part of the accompanying consolidated financial statements and the notes thereto, the Company has restated certain previously issued financial statements due to an error related to the Company's accounting for embedded convertible feature of senior convertible notes issued in March 2004, which was exchanged in August 2004, in accordance with Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, (SFAS 133).

The Company previously had incorrectly accounted for the conversion feature of senior convertible notes during 2004 and 2005 in additional paid in capital for the beneficial conversion feature of the notes under Emerging Issues Task Force (EITF) 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock, and EITF 00-27 Application of Issue No. 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios, to Certain Convertible Instruments. The Company had failed to identify and account for the conversion feature as an embedded derivative in accordance with SFAS 133.

The correction of the error to properly state the fair value of the embedded conversion feature of senior convertible notes in accordance with SFAS 133 resulted in recognition of \$7,595 as a conversion feature liability as of the issuance of the senior convertible note in March 2004 as the convertible notes are considered non-conventional convertible debt instrument. The correction resulted in recognition of the change in fair value of the embedded conversion feature in the Company's earnings as a gain of \$2,093 for the year ended December 31, 2004, as well as adjustments to amortization of debt discount as interest expense of \$2,974 for the year ended December 31, 2004, and an additional loss on extinguishment of debt of \$1,278 for the year ended December 31, 2004. Additionally, the Company recognized \$914 in additional paid in capital from redemption and conversion of convertible notes as of December 31, 2004 (see Note 15). As part of the restatement, reclassifications to prior period consolidated financial statements have been made for consistent presentation of our warrant liabilities, settlement payable, and

change in value of warrant liabilities.

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The effects of the restatements are as follows:

| | As of December 31, | |
|---|--------------------------------|------------------|
| | 2004 Previously Reported | 2004 Restated |
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 742 | \$ 742 |
| Restricted cash | 754 | 754 |
| Trade accounts receivables, net of allowance for doubtful accounts | 1,668 | 1,668 |
| Inventories | 2,353 | 2,353 |
| Prepaid expenses and other current assets | 930 | 930 |
| Total current assets | 6,447 | 6,447 |
| Property, plant and equipment, net | 16,434 | 16,434 |
| Idle equipment | 1,906 | 1,906 |
| Long-term inventory | 1,810 | 1,810 |
| Other intangibles, net | 1,143 | 1,143 |
| Other assets | 768 | 768 |
| Total assets | \$ 28,508 | \$ 28,508 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable and accrued expenses | \$ 4,969 | \$ 4,969 |
| Settlement payable | 3,246 | 3,246 |
| Deferred revenue | 900 | 900 |
| Short-term debt | | |
| Long-term debt, current portion, net of debt discount | 5,991 | 4,010 |
| Other liabilities, current portion | 1,032 | 1,032 |
| Warrant liabilities | 550 | 550 |
| Conversion feature liabilities | | 6,650 |
| Total current liabilities | 16,688 | 21,357 |
| Long-term debt, net of current portion and debt discount | | |
| March 31, 2006, December 31, 2005 and 2004, respectively | 2,618 | 2,618 |
| Other long-term liabilities, net of current portion | 342 | 342 |
| Total liabilities | 19,648 | 24,317 |
| Shareholder's equity (deficiency): | | |
| Common stock, \$0.001 par value; 100,000,000 shares authorized and 41,609,652 issued and outstanding at December 31, 2004 | 42 | 42 |
| Additional paid-in capital | 132,160 | 129,650 |
| Accumulated deficit | (125,313) | (127,472) |
| Accumulated other comprehensive income | 1,971 | 1,971 |
| Total shareholder's equity (deficiency) | 8,860 | 4,191 |
| Total liabilities and shareholder's equity (deficiency) | \$ 28,508 | \$ 28,508 |

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| | Years ended December 31, | |
|--|---------------------------------|-----------------|
| | 2004 | 2004 |
| | Previously | Restated |
| | Reported | |
| Revenue | \$ 17,429 | \$ 17,429 |
| Cost of sales | 12,168 | 12,168 |
| Gross (loss) profit | 5,261 | 5,261 |
| Operating expenses | | |
| Selling, general, and administrative | 11,591 | 11,591 |
| Research and development | 1,467 | 1,467 |
| Impairment of goodwill | | |
| Impairment of long lived assets | | |
| Total operating expenses | 13,058 | 13,058 |
| Loss before interest, other income, income taxes, minority interest, and discontinued operations | (7,797) | (7,797) |
| Loss from extinguishments of debt | (1,663) | (2,941) |
| Change in value of warrants, gain | 747 | 747 |
| Change in value of conversion feature, gain | | 2,093 |
| Other income | 302 | 302 |
| Interest expense | (3,603) | (6,577) |
| Interest income | 37 | 37 |
| Gain on sale of marketable securities held-for-sale | | |
| Loss before income taxes, minority interest and discontinued operations | (11,977) | (14,136) |
| Income taxes | | |
| Loss before minority interest and discontinued operations | (11,977) | (14,136) |
| Minority interest in loss of consolidated subsidiary | | |
| Loss from continuing operations | (11,977) | (14,136) |
| Discontinued operations: | | |
| Income (loss) from operations of discontinued operations, net | (749) | (749) |
| Gain (loss) from disposal of discontinued operations, net | | |
| Net Loss | (12,726) | (14,885) |
| Other comprehensive gain (loss): | | |
| Foreign exchange translation gain during the period | 1,716 | 1,716 |
| Net unrealized gain (loss) on marketable securities available-for-sale | | |
| Comprehensive loss | \$ (11,010) | \$ (13,169) |
| Per common share basic and diluted: | | |
| Loss per share - continuing operations | (0.29) | (0.34) |
| Loss per share - discontinuing operations | (0.02) | (0.02) |
| Loss per share basic and diluted | (0.31) | (0.36) |
| Number of weighted average shares - basic and diluted | 41,610 | 41,610 |

3. Going Concern / Liquidity

The Company has experienced losses from continuing operations during the last two fiscal years and has an accumulated deficit of \$127,472 as of December 31, 2004. Cash used for continuing operations for the year ended December 31, 2004 was \$6,397 and cash flow from continuing operations may be negative throughout fiscal year 2005. At December 31, 2004, the Company's principal source of liquidity is \$742 of cash and cash equivalents and trade accounts receivable of \$1,668. Such conditions raise substantial doubt that the Company will be able to continue as a

going concern for a reasonable period of time. These operating results occurred while the Company was developing and attempting to commercialize and manufacture products from an entirely new and unique technology. This business plan required significant spending related to start-up costs and capital expenditures. These factors have placed a significant strain on the financial resources of the Company. The ultimate success of the Company depends on its ability to continue reducing operating costs, generate higher revenue, and achieve positive cash flow from continuing operations and profitability. The consolidated financial statements do not include any adjustments that might result from the outcome of the uncertainty.

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Capital requirements during the next 12 months will depend on numerous factors, including the success of existing products, the development of new applications for Liquidmetal alloys, and the resources devoted to develop and support Liquidmetal alloy products. However, the Company anticipates capital expenditures in the next 12 months will be less than \$0.5 million. The Company expects to continue to devote limited capital to our research and development activities, to further develop and strengthen our manufacturing capabilities, and for working capital and other general corporate purposes.

Our cash flow projections from operations and, consequently, future cash needs are subject to uncertainty. If our available funds and cash generated from operations are insufficient to satisfy our liquidity requirements, we may need to raise additional capital to fund our operations and capital expenditure requirements. We cannot be certain that additional capital, whether through selling additional debt or equity securities or obtaining a line of credit or other loan, will be available to us or, if available, will be on terms acceptable to us. If we issue additional securities to raise funds, these securities may have rights, preferences, or privileges senior to those of the rights of our common stock and our stockholders may experience additional dilution.

4. Summary of Significant Accounting Policies

Principles of Consolidation. The consolidated financial statements include the accounts of Liquidmetal Technologies, Inc. and its wholly-owned subsidiaries, Liquidmetal Korea Co., Ltd. (LMT Korea), located in South Korea, Chusik Hoesa Dongyang Yudoro (Dongyang), now accounted for as a discontinued operations, and Liquidmetal Golf and its subsidiaries, which included the retail golf segment, now accounted for as a discontinued operations. The Company acquired its 51% interest in Dongyang in 2002. The aggregate purchase price was \$333 in cash. As of March 2004, the Company divested of its 51% ownership in Dongyang to the minority shareholder. In June 2004, the Company sold assets and liability of its Taesung equipment manufacturing division in Korea to a third party. Accordingly, the results of Dongyang and Taesung s operations have been reclassified in the consolidated financial statements as discontinued operations (see Note 18). Previously, the results of Donyang and Taesung s operations have been included in the consolidated financial statements from the acquisition date. All intercompany balances and transactions have been eliminated. A minority interest in Liquidmetal Golf is included in the consolidated financial statements as a component of the loss from operations of the discontinued retail golf segment (see Note 18). Effective in 2003, management closed the Japan operations and the Seoul office, which did not result in a significant impact on the financial position or results of operations for any of the periods presented. Also, effective in December 2003, management closed the Tampa office (see Note 13). In August 2004, the Company established a post-processing plant in the city of Weihai in Shandong province of China under Weihai Liquidmetal Company Limited, which is 100 percent owned by Liquidmetal Korea, to facilitate our bulk alloy manufacturing business.

Sales of Stock by Subsidiaries. Gains on sales of stock by Liquidmetal Golf are recognized as components of the Company s shareholders equity (deficiency).

Revenue Recognition. Revenue is recognized pursuant to applicable accounting standards including Securities and Exchange Commission (SEC) Staff Accounting Bulletin (SAB) No. 101 (SAB 101), *Revenue Recognition in Financial Statements* , and *SAB 104, Revenue Recognition*. SAB 101 as amended and SAB 104 summarize certain points of the SEC staff s views in applying generally accepted accounting principles to revenue recognition in financial statements and provides guidance on revenue recognition issues in the absence of authoritative literature addressing a specific arrangement or a specific industry. The Company s revenue recognition policy complies with the requirements of SAB 101 and SAB 104. Revenue is recognized at the time the Company ships its products, as this is when title passes to the customer and all other incidences of a sale have occurred. Revenue is deferred and included in liabilities when the Company receives cash in advance for services not yet performed or goods not yet delivered. Revenue from research and development contracts is recognized under the percentage of completion method.

Cash and Cash Equivalents. The Company considers all highly liquid investments with maturity dates of three months or less when purchased to be cash equivalents. The Company limits the amount of credit exposure to each individual

financial institution and places its temporary cash into investments of high credit quality. There are no significant concentrations of credit risk to the Company associated with cash and cash equivalents.

Restricted Cash. The Company considers all cash and cash equivalents held under restrictive accounts as restricted cash.

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Marketable Securities. The Company follows Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and classifies all of its investment securities as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses reported in Shareholders' Equity (Deficiency) under the caption Accumulated Other Comprehensive Income.

Trade Accounts Receivables. The Company grants credit to its customers generally in the form of short-term trade accounts receivable. The creditworthiness of customers is evaluated prior to the sale of inventory. As of December 31, 2004, two customers represented 30%, or \$497, of the total outstanding trade accounts receivable. Two customers represent 95%, or \$3,540, of total outstanding trade accounts receivable as of December 31, 2003.

The allowance for doubtful accounts reflects management's best estimate of probable losses inherent in the trade accounts receivable. Management primarily determines the allowance based on the aging of accounts receivable balances, historical write-off experience, customer concentrations, customer creditworthiness and current industry and economic trends. The Company's provisions for uncollectible receivables are included in selling, general and administrative expense in the accompanying consolidated statements of operations and comprehensive loss.

