INTEVAC INC
Form DEF 14A
April 05, 2011

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
SCHEDULE 14A INFORMATION
PROXY STATEMENT PURSUANT TO SECTION 14 (a)
OF THE SECURITIES EXCHANGE ACT OF 1934

Filed by the Registrant þ
Filed by a Party other than the Registrant o
Check the appropriate box:

o Preliminary Proxy Statement

o Confidential, for Use of the Commission Only (as permitted by Rule 14a 6 (e) (2))

þ Definitive Proxy Statement

o Definitive Additional Materials

o Soliciting Material Pursuant to Section 240.14a 11 (c) or Section 240.14a 12

INTEVAC, INC.

(Exact Name of Registrant as Specified in its Charter)

Payment of Filing Fee (Check the appropriate box):

þ No fee required.

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April 5, 2011

Dear Stockholder:

You are cordially invited to attend the 2011 Annual Meeting of Stockholders of Intevac, Inc., a Delaware corporation, which will be held Wednesday, May 18, 2011, at 4:30 p.m., local time, at our principal executive offices located at 3560 Bassett Street, Santa Clara, California 95054. The accompanying notice of Annual Meeting, proxy statement and form of proxy card are being distributed to you on or about April 7, 2011.

Details regarding admission to the Annual Meeting and the business to be conducted are described in the accompanying proxy materials. Also included is a copy of our 2010 Annual Report. We encourage you to read this information carefully.

Your vote is important. Whether or not you plan to attend the Annual Meeting, we hope you will vote as soon as possible. You may vote over the Internet, by telephone or by mailing a proxy card. Voting over the Internet, by telephone or by written proxy will ensure your representation at the Annual Meeting regardless of whether or not you attend in person. Please review the instructions on the proxy card regarding each of these voting options.

Thank you for your ongoing support of Intevac. We look forward to seeing you at the Annual Meeting. Please notify Joanne Diener at (408) 496-2242 if you plan to attend.

Sincerely yours,

Kevin Fairbairn
President and Chief Executive Officer

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INTEVAC, INC.
3560 Bassett Street
Santa Clara, California 95054

NOTICE OF ANNUAL MEETING
FOR 2011 ANNUAL MEETING OF STOCKHOLDERS

Time and Date:	Wednesday, May 18, 2011 at 4:30 p.m., Pacific daylight time.
Place:	Intevac s principal executive offices, located at: 3560 Bassett Street, Santa Clara, California 95054.
Items of Business:	(1) To elect directors to serve for the ensuing year or until their respective successors are duly elected and qualified. (2) To approve an amendment to the Intevac 2003 Employee Stock Purchase Plan to increase the number of shares reserved for issuance thereunder by 300,000 shares. (3) To approve an amendment to the Intevac 2004 Equity Incentive Plan to increase the number of shares reserved for issuance thereunder by 500,000 shares and approve the material terms of the plan. (4) To ratify the appointment of Grant Thornton LLP as Intevac s independent public accountants for the fiscal year ending December 31, 2011. (5) To recommend, by advisory vote, executive compensation. (6) To recommend, by advisory vote, the frequency of holding an advisory vote on executive compensation. (7) To transact such other business as may properly come before the Annual Meeting. These items of business are more fully described in the proxy statement accompanying this notice.
Adjournments and Postponements:	Any action on the items of business described above may be considered at the Annual Meeting at the time and on the date specified above or at any time and date to which the Annual Meeting may be properly adjourned or postponed.
Record Date:	You are entitled to vote if you were a stockholder of record as of the close of business on March 29, 2011.
Voting:	**Your vote is very important. Whether or not you plan to attend the Annual Meeting, we encourage you to read the proxy statement and submit your proxy card or vote on the Internet or by telephone as soon as possible. For specific instructions on how to vote your shares, please refer to the section entitled Questions and Answers About Procedural Matters and the instructions on the enclosed proxy card.**

All stockholders are cordially invited to attend the Annual Meeting in person.

By Order of the Board of Directors,

JEFFREY ANDRESON
Executive Vice President, Finance and Administration, Chief Financial Officer, Treasurer and Secretary

This notice of Annual Meeting, proxy statement and accompanying form of proxy card are being distributed on or about April 7, 2011

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INTEVAC, INC.
3560 Bassett Street
Santa Clara, California 95054

PROXY STATEMENT
FOR 2011 ANNUAL MEETING OF STOCKHOLDERS

QUESTIONS AND ANSWERS ABOUT PROCEDURAL MATTERS

Annual Meeting

Q: Why am I receiving these proxy materials?

A: The Board of Directors of Intevac, Inc. is providing these proxy materials to you in connection with the solicitation of proxies for use at the 2011 Annual Meeting of Stockholders (the Annual Meeting) to be held Wednesday, May 18, 2011 at 4:30 p.m., Pacific daylight time, or at any adjournment or postponement thereof for the purpose of considering and acting upon the matters set forth herein. The notice of Annual Meeting, this proxy statement and accompanying form of proxy card are being distributed to you on or about April 7, 2011.

Q: Where is the Annual Meeting?

A: The Annual Meeting will be held at Intevac s principal executive offices, located at 3560 Bassett Street, Santa Clara, California 95054. The telephone number at that location is 408-986-9888.

Q: Can I attend the Annual Meeting?

A: You are invited to attend the Annual Meeting if you were a stockholder of record or a beneficial owner as of March 29, 2011. You should bring photo identification for entrance to the Annual Meeting. The meeting will begin promptly at 4:30 p.m., Pacific daylight time.

Stock Ownership

Q: What is the difference between holding shares as a stockholder of record and as a beneficial owner?

A: *Stockholders of record* If your shares are registered directly in your name with Intevac s transfer agent, Computershare Trust Company, N.A., you are considered, with respect to those shares, the stockholder of record. These proxy materials have been sent directly to you by Intevac.

Beneficial owners Many Intevac stockholders hold their shares through a broker, trustee or other nominee, rather than directly in their own name. If your shares are held in a brokerage account or by a bank or another nominee, you are considered the beneficial owner of shares held in street name. In this case the proxy materials will have been forwarded to you by your broker, trustee or nominee, who is considered, with respect to those shares, the stockholder of record.

As the beneficial owner, you have the right to direct your broker, trustee or other nominee on how to vote your shares. For directions on how to vote shares beneficially held in street name, please refer to the voting instruction card provided by your broker, trustee or nominee. Since a beneficial owner is not the stockholder of record, you may not vote these shares in person at the Annual Meeting unless you obtain a legal proxy from the broker, trustee or nominee that holds your shares, giving you the right to vote those shares at the Annual Meeting.

Quorum and Voting

Q: How many shares must be present or represented to conduct business at the Annual Meeting?

A: The presence of the holders of a majority of the shares of Common Stock entitled to vote at the Annual Meeting is necessary to constitute a quorum at the Annual Meeting. Such stockholders are counted as present at the meeting if they (1) are present in person at the Annual Meeting or (2) have properly submitted a proxy.

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Under the General Corporation Law of the State of Delaware, abstentions and broker non-votes are counted as present and entitled to vote and are, therefore, included for purposes of determining whether a quorum is present at the Annual Meeting.

A broker non-vote occurs when a nominee holding shares for a beneficial owner does not vote on a particular proposal because the nominee does not have discretionary voting power with respect to that item and has not received instructions from the beneficial owner.

Q: Who is entitled to vote at the Annual Meeting?

A: Holders of record of Intevac s common stock, par value $0.001 per share (the Common Stock) at the close of business on March 29, 2011 (the Record Date) are entitled to receive notice of and to vote their shares at the Annual Meeting. Such stockholders are entitled to cast one vote for each share of Common Stock held as of the Record Date.

At the Record Date, we had 22,825,500 shares of our Common Stock outstanding and entitled to vote at the Annual Meeting, held by 110 stockholders of record. We believe that approximately 3,700 beneficial owners hold shares through brokers, fiduciaries and nominees. No shares of Intevac s preferred stock were outstanding.

Q: How can I vote my shares in person at the Annual Meeting?

A: Shares held in your name as the stockholder of record may be voted in person at the Annual Meeting. Shares held beneficially in street name may be voted in person at the Annual Meeting only if you obtain a legal proxy from the broker, trustee or other nominee that holds your shares giving you the right to vote the shares. Even if you plan to attend the Annual Meeting, we recommend that you also submit your proxy card or voting instructions as described below, so that your vote will be counted if you later decide not to attend the meeting.

Q: How can I vote my shares without attending the Annual Meeting?

A: Whether you hold shares directly as the stockholder of record or beneficially in street name, you may direct how your shares are voted without attending the Annual Meeting. If you are a stockholder of record, you may vote by submitting a proxy. If you hold shares beneficially in street name, you may vote by submitting voting instructions to your broker, trustee or nominee. For instructions on how to vote, please refer to the instructions below and those included on your proxy card or, for shares held beneficially in street name, the voting instructions provided to you by your broker, trustee or nominee.

By mail Stockholders of record of Intevac Common Stock may submit proxies by completing, signing and dating their proxy cards and mailing them in the accompanying pre-addressed envelopes. Proxy cards submitted by mail must be received by the time of the meeting in order for your shares to be voted. Intevac stockholders who hold shares beneficially in street name may vote by mail by completing, signing and dating the voting instructions provided by their brokers, trustees or nominees and mailing them in the accompanying pre-addressed envelopes.

By Internet Stockholders of record of Intevac Common Stock with Internet access may submit proxies by following the Vote by Internet instructions on their proxy cards until 11:00 p.m., Pacific daylight time, on May 17, 2011. Most Intevac stockholders who hold shares beneficially in street name may vote by accessing the website specified in the voting instructions provided by their brokers, trustees or nominees. Please check the voting instructions for Internet voting availability.

By telephone Stockholders of record of Intevac Common Stock who live in the United States, Puerto Rico or Canada may submit proxies by following the Vote by Phone instructions on their proxy cards until 11:00 p.m., Pacific daylight time, on May 17, 2011. Most Intevac stockholders who hold shares beneficially in street name may vote by phone by calling the number specified in the voting instructions provided by their brokers, trustees or nominees. Please check the voting instructions for telephone voting availability.

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Q: What proposals will be voted on at the Annual Meeting?

A: At the Annual Meeting, stockholders will be asked to vote on:

(1) The election of seven directors to serve for the ensuing year or until their respective successors are duly elected and qualified;

(2) An amendment to the Intevac 2003 Employee Stock Purchase Plan to increase the number of shares reserved for issuance thereunder by 300,000 shares;

(3) An amendment to the Intevac 2004 Equity Incentive Plan to increase the number of shares reserved for issuance thereunder by 500,000 shares and approve the material terms of the plan;

(4) The ratification of the appointment of Grant Thornton LLP as independent public accountants of Intevac for the fiscal year ending December 31, 2011;

(5) The recommendation, by advisory vote, of the executive compensation of the Named Executive Officers (NEOs); and

(6) The recommendation, by advisory vote, of the frequency of holding an advisory vote on executive compensation.

Q: What is the voting requirement to approve each of the proposals?

A: *Proposal One* A plurality of the votes cast is required for the election of directors. You may vote FOR or WITHHOLD on each of the seven nominees for election as director. The seven nominees for director receiving the highest number of affirmative votes will be elected as directors of Intevac to serve for a term of one year or until their respective successors have been duly elected and qualified. Abstentions and broker non-votes will not affect the outcome of the election.

Proposal Two The affirmative vote of a majority of votes represented and voting at the Annual Meeting, or votes cast , is required for approval of the amendment to add an additional 300,000 shares to the Intevac 2003 Employee Stock Purchase Plan. You may vote FOR, AGAINST or ABSTAIN on this proposal. **Abstentions are deemed to be votes cast and have the same effect as a vote against this proposal.** However, broker non-votes are not deemed to be votes cast and, therefore, are not included in the tabulation of the voting results on this proposal.

Proposal Three The affirmative vote of a majority of votes cast is required for approval of the amendment to add an additional 500,000 shares to the Intevac 2004 Equity Incentive Plan and approve the material terms of the plan. You may vote FOR, AGAINST or ABSTAIN on this proposal. **Abstentions are deemed to be votes cast and have the same effect as a vote against this proposal.** However, broker non-votes are not deemed to be votes cast and, therefore, are not included in the tabulation of the voting results on this proposal.

Proposal Four The affirmative vote of a majority of votes cast is required to ratify the appointment of Grant Thornton LLP as Intevac s independent public accountants. You may vote FOR, AGAINST or ABSTAIN on this proposal. **Abstentions are deemed to be votes cast and have the same effect as a vote against this proposal**. However, broker non-votes are not deemed to be votes cast and, therefore, are not included in the tabulation of the voting results on this proposal.

Stockholder ratification of the selection of Grant Thornton LLP as Intevac s independent public accountants is not required by our Bylaws or other applicable legal requirements. However, the Board is submitting the selection of Grant Thornton LLP to the stockholders for ratification as a matter of good corporate practice. If the stockholders fail to ratify the selection, the Audit Committee will reconsider whether or not to retain that firm. Even if the selection is ratified, the Audit Committee in its discretion may direct the appointment of a different independent accounting firm at any time during the year, if it determines that such a change would be in the best interests of Intevac and its stockholders.

Proposal Five The affirmative vote of a majority of votes cast is required to recommend, by advisory vote, the executive compensation of the NEOs. You may vote FOR, AGAINST or ABSTAIN on this proposal. **Abstentions are deemed to be votes cast and have the same effect as a vote against this proposal**. However,

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broker non-votes are not deemed to be votes cast and, therefore, are not included in the tabulation of the voting results on this proposal. Because your vote is advisory, it will not be binding on us or the Board. However, the Board will review the voting results and take them into consideration when making future decisions regarding executive compensation.

Proposal Six The frequency of the advisory vote on compensation of our NEOs every year, every two years or every three years receiving the highest number of votes at the Annual Meeting will be the frequency approved by the stockholders. Proxy cards marked abstain and broker non-votes will have no effect on the outcome of the vote. Because your vote is advisory, it will not be binding on us or the Board. However, the Board will review the voting results and take them into consideration when making future decisions regarding the frequency of the advisory vote on executive compensation.

Q: What is the effect of not casting a vote at the 2011 Annual Meeting?

A: If you are a stockholder of record and you do not cast your vote, no votes will be cast on your behalf on any of the items of business at the 2011 Annual Meeting.

If you are a beneficial owner of shares held in street name, it is critical that you cast your vote if you want it to count in the election of directors (Proposal One) in the approval of an amendment to Intevac s 2003 Employee Stock Purchase Plan (Proposal Two), in the approval of an amendment to Intevac s 2004 Equity Incentive Plan (Proposal Three), in the recommendation on executive compensation (Proposal Five), and in the recommendation on frequency on an advisory vote on executive compensation (Proposal Six). In the past, if you held your shares in street name and you did not indicate how you wanted your shares voted in the election of directors, your bank or broker was allowed to vote those shares on your behalf in the election of directors as they felt appropriate. Recent changes in regulation were made to take away the ability of your bank or broker to vote your uninstructed shares in the election of directors on a discretionary basis. Thus, if you hold your shares in street name and you do not instruct your bank or broker how to vote in the election of directors, approval of the amendments or advisory votes, no votes will be cast on your behalf. Your bank or broker will, however, continue to have discretion to vote any uninstructed shares on the ratification of the appointment of Intevac s independent public accountants (Proposal Four).

Q: How does the Board of Directors recommend that I vote?

A: The Board of Directors recommends that you vote your shares:

FOR the election of all of the nominees as director listed in Proposal One;

FOR the adoption of the amendment to add an additional 300,000 shares to the Intevac 2003 Employee Stock Purchase Plan;

FOR the adoption of the amendment to add an additional 500,000 shares to the Intevac 2004 Equity Incentive Plan and approve the material terms of the plan;

FOR the proposal to ratify the selection of Grant Thornton LLP as Intevac s independent public accountants for the fiscal year ending December 31, 2011;

FOR the (non-binding) vote recommending, on an advisory basis, the compensation of the Company s executives named in the 2010 Summary Compensation Table, as disclosed in the Company s Proxy Statement; and

FOR the (non-binding) vote recommending, on an advisory basis, the holding of an advisory vote on executive compensation once every 3 years.

Q: If I sign a proxy, how will it be voted?

A: All shares entitled to vote and represented by properly executed proxy cards received prior to the applicable deadlines described above (and not revoked) will be voted at the Annual Meeting in accordance with the instructions indicated on those proxy cards. If no instructions are indicated on a properly executed proxy card, the shares represented by that proxy card will be voted as recommended by the Board of Directors.

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Q: What happens if additional matters are presented at the Annual Meeting?

A: If any other matters are properly presented for consideration at the Annual Meeting, including, among other things, consideration of a motion to adjourn the Annual Meeting to another time or place (including, without limitation, for the purpose of soliciting additional proxies), the persons named in the enclosed proxy card and acting thereunder will have discretion to vote on those matters in accordance with their best judgment. Intevac does not currently anticipate that any other matters will be raised at the Annual Meeting.

Q: Can I change or revoke my vote?

A: Subject to any rules and deadlines your broker, trustee or nominee may have, you may change your proxy instructions at any time before your proxy is voted at the Annual Meeting.

If you are a stockholder of record, you may change your vote by (1) filing with Intevac s Secretary, prior to your shares being voted at the Annual Meeting, a written notice of revocation or a duly executed proxy card, in either case dated later than the prior proxy card relating to the same shares, or (2) attending the Annual Meeting and voting in person (although attendance at the Annual Meeting will not, by itself, revoke a proxy). A stockholder of record that has voted on the Internet or by telephone may also change his or her vote by making a timely and valid later Internet or telephone vote.

If you are a beneficial owner of shares held in street name, you may change your vote (1) by submitting new voting instructions to your broker, trustee or other nominee or (2) if you have obtained a legal proxy from the broker, trustee or other nominee that holds your shares giving you the right to vote the shares, by attending the Annual Meeting and voting in person.

Any written notice of revocation or subsequent proxy card must be received by Intevac s Secretary prior to the taking of the vote at the Annual Meeting. Such written notice of revocation or subsequent proxy card should be hand delivered to Intevac s Secretary or should be sent so as to be delivered to Intevac s principal executive offices, Attention: Secretary.

Q: Who will bear the cost of soliciting votes for the Annual Meeting?

A: Intevac will bear all expenses of this solicitation, including the cost of preparing and mailing these proxy materials. Intevac may reimburse brokerage firms, custodians, nominees, fiduciaries and other persons representing beneficial owners of Common Stock for their reasonable expenses in forwarding solicitation material to such beneficial owners. Directors, officers and employees of Intevac may also solicit proxies in person or by other means of communication. Such directors, officers and employees will not be additionally compensated but may be reimbursed for reasonable out-of-pocket expenses in connection with such solicitation. Intevac may engage the services of a professional proxy solicitation firm to aid in the solicitation of proxies from certain brokers, bank nominees and other institutional owners. Our costs for such services, if retained, will not be significant.

Q: Where can I find the voting results of the Annual Meeting?

A: We intend to announce preliminary voting results at the Annual Meeting and will publish final results in a Form 8-K within four business days after the Annual Meeting.

Stockholder Proposals and Director Nominations

Q: What is the deadline to propose actions for consideration at next year s annual meeting of stockholders or to nominate individuals to serve as directors?

A: You may submit proposals, including director nominations, for consideration at future stockholder meetings.

Requirements for stockholder proposals to be considered for inclusion in Intevac s proxy materials Stockholders may present proper proposals for inclusion in Intevac s proxy statement and for consideration at the next annual meeting of its stockholders by submitting their proposals in writing to Intevac s Secretary in a timely manner. Assuming a mailing date of April 7, 2011 for this proxy statement, in order to be included in the proxy statement for the 2012 annual meeting of stockholders, stockholder proposals must be received by

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Intevac s Secretary no later than December 9, 2011, and must otherwise comply with the requirements of Rule 14a-8 of the Securities Exchange Act of 1934, as amended (the Exchange Act).

Requirements for stockholder proposals to be brought before an annual meeting In addition, Intevac s bylaws establish an advance notice procedure for stockholders who wish to present certain matters before an annual meeting of stockholders. In general, nominations for the election of directors may be made by (1) the Board of Directors, (2) the Nominating and Governance Committee or (3) any stockholder entitled to vote who has delivered written notice to Intevac s Secretary no later than the Notice Deadline (as defined below), which notice must contain specified information concerning the nominees and concerning the stockholder proposing such nominations.

Intevac s bylaws also provide that the only business that may be conducted at an annual meeting is business that is (1) specified in the notice of meeting given by or at the direction of the Board of Directors, (2) properly brought before the meeting by or at the direction of the Board of Directors or (3) properly brought before the meeting by a stockholder who has delivered written notice to the Secretary of Intevac no later than the Notice Deadline (as defined below).

The Notice Deadline is defined as that date which is 120 days prior to the one year anniversary of the date on which Intevac first mailed its proxy materials to stockholders for the previous year s annual meeting of stockholders. As a result, assuming a mailing date of April 7, 2011 for this proxy statement the Notice Deadline for the 2012 annual meeting of stockholders is December 9, 2011.

If a stockholder who has notified Intevac of his or her intention to present a proposal at an annual meeting does not appear to present his or her proposal at such meeting, Intevac need not present the proposal for a vote at such meeting.

Q: How may I obtain a copy of the bylaw provisions regarding stockholder proposals and director nominations?

A: A copy of the full text of the bylaw provisions discussed above may be obtained by writing to the Secretary of Intevac. All notices of proposals by stockholders, whether or not to be included in Intevac s proxy materials, should be sent to Intevac s principal executive offices, Attention: Secretary.

Additional Information about the Proxy Materials

Q: What should I do if I receive more than one set of proxy materials?

A: You may receive more than one set of proxy materials, including multiple copies of this proxy statement and multiple proxy cards or voting instruction cards. For example, if you hold your shares in more than one brokerage account, you may receive a separate voting instruction card for each brokerage account in which you hold shares. If you are a stockholder of record and your shares are registered in more than one name, you will receive more than one proxy card. Please complete, sign, date and return each Intevac proxy card or voting instruction card that you receive to ensure that all your shares are voted.

Q: How may I obtain a separate set of proxy materials or the 2010 Annual Report?

A: If you share an address with another stockholder, each stockholder may not receive a separate copy of the proxy materials and 2010 Annual Report.

Stockholders who do not receive a separate copy of the proxy materials and 2010 Annual Report may request to receive a separate copy of the proxy materials and 2010 Annual Report by calling 408-986-9888 or by writing to

Investor Relations at Intevac s principal executive offices. Alternatively, stockholders who share an address and receive multiple copies of our proxy materials and 2010 Annual Report can request to receive a single copy by following the instructions above, although each stockholder of record or beneficial owner must still submit a separate proxy card.

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Q: What is the mailing address for Intevac s principal executive offices?

A: Intevac s principal executive offices are located at 3560 Bassett Street, Santa Clara, California 95054.

Any written requests for additional information, additional copies of the proxy materials and 2010 Annual Report, notices of stockholder proposals, recommendations of candidates to the Board of Directors, communications to the Board of Directors or any other communications should be sent to this address.

IMPORTANT NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS FOR THE STOCKHOLDERS MEETING TO BE HELD ON MAY 18, 2011.

The proxy statement and the 2010 Annual Report are available at www.intevac.com

PROPOSAL ONE

ELECTION OF DIRECTORS

At the Annual Meeting, seven directors (constituting the entire board) are to be elected to serve until the next Annual Meeting of Stockholders and until a successor for any such director is elected and qualified, or until the death, resignation or removal of such director. The seven candidates receiving the highest number of affirmative votes of the shares entitled to vote at the Annual Meeting will be elected directors of Intevac.

It is intended that the proxies will be voted for the seven nominees named below unless authority to vote for any such nominee is withheld. All seven nominees are currently directors of Intevac. Five of the nominees were elected to the Board by the stockholders at the last annual meeting. Each person nominated for election has agreed to serve if elected, and the Board of Directors has no reason to believe that any nominee will be unavailable or will decline to serve. In the event, however, that any nominee is unable or declines to serve as a director at the time of the Annual Meeting, the proxies will be voted for any other person who is designated by the current Board of Directors to fill the vacancy. The proxies solicited by this Proxy Statement may not be voted for more than seven nominees.

Nominees

Set forth below is information regarding the nominees to the Board of Directors.

Name of Nominee	Position(s) with Intevac	Age
Norman H. Pond	Chairman of the Board	72
Kevin Fairbairn	President and Chief Executive Officer (CEO)	57
David S. Dury	Director	62
Stanley J. Hill	Director	69
Thomas M. Rohrs	Director	60
John F. Schaefer	Director	68
Ping Yang	Director	58

The Board of Directors recommends a vote FOR all the nominees listed above.

Business Experience and Qualifications of Nominees for Election as Directors

Each nominee brings a strong and unique background and set of skills to the Board, giving the Board as a whole competence and experience in a wide variety of areas, including corporate governance and board service, executive management, financial management and operations. Set forth below are the conclusions reached by the Board with regard to each of its directors.