Inventories. Inventories are accounted for using the moving average basis and reported at the lower of cost or market. Inventories consist of raw materials, work in process, and finished goods. The Company records write-offs for inventory obsolescence when it is deemed that there is impairment of the value of the inventories on hand.

Property, Plant and Equipment. Property, plant and equipment are stated at cost less accumulated depreciation and amortization. Additions and major renewals are capitalized. Repairs and maintenance are charged to expense as incurred. Upon disposal, the related cost and accumulated depreciation are removed from the accounts, with the resulting gain or loss included in operating income. Depreciation is provided principally on the straight-line method over the estimated useful lives of the assets, which range from two to twenty years.

Leased property meeting certain criteria is capitalized and the present value of the related lease payments is recorded as a liability. Amortization of capitalized leased assets is provided on the straight-line method over the estimated useful lives of the assets, which is five years.

Intangible Assets. Intangible assets consist of the costs incurred to purchase patent rights and costs incurred to internally develop patents and trademarks. Intangible assets are reported net of accumulated amortization. Patents and trademarks are amortized using the straight-line method over a period based on their contractual lives ranging from eleven to seventeen years.

Goodwill. Beginning January 1, 2002, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets* (See New Accounting Pronouncements). According to this statement, goodwill and other intangible assets are no longer subject to amortization, but instead must be reviewed annually for impairment by applying a fair value-based test.

Impairment of Long-lived Assets. The Company reviews long-lived assets to be held and used in operations for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may be impaired. An impairment loss is recognized when the estimated fair value of the assets is less than the carrying value of the assets. During 2003, the Company recognized an impairment of long-lived assets in the amount of \$2,684 (see Note 8). There were no such impairment losses in 2004.

Fair Value of Financial Instruments. The estimated fair value of amounts reported in the consolidated financial statements have been determined using available market information and valuation methodologies, as applicable. The carrying amount of cash and cash equivalents, accounts receivable, accounts payable, and all other current assets and liabilities

approximate their fair value because of their short term maturities at December 31, 2004 and 2003, unless otherwise stated. The fair value of non-current assets and liabilities approximate their carrying value unless otherwise stated. The fair value of the Company's long-term debt is based on interest rates that would be available to the Company for the issuance of debt with similar terms.

Research and Development Expenses. Research and development expenses represent salaries, related benefits expense, expenses incurred for the design and testing of new processing methods and other expenses related to the research and development of Liquidmetal alloys. Development costs incurred in research and development activities are expensed as incurred.

Advertising and Promotion Expenses. Advertising and promotion expenses are expensed when incurred. Advertising and promotion expenses were \$239, \$136, and \$127 for the years ended December 31, 2004, 2003 and 2002, respectively.

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Debt Discount Amortization. Debt discounts for notes payable are amortized to interest expense, using a method that approximates the interest method over the term of the related debt instruments.

Stock-Based Compensation. The Company applies Accounting Principles Board (APB) Opinion No. 25 for options when the exercise price of options granted to employees is less than the fair value of the underlying stock on the date of grant. The Company applies Statement of Financial Accounting Standards (SFAS) No. 123 for options granted to non-employees who perform services for the Company.

Had the Company determined employee stock-based compensation cost based on the fair value at the grant date for stock options consistent with the method of SFAS No. 123, the Company's net loss and basic and diluted net loss per share would have been as follows:

| | For the years ended December 31, | | |
|---|----------------------------------|--------------|--------------------|
| | 2004 (Restated) | 2003 | 2002 (Restated) |
| Net loss from Continuing Operations: | | | |
| As reported | \$ (14,136) | \$ (32,768) | (21,095) |
| Add: stock-based employee compensation expense included in reported net loss, net of related tax effects | 276 | 123 | 2,203 |
| Deduct: total stock-based employee compensation expense determined under the fair value based method for all awards | (4,201) | (5,427) | (7,664) |
| Proforma net loss from continuing operations | \$ (18,061) | \$ (38,072) | \$ (26,556) |
| Basic and diluted net loss per share: | | | |
| As reported | \$ (0.34) | (0.79) | (0.54) |
| Proforma | (0.43) | (0.92) | (0.69) |

Income Taxes. Income taxes are provided under the asset and liability method as required by SFAS No. 109, *Accounting for Income Taxes*. Under this method, deferred income taxes are recognized for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. The effect of a tax rate change on deferred taxes is recognized in operations in the period that the change in the rate is enacted. Valuation allowances are established when necessary to reduce net deferred tax assets to the amount expected to be realized.

Translation of Foreign Currency. Upon consolidation of the Company's foreign subsidiaries into the Company's consolidated financial statements, any balances with the subsidiaries denominated in the foreign currency are translated at the exchange rate at year end. The financial statements of LMT Korea have been translated based upon Korean Won as the functional currency. LMT Singapore's and LMT Korea's assets and liabilities were translated using the exchange rate at year end and income and expense items were translated at the average exchange rate for the year. The resulting translation adjustment was included in other comprehensive income (loss).

The Company applies *FASB No. 52, Foreign Currency Translation*, for translating foreign currency into US dollars in our consolidation of the financial statements. Due to our restatement of 2002 financial statements, certain footnote disclosures and previously reported financial statements were adjusted to conform to retroactive applications of FASB No. 52. These adjustments did not have a material impact in the financial statements. See Note 2 in the notes to consolidated financial statements in the fiscal 2003 annual report on Form 10-K filed on November 10, 2004, which reflects the restatements of prior year transactions.

Earnings Per Share. Basic earnings per share (EPS) is computed by dividing earnings (losses) attributable to common

shareholders by the weighted average number of common shares outstanding for the periods. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported periods. Actual results could differ from those estimates. These management estimates are primarily related to impairment of long-lived assets, inventory valuation, product warranty, and the allowance for bad debt account balances.

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Reclassifications. Certain amounts from prior years have been reclassified to conform to the current year's presentation.

New Accounting Pronouncements.

In December 2003, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition. SAB 104 supersedes SAB 101, Revenue Recognition in Financial Statements. SAB 104's primary purpose is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superseded as a result of the issuance of EITF 00-21, Accounting for Revenue Arrangements with Multiple Deliverables. Additionally, SAB 104 rescinds the SEC's Revenue Recognition in Financial Statements Frequently Asked Questions and Answers (the FAQ) issued with SAB 101 that had been codified in SEC Topic 13, Revenue Recognition. Selected portions of the FAQ have been incorporated into SAB 104. While the wording of SAB 104 has changed to reflect the issuance of EITF 00-21, the revenue recognition principles of SAB 101 remain largely unchanged by the issuance of SAB 104, which was effective upon issuance. The adoption of SAB 104 did not impact the consolidated financial statements.

In March 2004, the FASB approved the consensus reached on the Emerging Issues Task Force (EITF) Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. The objective of this Issue is to provide guidance for identifying impaired investments. EITF 03-1 also provides new disclosure requirements for investments that are deemed to be temporarily impaired. In September 2004, the FASB issued a FASB Staff Position (FSP) EITF 03-1-1 that delays the effective date of the measurement and recognition guidance in EITF 03-1 until after further deliberations by the FASB. The disclosure requirements are effective only for annual periods ending after June 15, 2004. The Company has evaluated the impact of the adoption of the disclosure requirements of EITF 03-1 and does not believe the impact will be significant to the Company's overall results of operations or financial position. Once the FASB reaches a final decision on the measurement and recognition provisions, the company will evaluate the impact of the adoption of EITF 03-1.

In November 2004, the FASB issued SFAS No. 151 Inventory Costs, an amendment of ARB No. 43, Chapter 4. The amendments made by Statement 151 clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The guidance is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 23, 2004. The Company has evaluated the impact of the adoption of SFAS 151, and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In December 2004, the FASB issued SFAS No. 153, Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions. The amendments made by Statement 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. Opinion 29 provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. The Board believes that exception required that some nonmonetary exchanges, although commercially substantive, be recorded on a carryover basis. By focusing the exception on exchanges that lack commercial substance, the Board believes this Statement produces financial reporting that more faithfully represents the economics of the transactions. The Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of this Statement shall be applied prospectively. The Company has evaluated the impact of the adoption of SFAS 153, and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), Share-Based Payment. Statement 123(R) will provide investors and other users of financial statements with more complete and neutral financial information by requiring that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. Statement 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. Statement 123(R) replaces FASB Statement No. 123, Accounting for Stock-Based Compensation, and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. Statement 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that Statement permitted entities the option of continuing to apply the guidance in Opinion 25, as long as the footnotes to financial statements disclosed what net income would have been had the preferable fair-value-based method been used. Public entities (other than those filing as small business issuers) will be required to apply Statement 123(R) as of the first interim or annual reporting period that begins after June 15, 2005. The Company has evaluated the impact of the adoption of SFAS 123(R), and does not believe the impact will be significant to the Company's overall results of operations or financial position.

In December 2004 the Financial Accounting Standards Board issued two FASB Staff Positions FSP FAS 109-1, *Application of FASB Statement 109 Accounting for Income Taxes to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*, and FSP FAS 109-2 *Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004*. Neither of these affected the Company as it does not participate in the related activities.

5. Marketable Securities

On July 29, 2002, the Company invested \$2,000 in Growell Metal, Inc. (Growell), a metals processing company located in South Korea and publicly traded on South Korea's KOSDAQ stock market. The Company acquired 891,100 shares (or approximately 5%) of Growell's outstanding common stock in this transaction. During the fourth quarter of 2002, Growell's spin-off of its electronics division resulted in the creation of a new company named Growell Electronics, Inc. (Growell Electronics). As a result of the spin-off, 30% of the Company's 891,100 common shares of Growell were exchanged for an equal number of shares in the common stock of Growell Electronics. During the year ended December 31, 2002, the Company sold its shares in Growell Electronics for approximately \$1,432, which was based on the market price of the stock on the KOSDAQ stock market on the date of sale. This sale resulted in a realized gain of \$832. At December 31, 2002, the change in fair value of the remaining investment in Growell resulted in an unrealized gain of \$1,668, which is reported as other comprehensive income in the accompanying consolidated financial statements. In April 2003, the Company sold the stock owned in Growell, which resulted in a realized gain of \$1,178. A reclassification adjustment of (\$1,668) for net realized gains included in net loss is included in Other comprehensive loss on the accompanying Statement of Operations and Comprehensive Loss for the year ended December 31, 2003.

6. Trade accounts receivable

Trade accounts receivables from continuing operations were comprised of the following:

| | December 31, | |
|---------------------------------------|--------------|----------|
| | 2004 | 2003 |
| Trade accounts receivable | \$ 1,776 | \$ 3,875 |
| Less: Allowance for doubtful accounts | (108) | (127) |
| Trade accounts receivable, net | \$ 1,668 | \$ 3,748 |

7. Inventories

Inventories were comprised of the following:

| | December 31, | |
|---------------------------|--------------|----------|
| | 2004 | 2003 |
| Raw materials | \$ 1,688 | \$ 643 |
| Work in process | 352 | 284 |
| Finished goods | 313 | 442 |
| Machines held by customer | | 691 |
| Total current inventories | 2,353 | 2,060 |
| Long-term inventories | 1,810 | |
| Total inventories | \$ 4,163 | \$ 2,060 |

During 2003, the Company experienced significant operational difficulties as a result of problems and delays encountered in manufacturing bulk amorphous parts. These issues led the Company to begin assessing its long-term strategy. As a result of changes made to the Company's manufacturing objectives, the Company determined that it held excessive volumes of certain raw materials at December 31, 2003. Accordingly, the Company reduced the carrying value of raw materials held by its subsidiary, Liquidmetal Korea, by the amounts considered to be obsolete. The write-downs amounted to \$1,004 and are included in Cost of Sales in the accompanying Statement of Operations and Comprehensive Loss for the year ended December 31, 2003. As of December 31, 2004, the write-downs included in Cost of Sales in the accompanying Statement of Operations and Comprehensive Loss amounted to \$605, which includes a \$406 charge incurred during the fourth quarter of 2004 related to certain hinge finished goods used in our customer's cell phone models which were nearing its end of life.