As described elsewhere in this proxy under the heading Policy Regarding Board Nominees , the Company believes that Board members should possess a balance of knowledge, experience and capability on the Board, and considers the following issues: the current size and composition of the Board and the needs of the Board and the respective committees of the Board, such factors as issues of character, judgment, diversity, age, expertise, business experience, length of service, independence, other commitment and the like, the relevance of the candidate s skills and experience to the business, and such other factors as the Nominating and Governance Committee may consider appropriate. In addition to fulfilling the above criteria, 5 of the 7 directors named above are considered independent under the applicable Nasdaq rules.

Mr. Pond is a founder of Intevac and has served as Chairman of the Board since February 1991. Mr. Pond served as President and CEO from February 1991 until July 2000 and again from September 2001 through January 2002. Mr. Pond also held executive management positions at Varian Associates, Inc. and Teledyne. Mr. Pond holds a BS in physics from the University of Missouri at Rolla and an MS in physics from the University of California at Los Angeles. The Board believes Mr. Pond s qualifications to sit on our Board include his years of experience in the hard disk drive, semiconductor, communication and defense industries including as our Chairman for 20 years and as our President and CEO for 10 years and prior executive management experience.

Mr. Fairbairn joined Intevac as President and CEO in January 2002 and was appointed a director in February 2002. Before joining Intevac, Mr. Fairbairn was employed by Applied Materials from July 1985 to January 2002, most recently as Vice President and General Manager of the Conductor Etch Organization with responsibility for

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the Silicon and Metal Etch Divisions. From 1996 to 1999, Mr. Fairbairn was General Manager of Applied s Plasma Enhanced Chemical Vapor Deposition Business Unit and from 1993 to 1996 he was General Manager of Applied s Plasma Silane CVD Product Business Unit. Mr. Fairbairn holds an MA in engineering sciences from Cambridge University. The Board believes Mr. Fairbairn s qualifications to sit on our Board include his years of executive experience for a large multinational company in the high technology and semiconductor industries including as our CEO for 9 years, his strong leadership abilities, management skills and technical expertise.

Mr. Dury has served as a director of Intevac since July 2002. Mr. Dury is a co-founder of Mentor Capital Group, a venture capital firm formed in July 2000. From 1996 to 2000, Mr. Dury served as Senior Vice President and Chief Financial Officer of Aspect Development, a software development firm. Mr. Dury holds a BA in psychology from Duke University and an MBA from Cornell University. The Board believes Mr. Dury s qualifications to sit on our Board include his experience as a CEO of a venture capital firm, his experience with financial accounting matters as a previous CFO, as well as his operational, management and corporate governance expertise working on other companies boards of directors.

Mr. Hill was appointed as a director of Intevac in March 2004. Mr. Hill joined Kaiser Aerospace and Electronics Corporation, a privately held manufacturer of electronic and electro-optical systems, in 1969 and served as CEO and Chairman of both Kaiser and K Systems, Inc., Kaiser s parent company, from 1997 until his retirement in 2000. Prior to his appointment as CEO, Mr. Hill served in a number of executive positions at Kaiser. Mr. Hill holds a BS in mechanical engineering from the University of Maine, an MS in engineering from the University of Connecticut and has completed post-graduate studies at the Santa Clara University business school. He is also a director of First Aviation Services, Inc. The Board believes Mr. Hill s qualifications to sit on our Board include his operational and corporate governance expertise, which he obtained through experience as a CEO leading a complex global organization, and his years of experience in the government, military and electro-optical industries.

Mr. Rohrs was appointed as a director of Intevac in October 2010. Mr. Rohrs is the CEO of Skyline Solar and has held executive positions at leading Silicon Valley technology companies. Prior to Skyline Solar, Mr. Rohrs was the CEO of Electroglas from 2006 through 2009, Senior Vice President of Global Operations for Applied Materials from 1997 through 2002 and Vice President of Worldwide Operations for Silicon Graphics from 1992 through 1997. Mr. Rohrs currently serves on the Board of Directors of Advanced Energy and Magma Design Automation. He received a MBA from Harvard Business School and a BS in mechanical engineering from the University of Norte Dame. The Board believes Mr. Rohrs qualifications to sit on our Board include his experience as a CEO of a solar photovoltaic manufacturing company, his operational, management and corporate governance expertise working on other companies boards of directors and his years of experience in the semiconductor and electronics industries.

Mr. Schaefer was appointed as a director of Intevac in July 2010. Mr. Schaefer served as the Chairman and CEO of Phase Metrics from 1994 through 2001, President, Chief Operating Officer and Director of McGaw Incorporated from 1992 to 1994, President, CEO and Director of Levolor Corporation from 1989 to 1999, and Corporate Officer and Director of Baker Hughes Incorporated from 1974 to 1988. Mr. Schaefer also served as a Staff Assistant to the President of the United States between 1971 and 1974. Mr. Schaefer currently serves on the Board of Directors of Websense. He received a BS in engineering from the United States Naval Academy and a MBA from Harvard Business School. The Board believes Mr. Schaefer s qualifications to sit on our Board include his experience as a CEO of a manufacturing company, his operational, management and corporate governance expertise working on other companies boards of directors and his years of experience in the hard disk drive and oil and gas capital equipment industries.

Dr. Yang was appointed as a director of Intevac in March 2006. Dr. Yang was employed by Taiwan Semiconductor Manufacturing Company beginning in 1997 and served as Vice President of Research and Development from 1999 until 2005. Prior to joining TSMC, Dr. Yang worked at Texas Instruments from 1980 to 1997 where he was Director of Device and Design Flow. Dr. Yang is currently an independent consultant. Dr. Yang holds a BS in physics from National Taiwan University, and an MS and a PhD in electrical engineering from the University of Illinois. He is also a director of LTX Credence and Apache Design Solutions. The Board believes Dr. Yang s qualifications to sit on our Board include his extensive experience with global companies, his years of experience in the semiconductor industry, his experience providing strategic advisory services to complex organizations, as well as his operational, management and corporate governance expertise working with other companies boards of directors.

PROPOSAL TWO

APPROVAL OF AN AMENDMENT TO THE INTEVAC 2003 EMPLOYEE STOCK PURCHASE PLAN TO INCREASE THE NUMBER OF SHARES RESERVED THEREUNDER BY 300,000 SHARES

The Intevac 2003 Employee Stock Purchase Plan (the 2003 ESPP) was adopted by our Board of Directors and approved by our stockholders in 2003. Employees have participated in the 2003 ESPP or its predecessor plan, the 1995 Employee Stock Purchase Plan, since 1995.

Our Board of Directors has determined that it is in our best interests and the best interests of our stockholders to make an additional 300,000 shares available for purchase under the 2003 ESPP. As such, the Board of Directors has put forth for approval of our stockholders an amendment to the 2003 ESPP to increase the number of shares reserved thereunder by 300,000 shares. If our stockholders approve the adoption of the amendment, the aggregate number of shares available for issuance under the 2003 ESPP since its inception will be 1,658,000, and the total number of shares that remain available to be issued in the future under such plan will be approximately 536,000 shares.

The Board of Directors recommends a vote FOR the amendment to the 2003 Employee Stock Purchase Plan to increase the number of shares reserved for issuance thereunder by 300,000 shares.

Summary of the 2003 Employee Stock Purchase Plan

The following paragraphs provide a summary of the principal features of the 2003 ESPP and its operation. The following summary is qualified in its entirety by reference to the 2003 ESPP.

General

The 2003 ESPP was adopted by our Board of Directors in January 2003 and approved by our stockholders in May 2003. The purpose of the 2003 ESPP is to provide employees with an opportunity to purchase our Common Stock through payroll deductions.

Administration

Our Board of Directors or a committee appointed by the Board administers the 2003 ESPP. All questions of interpretation or application of the 2003 ESPP are determined by the Board or the committee, and its decisions are final, conclusive and binding upon all participants.

Eligibility

Each of our employees, or the employees of our designated subsidiaries, whose customary employment is for at least twenty hours per week and more than five months per year is eligible to participate in the 2003 ESPP; except that no employee may be granted a purchase right under the 2003 ESPP (i) to the extent that, immediately after the grant, such employee would own our stock or the stock of any of our subsidiaries and/or hold outstanding options to purchase stock possessing 5% or more of the total voting power or total value of all classes of our stock or any of our subsidiaries, or (ii) to the extent that his or her rights to purchase stock under all of our employee stock purchase plans or those of our subsidiaries accrues at a rate which exceeds $25,000 worth of stock (determined at the fair market value of the shares at the time such purchase right is granted) for each calendar year. Eligible employees have the opportunity to elect to participate in the 2003 ESPP approximately twice per year.

Offering Period

Shares of our Common Stock are offered for purchase under the 2003 ESPP through a series of successive offering periods, each with a maximum duration of approximately twenty-four (24) months. Each offering period is of a duration determined by the plan administrator prior to the start date and is comprised of a series of one or more successive purchase intervals. Purchase intervals within each offering period last approximately six (6) months and run from the first trading day in February to the last trading day in July each year and from the first trading day in August each year to the last trading day in January of the following year. Should the fair market value of our

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Common Stock on any semi-annual purchase date within an offering period be less than the fair market value per share on the start date of that offering period, then that offering period automatically terminates immediately after the purchase of shares on such purchase date, and a new offering period commences on the next trading day following the purchase date. The plan administrator may shorten the duration of such new offering period within five (5) trading days following the start date of such new offering period.

Purchase Price

The purchase price of our Common Stock acquired under the 2003 ESPP is equal to eighty-five percent (85%) of the lower of (i) the fair market value per share of our Common Stock on the first day of the offering period or on the participant s entry date into the offering period or (ii) the fair market value on the semi-annual purchase date. The fair market value of our Common Stock on any relevant date will be the closing sales price per share as reported on the Nasdaq National Market (or the closing bid, if no sales were reported), or the mean of the closing bid and asked prices if our common stock is regularly quoted by a recognized securities dealer but selling prices are not reported, as quoted on such exchange or reported in the Wall Street Journal.

Payment of Purchase Price; Payroll Deductions

Each participant s purchase price of the shares is accumulated by payroll deductions throughout each purchase interval. A participant may elect to have up to 10% of his or her compensation deducted each payroll period. The number of shares of our Common Stock a participant may purchase in each purchase interval during an offering period is determined by dividing the total amount of payroll deductions withheld from the participant s compensation during that purchase interval by the purchase price; provided, however, that a participant may not purchase more than 750 shares each purchase interval.

Withdrawal

Generally, a participant may withdraw from an offering period at any time by written notice without affecting his or her eligibility to participate in future offering periods. However, once a participant withdraws from a particular offering period, that participant may not participate again in the same purchase interval and, unless he or she re-enters the 2003 ESPP at a semi-annual entry date in accordance with the terms of the plan may not participate in the same offering period. To participate again in the 2003 ESPP, the participant must deliver to us a new subscription agreement in accordance with the terms of the plan.

Termination of Employment

Upon termination of a participant s employment for any reason, including disability or death, his or her participation in the 2003 ESPP will immediately cease. The payroll deductions credited to the participant s account, but not used to make a purchase will be returned to him or her or, in the case of death, to the person or persons entitled thereto as provided pursuant to the 2003 ESPP.

Adjustments; Merger or Change in Control

In the event of any dividend or other distribution, recapitalization, stock split, reverse stock split, reorganization, merger consolidation, split-up, spin-off, combination, repurchase or exchange of common stock or other securities of the company or other change in our capital structure, appropriate adjustments will be made in the number and class of shares available for purchase under the 2003 ESPP (including purchase interval limitations) and the purchase price and number of shares covered by each purchase right under the 2003 ESPP as determined by the plan administrator in its sole discretion.

In the event of any merger or change of control, as defined in the 2003 ESPP, the successor corporation or a parent or subsidiary of such successor corporation shall assume or substitute an equivalent purchase right for each outstanding purchase right. In the event the successor corporation refuses to do so, the purchase interval then in progress shall be shortened by setting a new purchase date before the merger or change of control, and the current purchase interval and offering period shall end on the new purchase date. The plan administrator shall notify each participant of the new purchase date at least 10 business days prior to such date, and the participant s purchase right shall be exercised on such new purchase date, unless the participant withdraws prior to such date.

Certain Federal Income Tax Information

The following brief summary of the effect of U.S. federal income taxation upon the participant and Intevac with respect to the shares purchased under the 2003 ESPP does not purport to be complete, and does not discuss the tax consequences of a participant s death or the income tax laws of any state or foreign country in which the participant may reside.