Machines held by customer represent machines conditionally sold to Growell in 2002 and 2003. These machines are subject to put options whereby Growell has the right to require the Company to buy back the machines if certain conditions are not met. The Company recorded a write-down of \$2,765 of raw material and machine inventory associated with the settlement of a dispute with Growell in December 2003 (see Note 12). These amounts are included in Cost of Sales in the accompanying Statement of Operations and Comprehensive Loss for the years ended December 31, 2003 and 2002 respectively.

The Company maintains certain of its raw material inventory in amounts excess of our operating cycle of one year due to the nature of our manufacturing process, production lead time, and the recyclability of our raw material. Therefore, the Company has determined and allocated \$1,810 of raw material as long term inventory in 2004. Long term inventory was \$0 in 2003 as our business strategy of selling Liquidmetal ingots that were included in raw material inventory were within our one year operating cycle.

8. Property, Plant and Equipment

Property, plant and equipment consists of the following:

| | December 31, 2004 | 2003 |
|--|----------------------|-----------|
| Machinery and equipment | \$ 12,600 | \$ 11,122 |
| Computer equipment | 1,357 | 1,355 |
| Office equipment, furnishings and improvements | 1,910 | 1,838 |
| Buildings | 9,719 | 8,503 |
| Total | 25,586 | 22,818 |
| Accumulated depreciation | (9,152) | (5,075) |
| Total property, plant and equipment, net | \$ 16,434 | \$ 17,743 |

Depreciation expense is classified as follows:

| | Years ended December 31, | | |
|-------------------------------------|--------------------------|----------|--------------------|
| | 2004 | 2003 | 2002 (Restated) |
| Cost of sales | \$ 2,623 | \$ 2,908 | \$ 403 |
| Selling, general and administrative | 700 | 627 | 229 |
| Research and development | 8 | 730 | 799 |
| Total depreciation expense | \$ 3,331 | \$ 4,265 | \$ 1,431 |

During 2003, the Company experienced significant operational difficulties as a result of problems and delays encountered in manufacturing bulk amorphous parts. These events, along with the Company's history of operating or cash flow losses and uncertainty surrounding its future cash flows, led the Company to evaluate its long-lived assets for recoverability as of December 31, 2003. As a result, the Company determined that the carrying value of its manufacturing plant in Pyongtaek, South Korea exceeded its fair value as of December 31, 2003 in the amount of \$2,684. The fair value of the building was based on the average of two independent appraisals of the building. This impairment loss is recorded in operating expenses as Impairment of long lived assets in the accompanying Consolidated Statement of Operations and Comprehensive Loss for the year ended December 31, 2003.

9. Idle Equipment

Idle equipment consists of certain equipment held by the Company for use in expansion of bulk alloy parts manufacturing in 2005. The equipment was presented as machines held by a customer in 2003 as inventory, which represented machines conditionally sold to Growell in 2002 and 2003 (see Note 7). The equipment was included in inventory as of December 31, 2003 as the Company was anticipating the sale of the equipment to a customer in 2004. However, the anticipated sale did not take place during 2004. While the Company is actively marketing the equipment for ultimate sale, the equipment may be used internally to meet future capacity requirements for expansion of our business. As of December 31, 2004, the idled equipment includes a foreign currency translation gain of \$235.

10. Other Intangible Assets

Intangible assets consist of the following:

| | December 31, | |
|--------------------------------------|---------------------|-------------|
| | 2004 | 2003 |
| Purchased and licensed patent rights | \$ 555 | \$ 517 |
| Internally developed patents | 1,056 | 824 |
| Trademarks | 85 | 83 |
| Total | 1,696 | 1,424 |
| Accumulated amortization | (553) | (440) |
| Total intangible assets, net | \$ 1,143 | \$ 984 |

Amortization expense was \$113, \$100, and \$82, for the years ended December 31, 2004, 2003, and 2002, respectively. The estimated aggregate amortization expense for each of the five succeeding years is as follows:

| December 31, | Aggregate Amortization Expense |
|--------------|---------------------------------------|
| 2005 | \$ 107 |
| 2006 | 104 |
| 2007 | 102 |
| 2008 | 100 |
| 2009 | 98 |

Accumulated Amortization for the years ended December 31, 2004 and 2003 is as follows:

| | December 31, | |
|--------------------------------------|---------------------|-------------|
| | 2004 | 2003 |
| Purchased and licensed patent rights | \$ (181) | \$ (126) |
| Internally developed patents | (352) | (302) |
| Trademarks | (20) | (12) |
| Total | \$ (553) | \$ (440) |

The weighted average amortization periods for each of the years ended December 31, 2004, 2003, and 2002 is as follows:

| | December 31, | | |
|-------------------------------------|---------------------|-------------|-------------|
| | 2004 | 2003 | 2002 |
| Purchased and licensed patent right | 17.0 | 17.0 | 17.0 |
| Internally developed patents | 17.0 | 17.0 | 17.0 |
| Trademarks | 10.0 | 10.0 | 10.0 |
| Total weighted | 13.5 | 13.5 | 13.5 |

Purchased patent rights represent the exclusive right to commercialize the bulk amorphous alloy and other amorphous alloy technology acquired from California Institute of Technology (Caltech), a shareholder, through a license agreement with Caltech (License Agreement). Under the License Agreement, the Company has the exclusive right to make, use, and sell products from all of Caltech 's inventions, proprietary information, know-how, and other technology relating to amorphous alloys in existence as of September 1, 2001. The Company also has an exclusive license to nine issued patents and four patent applications held by Caltech relating to amorphous alloy technology, as well as all related foreign counterpart patents and patent applications. Of the patents currently issued to Caltech and licensed by the Company, the earliest expiration date is 2013 and the latest expiration date is 2021. Furthermore, the license agreement gives the Company the exclusive right to make, use, and sell products from substantially all amorphous alloy technology that is developed in Professor William Johnson 's Caltech laboratory

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during the period September 1, 2001 through August 31, 2005. All fees and other amounts payable by the Company for these rights and licenses have been paid or accrued in full, and no further royalties, license fees or other amounts will be payable in the future under the License Agreements.

In addition to the patents and patent applications under the License Agreement with Caltech, the Company has internally developed patents. Internally developed patents include legal and registration costs incurred to obtain the respective patents. The Company currently holds various patents and numerous pending patent applications in the United States, as well as numerous foreign counterparts to these patents outside of the United States.

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11. Goodwill

During 2002, the Company completed an impairment review and did not recognize any impairment of goodwill. Accordingly, for 2002, the Company has forgone all related goodwill amortization expense. During 2003, Dongyang experienced net losses as a result of a continuing economic downturn in markets for its machinery products. These events, along with Dongyang's operating loss, cash flow losses and uncertainty surrounding its future cash flows, led the Company to evaluate its investment for recoverability as of December 31, 2003. As a result, the Company determined that the carrying value of its investment in Dongyang exceeded its fair value as of December 31, 2003 in the amount of \$184. This impairment loss is recorded in operating expenses as Impairment of Goodwill in the accompanying Statement of Operations and Comprehensive Loss for the year ended December 31, 2003.

In March 2004, the Company sold its 51% investment in Dongyang to the 49% minority shareholder (see Note 18).

12. Settlement Payable

The settlement payable balance consists of payables to Growell Metal Co., Ltd., a South Korean metals processing company (Growell), as a result of a settlement agreement executed in January 2004. Under terms of the January 2004 settlement of the dispute over certain sales transactions from 2003 and 2002 between Liquidmetal Korea and Growell, Liquidmetal Korea agreed to pay Growell \$4,895 to purchase Growell's investment in alloy inventories, proprietary alloying equipment purchased from Liquidmetal Korea, and supporting equipment purchased from other suppliers. Also as part of the settlement, Growell satisfied in full a balance of \$2,058 owed to Liquidmetal Korea for the die casting machines Growell purchased from Liquidmetal Korea in the first quarter of 2003 as part of a license agreement to manufacture Liquidmetal alloy parts for the South Korean automotive industry. **The remaining settlement payable of \$2,837 and trade accounts payable of \$14 were to be paid to Growell (in cash or stock at the Company's discretion) by December 31, 2004. As of December 31, 2004, the settlement payable was not paid to Growell due to Growell's breach of warranty on equipment repurchased by Liquidmetal Korea. The outstanding balance of payables to Growell from the settlement as of December 31, 2004 was \$3,246, net of foreign exchange translation loss. In January 2005, Growell was acquired by a third party and the Company is currently in negotiations to settle this balance with the third party.**

The Company recorded a loss on the settlement at December 31, 2003 of \$2,765 which is included in Cost of Sales in the December 31, 2003 Consolidated Statements of Operations and Comprehensive Loss. The loss on settlement reflects the write-down of the assets received in the settlement to their fair market value. The sale of the die casting machines to Growell was reflected in the first quarter of 2004. Under the settlement agreement between the parties, the Company and Growell granted to the other party (and the other party's affiliates) a release of all known and unknown claims of any nature arising between the parties through the date of settlement, as well as a release against future claims under agreements between the parties that were terminated as a part of the settlement. The settlement agreement provided that all agreements of any nature between the parties and their respective affiliates were terminated as of the date of settlement, with the exception of certain confidentiality agreements, a Liquidmetal coatings distribution agreement, and future rights under the die casting agreement pursuant to which Growell purchased the die casting machines and obtained a license to make auto parts from Liquidmetal alloys. The settlement agreement also includes, as an accommodation to Growell, if the Company becomes aware of any prospective customer that desires to purchase a proprietary Company casting machine at a time when Growell desires to sell any of its Liquidmetal die casting machines, then the Company will not sell such die casting machine to the prospective customer unless the Company first directs the prospective customer to Growell and encourages the prospective customer to purchase the machine from Growell.

13. Other Liabilities

The other liabilities balance consists of accrued severance and operating lease costs associated with the Company's cost reduction measures for the Tampa, Florida executive offices, a capital lease obligation for office furniture and furnishings and capital lease obligations for a SEM Microscope and a JSM Electron Microscope used in the laboratory in Lake Forest, California.

| | December 31, | |
|-------------------------------|--------------|----------|
| | 2004 | 2003 |
| Accrued severance | \$ 579 | \$ 1,683 |
| Accrued operating lease costs | 596 | 758 |
| Accrued capital lease costs | 213 | 348 |
| Total | 1,388 | 2,789 |
| Imputed interest | (14) | (35) |

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| | | |
|---|----------|----------|
| Total | 1,374 | 2,754 |
| Less current portion | (1,032) | (1,940) |
| Other long term liabilities, less current portion | \$ 342 | \$ 814 |

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During 2003, the Company initiated activities to substantially reduce the number of employees and consolidate manufacturing and administrative facilities to improve operational effectiveness and efficiency and reduce expenses. During the year ended December 31, 2003, there was a total of 225 employees terminated. The total amount of severance granted to the terminated employees is \$2,718 which is included in Cost of Sales in the amount of \$199, Selling, general and administrative in the amount of \$2,253, and Research and Development in the amount of \$266 in the accompanying Consolidated Statement of Operations for the year ended December 31, 2003. The amount of severance paid was \$1,104, and \$1,035 as of December 31, 2004 and 2003, respectively. The remaining severance owed to the terminated employees is \$579 and \$1,683 as of December 31, 2004 and 2003, respectively. The total severance granted to terminated employees of \$2,718 is separated into the following reportable segments as of December 31, 2003: Coatings at \$75 and Bulk alloy at \$2,643. The categories of employees that were eliminated include the following: Product management positions at various levels, including Vice President; entry level technicians; accounting and finance positions from entry level through executive; marketing mid to senior level positions; engineering mid to senior levels positions; information technology support; administrative, legal and executive support; senior internal legal counsel; human resources and senior executives. Also, there are other relocation expenses associated with relocating the Tampa, Florida office to Lake Forest, California totaling \$759, which includes the accrual of all remaining facility and telecommunication lease payments for the Tampa, Florida office. Total liability accrued from the relocation and terminations in 2003, including the severance and lease accruals, were \$1,175 and \$2,441 as of December 31, 2004 and 2003, respectively. The Company has substantially concluded all cost reduction and restructuring activities as of March 31, 2004. The current portion of the 2003 termination and relocation liability is \$909 and the long-term portion of the liability is \$266 at December 31, 2004. At December 31, 2003, the current portion of the 2003 termination and relocation liability was \$1,826 and the long-term portion of the liability was \$615.

All leases with an initial term greater than one year are accounted for under SFAS No. 13 *Accounting for Leases*. These leases are classified as either capital leases or operating leases, as appropriate. Assets under capital leases are capitalized using interest rates appropriate at the inception of each lease. At December 31, 2004, the cost recorded for the office furniture and furnishings, the SEM Microscope and the JSM 6360 Electron Microscope under the capital lease was \$107, \$47 and \$289, respectively, and the accumulated amortization was \$57, \$22 and \$89, respectively. At December 31, 2003, the cost recorded for the office furniture and furnishings, the SEM Microscope and the JSM 6360 Electron Microscope under the capital lease was \$107, \$47 and \$289, respectively and the accumulated amortization was \$36, \$17 and \$31, respectively. Future minimum lease payments for the above assets under capital leases during subsequent years are as follows.

| December 31, | Minimum Payments |
|--|---------------------|
| 2005 | \$ 134 |
| 2006 | 71 |
| 2007 | 7 |
| Total | 212 |
| Imputed interest | (14) |
| Total | 198 |
| Less current portion | (123) |
| Capital lease obligation, net of current portion | \$ 75 |

14. Product Warranty

Management estimates product warranties as a percentage of bulk alloy product revenues. During the years ended December 31, 2003 and 2004, the Company's product warranty accrual balance had the following activity:

| | |
|----------------------------|--------|
| Balance, December 31, 2002 | \$ 237 |
| Expense accrual | (297) |
| Warranty charges | 363 |
| Balance, December 31, 2003 | \$ 303 |
| Expense accrual | 288 |
| Warranty charges | (72) |
| Balance, December 31, 2004 | \$ 519 |

The product warranty accrual balance was included in accounts payable and accrued expenses at December 31, 2004 and December 31, 2003.

15. Notes Payable

Senior Convertible Note

On March 3, 2004, the Company issued \$9.9 million of 6.0% senior convertible notes due 2007 (the March Notes) to investor groups in a transaction led by Michigan Venture Capital Co., Ltd, a South Korea-based institutional investment firm, and IndiGo Ventures LLC, a New York-based investment firm (the Placement Agents) that served as a financial advisor to the Company for the transaction. The notes were collateralized by the patents held by the Company and second priority mortgage interest in plant facilities and certain equipment in South Korea. The notes were convertible at any time into common stock at a price of \$3.00 per share. Investors in the private placement and the Placement Agents received warrants to purchase an aggregate amount of up to approximately 1.2 million shares of common stock, exercisable at \$3.00 per share for varying periods but no later than 100 days following the effectiveness of a registration statement covering the resale of shares issuable upon exercise of the warrants. In addition, the investors had the right to call for repayment of the notes prior to maturity at any time after the second anniversary of the closing of the transaction.

Pursuant to Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, EITF 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock, EITF 00-27, Application of Issue No. 98-5 to Certain Convertible Instruments, and EITF 05-2 The Meaning of Conventional Convertible Debt Instrument in EITF Issue No. 00-19, the original fair value of the embedded conversion feature of \$7,595 have been recorded as conversion feature liabilities as the debt is considered non-conventional convertible debt. The original fair value was computed using the Black-Scholes model under the following assumptions: (1) expected life of 3 years; (2) volatility of 82%; (3) risk free interest of 2.15% and dividend rate of 0%. The fair value of the conversion feature on the date of issuance has been recorded as debt discount to be amortized over the life the debt.

Pursuant to EITF 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock, the original fair value of the 1.2 million warrants of \$1,302 has been recorded as warrant liabilities as the shares issuable under the warrants have not been registered. The original fair value was computed using the Black-Scholes pricing model under the following assumptions: (1) expected life of 3 years; (2) volatility of 82%, (3) risk free interest of 0.95% and dividend rate of 0%.

In March 2004, the original fair value of the embedded conversion feature of \$7,595 and the original fair value of the 0.6 million warrants issued to investors of \$584, and the original fair value of 0.6 million warrants issued to Placement Agents of \$718 were recorded as discounts of the convertible note. In addition, \$581 direct costs incurred relating to issuance of the convertible note were recorded as debt issuance cost in other assets.

From June through August 2004, the Company redeemed \$4,465 of the outstanding note balance in cash. The redemption resulted in a write down of debt issuance costs and debt discount of \$3,571 to interest expense and a reduction in conversion feature liabilities of \$914 from cancellation of the embedded conversion feature of the redeemed notes to additional paid in capital during the year ended December 31, 2004. Further, 500,000 of warrants originally issued to a financial advisor for the transaction expired during June 2004 and 163,748 of unexercised warrants originally issued to investors were cancelled as a result of the Company's redemption of the note balances during the year ended December 31, 2004. The 663,748 total expired and canceled warrants immediately prior to the expiration and cancellation resulted in a reduction of warrant liability of \$7 and \$279 to additional paid in capital and change in value of warrants, respectively, during the year ended December 31, 2004.

On August 19, 2004, the Company completed a private exchange offer for its March Notes with the remaining holders after the redemption. Under terms of the exchange offer, approximately \$5.5 million in aggregate principal amount of the March Notes have been exchanged for an aggregate of (i) \$2.75 million of 6% Senior Secured Notes Due 2007 (the Long-Term Notes) and (ii) \$2.75 million of 10% Senior Secured Notes Due 2005 (the Short-Term Notes), collectively referred to as Exchange Notes . The Exchange Notes are collateralized by certain patents owned by the Company and second priority mortgage interest in plant facilities and certain equipment at our South Korea plant. The Short-Term Notes have a maturity date of July 29, 2005, and a conversion price of \$2.00 per share (compared to a conversion price of \$3.00 per share under the March Notes). The Long-Term Notes have a maturity date of July 29, 2007, and a conversion price of \$1.00 per share. Further, the exchange notes are convertible into Common Stock, at the option of the Company, if at any time after the issuance of the notes, the closing per share price of the Common Stock exceeds

\$4.00 (as adjusted for stock splits, reverse splits, stock dividends, and recapitalizations) for 30 consecutive trading days, and further provided that there has been effective registration during such period. Holders of the Long-Term Notes also have the right to call for repayment of the Long-Term Notes prior to maturity at any time after the second anniversary of the closing of the exchange offer.

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A total of 563,151 warrants to purchase our common stock at an exercise price of \$3.00 per share all of which were previously issued in connection with the purchase of the March Notes have been amended to provide for an extended expiration date of March 1, 2006.

The exchange offer was treated as an extinguishment of the March Notes in accordance with Emerging Issues Task Force No. 96-19, Debtors Accounting for a Modification or Exchange of Debt Instruments. The exchange resulted in a \$2,941 loss from extinguishment of the March Notes, which consisted of write down of \$352 of deferred issue costs in other assets, \$670 of debt discount, and an increase of \$1,919 in conversion feature liability as a result of the change in carrying value of exchanged notes.

In connection with the private exchange offer, the Company issued \$250 of private placement notes to certain Placement Agents as issuance costs. Of the \$250 notes issued, \$125 was paid in the form of long-term notes which is due in 2007 with interest rate of 6% per annum (Long-Term Notes) and \$125 was paid in the form of short-term notes which is due in 2005 with interest rate of 10% per annum (Short-Term Notes). The Short-Term and Long-Term Notes are convertible into Common Stock at \$2.00 and \$1.00, respectively, and have the same terms as the Exchange Notes issued to the investors. Further, \$143 of original fair value of the embedded conversion feature of \$250 notes issued to Placement Agents was recorded during August 2004.

As of December 31, 2004, our gross outstanding loan balance totaled \$5,709, un-amortized discounts for beneficial conversion feature and warrants totaled \$2,831 and other asset debt issuance costs totaled \$183. Interest expense for the amortization of debt issuance cost and discount on note was \$789 for the year ended December 31, 2004. As of December 31, 2004, the effective interest rates for the Short-Term and the Long-Term Notes were 40% and 37%, respectively.

The Company was obligated, pursuant to a Registration Rights Agreement, as amended by the Exchange Notes, between the Company, the Placement Agents and the note holders to file a registration statement with the Securities and Exchange Commission (SEC) to register the shares of Common Stock issuable upon conversion of the notes payable and the related warrants within 90 days following the effective closing date of the exchange notes (July 29, 2004), and to use best efforts to cause such registration statement to become effective within 60 days following the SEC's first written comments on the registration statement. Further, if the Company is not in compliance with the registration or listing requirements, the holders have rights to late registration payments equal to 2 percent of the purchase price paid for the unconverted notes for the first 30 business days of late registration, and 1 percent for each 30 business days thereafter, but no more than 10 percent of the purchase price of the unconverted note balance. The \$5,709 balance of the note and un-amortized discounts for beneficial conversion feature and warrants of \$2,831 is presented as short-term liability as of December 31, 2004 as the note holders have the right to call for payment on demand as the registration statement has not been filed in accordance with the amended Registration Rights Agreement. As of the filing of this report, the Company has not received any demands for payment from the note holders.

Pursuant to Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, the Company is required to report a value of the conversion liability as a fair value and record the fluctuation to the fair value of the conversion feature liability to current operations. The change in the fair value of the conversion feature liability resulted in a gain of \$2,093 for the year ended December 31, 2004. The fair value of conversion feature liability outstanding at December 31, 2004 was \$6,650. The fair value of conversion features outstanding at December 31, 2004 was computed using the Black-Scholes model under the following assumptions: (1) 0.58~2.58 years; (2) volatility of 124%, (3) risk free interest of 2.75%~3.25% and dividend rate of 0%.

Pursuant to EITF 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock, the original relative fair values of the warrants of \$1,302 have been recorded as other liability as the Company has not yet filed the registration statement. In addition, the Company is required to report a value of the warrant as a fair value and record the fluctuation to the fair value of the warrant liability to current operations. The change in the relative fair value of the warrants resulted in a net gain of \$747 for the year ended December 31, 2004. The fair value of warrants outstanding at December 31, 2004 of \$550 was computed using the Black-Scholes model under the following assumptions: (1) expected life of 1.17 years; (2) volatility of 124%, (3) risk free interest of 3.08% and dividend rate of 0%.