The 2003 ESPP, and the right of participants to make purchases thereunder, is intended to qualify under the provisions of Sections 421 and 423 of the Internal Revenue Code. Under these provisions, no income will be taxable to a participant until the shares purchased under the 2003 ESPP are sold or otherwise disposed of. Upon the sale or other disposition of the shares, the participant will generally be subject to tax in an amount that depends upon the holding period. If the shares are sold or otherwise disposed of more than (1) two years from the first day of the applicable offering period (or, if later, the first day the participant entered the offering period) and (2) one year from the applicable date of purchase, the participant will recognize ordinary income measured as the lesser of (a) the excess of the fair market value of the shares at the time of such sale or disposition over the purchase price, or (b) an amount equal to 15% of the fair market value of the shares as of the first day the participant entered the applicable offering period. Any additional gain will be treated as long-term capital gain. If the shares are sold or otherwise disposed of before the expiration of these holding periods, the participant will recognize ordinary income generally measured as the excess of the fair market value of the shares on the date the shares were purchased over the purchase price. Any additional gain or loss on such sale or disposition will be long-term or short-term capital gain or loss, depending on how long the shares have been held from the date of purchase.

Intevac generally is not entitled to a deduction for amounts taxed as ordinary income or capital gain to a participant, except to the extent of ordinary income recognized by participants upon a sale or disposition of shares prior to the expiration of the holding periods described above.

Amendment and Termination of the Plan

Our Board of Directors may at any time terminate or amend the 2003 ESPP. No amendment shall be effective unless it is approved by the stockholders, if such amendment would require stockholder approval in order to comply with Section 423 of the Internal Revenue Code.

Purchase Plan Transactions for Certain Individuals and Groups

Given that the number of shares that may be purchased under the 2003 ESPP is determined, in part, on our Common Stock s value on the enrollment date of each participant and the last day of the purchase interval and given that participation in the 2003 ESPP is voluntary on part of employees, the actual number of shares that may be purchased by an individual is not determinable.

The table below shows, as to each of Intevac s executive officers named in the 2010 Summary Compensation Table and the various indicated groups, the number of shares of Common Stock purchased under the 2003 ESPP during the last fiscal year, together with the weighted average purchase price paid per share.

	Number of	Weighted Average

Name of Individual or Group	Purchased Shares	Purchase Price
Kevin Fairbairn	1,500	$ 3.73
Jeffrey Andreson	1,500	$ 3.73
Luke Marusiak	730	$ 9.35
Joseph Pietras	1,500	$ 3.73
Michael Russak	1,377	$ 3.73
All executive officers, as a group	9,607	$ 4.59
All employees who are not executive officers, as a group	245,832	$ 4.02

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Required Vote

The affirmative vote of the holders of a majority of the shares represented and voting at the Annual Meeting (provided that that vote also constitutes the affirmative vote of a majority of the required quorum) will be required for approval of the amendment to add an additional 300,000 shares to the Intevac 2003 Employee Stock Purchase Plan.

Summary

We believe strongly that approval of the amendment to the Intevac 2003 Employee Stock Purchase Plan is essential to our continued success. Awards such as those provided under the 2003 ESPP constitute an important incentive for our employees and help us to attract, retain and motivate people whose skills and performance are critical to our success. Our employees are our most valuable assets. We strongly believe that the 2003 ESPP is essential for us to compete for talent in the labor markets in which we operate.

PROPOSAL THREE

APPROVAL OF AN AMENDMENT TO THE INTEVAC 2004 EQUITY INCENTIVE PLAN TO INCREASE THE NUMBER OF SHARES RESERVED FOR ISSUANCE THEREUNDER BY 500,000 SHARES AND APPROVE THE MATERIAL TERMS OF THE PLAN

We have historically provided stock options as an incentive to our employees, directors and consultants to promote increased stockholder value. The Board of Directors and management believe that stock options and other types of equity awards are one of the primary ways to attract and retain key personnel responsible for the continued development and growth of our business, and to motivate all employees to increase stockholder value. In addition, stock options are considered a competitive necessity in the high technology sector in which we compete.

The Board of Directors recommends that stockholders vote FOR the adoption of the amendment to add an additional 500,000 shares to the Intevac 2004 Equity Incentive Plan and Approval of the Material Terms of the Plan.

As a result of the desire to attract, give further incentive to and retain current employees, officers and directors, options to purchase 763,000 shares were granted from the 2004 Equity Incentive Plan (the 2004 Plan) during fiscal 2010. As of December 31, 2010, there were 3,385,000 unexercised options outstanding and 537,000 shares available for grant under the 2004 Plan, not including the 500,000 share increase subject to stockholder approval at this 2011 Annual Meeting. The unexercised options and shares available for grant represent 17% of the total Intevac shares outstanding at December 31, 2010. Including the 500,000 shares subject to stockholder approval at this Annual Meeting, the percentage will increase to 20% of the shares outstanding. We are also seeking stockholder approval of the material terms of the 2004 Plan for purposes of complying with Section 162(m) of the Internal Revenue Code.

Proposed Amendment

At the 2011 Annual Meeting, we are asking our stockholders to approve an amendment to the 2004 Plan to increase the number of shares reserved for issuance under the 2004 Plan by 500,000 shares, to an aggregate of 4,400,000 shares reserved for issuance thereunder plus shares remaining from or that otherwise would return to the 1995 Stock Option/Stock Issuance Plan (up to a maximum of 1,500,000 such shares). The Board of Directors approved the proposed amendment to the 2004 Plan in February 2011, subject to stockholder approval at this 2011 Annual Meeting. The amendment to increase the number of shares reserved under the 2004 Plan is proposed in order to give the Board and the Compensation Committee of the Board continued flexibility to grant stock options and other types of equity awards. We are also seeking stockholder approval of the material terms of the 2004 Plan for purposes of complying with Section 162(m) of the Internal Revenue Code. If stockholders approve amending and restating the 2004 Plan, the amended and restated 2004 Plan will replace the current version of the 2004 Plan.

The Board and management believe that granting equity awards motivates higher levels of performance, aligns the interests of employees and stockholders by giving employees the perspective of owners with equity stakes in Intevac, and provides an effective means of recognizing employee contributions to our success. The Board and management also believe that equity awards are of great value in recruiting and retaining highly qualified technical and other key personnel who are in great demand, as well as rewarding and encouraging current employees and other service providers. Finally, the Board and management believe that the ability to grant equity awards will be important to our future success by helping us to accomplish these objectives. If our stockholders approve its material terms, our 2004 Plan will continue to provide the Company with the potential to continue to take tax deductions associated with certain executive compensation, particularly with respect to certain full-value awards subject to vesting based upon the attainment of specified objective performance criteria.

Awards granted under 2004 Plan may be designed to qualify as performance-based compensation within the meaning of Section 162(m) of the Internal Revenue Code. Pursuant to Section 162(m), the company generally may not deduct for federal income tax purposes compensation paid to our Chief Executive Officer or certain other executive officers to the extent that any of these persons receive more than $1 million in compensation in any single year. However, if the compensation qualifies as performance-based for Section 162(m) purposes, the company may deduct for federal income tax purposes the compensation paid even if such compensation exceeds $1 million in a single year. For certain awards granted under the 2004 Plan to qualify as performance-based compensation under Section 162(m), among other things, our stockholders must approve the material terms of 2004 Plan. A favorable vote for this proposal will allow us to continue to deduct certain executive compensation in excess of $1 million and provide us with potentially significant future tax benefits and associated cash flows.

Summary of the 2004 Equity Incentive Plan

The following paragraphs provide a summary of the principal features of the 2004 Plan and its operation. The following summary is qualified in its entirety by reference to the 2004 Plan.

Background and Purpose of the Plan

The 2004 Plan permits the grant of the following types of incentive awards: (1) stock options, (2) stock appreciation rights, (3) restricted stock, (4) performance units, and (5) performance shares (individually, an Award). The 2004 Plan is intended to help us to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentives to employees, directors and consultants, and to promote the success of Intevac.

Administration of the Plan

Our Board of Directors or the Compensation Committee of our Board of Directors (in either case, the Committee) administers the 2004 Plan. Members of the Committee generally must qualify as outside directors under Section 162(m) of the Internal Revenue Code (so that we are entitled to receive a federal tax deduction for certain compensation paid under the 2004 Plan) and generally must meet such other requirements as are established by the Securities and Exchange Commission for plans intended to qualify for exemption under Rule 16b-3. For the plan to qualify for exemption under Rule 16b-3, members of the Committee must be non-employee directors. Notwithstanding the foregoing, the Board of Directors also may appoint one or more separate committees to administer the 2004 Plan.

Subject to the terms of the 2004 Plan, the Committee has the sole discretion to select the employees, directors and consultants who will receive Awards, determine the terms and conditions of Awards (for example, the vesting schedule), interpret the provisions of the Plan and outstanding Awards, and with the consent of the stockholders implement an exchange program under which outstanding Awards are exchanged for different awards and/or cash or the exercise price of an outstanding Award is reduced.

A total of 1,200,000 shares of our Common Stock were originally reserved for issuance under the 2004 Plan, and an additional 500,000, 500,000, 900,000 and 800,000 shares were reserved and approved by the stockholders at the Company s 2010, 2008, 2007 and 2006 annual meetings, respectively. Proposal Three, if approved, will raise the number of shares reserved by 500,000 shares, to 4,400,000 shares. No more than 20% of the shares reserved for issuance under the 2004 Plan may be issued pursuant to Awards that are not stock options or stock appreciation rights that are granted at exercise prices equal to 100% of the fair market value on the date of grant (that is, pursuant to Awards of restricted stock, performance units, performance shares, discounted stock options or discounted stock appreciation rights). In addition, shares which were reserved but not issued under our 1995 Stock Option/ Stock Issuance Plan (the 1995 Plan) as of the effective date of the 2004 Plan, as well as any shares that would otherwise return to the 1995 Plan, upon termination of stock options or repurchase of shares issued under the 1995 Plan, are available for issuance under the 2004 Plan up to a maximum of 1,500,000 shares.

If an Award expires or is cancelled without having been fully exercised or vested, the unvested or cancelled shares generally will be returned to the available pool of shares reserved for issuance under the 2004 Plan. With respect to stock appreciation rights, only shares actually issued pursuant to such an award cease to be available under the 2004

Plan, and to the extent any award under the 2004 Plan is paid out in cash rather than stock, such cash payment will not reduce the number of shares available for issuance under the 2004 Plan. Also, if we experience a stock split, reverse stock split, stock dividend, combination or reclassification of our Common Stock or other similar change in our capital structure, the Committee shall adjust the number of shares available for issuance under the 2004 Plan, the price and number of shares subject to outstanding Awards, and the per-person limits on Awards, as appropriate to reflect the stock dividend or other change.

Eligibility to Receive Awards

The Committee selects the directors who will be granted Awards under the 2004 Plan and grants Awards for employees and consultants under management s recommendations. The actual number of individuals who will receive an Award under the Plan cannot be determined in advance because the Committee has the discretion to select the participants. As of March 29, 2011, approximately 255 employees, directors and consultants would be eligible to participate in the 2004 Plan.

Stock Options

A stock option is the right to acquire shares of our Common Stock at a fixed exercise price for a fixed period of time. Under the 2004 Plan, the Committee may grant non-statutory stock options and/or incentive stock options (which entitle employees, but not Intevac, to more favorable tax treatment). Only employees are eligible to receive incentive stock options. The Committee determines the number of shares covered by each option, but during any fiscal year, no participant may be granted a combination of options and stock appreciation rights for more than 200,000 shares, except that a participant may be granted a combination of options and stock appreciation rights for an additional 300,000 shares in connection with his or her initial employment.

The exercise price of the shares subject to each option is set by the Committee but cannot be less than 100% of the fair market value (on the date of grant) of the shares covered by incentive stock options or by non-statutory options that are intended to qualify as performance-based under Section 162(m) of the Internal Revenue Code. In addition, the exercise price of an incentive stock option must be at least 110% of fair market value if (on the grant date) the participant owns stock possessing more than 10% of the total combined voting power of all classes of our stock or any of our subsidiaries. The aggregate fair market value of the shares (determined on the grant date) covered by incentive stock options that first become exercisable by any participant during any calendar year also may not exceed $100,000.

An option granted under the 2004 Plan generally cannot be exercised until it becomes vested. Options become exercisable at the times and on the terms established by the Committee at the time of grant. Options granted under the 2004 Plan expire at the times established by the Committee, but the term of an incentive stock option cannot be greater than 10 years after the grant date (5 years in the case of an incentive stock option granted to a participant who owns stock possessing more than 10% of the total combined voting power of all classes of our stock or any of our subsidiaries).

The exercise price of each option granted under the 2004 Plan must be paid in full at the time of exercise. The exercise price may be paid in any form determined by the Committee, including, but not limited to, cash, check, surrender of certain shares, or pursuant to a cashless exercise program. The Committee may also permit, in some cases, the exercise price to be paid by means of a promissory note or through a reduction in the amount of our liability to the participant.

After a termination of service with Intevac, a participant will be able to exercise the vested portion of his or her option for the period of time stated in the option agreement. If no such period of time is stated in the participant s option agreement, the participant will generally be able to exercise his or her option for (i) three months following his or her termination for reasons other than death or disability, and (ii) twelve months following his or her termination due to death or disability.

Stock Appreciation Rights

Stock appreciation rights are awards that grant the participant the right to receive an amount, payable in cash or stock (or a combination of cash and stock) as specified at the time of grant, equal to (1) the number of shares exercised, times (2) the amount by which our then current stock price exceeds the exercise price. The exercise price will be set on the date of grant, but can vary in accordance with a predetermined formula. An individual will be able to profit from a stock appreciation right only if the fair market value of our stock increases above the exercise price.

Awards of stock appreciation rights may be granted in connection with all or any part of an option, either concurrently with the grant of an option or at any time thereafter during the term of the option, or may be granted independently of options. There are three types of stock appreciation rights available for grant under the 2004 Plan.

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A tandem stock appreciation right is a stock appreciation right granted in connection with an option that entitles the participant to exercise the stock appreciation right by surrendering to us a portion of the unexercised related option. A tandem stock appreciation right may be exercised only with respect to the shares for which its related option is then exercisable. An affiliated stock appreciation right is a stock appreciation right granted in connection with an option that is automatically deemed to be exercised upon the exercise of the related option, but does not necessitate a reduction in the number of shares subject to the related option. A freestanding stock appreciation right is one that is granted independent of any options. No participant may be granted a combination of options or stock appreciation rights covering more than 200,000 shares in any fiscal year, except that a participant may be granted a combination of options or stock appreciation rights covering an additional 300,000 shares in connection with his or her initial employment.

The Committee determines the terms of stock appreciation rights, except that the exercise price of a tandem or affiliated stock appreciation right must be equal to the exercise price of the related option. When a tandem stock appreciation right granted in connection with an option is exercised, the related option, to the extent surrendered, will cease to be exercisable. A tandem or affiliated stock appreciation right that is granted in connection with an option will be exercisable until, and will expire no later than, the date on which the related option ceases to be exercisable or expires. A freestanding stock appreciation right that is granted without a related option will be exercisable, in whole or in part, at such time as the Committee specifies in the stock appreciation right agreement.

No stock appreciation right may have a term of more than ten years from the date of grant. After termination of service with Intevac, a participant will be able to exercise the vested portion of his or her stock appreciation right for the period of time stated in the Award agreement. If no such period of time is stated in a participant s Award agreement, a participant will generally be able to exercise his or her vested stock appreciation rights for the same period of time as applies to stock options.

Restricted Stock

Awards of restricted stock are shares that are issued to participants but that vest in accordance with the terms and conditions established by the Committee. For example, the Committee may set restrictions based on the achievement of specific performance goals or continued employment. The Committee, in its discretion, may accelerate the time at which any restrictions will lapse or be removed.

The Committee determines the number of shares of restricted stock granted to any employee or consultant, but no participant may be granted more than 125,000 shares of restricted stock in any fiscal year, except that a participant may be granted up to an additional 175,000 shares of restricted stock in connection with his or her initial employment.

In determining whether an Award of restricted stock should be made, and/or the vesting schedule for any such Award, the Committee may impose whatever conditions to vesting as it determines to be appropriate. Upon termination of service, unvested shares of restricted stock generally will be forfeited.

Performance Units and Performance Shares

Performance units and performance shares are Awards that will result in a payment to a participant only if performance objectives established by the Committee are achieved or the Awards otherwise vest. The applicable performance objectives will be determined by the Committee, and may be based upon the achievement of Company-wide, divisional or individual goals or upon any other basis determined by the Committee. Performance units have an initial value that is established by the Committee on or before the date of grant. Performance shares have an initial value equal to the fair market value of a share on the date of grant. The Committee determines the number of performance units and performance shares granted to a participant, but no participant may be granted performance units with an initial value greater than $750,000 or granted more than 125,000 performance shares in any fiscal year, except that a participant may be granted performance units with an initial value up to an additional $750,000 and/or an additional 175,000 performance shares in connection with his or her initial employment.

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Performance Goals

Under Section 162(m) of the Internal Revenue Code, the annual compensation paid to our CEO and to certain of our other executive officers may not be deductible to the extent it exceeds $1 million. However, we are able to preserve the deductibility of compensation in excess of $1 million if the conditions of Section 162(m) are met. These conditions include stockholder approval of the 2004 Plan (including this amendment), setting limits on the number of Awards that any individual may receive and, for Awards other than options and stock appreciation rights, establishing performance criteria that must be met before the Award actually will vest or be paid.

We have designed the 2004 Plan so that it permits us to pay compensation that qualifies as performance-based under Section 162(m). Thus, the Committee (in its discretion) may make performance goals applicable to a participant with respect to an Award. At the Committee s discretion, one or more of the following performance goals may apply (all of which are defined in the 2004 Plan): cost of sales as a percentage of sales, earnings per share, free cash flow, marketing and sales expenses as a percentage of sales, net income as a percentage of sales, operating margin, revenue, total stockholder return and working capital. The performance goals may differ from participant to participant and from Award to Award, may be used alone or in combination, may be used to measure the performance of Intevac in absolute terms, relative terms, on a per share basis, against the performance of Intevac as a whole or a segment of the business and/or on a pre-tax or after-tax basis. With respect to an Award intended to qualify as performance-based, prior to the last possible date that would not jeopardize an Award s qualification as performance-based compensation for purposes of Section 162(m), the Committee may determine whether any elements or items shall be included in or excluded from the calculation of any of the above performance goals.

Change of Control

In the event of a change in control of Intevac, the successor corporation may either assume or provide a substitute award for each outstanding Award. In the event the successor corporation refuses to assume or provide a substitute award, the Award will immediately vest and become exercisable as to all of the shares subject to such Award. In such case, the Committee will provide at least 15 days notice of the immediate vesting and exercisability of stock options and stock appreciation rights that will not be assumed or substituted for. The Award will then terminate upon the expiration of the notice period.

Limited Transferability of Awards

Awards granted under the 2004 Plan generally may not be sold, transferred, pledged, assigned or otherwise alienated or hypothecated, other than by will or by the applicable laws of descent and distribution.

Federal Tax Aspects

The following brief summary of the effect of U.S. federal income taxation of an Award upon the participant and Intevac with respect to Awards granted under the 2004 Plan does not purport to be complete, and does not discuss the tax consequences of a participant s death or the income tax laws of any state or foreign country in which the participant may reside.

Non-statutory Stock Options

No taxable income generally is reportable when a non-statutory stock option is granted to a participant. Upon exercise, the participant will recognize ordinary income in an amount equal to the excess of the fair market value (on the exercise date) of the shares purchased over the exercise price of the option. Any additional gain or loss recognized upon any later disposition of the shares will be capital gain or loss, which may be long- or short-term depending on the holding period after exercise.

As a result of Section 409A of the Code and the Treasury regulations promulgated thereunder (Section 409A), however, non-statutory stock options and stock appreciation rights granted with an exercise price below the fair market value of the underlying stock or with a deferral feature may be taxable to the recipient in the year of vesting in an amount equal to the difference between the then fair market value of the underlying stock and the exercise price of such Awards and may be subject to an additional 20% federal income tax plus penalties and interest. In addition, certain states, such as California, have adopted similar tax provisions.

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Incentive Stock Options

No taxable income is reportable when an incentive stock option is granted or exercised, unless the alternative minimum tax rules apply, in which case taxation occurs upon exercise. If the participant exercises the option and then later sells or otherwise disposes of the shares more than two years after the grant date and more than one year after the exercise date, the difference between the sale price and the exercise price will be taxed as long-term capital gain or loss. If the participant exercises the option and then later sells or otherwise disposes of the shares before the end of the two- or one-year holding periods described above, he or she generally will have ordinary income at the time of the sale equal to the fair market value of the shares on the exercise date (or the sale price, if less) minus the exercise price of the option. Any additional gain or loss generally will be taxable at long-term or short-term capital gain rates, depending on whether the participant has held the shares for more than one year.

Stock Appreciation Rights

No taxable income generally is reportable when a stock appreciation right is granted to a participant. Upon exercise, the participant will recognize ordinary income in an amount equal to the amount of cash received and the fair market value of any shares received. Any additional gain or loss recognized upon any later disposition of the shares would be capital gain or loss. As a result of Section 409A, however, stock appreciation rights granted with an exercise price below the fair market value of the underlying stock may be taxable to the participant before exercise of an award.

Restricted Stock, Performance Units and Performance Shares

A participant generally will not have taxable income upon grant of restricted stock, performance units or performance shares. Instead, he or she generally will recognize ordinary income at the time of vesting equal to the fair market value (on the vesting date) of the shares or cash received minus any amount paid for the shares. However, the recipient of a restricted stock Award may elect to recognize income at the time he or she receives the Award in an amount equal to the fair value of the shares underlying the Award (less any cash paid for the shares) on the date the Award is granted.

Section 409A

Section 409A, which was added by the American Jobs Creation Act of 2004, provides certain requirements applicable to non-qualified deferred compensation arrangements. Awards granted under the 2004 Plan with a deferral feature will be subject to the requirements of Section 409A, including discount stock options and stock appreciation rights discussed above. If an Award is subject to and fails to satisfy the requirements of Section 409A, the recipient of that Award may recognize ordinary income on the amounts deferred under the Award, to the extent vested, which may be prior to when the compensation is actually or constructively received. Also, if an Award that is subject to Section 409A fails to comply with Section 409A s provisions, Section 409A imposes an additional 20% federal income tax on compensation recognized as ordinary income, as well as interest on such deferred compensation. Some states may also apply a penalty tax (for instance, California imposes a 20% penalty tax in addition to the 20% federal penalty tax). **We strongly encourage recipients of such Awards to consult their tax, financial, or other advisor regarding the tax treatment of such Awards**.

Tax Effect for the Company Section 162(m)

Intevac generally will be entitled to a tax deduction in connection with an Award under the 2004 Plan in an amount equal to the ordinary income realized by a participant at the time the participant recognizes such income (for example, upon the exercise of a non-statutory stock option). Special rules limit the deductibility of compensation paid to our CEO (i.e., our principal executive officer) and to each of our three most highly compensated executive officers for the taxable year (other than the principal executive officer or principal financial officer). Under Section 162(m) of the

Code, the annual compensation paid to any of these specified executives will be deductible only to the extent that it does not exceed $1 million. However we can preserve the deductibility of certain compensation in excess of $1 million if the conditions of Section 162(m) are met. These conditions include stockholder approval of the 2004 Plan, and its material terms, setting limits on the number of Awards that any

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individual may receive and for Awards other than certain stock options, establishing performance criteria (see the discussion under Performance Goals above) that must be met before the Award actually will vest or be paid. The 2004 Plan has been designed to permit the Committee to grant Awards that qualify as performance-based for purposes of satisfying the conditions of Section 162(m), thereby permitting Intevac to continue to receive a federal income tax deduction in connection with such Awards.

Amendment and Termination of the 2004 Plan

The Board generally may amend or terminate the 2004 Plan at any time and for any reason. Amendments will be contingent on stockholder approval if required by applicable law or stock exchange listing requirements. By its terms, the 2004 Plan automatically will terminate in 2014, although any Awards outstanding at that time will continue for their terms.

Awards to be Granted to Certain Individuals and Groups

The number of Awards that an employee, director or consultant may receive under the 2004 Plan is in the discretion of the Committee and therefore cannot be determined in advance. Our executive officers and our non-employee directors have an interest in this proposal, because they are eligible to receive discretionary Awards under the 2004 Plan.

As of the date of this proxy statement, there has been no determination by the Committee with respect to future awards under the 2004 Plan. Accordingly, future awards are not determinable. The following table, however, sets forth information with respect to the grant of options under the 2004 Plan to the executive officers named in the Summary Compensation Table below, to executive officers as a group, to all non-employee directors as a group and to all other employees as a group during the Company s last fiscal year:

Name of Individual or Group	Number of Shares Granted	Average per Share Exercise Price
Kevin Fairbairn	75,000	$ 11.84
Jeffrey Andreson	25,000	$ 11.84
Luke Marusiak(1)	50,000	$ 16.49
Joseph Pietras	25,000	$ 11.84
Michael Russak	25,000	$ 11.84
All executive officers, as a group	267,000	$ 12.20
All directors who are not executive officers, as a group	84,000	$ 11.59
All employees who are not executive officers, as a group	411,525	$ 12.36

(1) Mr. Marusiak was rehired by the Company on January 18, 2010 and received a new hire grant of 50,000 options at that time.