The following is a repayment schedule of the Short-Term and Long-Term Notes based on maturity date of the notes:

Senior Convertible Notes

| Repayment Schedule December 31, | Minimum Payments |
|------------------------------------|---------------------|
| 2005 | \$ 2,854 |
| 2006 | |
| 2007 | 2,855 |
| Total | \$ 5,709 |

Kookmin Note

On February 4, 2003, our Korean subsidiary received 6,500,000 in South Korean Won, or approximately \$5,488, under a loan from Kookmin Bank of South Korea. The loan bears interest at an annual rate of 7.1%. In the event of delayed repayment, the interest increases to a maximum of 21%, depending on the length of time the repayment is delayed. This loan is collateralized by the plant facilities and certain equipment in South Korea. During the first eighteen months from the origination date, interest was payable on a monthly basis. In October 2003, the Company paid \$873 of principal at the request of Kookmin Bank due to the sale of machines that had been part of the collateral on the loan. Subsequent to October 31, 2003, Kookmin Bank requested that the Company pay an additional \$866 of principal by February 2004 due to the Company's current credit rating. The Company made two payments on the requested additional loan pay down in November and December 2003 of \$320 and \$205, respectively. The remaining payment of \$341 was subsequently made in February 2004. Beginning in September 2004, the Company is required to make equal monthly installments of principal and interest to repay the remaining balance of the loan over a 36-month period. For the year ended December 31, 2004, principal payments made to Kookmin Bank totaled \$296, which includes \$422 of foreign exchange translation loss.

The notes payable from Kookmin Loan as of December 31, 2004 and 2003 and the activity for the year ended December 31, 2004 is shown in the following table:

| | December 31, 2003 | Borrowings | Repayments | December 31, 2004 |
|--------------------------------------|----------------------|------------|------------|----------------------|
| Kookmin Loan 7.1%, principal \$5,488 | \$ 4,047 | \$ | \$ (296) | \$ 3,751 |

Kookmin Repayment Schedule

| December 31, | Minimum Payments |
|--------------|---------------------|
| 2005 | \$ 1,208 |
| 2006 | 1,208 |
| 2007 | 1,208 |
| 2008 | 127 |
| Total | \$ 3,751 |

Shinhan Credit Agreement

On August 23, 2003, the Company entered into a short-term credit agreement with Shinhan Bank of South Korea in the amount of \$1,000, which expired on May 30, 2004. The credit agreement is solely for the issuance of a letter of credit to vendors when the Company's Korean subsidiary imports raw materials and other goods into South Korea. The facility is secured by any raw material or goods financed through the credit facility. As of December 31, 2003, there were no borrowings outstanding under this agreement, and the Company has not renewed the agreement as of December 31, 2004.

16. Shareholders' Equity (Deficiency)

Initial Public Offering. Pursuant to the Company's Registration Statement (Registration No. 333-73716) on Form S-1, as amended, initially filed with the Securities and Exchange Commission on November 20, 2001 and declared effective May 21, 2002, the Company closed an initial public offering of 5,000,000 registered shares of common stock on May 28, 2002, plus an additional 229,000 shares on June 10, 2002 pursuant to an over allotment option, at a price of \$15.00 per share (which sale is referred to herein as the Offering). The Offering generated net cash proceeds for the Company during the second quarter 2002 of approximately \$70,721, net of underwriting commissions of \$5,490 and

other transaction fees of approximately \$2,224.

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Stock Split. On June 29, 2001 the Company declared a ten-for-one stock split to its common shareholders of record on June 29, 2001. This stock split was effected in the form of a stock dividend. On April 4, 2002, the Company declared a one-for-3.1 reverse stock split to its common shareholders of record on April 4, 2002. The consolidated financial statements and accompanying notes have been retroactively adjusted to reflect the effects of the split and reverse split.

Reincorporation. On May 21, 2003, the Company completed a reincorporation by transitioning from a California corporation to a Delaware corporation. The reincorporation was effected through the merger of the former California entity into its newly created wholly owned Delaware subsidiary. In connection with the reincorporation, the number of authorized common shares was reduced from 200,000,000 to 100,000,000. Additionally, the par value of the common stock was changed from no par value common stock to common stock with a par value of \$0.001 per share. For purposes of these notes, the term Company refers to the former California entity with respect to periods prior to May 21, 2003.

Preferred Stock. As of December 31, 2001, the Company received net proceeds of \$5,577 from the sale of the preferred stock at a per share price of \$12.40, as adjusted for the revised stock split. Upon the completion of the Offering, each share of preferred stock was converted automatically into one share of Class A common stock pursuant to the terms of the preferred stock issued.

Warrants

As of December 31, 2004, outstanding warrants to acquire shares of the Company's common stock are as follows:

| Number of Shares | Exercise Price | Expiration Date |
|------------------|----------------|-------------------|
| 645,162 | 4.65 | December 31, 2005 |
| 563,151 | 3.00 | March 1, 2006 |
| 1,208,313 | | |

17. Stock Compensation Plan

Under the Company's 1996 Stock Option Plan (1996 Company Plan) the Company could grant to employees, directors or consultants options to purchase up to 12,903,226 shares of common stock as adjusted for the reverse stock split. The stock options are exercisable over a period determined by the Board of Directors or the Compensation Committee, but no longer than 10 years.

On April 4, 2002, our shareholders and board of directors adopted the 2002 Equity Incentive Plan (2002 Equity Plan). The 2002 Equity Plan provides for the grant of stock options to officers, employees, consultants and directors of the Company and its subsidiaries. In addition, the plan permits the granting of stock appreciation rights with, or independently of, options, as well as stock bonuses and rights to purchase restricted stock. A total of 10,000,000 shares of our common stock may be granted under the 2002 Equity Plan. As of December 31, 2004, there are 1,505,379 options outstanding under the 2002 Equity Plan.

Prior to the approval of the 2002 Equity Plan, options were primarily granted under the Company's 1996 Stock Option Plan (1996 Company Plan). On April 4, 2002, our board of directors terminated the 1996 Company Plan. The termination will not affect any outstanding options under the 1996 Company Plan and all such options will continue to remain outstanding and be governed by the Plan. No additional options may be granted under the 1996 Company Plan. As of December 31, 2004, there were 3,426,622 options outstanding under the 1996 Company Plan.

On April 4, 2002, our shareholders and board of directors adopted the 2002 Non-employee Director Stock Option Plan (2002 Director Plan). Only non-employee directors are eligible for grants under the 2002 Director Plan. A total of 1,000,000 shares of the Company's Common Stock may be granted under the 2002 Director Plan. There are 122,000 options outstanding under the 2002 Director Plan as of December 31, 2004.

Additionally, the Company has 1,845,163 options outstanding at December 31, 2004 which were granted outside the 1996 Company Plan, 2002 Equity Plan and 2002 Director Plan.

The Company applies APB Opinion No. 25 for options when the exercise price of options granted to employees is less than the fair value of the underlying stock on the date of grant. The Company applies SFAS No. 123 for options granted to non-employees who perform services for the Company. Stock-based compensation expense was recognized as follows for the year ended December 31, 2004:

| | In accordance with APB Opinion No. 25 | SFAS No. 123 | Total |
|----------------------------|---------------------------------------|--------------|--------|
| General and administrative | \$ | \$ 240 | \$ 240 |
| Research and development | | 36 | 36 |
| Total | \$ | \$ 276 | \$ 276 |

Stock-based compensation expense was recognized as follows for the year ended December 31, 2003:

| | In accordance with APB Opinion No. 25 | SFAS No. 123 | Total |
|----------------------------|---------------------------------------|--------------|-------|
| General and administrative | \$ 50 | \$ 5 | \$ 55 |
| Research and development | 6 | 62 | 68 |

| | | | | | | |
|-------|----|----|----|----|----|-----|
| Total | \$ | 56 | \$ | 67 | \$ | 123 |
|-------|----|----|----|----|----|-----|

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Stock-based compensation expense was recognized as follows for the year ended December 31, 2002 (as restated):

| | In accordance with APB Opinion No. 25 | SFAS No. 123 | Total |
|----------------------------|---|-----------------|----------|
| General and administrative | \$ 50 | \$ 655 | \$ 705 |
| Research and development | | 1,498 | 1,498 |
| Total | \$ 50 | \$ 2,153 | \$ 2,203 |

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants for the years ended December 31, 2004, 2003, and 2002, respectively: expected volatility of 100% for all periods; dividend yield of 0.0% for all periods; expected option life of approximately 5 years; and risk-free interest rate ranging from 2.57% and 6.38%, as appropriate.

The following table summarizes the Company's stock option transactions for the three years ended December 31, 2004:

| | Number of Shares | Weighted Average Exercise Price |
|--|---------------------|--|
| Options outstanding at December 31, 2001 | 8,053,155 | \$ 4.55 |
| Granted | 643,202 | 13.71 |
| Exercised | (299,873) | 1.68 |
| Forfeited | (79,297) | 8.39 |
| Options outstanding at December 31, 2002 | 8,317,187 | 5.33 |
| Granted | 1,810,920 | 3.07 |
| Exercised | (684,165) | 1.68 |
| Forfeited | (1,272,481) | 5.43 |
| Options outstanding at December 31, 2003 | 8,171,461 | 5.11 |
| Granted | 695,843 | 1.82 |
| Exercised | | |
| Forfeited | (1,968,140) | 4.54 |
| Options outstanding at December 31, 2004 | 6,899,164 | \$ 4.95 |

The weighted average fair value of options granted during the years ended December 31, 2004, 2003, and 2002 was \$1.29, \$2.41, and \$10.42 respectively. There were 5,752,412 options with a weighted average exercise price of \$5.22 exercisable at December 31, 2004, 5,080,557 options with a weighted average exercise price of \$5.12 exercisable at December 31, 2003 and 4,353,030 options with a weighted average exercise price of \$4.36 exercisable at December 31, 2002.

Included in the above tables are certain options granted where their exercise prices were below the fair market value of the common stock at the grant date (measurement date). Such options totaled 358,582 with a weighted average fair value of \$11.22 were outstanding at December 31, 2004; 1,327,314 with a weighted average fair value of \$4.96 were outstanding at December 31, 2003; and 1,343,444 with a weighted average fair value of \$5.01 were outstanding at December 31, 2002.

The following table summarizes the Company's stock options outstanding and exercisable by ranges of option prices as of December 31, 2004:

| Options Outstanding | | | | Options Exercisable | |
|-----------------------------|----------------------------------|---|---------------------------------------|-------------------------------------|---------------------------------------|
| Range of Exercise Prices | Number of options Outstanding | Weighted Average Remaining Contractual Life (Years) | Weighted Average Exercise Price | Number of Options Exercisable | Weighted Average Exercise Price |
| \$ 0.00 - 1.55 | 380,359 | 9.5 | \$ 1.34 | 0 | \$ |

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| | | | | | |
|---------|-----------|-----|-------|-----------|-------|
| 1.56 - | | | | | |
| 3.10 | 1,713,024 | 6.9 | 2.52 | 1,202,026 | 2.54 |
| 3.11 - | | | | | |
| 4.65 | 1,853,357 | 6.2 | 4.61 | 1,766,485 | 4.65 |
| 4.66 - | | | | | |
| 6.20 | 2,592,810 | 6.4 | 6.20 | 2,559,853 | 6.20 |
| 7.76 - | | | | | |
| 9.30 | 11,507 | 7.9 | 8.80 | 4,602 | 8.80 |
| 9.31 - | | | | | |
| 10.85 | 12,613 | 6.4 | 9.83 | 4,613 | 9.87 |
| 10.86 - | | | | | |
| 12.40 | 222,585 | 6.6 | 12.40 | 165,803 | 12.40 |
| 13.95 - | | | | | |
| 15.50 | 112,909 | 6.9 | 15.00 | 49,030 | 15.00 |
| Total | 6,899,164 | | | 5,752,412 | |

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18. Discontinued Operations*Dongyang*

On June 28, 2002, the Company acquired a 51% interest in Chusik Hoesa Dongyang Yudoro (Dongyang). During 2003, Dongyang experienced net losses as a result of a continuing economic downturn in markets for its machinery products. These events, along with Dongyang's operating loss, cash flow losses and uncertainty surrounding its future cash flows, led the Company to evaluate its investment for recoverability as of December 31, 2003. As a result, the Company determined that the carrying value of its investment in Dongyang exceeded its fair value as of December 31, 2003 in the amount of \$184. This impairment loss was recorded in operating expenses for the year ended December 31, 2003.

In March 2004, the Company sold its 51% investment in Dongyang to the 49% minority shareholder. The selling price of the Company's 51% interest in Dongyang was \$80, which was equal to the Company's net carrying value for the 51% ownership held. Further, the Company agreed to pay Dongyang \$155 for the purchase of a receivable balance from Growell. The transaction resulted in net payable to Dongyang of \$75 and a loss of \$46 from transfer of the Company's interest in Dongyang to the minority shareholder. The net payable balance of \$75 is to be paid in quarterly installments throughout 2004, with \$25 to be paid subsequent to 2004. The outstanding amount payable to Dongyang is \$25 as of December 31, 2004 and is included in accounts payable and accrued liabilities.

The Company has adopted SFAS 144 and as a result the 2003 balances have been restated in order to conform with the presentation of 2004 financial statements. Dongyang is reported as part of the assets available for sale on the balance sheet for 2003.

As Dongyang was sold prior to December 31, 2004, and there are no assets and liabilities of Dongyang as of December 31, 2004. The following is a listing of the major classes of assets and liabilities of Dongyang as of December 31, 2003.

| | December 31, 2003 |
|---|------------------------------|
| Current Assets: | |
| Cash and cash equivalents | \$ 1 |
| Accounts receivable, net | 181 |
| Inventories | 1,572 |
| Prepaid expenses and other current assets | 56 |
| Total current assets | 1,810 |
| Property, plant and equipment, net | \$ 58 |
| Other Assets | 29 |
| Total assets | \$ 1,897 |
| Current Liabilities: | |
| Accounts payable and accrued expenses | \$ 233 |
| Deferred revenue | 1,583 |
| Total current liabilities | \$ 1,816 |

Summarized operating results of Dongyang's discontinued operations are as follows.

| | Year Ended December 31, 2004 | | 2003 |
|---|---|----------|-------------|
| Revenue | \$ 22 | \$ 1,019 | |
| Loss from discontinued equipment manufacturing operations, net of tax | (96) | (268) | |

Taesung

On June 14, 2004, the Company entered into an Asset Purchase Agreement whereby all the assets and liabilities of its Taesung equipment manufacturing division in Korea were sold to a third party for \$345 which is payable by the third party in four equal installments with the last installment being due on June 30, 2005. The sale resulted in a loss of \$184 and is included in the loss from discontinued equipment manufacturing operations as of December 31, 2004. The loss from operations for the year ended December 31, 2004 totaled \$653 and is

included in the loss from discontinued equipment manufacturing operations for the period.

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The Company has adopted SFAS 144 and as a result the 2003 balances have been restated in order to conform with the presentation of 2004 financial statements.

As Taesung was sold during the period ended June 30, 2004, there are no assets and liabilities of Taesung as of December 31, 2004. The following is a listing of the major classes of assets and liabilities of Taesung as of December 31, 2003.

| | December 31, 2003 |
|---|------------------------------|
| Current Assets: | |
| Cash and cash equivalents | \$ 1 |
| Accounts receivable, net | 256 |
| Inventories | 477 |
| Prepaid expenses and other current assets | 113 |
| Total current assets | 847 |
| Property, plant and equipment, net | \$ 157 |
| Other Assets | 100 |
| Total assets | \$ 1,104 |
| Current Liabilities: | |
| Accounts payable and accrued expenses | \$ 358 |

Summarized operating results of Taesung's operations are as follows.

| | Year Ended Ended December, 2004 | | 2003 |
|---|--|----|-------------|
| Revenue | \$ 172 | \$ | 2,177 |
| Loss from discontinued equipment manufacturing operations, net of tax | (653 |) | (696) |

Liquidmetal Golf

On April 30, 2002, management terminated the operations of the retail golf segment by means of liquidating substantially all of the retail golf assets and liabilities. The disposition of the retail golf operations represents the disposal of a business segment. Accordingly, the accompanying consolidated financial statements reflect the retail golf segment as a discontinued operation for all periods presented.

For the year ended December 31, 2003, there was a net gain of \$127 in the estimate of expenses associated with the disposal of the discontinued retail golf operations. The change resulted from reducing the net liabilities of the discontinued operations to \$0 as there are no additional expenditures associated with the discontinued retail golf operations. There were no assets associated with discontinued retail golf operations at December 31, 2003 and 2004.

For the year ended December 31, 2002, the Company had a net gain change in estimate of \$1,556 on the disposal of the discontinued retail golf segment that was primarily due to a change in estimated value of stock-based compensation. The change in estimated value of the stock-based compensation was a result of the cumulative decrease in the fair market value of the common shares underlying the options granted to Paul Azinger of \$2,129 and a decrease of \$250 in the estimate of fees related to the termination of the endorsement agreement. Additionally, there was a \$98 gain due to the reversal of the accumulated foreign exchange gains after the liquidation of Liquidmetal Golf Europe Inc, and a decrease in the estimated warranty cost of \$128. These gains were partially offset by other changes in the estimated loss on disposal that included \$530 of additional operating expenses, a \$57 increase in the allowance for doubtful accounts and \$462 primarily for the reduction of the estimated disposal value of work-in-process inventory and equipment.

The results of operations for all periods presented have been restated for discontinued operations. The operating results of the discontinued operations are as follows:

| | Years Ended December 31, | | |
|--|--------------------------|--------|----------|
| | 2004 | 2003 | 2002 |
| Net gain (loss) on disposal | | 127 | 1,556 |
| Foreign exchange translation gain (loss) during the period | | | (98) |
| Comprehensive gain (loss) | \$ | \$ 127 | \$ 1,458 |

Stock Compensation Plan. Historically, Liquidmetal Golf granted its own options to employees, directors and consultants under a stock option plan (1997 Golf Plan) approved by Liquidmetal Golf's Board of Directors pursuant to which Liquidmetal Golf could have granted stock options exercisable over a period determined by the Board of Directors to purchase up to 500,000 shares of common stock of Liquidmetal Golf. In connection with the Company's plan to discontinue the retail golf operations, the Company does not intend to issue additional options under the 1997 Golf Plan.

Liquidmetal Golf applies APB Opinion No. 25 and related interpretations in accounting for its plans. Accordingly, Liquidmetal Golf recognized compensation when the exercise price of the options was less than the fair value of the underlying stock on the date of grant. There was no compensation expense recorded during the years ended December 31, 2004, 2003, and 2002.

Had compensation cost been determined based on the fair value at the grant dates for awards under those plans consistent with the method of SFAS No. 123, Liquidmetal Golf's net loss would have been as follows:

| | Years ended December 31, | | |
|-------------|--------------------------|--------|----------|
| | 2004 | 2003 | 2002 |
| As reported | \$ | \$ 127 | \$ 1,556 |
| Pro forma | \$ | \$ 15 | \$ 1,405 |

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants for the fiscal years ended December 31, 2004, 2003, and 2002: expected volatility of 100% for all periods; dividend yield of 0.0% for all periods; expected option life of approximately 5 years; and a risk-free interest rate ranging from 5.2% to 6.2%, as appropriate.

The following table summarizes Liquidmetal Golf's stock option transactions for the three years ended December 31, 2004:

| | Number of Shares | Weighted Average Price |
|--|------------------|------------------------|
| Options outstanding at December 31, 2001 | 253,000 | 5.71 |
| Granted | | |
| Exercised | | |
| Forfeited | (137,500) | 3.53 |
| Options outstanding at December 31, 2002 | 115,500 | 8.31 |
| Granted | | |
| Exercised | (300) | 16.00 |
| Forfeited | (16,500) | 5.73 |
| Options outstanding at December 31, 2003 | 98,700 | 8.72 |
| Granted | | |
| Exercised | | |
| Forfeited | (10,000) | 8.00 |

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| | | | |
|--|--------|----|------|
| Options outstanding at December 31, 2004 | 88,700 | \$ | 8.80 |
|--|--------|----|------|

There were 88,700 options with a weighted average exercise price of \$8.80 exercisable at December 31, 2004. There were 98,700 options with a weighted average exercise price of \$8.72 exercisable at December 31, 2003 and 115,500 options with a weighted average exercise price of \$8.31 exercisable at December 31, 2002.

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Included in the above tables are certain options granted where their exercise prices were below the fair market value of the common stock at the grant date. Such options totaled 10,000, 131,250 and 131,250 with weighted average fair values of \$5.74, \$5.74 and \$5.74 were outstanding at December 31, 2004, 2003 and 2002, respectively.

The following summarizes Liquidmetal Golf's stock options outstanding and exercisable by the different exercise prices at December 31, 2004:

| Exercise Price | | Number of Options Outstanding at December 31, 2003 | Weighted Average Remaining Contract Life (Years) | Number of Options Exercisable at December 31, 2004 |
|----------------|-------|--|--|--|
| \$ | 0.50 | 10,000 | 2.33 | 10,000 |
| \$ | 8.00 | 63,000 | 4.81 | 63,000 |
| \$ | 16.00 | 13,200 | 3.33 | 13,200 |
| \$ | 24.00 | 2,500 | 3.58 | 2,500 |
| | | 88,700 | | 88,700 |

19. Income Taxes

For all financial statement periods presented, there was no provision for domestic income taxes. However, there was approximately \$8 and \$123 of tax expense during the twelve months ended December 31, 2003 and 2002, respectively, related to foreign taxes incurred by Dongyang, a 51% owned subsidiary, which is included as part of loss from discontinued operations on the consolidated statements of operations and comprehensive loss (see Note 18).

The Company has restated certain previously issued financial statements for due to an error related to the Company's accounting for embedded convertible feature of senior convertible notes (see Note 2).