Required Vote

The affirmative vote of the holders of a majority of the shares represented and voting at the Annual Meeting (provided that that vote also constitutes the affirmative vote of a majority of the required quorum) will be required for approval of the addition of 500,000 shares to the Intevac 2004 Equity Incentive Plan and the approval of the material terms of the plan.

Summary

We believe strongly that approval of the amendment to the 2004 Plan and its material terms is essential to our continued success. Awards such as those provided under the 2004 Plan constitute an important incentive for our key employees and other service providers and help us to attract, retain and motivate people whose skills and performance are critical to our success. Our employees are our most valuable assets. We strongly believe that the 2004 Plan is essential for us to compete for talent in the labor markets in which we operate.

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PROPOSAL FOUR

RATIFICATION OF INDEPENDENT PUBLIC ACCOUNTANTS

The Audit Committee of the Board of Directors has selected Grant Thornton LLP as our independent public accountants for the fiscal year ending December 31, 2011. Grant Thornton LLP began auditing our financial statements in 2000. Its representatives are expected to be present at the Annual Meeting, will have an opportunity to make a statement if they desire to do so, and will be available to respond to appropriate questions.

The Board of Directors recommends a vote FOR ratification of the selection of Grant Thornton LLP as Intevac s independent registered public accounting firm for the fiscal year ending December 31, 2011.

Principal Accountant Fees and Services

The following table presents fees billed for professional audit services and other services rendered to us by Grant Thornton LLP for the years ended December 31, 2010 and 2009.

	2010	2009
Audit Fees(1)	$ 1,092,907	$ 1,097,443
Audit-Related Fees(2)		
Tax Fees(3)	73,324	321,429
All Other Fees(4)		
Total Fees	$ 1,166,231	$ 1,418,872

(1) Audit fees consist of fees billed for professional services rendered for the audit of our annual consolidated financial statements and review of the interim consolidated financial statements included in our Quarterly Reports on Form 10-Q and fees for services that are normally provided by Grant Thornton LLP in connection with statutory and regulatory filings or engagements. In addition, audit fees include those fees related to Grant Thornton s audit of the effectiveness of our internal controls over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act. This category also includes advice on accounting matters that arose during, or as a result of, the audit or the review of the interim consolidated financial statements.

(2) Audit related fees consist of assurance and related services provided by Grant Thornton LLP that are reasonably related to the performance of the audit of our consolidated financial statements and are not reported under Audit Fees . There were no services provided under this category in fiscal 2009 or fiscal 2010.

(3) Tax fees consist of fees billed for tax compliance, consultation and planning services, and include fees associated with a research and development tax credit study. The Company did not engage Grant Thornton LLP for professional services in connection with tax compliance in fiscal 2010 for the year ended December 31, 2009.

(4) All other fees consist of fees for other corporate related services. There were no services provided under this category in fiscal 2009 or fiscal 2010.

In making its recommendation to ratify the appointment of Grant Thornton LLP as our independent auditor for the fiscal year ending December 31, 2011, the Audit Committee has considered whether services other than audit and audit-related services provided by Grant Thornton LLP are compatible with maintaining the independence of Grant Thornton LLP and has determined that such services are compatible.

Pre-Approval of Audit and Permissible Non-Audit Services

Our Audit Committee approves in advance all engagements with Grant Thornton LLP, including the audit of our annual financial statements, the review of the financial statements included in our Quarterly Reports on Form 10-Q and tax compliance services. Fees billed by Grant Thornton LLP are reviewed and approved by the Audit Committee on a quarterly basis.

PROPOSAL FIVE

ADVISORY VOTE ON EXECUTIVE COMPENSATION

The Company asks that you indicate your support for its executive compensation policies and practices as described in the Company s Compensation Discussion and Analysis, accompanying tables and related narrative contained in this Proxy Statement. This proposal is commonly known as a say-on-pay proposal, and gives our stockholders the opportunity to express their views on the compensation of our NEOs. Your vote is advisory and so will not be binding on the Board. However, the Board will review the voting results and take them into consideration when making future decisions regarding executive compensation.

Compensation Program and Philosophy

As described in detail under the headings Executive Compensation and Related Information and Compensation Discussion and Analysis, our NEO compensation program is designed to attract, retain, motivate and reward high-performing executives who are critical to our success while maintaining strong and direct links between executive pay, individual performance, the Company s financial performance and performance for our stockholders. The Compensation Committee believes that the Company s executive compensation programs should support the Company s objective of creating value for its stockholders.

Accordingly, the Compensation Committee believes that NEOs should have a significant interest in the Company s stock performance, and compensation programs should link executive compensation to stockholder value. One of the ways that the Company has sought to accomplish these goals is by making a significant portion of individual NEO compensation directly dependent on the Company s profitability. In addition, the Company makes annual grants of stock options, which focus the NEO on creating stockholder value while encouraging executives to build an equity interest in the Company. Finally, the Company generally pays NEOs compensation that will be above peer company executive compensation when Company performance is above its peer companies and below peer company executive compensation when the Company s financial performance is below that of its peer companies.

The Compensation Committee will continue to emphasize compensation arrangements that align the financial interests of Intevac s NEOs with the long-term interests of stockholders. Please refer to the section of this proxy statement entitled Executive Compensation for a detailed discussion of Intevac s executive compensation practices and philosophy.

We are asking our stockholders to indicate their support for our NEO compensation as described in this Proxy Statement. This vote is not intended to address any specific item of compensation, but rather the overall compensation of our NEOs and the philosophy, policies and practices described in this Proxy Statement. Accordingly, we ask our stockholders to vote FOR the following resolution at the 2011 Annual Meeting:

RESOLVED, that the Company s stockholders approve, on an advisory basis, the compensation of the named executive officers, as disclosed in the company s Proxy Statement for the 2011 Annual Meeting of Stockholders pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the Compensation Discussion and Analysis, the tabular disclosure regarding such compensation and the accompanying narrative disclosure.

The Board of Directors recommends a vote FOR the (non-binding) vote approving, on an advisory basis, the compensation of the Company s executives named in the 2010 Summary Compensation Table, as disclosed in the

Company s Proxy Statement pursuant to the executive compensation disclosure rules of the Securities and Exchange Commission, which disclosure includes the Compensation Discussion and Analysis, the compensation tables and other executive compensation disclosures.

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PROPOSAL SIX

FREQUENCY OF ADVISORY VOTE ON EXECUTIVE COMPENSATION

The Dodd-Frank Wall Street Reform and Consumer Protection Act requires us to provide an advisory stockholder vote to determine how often to present the advisory stockholder vote to approve the compensation of Intevac s NEOs (the say-on-pay vote). Intevac must solicit your advisory vote on whether to have the say-on-pay vote every 1, 2 or 3 years. Stockholders may vote as to whether the say-on-pay vote should occur every 1, 2 or 3 years, or may abstain from voting on the matter. The frequency (every 1, 2 or 3 years) that receives the highest number of votes will be deemed to be the choice of the stockholders.

The Board values the opinion of our stockholders and welcomes communication regarding Intevac s executive compensation policies and practices. After taking into account various considerations described below, the Board believes that a triennial vote will provide stockholders with the ability to express their views on Intevac s executive compensation policies and practices while providing the Board with an appropriate amount of time to consult with the stockholders, to consider their input, to follow consistent compensation programs and to allow such programs to be effective.

Intevac s executive compensation program is administered by the Compensation Committee, as described in this proxy statement. Compensation decisions are complex and, with respect to Intevac s NEOs, are disclosed in the proxy statement. The Board believes that establishing a three-year time frame for holding stockholder advisory votes on executive compensation will both enhance stockholder communication and provide the Company time to consider, engage with and respond to stockholders, in terms of expressed concerns or other feedback. In addition, the Board also believes that a triennial vote is consistent with our long-term business strategy.

You may cast your vote on your preferred voting frequency by choosing the option of 1, 2 or 3 years or abstain from voting when you vote in response to the resolution set forth below.

RESOLVED, that the option of once every 1, 2 or 3 years that receives the highest number of votes cast for this resolution will be determined to be the preferred frequency with which the Company is to hold an advisory stockholder vote to approve the compensation of the named executive officers, as disclosed pursuant to the Securities and Exchange Commission s compensation disclosure rules, including the Compensation Discussion and Analysis, the tabular disclosure regarding such compensation and the accompanying narrative disclosure.

The option of 3 years, 2 years or 1 year that receives the highest number of votes cast by stockholders will be the frequency for the advisory vote on the compensation of our NEOs that has been selected by stockholders. Although, as an advisory vote, this vote is not binding upon the Company or the Board, the Board will carefully consider the stockholder vote on this matter, along with all other expressions of stockholder views it receives on this matter.

While you have the opportunity to vote for every 1, 2 or 3 years, or abstain from voting on the frequency of say-on-pay votes the Board of Directors recommends a vote FOR a frequency of say-on-pay votes of every 3 years.

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CORPORATE GOVERNANCE MATTERS

Code of Business Conduct and Ethics

We have adopted a Code of Business Conduct and Ethics that applies to all of our employees, including our principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions. We have also adopted a Director Code of Ethics that applies to all of our directors. You can find both our Code of Business Conduct and Ethics and our Director Code of Ethics on our website at www.intevac.com. We post any amendments to the Code of Business Conduct and Ethics and the Director Code of Ethics, as well as any waivers, which are required to be disclosed by the rules of either the Securities and Exchange Commission (SEC) or The NASDAQ Global Select Market (Nasdaq) on our website.

Independence of the Board of Directors

The Board of Directors has determined that, with the exception of Mr. Pond and Mr. Fairbairn, all of its members are independent directors as that term is defined in the listing standards of Nasdaq.

Board Meetings and Committees

During 2010, the Board of Directors held a total of 7 meetings (including regularly scheduled and special meetings) and also took certain actions by written consent. All members of the Board of Directors during fiscal 2010 attended at least seventy-five percent of the aggregate of the total number of meetings of the Board of Directors held during the fiscal year and the total number of meetings held by all committees of the Board on which each such director served (based on the time that each member served on the Board of Directors and the committees). The Board of Directors has an Audit Committee, a Compensation Committee and a Nominating and Governance Committee.

Audit Committee

The Audit Committee, which has been established in accordance with Section 3(a)(58)(A) of the Exchange Act, currently consists of Mr. Dury, Mr. Rohrs and Dr. Yang, each of whom is independent as such term is defined for audit committee members by the Nasdaq listing standards. Mr. Dury is the chairman of the Audit Committee. The Board of Directors has determined that Mr. Dury and Mr. Rohrs are audit committee financial experts as defined under the rules of the SEC. The Audit Committee met 8 times during 2010.

The Audit Committee is responsible for:

- Overseeing our accounting and financial reporting processes and audits of our financial statements;
- Assisting the Board in overseeing and monitoring (i) the integrity of our financial statements, (ii) our compliance with legal and regulatory requirements related to financial affairs and reporting, (iii) our independent auditor s qualifications, independence and performance, and (iv) our internal accounting and financial controls;
- Preparing the report that the rules of the SEC require be included in this proxy statement;
- Periodically providing the Board with the results of its monitoring and recommendations derived therefrom; and

Providing to the Board additional information and materials as it deems necessary to make the Board aware of significant financial matters that require the attention of the Board.

The Audit Committee has adopted a written charter approved by the Board of Directors, which is available on Intevac s website at www.intevac.com under Company Governance.

The Audit Committee Report is included in this proxy statement on page 49.

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Compensation Committee

The Compensation Committee currently consists of Mr. Hill (chairman), Mr. Rohrs and Mr. Schaefer, each of whom is independent as such term is defined by the Nasdaq listing standards. The Compensation Committee met 9 times during 2010.

The Compensation Committee is responsible for:

- Overseeing the entirety of our compensation and benefit policies, plans and programs;
- Overseeing the annual report on executive compensation for inclusion in our proxy statement; and
- Overseeing executive succession planning.

See Executive Compensation Compensation Discussion and Analysis and Executive Compensation Compensation of Directors below for a description of Intevac s processes and procedures for the consideration and determination of executive and director compensation.

The Compensation Committee has adopted a written charter approved by the Board of Directors, a copy of which is available on Intevac s website at www.intevac.com under Company Governance.

The Compensation Committee Report is included in this proxy statement on page 39.