The significant components of deferred tax assets were as follows:

| | Years Ended December 31, | | |
|-----------------------------------|--------------------------|-----------|-----------|
| | 2004 | 2003 | 2002 |
| Non-employee stock compensation | \$ 109 | \$ 51 | \$ 103 |
| Allowance for bad debt | 37 | 44 | 52 |
| Loss from discontinued operations | | | |
| Loss carry forwards | 32,087 | 27,202 | 24,175 |
| Other | 1,244 | 1,569 | 1,071 |
| Total deferred tax asset | 33,477 | 28,866 | 25,401 |
| Valuation allowance | (33,477) | (28,866) | (25,401) |
| Total deferred tax asset, net | \$ | \$ | \$ |

The following table accounts for the differences between the actual tax provision and the amounts obtained by applying the statutory U.S. Federal income tax rate of 34% to income (loss) before income taxes:

| | Years Ended December 31, | | |
|--|--------------------------|-----------|-----------|
| | 2004 | 2003 | 2002 |
| Federal tax expense | (34.00)% | (34.00)% | (34.00)% |
| State tax expense, net | (4.91)% | (1.62)% | (3.40)% |
| Foreign income not subject to income tax | 4.24 % | 24.16 % | 13.36 % |
| Other | 0.68 % | 0.36 % | 1.26 % |
| Increase in valuation allowance | 33.99 % | 11.13 % | 22.82 % |
| Total tax provision | 0.0 % | 0.03 % | 0.04 % |

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As of December 31, 2004, the Company had approximately \$88,000 of net operating loss (NOL) carry forwards for U.S. federal income tax purposes expiring in 2005 through 2024. In addition, the Company has state NOL carryforwards of approximately \$40,000 expiring in 2005 through 2009. The Company and Liquidmetal Golf filed on a separate company basis for federal income tax purposes. Accordingly, the federal NOL carryforwards of one legal entity are not available to offset federal taxable income of the other. As of December 31, 2004, Liquidmetal Technologies, Inc. had approximately \$50,000 in federal NOL carryforwards, expiring in 2005 through 2024 and approximately \$17,000 in state NOL carryforwards, expiring in 2005 through 2009. Liquidmetal Golf, Inc. had approximately \$38,000 of federal NOL carryforwards, expiring in 2012 through 2023 and approximately \$23,000 in state NOL carryforwards expiring in 2004 through 2008.

As of December 31, 2004, the Company had approximately \$317 of Research & Development (R&D) credit carryforwards for U.S. federal income tax purposes expiring in 2016 through 2018. In addition, the Company has California R&D credit carryforwards of approximately \$279, which do not expire under current California law.

Section 382 of the Internal Revenue Code (IRC) imposes limitations on the use of NOL s and credits following changes in ownership as defined in the IRC. The limitation could reduce the amount of benefits that would be available to offset future taxable income each year, starting with the year of an ownership change. The Company has not completed the complex analysis required by the IRC to determine if an ownership change has occurred.

The ability to realize the tax benefits associated with deferred tax assets, which includes benefits related to NOL s, is principally dependent upon the Company s ability to generate future taxable income from operations. The Company has provided a full valuation allowance for its net deferred tax assets due to the Company s net operating losses.

20. Segment Reporting and Geographic Information

SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, requires companies to provide certain information about their operating segments. In April 2002, the Company began classifying operations into two reportable segments: Liquidmetal alloy industrial coatings and bulk Liquidmetal alloys. The Liquidmetal alloy industrial coatings are used primarily as a protective coating for industrial machinery and equipment, such as drill pipe used by the oil drilling industry and boiler tubes used by coal burning power plants. Bulk Liquidmetal alloys include market opportunities to manufacture and sell casing components for electronic devices, medical devices, sporting goods, tooling, prototype sampling, defense applications and metal processing equipment. The expenses incurred by the bulk Liquidmetal alloy segment are manufacturing, research and development costs, and selling expenses associated with identifying and developing market opportunities. Bulk Liquidmetal alloy products can be distinguished from Liquidmetal alloy coatings in that the bulk Liquidmetal alloy can have significant thickness, up to approximately one inch, which allows for their use in a wider variety of applications other than a thin protective coating applied to machinery and equipment. Revenue and expenses associated with research and development services are included in the bulk Liquidmetal alloy segment. The accounting policies of the reportable segments are the same as those described in Note 4 above.

The Company has restated certain previously issued financial statements for due to an error related to the Company s accounting for embedded convertible feature of senior convertible notes (see Note 2).

Summarized financial information concerning the Company s reportable segments is shown in the following tables:

| | Coatings | Bulk Alloy | Segment Totals |
|--|----------|------------|-------------------|
| Year ended December 31, 2004: | | | |
| Revenue to external customers | \$ 3,956 | \$ 13,473 | \$ 17,429 |
| Gross profit | 1,807 | 3,454 | 5,261 |
| Total segment income | 1,227 | 2,330 | 3,557 |
| Total identifiable assets at end of period | 842 | 22,635 | 23,477 |
| Year ended December 31, 2003: | | | |
| Revenue to external customers | \$ 2,997 | \$ 10,661 | \$ 13,658 |
| Gross profit (loss) | 1,466 | (5,970) | (4,504) |
| Total segment income (loss) | 369 | (21,140) | (20,771) |
| Total identifiable assets at end of period | 959 | 23,832 | 24,791 |
| Year ended December 31, 2002 (restated): | | | |
| Revenue to external customers | \$ 4,587 | \$ 4,551 | \$ 9,138 |
| Gross profit | 2,171 | 1,311 | 3,482 |
| Income (loss) before minority interest, interest expense and discontinued operations | 1,425 | (13,179) | (11,754) |
| Total identifiable assets at end of period | 1,969 | 29,441 | 31,410 |

Reconciling information for the statements of operations between reportable segments and the Company's consolidated totals is shown in the following table:

| | For the Years ended December 31, | | 2002 |
|--|---|--------------|-------------------|
| | 2004 | 2003 | (Restated) |
| | (Restated) | | |
| Total segment income (loss) before minority interest, interest expense and discontinued operations | \$ 3,557 | \$ (20,771) | \$ (11,754) |
| General and administrative expenses, excluded | (11,354) | (13,110) | (9,688) |
| Consolidated loss before interest, other income, income taxes, minority interest and discontinued operations | (7,797) | (33,881) | (21,442) |
| Loss from extinguishments of debt | (2,941) | | |
| Change in value of warrants, gain | 747 | | |
| Change in value of conversion feature, gain | 2,093 | | |
| Other income | 302 | | |
| Interest expense | (6,577) | (390) | (1,109) |
| Interest income | 37 | 304 | 506 |
| Gain on sale of marketable securities held-for-sale | | 1,178 | 832 |
| Income taxes | | | |
| Minority interest in loss of consolidated subsidiary | | 21 | 118 |
| Gain (loss) from discontinued operations, net | (749) | (837) | 1,639 |
| Consolidated net loss | \$ (14,885) | \$ (33,605) | \$ (19,456) |

Excluded general and administrative expenses are attributable to the Company's corporate headquarters. These expenses primarily include corporate salaries, consulting, professional fees and facility costs. Research and development expenses are included in the operating costs of the segment that performed the research and development.

Included in our bulk alloy revenue to external customers are equipment sales from our Dongyang subsidiary and Taesung equipment division in Korea, both of which were divested in March and June 2004 respectively. External revenue from our discontinued equipment manufacturing operations includes \$3.2 million and \$0.2 million for the years ended December 31, 2003 and 2004, respectively.

Reconciling information for the balance sheets between reportable segments and the Company's consolidated totals is shown in the following table:

| | December 31, | |
|---|---------------------|-------------|
| | 2004 | 2003 |
| Total segment assets | \$ 23,477 | \$ 24,791 |
| Cash and cash equivalents | 742 | 3,127 |
| Restricted cash | 754 | |
| Prepaid expenses and other current assets | 801 | 322 |
| Other property, plant and equipment | 975 | 1,563 |
| Intangibles, net | 1,143 | 984 |
| Other assets | 616 | 65 |
| Total Consolidated Assets | \$ 28,508 | \$ 30,852 |

Assets excluded from segments include assets attributable to the Company's corporate headquarters. The largest asset represents the Company's intangible assets, consisting primarily of the Company's patents and trademarks.

Certain customers accounted for more than 10% of revenues from continuing operations as follows:

| | Year Ended December 31, | | 2002 | | | |
|--------------------------|-------------------------|------|------------|---|----|---|
| | 2004 | 2003 | (restated) | | | |
| Samsung | 5 | % | 10 | % | 15 | % |
| Charm Tech | 32 | % | | | | |
| Pntel | 30 | % | 2 | % | | |
| United States Government | 10 | % | 16 | % | 16 | % |
| Growell Metal | 12 | % | | | | |
| LLPG | | | 12 | % | | |

The revenue related to the United States Government was earned under three defense-related research and development contracts.

Revenues from sales to companies in the United States of America were \$5,546 and \$6,050 during the years ended December 31, 2004 and 2003, respectively. The revenue related to the United States of America was earned under three defense-related research and development contracts and sales of coatings products.

During the year ended December 31, 2004, the Company had revenue on sales to companies outside of the United States of \$11,883 of which \$9,545 represented sales to companies located in South Korea. During the year ended December 31, 2003, the Company had revenue on sales to companies outside of the United States of \$7,608, of which \$4,559 represented sales to companies located in South Korea. During the year ended December 31, 2002, the Company did not generate significant sales to companies located outside of the United States.

Long-lived assets include net property, plant, and equipment and net intangible assets. The Company had long-lived assets of \$1,594 and \$2,547 located in the United States at December 31, 2004 and 2003, respectively. The Company had long-lived assets of \$15,422 and \$16,395 located in South Korea at December 31, 2004 and December 31, 2003, respectively. Of the assets located in South Korea at December 31, 2003, \$215 was from long-lived assets of our discontinued equipment manufacturing business. Further, the Company has long lived assets of \$47 at December 31, 2004 located in China as a result of a new plant opened during August 2004 (see Note 1).

21. Income (Loss) Per Common Share

Basic EPS is computed by dividing earnings (loss) attributable to common shareholders by the weighted average number of common shares outstanding for the periods. Diluted EPS reflects the potential dilution of securities that could share in the earnings. A reconciliation of the number of common shares used in calculation of basic and diluted EPS is presented below:

| | Years Ended December 31, | | |
|---------------------------------|--------------------------|------------|------------|
| | 2004 | 2003 | 2002 |
| Weighted average basic shares | 41,609,652 | 41,505,218 | 38,713,878 |
| Effect of dilutive securities: | | | |
| Stock options | | | |
| Conversion of notes payable | | | |
| Weighted average diluted shares | 41,609,652 | 41,505,218 | 38,713,878 |

Options to purchase approximately 6,899,164 shares of common stock at prices ranging from \$1.18 to \$15.00 per share were outstanding at December 31, 2004, but were not included in the computation of diluted EPS for the same period because the inclusion would have been antidilutive. Options to purchase approximately 8,171,461 shares of common stock at prices ranging from \$1.16 to \$15.50 per share were outstanding at December 31, 2003, but were not included in the computation of diluted EPS for the same period because the inclusion would have been antidilutive. Options to purchase approximately 8,317,187 shares of common stock at prices ranging from \$0.78 to \$15.50 per share were outstanding at December 31, 2002, but were not included in the computation of diluted EPS for the same period because the inclusion would have been antidilutive.

Warrants to purchase 1,208,313 shares of common stock between \$3.00 and \$4.65 per share were outstanding at December 31, 2004 but were not included in the computation of diluted EPS for the same period because the inclusion would have been antidilutive. Warrants to purchase 645,162 shares of common stock at \$4.65 per share were outstanding at December 31, 2003 and December 31, 2002.

22. Commitments and Contingencies

During September 2004, as part of a security agreement to finance a certain insurance policy, the Company used certificates of deposits with maturities of less than one year as collateral. The \$754 held in certificates of deposits is presented as restricted cash at December 31, 2004.

The Company is from time to time a party to certain legal proceedings arising in the ordinary course of business. Although outcomes cannot be predicted with certainty, the Company does not believe that any legal proceeding to which it is a party will have a material adverse effect on the Company's financial position, results of operations, and cash flows.