Nominating and Governance Committee

The Nominating and Governance Committee currently consists of Dr. Yang, Mr. Hill and Mr. Schaefer, each of whom is independent as such term is defined by the Nasdaq listing standards. The composition of the Nominating and Governance Committee underwent changes in 2010, with the appointment of a new Nominating and Governance Committee Chairman, Dr. Yang. The Nominating and Governance Committee met 2 times during 2010.

The primary focus of the Nominating and Governance Committee is on the broad range of issues surrounding the composition and operation of the Board of Directors. The Nominating and Governance Committee provides assistance to the Board, the Chairman and the CEO in the areas of membership selection, committee selection and rotation practices, evaluation of the overall effectiveness of the Board, and review and consideration of developments in corporate governance practices. The Nominating and Governance Committee s goal is to ensure that the composition, practices, and operation of the Board contribute to value creation and effective representation of Intevac stockholders.

The Nominating and Governance Committee will consider recommendations of candidates for the Board of Directors submitted by the stockholders of Intevac; for more information, see Policy Regarding Board Nominees below.

The Nominating and Governance Committee has adopted a written charter approved by the Board of Directors, a copy of which is available on Intevac s website at www.intevac.com under Company Governance.

Compensation Committee Interlocks and Insider Participation

Mr. Hill, Mr. Dury, Mr. Schaefer and Dr. Yang served as members of the Compensation Committee during fiscal 2010. No interlocking relationship exists between any member of Intevac s Board of Directors or Compensation Committee and any member of the board of directors or compensation committee of any other company, nor has any such interlocking relationship existed in the past. No member of the Compensation Committee is or was formerly an officer or an employee of Intevac.

Attendance at Annual Stockholder Meetings by the Board of Directors

Intevac encourages members of the Board of Directors to attend the annual meeting of stockholders, but does not have a policy requiring attendance. Mr. Fairbairn, Mr. Pond, Mr. Dury and Dr. Yang attended Intevac s 2010 annual meeting of stockholders.

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Lead Director

Mr. David Dury serves as Lead Director and liaison between management and the other non-employee directors. The Lead Director schedules and chairs meetings of the independent directors. The independent directors (including the Lead Director) hold a closed session at each regularly scheduled Board meeting.

Board Leadership Structurize:10pt;">
$
—

Certificates of deposit
14,920

—

14,920

—

Corporate notes and obligations
26,774

—

26,774

—

Municipal obligations
3,830

—

3,830

—

U.S. government and government agency obligations
60,018

11,428

48,590

—

$
121,973

$
27,859

$
94,114

$
—

Financial instruments include cash, cash equivalents and investments including investment-grade interest-bearing securities such as money market accounts, certificates of deposit, commercial paper, corporate bonds, municipal and government agency obligations and guaranteed obligations of the U.S. government. We classify our money market funds and U.S. government obligations as Level 1 instruments due to the use of observable market prices for identical securities that are traded in active markets.

When the Company uses observable market prices for identical securities that are traded in less active markets, the Company classifies its marketable financial instruments as Level 2. When observable market prices for identical securities are not available, the Company prices its marketable financial instruments using non-binding market consensus prices that are corroborated with observable market data; quoted market prices for similar instruments; or pricing models with all significant inputs derived from or corroborated with observable market data. Non-binding market consensus prices are based on the proprietary valuation models of pricing providers. These valuation models incorporate a number of inputs, including non-binding and binding broker quotes; observable market prices for identical or similar securities; and the internal assumptions of pricing providers or brokers that use observable market inputs and, to a lesser degree, unobservable market inputs. The Company corroborates non-binding market consensus prices with observable market data as such data exists.

As of March 31, 2014 and December 31, 2013, the Company did not have any assets or liabilities that were valued using Level 3 inputs. For the three months ended March 31, 2014 and 2013, there were no transfers of financial instruments among Level 1, Level 2 or Level 3 classifications.

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For the three months ended March 31, 2014 and 2013, the Company recognized interest income from financial instruments of $0.1 million and $0.2 million, respectively. Gross realized gains and gross realized losses from the sale of investments were not significant during the three months ended March 31, 2014 and 2013.

The carrying amounts, gross unrealized gains and losses and estimated fair value of cash and cash equivalents and both short and long-term investments consisted of the following:

	March 31, 2014			
	Amortized cost	Unrealized gains	Unrealized losses	Carrying or fair value
	(in thousands)			
Cash and cash equivalents:				
Cash	$11,248	$—	$—	$11,248
Money market funds	15,175	—	—	15,175
	$26,423	$—	$—	$26,423
Investments:				
Corporate notes and obligations	$29,184	$25	$(13)	$29,196
Certificates of deposit	15,000	11	(13)	14,998
Municipal obligations	3,108	7	—	3,115
U.S. government notes	20,662	6	(46)	20,622
U.S. government agency securities	38,934	18	(32)	38,920
	$106,888	$67	$(104)	$106,851

	December 31, 2013			
	Amortized cost	Unrealized gains	Unrealized losses	Carrying or fair value
	(in thousands)			
Cash and cash equivalents:				
Cash	$14,092	$—	$—	$14,092
Money market funds	16,431	—	—	16,431
U.S. government agency securities	2,939	—	—	2,939
	$33,462	$—	$—	$33,462
Investments:				
Corporate notes and obligations	$26,770	$17	$(13)	$26,774
Certificates of deposit	14,945	1	(26)	14,920
Municipal obligations	3,827	5	(2)	3,830
U.S. government notes	11,430	3	(5)	11,428
U.S. government agency securities	45,672	12	(26)	45,658
	$102,644	$38	$(72)	$102,610

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The following table shows the gross unrealized losses and the related fair values of our investments that have been in a continuous unrealized loss position:

	March 31, 2014					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized losses	Fair Value	Unrealized losses	Fair Value	Unrealized losses
	(in thousands)					
Corporate notes and obligations	$9,336	$(13)	$—	$—	$9,336	$(13)
Certificates of deposit	6,412	(13)	—	—	6,412	(13)
U.S. government notes	7,780	(46)	—	—	7,780	(46)
U.S. government agency securities	16,272	(32)	—	—	16,272	(32)
	$39,800	$(104)	$—	$—	$39,800	$(104)

	December 31, 2013					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized losses	Fair Value	Unrealized losses	Fair Value	Unrealized losses
	(in thousands)					
Corporate notes and obligations	$6,403	$(13)	$—	$—	$6,403	$(13)
Certificates of deposit	12,714	(26)	—	—	12,714	(26)
Municipal obligations	552	(2)	—	—	552	(2)
U.S. government notes	4,361	(5)	—	—	4,361	(5)
U.S. government agency securities	20,614	(26)	—	—	20,614	(26)
	$44,644	$(72)	$—	$—	$44,644	$(72)

The following table summarizes the maturities of the Company’s investments at March 31, 2014:

	Carrying or fair value (in thousands)
Remainder of 2014	$32,348
2015	39,990
2016	26,186
2017	8,327
Total	$106,851

Actual maturities may differ from the contractual maturities because borrowers may have the right to call or prepay certain obligations.

NOTE 5—Acquisition

On January 15, 2014, the Company acquired substantially all the assets of ARG Interactive, LLC (dba MortgageCEO), a software as a service ("SaaS") company specializing in customer relationship management and marketing solutions for the residential mortgage industry. The Company acquired the MortgageCEO business in order to add functionality to its product offerings. The transaction was accounted for as a business combination and, accordingly, the total purchase price was allocated to the assets acquired based on their respective fair values. The Company expensed all transactions costs, which were insignificant, in the period in which they were incurred.

The total purchase price was $5.0 million, of which $4.5 million was paid at the time of closing. The remaining $0.5 million (the "holdback funds") has been retained from the purchase price to cover closing capital settlement adjustments and any indemnity claims. Any unused portion of the holdback funds will be paid on July 15, 2015.

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The allocation of the consideration of $5.0 million to the identifiable tangible and intangible assets acquired and liabilities assumed under the purchase method of accounting, based on their estimated fair values as of the acquisition date, is summarized in the following table (in thousands):

Amortizable intangible assets:	
Developed technology	$2,927
Customer relationships	643
Trade name	41
Goodwill	1,409
Total purchase price	$5,020

Developed technology consists of the technology underlying MortgageCEO's existing products. The value of the developed technology was determined by discounting the estimated net future cash flows of these products. The Company is amortizing the developed technology on a straight-line basis over an estimated life of 5 years.
Customer relationships relate to the Company’s ability to sell existing and future versions of the Company’s products and services to existing MortgageCEO customers. The fair value of the customer relationships was determined by discounting the estimated net future cash flows from the customer contracts. The Company is amortizing customer relationships on a straight-line basis over an estimated life of 5 years.
Trade name represents the right to use the MortgageCEO name. The fair value of the trade name was determined by estimating a benefit from owning the asset rather than paying a royalty to a third party for the use of the asset. The Company is amortizing the asset on a straight-line basis over an estimated life of 2 years.
Goodwill represents the excess of the purchase price over the fair value of the identifiable assets acquired and is not deductible for tax purposes. Among the factors that contributed to a purchase price in excess of the fair value of the identifiable assets was the acquisition of an assembled workforce and synergies between the Company's products and MortgageCEO's products.
MortgageCEO’s results of operations since the closing date of January 15, 2014 have been included in the Company’s consolidated statements of income for the three months ended March 31, 2014. If the acquisition had occurred as of January 1, 2014, the revenue and earnings of the combined entity for the current reporting period would have been approximately the same. MortgageCEO's revenues and earnings for the three months ended March 31, 2014 and 2013 were not significant.

NOTE 6— Goodwill and Other Intangible Assets

The changes in the carrying value of goodwill during the three months ended March 31, 2014 were as follows (in thousands):

Balance at January 1, 2014	$51,051
Addition: MortgageCEO acquisition	1,409
Balance at March 31, 2014	$52,460

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Other intangible assets, net, consisted of the following:

	March 31, 2014			
	Gross carrying amount	Accumulated amortization	Net intangibles	Weighted Average Remaining Useful Life
	(in thousands)			(in years)
Developed technology	$4,801	$(1,704)	$3,097	4.5
Customer relationships	7,943	(2,932)	5,011	4.9
Trade names	301	(213)	88	1.2
	$13,045	$(4,849)	$8,196	4.7

	December 31, 2013			
	Gross carrying amount	Accumulated amortization	Net intangibles	Weighted Average Remaining Useful Life
	(in thousands)			(in years)
Developed technology	$1,874	$(1,500)	$374	1.2
Customer relationships	7,300	(2,653)	4,647	5.1
Trade names	260	(192)	68	1.0
	$9,434	$(4,345)	$5,089	4.8

Amortization expense associated with other intangible assets was $0.5 million for the three months ended March 31, 2014 and $0.4 million for the three months ended March 31, 2013. There was no impairment of intangible assets during the three months ended March 31, 2014 and 2013.

Minimum future amortization expense for other intangible assets at March 31, 2014 was as follows:

	Amortization
	(in thousands)
Remainder of fiscal 2014	$1,605
2015	1,767
2016	1,643
2017	1,642
2018	978
2019	295
Thereafter	266
	$8,196

NOTE 7—Income Taxes

We compute our interim provision for income taxes by applying the estimated annual effective tax rate to the year-to-date income from recurring operations and adjust the provision for discrete tax items recorded in the period. We evaluate and update our estimated annual effective income tax rate on a quarterly basis. The estimated effective tax rate for the three months ended March 31, 2014 and 2013 was 33.4% and 26.6%, respectively.

The difference between the federal statutory rate of 35% and our estimated effective tax rate for the three months ended March 31, 2014 was primarily due to our state income tax provision and non-deductible stock-based compensation expenses and limitations of tax deductions under Internal Revenue Code ("IRC") Section 162(m) for compensation paid to our executive officers, offset by the domestic production activities deduction under IRC Section 199 and disqualifying dispositions of stock-based awards.

Our tax positions are subject to income tax audits by multiple tax jurisdictions. We account for uncertain tax positions and believe that we have provided adequate reserves for our unrecognized tax benefits for all tax years still open for

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assessment. We also believe that we do not have any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within the next twelve months.

We have a policy to classify accrued interest and penalties associated with uncertain tax positions together with the related liability in the balance sheet, and to include the expenses incurred related to such accruals in the provision for income taxes. During the three months ended March 31, 2014, we included interest and penalties of $20 thousand in the provision for income taxes.

NOTE 8—Commitments and Contingencies

Leases

In January 2014, we entered into a lease agreement to finance the purchase of computer equipment with payments of $50,000 per month over the 36 month term of the agreement.