Liquidmetal Technologies and certain of its present and former officers and directors were named as defendants in nine purported class action complaints filed in the United States District Courts for the Middle District of Florida, Tampa Division, and the Central District of California, Southern Division, alleging violations of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. In August 2004, four complaints were consolidated in the United States District Court for the Middle District of Florida under the caption *Primavera Investors v. Liquidmetal Technologies, Inc., et al.*, Case No. 8:04-CV-919-T-23EAJ. John Lee, Chris Cowley, Dwight Mamanteo, Scott Purcell and Mark Rabold, were appointed co-lead plaintiffs (the Lead Plaintiffs). In September 2004, the other five complaints filed in the Central District of California were transferred to the Middle District of Florida for consolidation with the *Primavera Investors* action. The Lead Plaintiffs served their Consolidated Amended Class Action Complaint on January 12, 2005. The Amended Complaint alleges that the Prospectus issued in connection with the Company's initial public offering in May 2002 contained material misrepresentations and omissions regarding the Company's historical financial condition and regarding a personal stock transaction by the Company's chief executive officer. The Lead Plaintiffs further generally allege that during the proposed Class Period of May 21, 2002, through May 13, 2004, the defendants engaged in improper revenue recognition with respect to certain of the Company's business transactions, failed to maintain adequate internal controls, and knowingly disclosed unrealistic but favorable information about market demand for and commercial viability of the Company's products to artificially inflate the value of the Company's stock. The Amended Complaint seeks unspecified compensatory damages and other relief. Defendants' motion to dismiss will be due on March 28, 2005. The Company intends to vigorously defend against the class action. The Company cannot currently predict the impact or resolution of this litigation or reasonably estimate a range of possible loss, which could be material.

In addition to the above, certain present and former officers and directors of Liquidmetal Technologies, as well as Liquidmetal Technologies as a nominal defendant, have been named in three shareholder derivative actions. Two shareholder derivative complaints were filed in California state court styled *Brian Clair, Derivatively on Behalf of Liquidmetal Technologies, Inc. v. John Kang, et al.*, Case No. 04CC00551, and *Joseph Durgin Derivatively on Behalf of Liquidmetal Technologies, Inc. v. John Kang, et al.*, Case No. 04CC00553, both commenced in the Superior Court of Orange County, California. A third shareholder derivative complaint was filed in Florida federal court styled *Robert Story v. John Kang, et al.*, Case No. 8:04-CV-1587-T23TBM, commenced in the Middle District of Florida, Tampa Division. These shareholder derivative lawsuits allege that the defendants breached various fiduciary duties and otherwise violated state law based primarily upon the same underlying facts and circumstances as alleged in the federal shareholder class action. The plaintiffs seek unspecified compensatory damages, restitution and disgorgement of profits, equitable and/or injunctive relief as permitted by law and other relief. The two shareholder derivative complaints in California state court have been consolidated. Plaintiffs served a Consolidated Shareholder Derivative Complaint on October 12, 2004. The defendants served a Demurrer to the Consolidated Shareholder Derivative Complaint on November 22, 2004, seeking dismissal of that complaint. At a hearing on February 10, 2005, the court sustained the demurrer, dismissing the Consolidated Shareholder Derivative Complaint but giving the plaintiffs 45 days within which to amend the complaint. The amended complaint is due on March 28, 2005. In the Florida derivative action, the Plaintiff filed a First Amended Shareholder Derivative Complaint on November 22, 2004. The Company's Motion to Dismiss was filed on December 20, 2004. Plaintiff's Response and Objection to the Motion to Dismiss was filed on February 4, 2005. The Company cannot anticipate when the Court will rule on the Motion to Dismiss. The Company intends to vigorously defend against the derivative actions. We cannot currently predict the impact or resolution of this litigation or reasonably estimate a range of possible loss, which could be material.

In March 1996, the Company entered into a distribution agreement whereby it granted to a third party exclusive rights to market and sell golf products incorporating Liquidmetal Technology to certain Japanese sporting equipment companies. The third party paid the Company a \$1.0 million distribution fee as part of this agreement, of which a portion was refundable according to a formula based on the gross profit earned by the third party. The remaining unearned distribution fee of \$830 has not been refunded as of December 31, 2004. On March 28, 2003, the distribution agreement was terminated and the Company entered into a new agreement to pay to the same third party a commission on the net sales price of all Liquidmetal golf equipment that is shipped by the Company or its affiliates to Japanese golf companies for sale into the Japanese end-market. This commission will apply to golf equipment shipped by the Company or its affiliates during the period beginning on March 28, 2003 and ending on March 28, 2006. If, by March 28, 2006, the Company has not paid \$350 in commission payments, the balance between commission paid and \$350 will be paid by April 30, 2006, thereby guaranteeing the third party a \$350 minimum payment during the term of the agreement. The Company will recognize the unearned distribution fee of \$830 as revenue proportionately with the payment of commissions under the new agreement. As of December 31, 2004, the unearned distribution fee remained unchanged at \$830.

In August 2004, the Company entered into a consulting agreement whereby the Company was to receive services from a third party to improve the Company's bulk alloy manufacturing process. The service is to be provided from 2004 through February 2006. The total amount of service fees is \$172, of which \$15 was included in trade accounts payable as of December 31, 2004.

Operating Leases

The Company leases its offices and warehouse facilities under various lease agreements, certain of which are subject to escalations based upon increases in specified operating expenses or increases in the Consumer Price Index. Future minimum lease payments under non-cancelable operating leases during subsequent years are as follows:

| December 31, | Minimum Payments |
|--------------|---------------------|
| 2005 | \$ 1,215 |
| 2006 | 530 |
| 2007 | 317 |
| 2008 | 105 |
| 2009 | 73 |
| Total | \$ 2,240 |

Rent expense was \$479, \$1,419, and \$955 for the years ended December 31, 2004, 2003, and 2002, respectively.

23. 401(k) Savings Plan

The Company has a tax-qualified employee savings and retirement plan, or 401(k) plan, which covers all of its United States-based employees. Our Korean employees are covered under a government sponsored pension program and do not participate in the U.S. based 401(k) program.

Under the U.S. based 401 (k) plan, participants may elect to reduce their current compensation, on a pre-tax basis, by up to 15% of their taxable compensation or of the statutorily prescribed annual limit, whichever is lower, and have the amount of the reduction contributed to the 401(k) plan. The 401(k) plan permits the Company, in its sole discretion, to make additional employer contributions to the 401(k) plan. However, the Company did not make employer contributions to the 401(k) plan during any of the periods presented in the accompanying consolidated financial statements.

24. Related Party Transactions

In June 2003, the Company entered into an exclusive, ten-year license agreement with LLPG, Inc. (LLPG), a corporation headed by a former director of the Company. Under the terms of the agreement, LLPG has the right to commercialize Liquidmetal alloys, particularly precious-metal based compositions, in jewelry and high-end luxury product markets. The Company, in turn, will receive royalty payments over the life of the contract on all Liquidmetal products produced and sold by LLPG. In conjunction with its technology licensing contract, LLPG purchased two proprietary Liquidmetal alloy melting machines and three proprietary Liquidmetal alloy casting machines for a total purchase price of \$2,000. At December 31, 2003, the Company had a remaining receivable balance of \$500 due from LLPG, which was paid in full in March 2004.

The Company is a party to a license agreement with California Institute of Technology (Caltech) under which the Company exclusively licenses from Caltech certain inventions and technology relating to amorphous alloys. Professor William Johnson, a member of the Company's Board of Directors, is a professor at Caltech, and substantially all of the amorphous alloy technology licensed to the Company under the Caltech license agreement was developed in Professor Johnson's Caltech laboratory. During 2003, the Company paid \$50 to Caltech representing the second and final installments on the \$150 aggregate fees related to this agreement. Additionally, the Company reimburses Caltech for laboratory expenses incurred by Professor Johnson's Caltech laboratory, which during the years ended December 31, 2004 and 2003, amounted to \$0 and \$22 in reimbursements, respectively.

A company managed and partially owned by one of the Company's former directors provides technical support services and computer equipment to the Company. During the year ended December 31, 2003, the Company incurred \$20 of expenses and equipment purchases related to this arrangement. There were no expenses and payables to this Company as of December 31, 2004.

We are a party to a consulting agreement with Chitnis Consulting, Inc., which is owned 100% by Shekhar Chitnis, a former director and executive officer of our company. Under this agreement, we have engaged Chitnis Consulting to provide consulting services on an as-needed basis through December 31, 2005. During 2003, we incurred \$50 in consulting fees from Chitnis Consulting and incurred \$54 as of December 31, 2004.

Soo Buchanan, the sister of John Kang and James Kang, was employed by our company and was paid aggregate compensation of \$76 and \$43 as of December 31, 2003 and 2004. Additionally, Otis Buchanan, the husband of Ms. Buchanan, was employed by the Company and was paid aggregate compensation of \$90 and \$54 as of December 31, 2003 and 2004, respectively.

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

The Audit Committee of our Board of Directors conducted an independent inquiry into the above-described transactions with the aid of independent legal counsel and, as a result of such inquiry, the Audit Committee concluded that the transactions should have resulted in a liability to the Company under Section 16(b) in the amount of \$302. Mr. Kang has acknowledged this liability, and in an agreement negotiated between Mr. Kang and the Audit Committee and approved by the full Board, Mr. Kang will pay this liability through periodic installments in 2005 and 2006. As a result, the Company accrued for the \$302 receivable in other assets and other income as of December 31, 2004. The above-described transactions involving Growell Metal was reported on a new Form 4 filed by Mr. Kang on November 15, 2004, and the open-market purchases were previously reported on a timely basis in August 2002.

25. Fourth Quarter Adjustments and Transactions

During the fourth quarter of 2004, the Company recognized \$406 write-downs of inventory included in Cost of Sales in the accompanying Statement of Operations and Comprehensive Loss related to certain hinge finished goods used in our customer's cell phone models which were nearing its end of life (see Note 7).

Further, the Company amended its quarterly financial statements originally filed on Form 10-Q for fiscal year 2004, to properly account for the conversion feature of the senior convertible notes issued in March 2004, which were exchanged in August 2004 (see Note 2).

Schedule II Valuation and Qualifying Accounts

| | Balance at Beginning of Period | Additions Charged to Expenses | Write-offs and Payments | Balance at End of Period |
|---|--------------------------------------|-------------------------------------|-------------------------------|--------------------------------|
| Allowance for doubtful accounts | | | | |
| Year ended December 31, 2004 | \$ 127 | \$ 84 | \$ (103) | \$ 108 |
| Year ended December 31, 2003 | 450 | (28) | (295) | 127 |
| Year ended December 31, 2002 | 30 | 921 | (501) | 450 |
| Product warranty accrual | | | | |
| Year ended December 31, 2004 | \$ 303 | \$ 288 | \$ (72) | \$ 519 |
| Year ended December 31, 2003 | 237 | (297) | 363 | 303 |
| Year ended December 31, 2002 | | | | |
| Deferred tax asset valuation allowance * | | | | |
| Year ended December 31, 2004 | \$ 28,866 | \$ 4,611 | \$ | \$ 33,477 |
| Year ended December 31, 2003 | 25,401 | 3,465 | | 28,866 |
| Year ended December 31, 2002 | 23,796 | 1,605 | | 25,401 |

* The deferred tax asset valuation allowance represents a 100% reserve against the deferred tax asset accounts at December 31, 2004, 2003 and 2002, respectively.