Legal Proceedings

On March 25, 2011, Industry Access Incorporated ("Industry Access") filed a patent infringement lawsuit against us and another defendant in the U.S. District Court for the Central District of California. The complaint alleges, among other things, that certain aspects of our Encompass loan management software system and related operations infringe a single patent, and seeks declaratory relief and unspecified damages from the defendants, including enhanced damages for willful infringement and reasonable attorneys' fees. On June 24, 2011, the Court issued an order requiring plaintiff to serve the complaint on all defendants within three days of the order. On June 28, 2011, plaintiff served us with the complaint and we filed its answer on August 5, 2011 denying all material allegations of the complaint. On November 18, 2011 the other defendant filed with the United States Patent and Trademark Office (the "PTO") a request for ex parte reexamination of Industry Access' US Patent No 7,769,681, which the PTO granted on February 14, 2012. On December 15, 2011, we filed a motion to stay the litigation pending the reexamination, which the Court granted on February 28, 2012. On October 9, 2012, the PTO issued the reexamination certificate. The Court granted a motion to dismiss the other defendant from this action on April 7, 2013 and lifted the stay on April 11, 2013. The parties are in the claims construction phase of the litigation with a claim construction hearing that was scheduled for December 2, 2013. Discovery is ongoing and the trial has been rescheduled for December 2014 as further discussed below.

On March 19, 2013, Industry Access filed a second patent infringement lawsuit against us in the U.S. District Court for the Central District of California. The complaint alleges, among other things, that our Encompass loan management software system, including the Encompass software, the Ellie Mae Network, Encompass Originator, Encompass Compliance Service, Encompass CenterWise, Encompass Electronic Document Management, Encompass Docs Solution and Encompass Product and Pricing Service, infringes U.S. Patent Nos. 8,117,120 and 8,145,563, which are continuations of U.S. Patent No. 7,769,681, asserted in the lawsuit described above. Plaintiff is seeking unspecified damages. On June 12, 2013, we filed a motion to dismiss or, in the alternative, to transfer this case to the Northern District of California, which the Court denied on September 18, 2013. Trial is set for December 2014.

On September 12, 2013, we filed a motion to relate and consolidate the two Industry Access lawsuits so that all of Industry Access' related patent infringement claims would be heard before the same judge on the same schedule. Industry Access responded to this motion on October 11, 2013. The Court granted our motion to consolidate on October 31, 2013. The Court has scheduled the claim construction hearing for June 2, 2014. Trial is set for December 2014.

We believe that we have substantial and meritorious defenses in the newly consolidated case and, if similar claims are pursued, we intend to defend these and similar claims vigorously.

We are also subject to various other legal proceedings and claims arising in the ordinary course of business. With respect to these matters and the litigations described above, we cannot predict the ultimate outcome of these legal proceedings and the amounts and ranges of potential damages associated with such proceedings cannot be estimated or assessed. An unfavorable outcome of these or the litigation could materially adversely affect our business, financial condition and results of operations.

NOTE 9—Stock Incentive Plans

We recognize stock-based compensation related to awards granted under our 2009 Stock Option and Incentive Plan (the "2009 Plan"), 2011 Equity Incentive Award Plan (the "2011 Plan") and ESPP.

Total stock-based compensation expense recognized consisted of:

	Three Months ended March 31,	
	2014	2013
	(in thousands)	
Cost of revenues	$238	$99
Sales and marketing	333	136
Research and development	736	685
General and administrative	2,003	2,453
	$3,310	$3,373

Capitalized stock-based compensation for the three months ended March 31, 2014 was $54,000. Capitalized stock-based compensation for the three months ended March 31, 2013 was $15,000.

2009 Stock Option and Incentive Plan and 2011 Equity Incentive Award Plan

Stock Options

The following table summarizes our stock option activity under the 2009 Plan and 2011 Plan:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2013	3,284,672	$11.17		
Granted	170,753	$25.87		
Exercised	(275,211)	$5.27		
Forfeited or expired	(9,153)	$17.45		
Outstanding at March 31, 2014	3,171,061	$12.46	7.30	$51,998
Ending vested and expected to vest at March 31, 2014	3,039,823	$12.12	7.24	$50,856
Exercisable at March 31, 2014	1,660,712	$7.99	6.20	$34,622

Stock options granted during the three months ended March 31, 2014 were made under the 2011 Plan. There were no grants under the 2009 Plan during the three months ended March 31, 2014.

Intrinsic value of an option is the difference between the fair value of our common stock at the time of exercise and the exercise price to be paid. The aggregate intrinsic value for options outstanding at March 31, 2014 in the table above represents the total intrinsic value, based on our closing stock price of $28.84 as of March 31, 2014, which would have been received by option holders had all option holders exercised their in-the-money options as of that date. Options outstanding that are expected to vest are net of estimated future option forfeitures.

Following is additional information pertaining to our stock option activity:

	Three Months ended March 31,	
	2014	2013
	(in thousands, except per option amounts)	
Weighted average fair value per option granted	$13.30	$10.49
Grant-date fair value of options vested	$1,467	$1,024
Intrinsic value of options exercised	$6,425	$3,359
Proceeds received from options exercised	$1,448	$427

As of March 31, 2014, total unrecognized stock-based compensation expense related to unvested stock options, adjusted for estimated forfeitures, was $13.5 million and is expected to be recognized over a weighted average period of 2.5 years.

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Restricted Stock Units and Performance Awards

In August 2012, the Company granted 147,000 Performance Awards ("2012 Performance Awards") to designated participants under the 2011 Plan. The 2012 Performance Awards represented the right to receive between zero and 4 shares of the Company's common stock upon achievement of certain performance goals during the performance period of July 1, 2012 through June 30, 2013. After the Company filed with the SEC its Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, the Compensation Committee determined the level of achievement of the performance goals (the "Determination Date"), at which time the designated participants earned an aggregate of 588,000 shares of common stock. Of the issued shares, 25% were vested upon issuance and the remaining shares will vest 25% on each of the first three anniversaries of the Determination Date, subject to the continuous employment of the participant through such dates. No forfeitures are expected.

In February 2013, the Company granted 113,000 Performance Awards ("2013 Performance Awards") to designated participants under the 2011 Plan. The 2013 Performance Awards represent the right to receive shares of the Company's common stock upon achievement of certain performance goals during the performance period of January 1, 2013 through December 31, 2013. In March 2014, after the Company filed with the SEC its Annual Report on Form 10-K for the year ended December 31, 2013, the Compensation Committee determined the level of achievement of the performance goals (the "2013 Award Determination Date"), at which time it was determined that the designated participants had earned an aggregate of 124,300 shares of common stock. The earned shares were issued in April 2014, with 25% of the shares vested upon issuance and the remaining shares to vest 25% on each of the first three anniversaries of the 2013 Award Determination Date, subject to the continuous employment of the participant through such dates. No forfeitures are expected.

In February 2014, the Company granted 62,500 Performance Awards ("2014 Performance Awards") to designated participants under the 2011 Plan. The 2014 Performance Awards represent the right to receive shares of the Company's common stock upon achievement of certain performance goals during the performance period of January 1, 2014 through December 31, 2014. After the Company files with the SEC its Annual Report on Form 10-K for the year ending December 31, 2014, the Compensation Committee will determine the level of achievement of the performance goals (the "2014 Award Determination Date"), at which time the designated participants may earn between zero and 2.5 shares of common stock for each 2014 Performance Award. Shares of common stock earned, if any, will be issued after the 2014 Award Determination Date with 25% of the shares to vest upon issuance and the remaining shares to vest 25% on each of the first three anniversaries of the 2014 Award Determination Date, subject to the continuous employment of the participant through such dates. As of March 31, 2014, we expect that each award will convert to 1.45 shares of common stock on the 2014 Award Determination Date. No forfeitures are expected.

The following table summarizes our RSU and Performance Award activity:

	RSUs		Performance Awards	
	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Outstanding at December 31, 2013	257,378	$23.10	565,300	$24.43
Granted	153,162	27.91	90,625	24.93
Released	(3,125)	8.90	—	—
Forfeited or expired	(2,205)	24.13	—	—
Outstanding at March 31, 2014	405,210	$23.47	655,925	$24.50
Ending vested and expected to vest at March 31, 2014	342,669		655,925	

RSUs and Performance Awards that are expected to vest are net of estimated future forfeitures. RSUs released during the three months ended March 31, 2014 and 2013 had an aggregate intrinsic value of $98 thousand and $62 thousand, respectively and had an aggregate grant-date fair value of $28 thousand and $28 thousand, respectively. There were no Performance Awards released during the three months ended March 31, 2014 and 2013. The number of RSUs released includes shares that we withheld on behalf of employees to satisfy the minimum statutory tax withholding requirements.

As of March 31, 2014, total unrecognized compensation expense related to unvested RSUs and Performance Awards was $18.1 million and is expected to be recognized over a weighted average period of 2.7 years.

Employee Stock Purchase Plan

For the three months ended March 31, 2014 and 2013, employees purchased 45,746 shares and 54,728 shares, respectively, under the ESPP for a total of $1.2 million and $0.9 million, respectively. As of March 31, 2014, unrecognized compensation expense related to the current ESPP period, which ends on August 29, 2014, was $0.4 million and is expected to be recognized over five months.

Valuation Information

The fair value of stock options and stock purchase rights granted under the 2009 Plan, the 2011 Plan and the ESPP were estimated at the date of grant using the Black-Scholes option valuation model with the following weighted average assumptions:

	Three Months ended March 31,			
	2014		2013	
Stock option plans:				
Risk-free interest rate	1.85-1.98	%	1.15	%
Expected life of options (in years)	6.08		6.08	
Expected dividend yield	—	%	—	%
Volatility	51-53	%	53	%
Employee Stock Purchase Plan:				
Risk-free interest rate	0.08	%	0.13	%
Expected life of options (in years)	0.50		0.50	
Expected dividend yield	—	%	—	%
Volatility	39	%	37	%

Common Stock

The following numbers of shares of common stock were reserved and available for future issuance at March 31, 2014:

	Reserved Shares
Options and awards outstanding under stock incentive plans	4,232,196
Shares available for future grant under the stock incentive plan	3,113,550
Shares available under the Employee Stock Purchase Plan	1,082,886
Total	8,428,632

In February 2014, 276,240 additional shares were reserved under the ESPP and 1,381,201 additional shares were reserved under the 2011 Plan, pursuant to the automatic increase provisions in each plan.

NOTE 10—Segment Information

We operate in one industry—mortgage-related software and services. Our chief operating decision makers are our chief executive officer and president and chief operating officer, who make decisions about resource allocation and review financial information presented on a consolidated basis. Accordingly, we have determined that we have a single reporting segment and operating unit structure, specifically technology-enabled solutions to help streamline and automate the residential mortgage origination process for our network participants.

We are organized primarily on the basis of service lines. Supplemental disclosure of revenues by type is as follows:

	Three Months ended March 31,	
	2014	2013
	(in thousands)	
On-demand revenues	$30,146	$27,951
On-premise revenues	2,032	2,904
	$32,178	$30,855

In the Notes to our condensed consolidated financial statements on our Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, we included all revenues from professional services in on-premise revenues in our disclosure related to revenues by type. For the quarter ended March 31, 2014, we included professional services revenues in either on-demand revenues or on-premise revenues as determined by the related service or software license revenue. We have retrospectively reclassified our disclosure of on-demand and on-premise revenues for the three months ended

March 31, 2013 in order to conform to the current presentation.

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

This Quarterly Report on Form 10-Q, including this Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These statements relate to future events or our future financial performance. Forward-looking statements may include words such as "may," "will," "should," "expect," "plan," "intend," "anticipate," "believe," "estimate," "predict," "potential," "continue" or other wording indicating future results or expectations. Forward-looking statements are subject to risks and uncertainties and actual events or results may differ materially. Factors that could cause our actual results to differ materially include, but are not limited to, those discussed under "Risk Factors" in this report. We also face risks and uncertainties relating to our business including: outages and other system interruptions in the Ellie Mae Network service, our hosted Encompass software and any related impact on our reputation; fluctuations in mortgage lending volume; the volume of mortgages originated by our Encompass users; the impact of changes in mortgage interest rates; changes in mortgage originator, lender, investor or service provider behavior and any related impact on the residential mortgage industry; our ability to accurately forecast revenues and appropriately plan our expenses; the number of Encompass users, including contracted SaaS Encompass users; the effectiveness of our marketing and sales efforts to attract new and retain existing SaaS Encompass users and Ellie Mae Network participants; transaction volume on the Ellie Mae Network; the level of demand for our Encompass Docs Solution and other services we offer; the level of adoption of our Total Quality Loan, or TQL, program; the timing of the introduction and acceptance of new Ellie Mae Network offerings and new on-demand services; our ability to protect the confidential information of our Encompass users, Ellie Mae Network participants and their respective customers; customer renewal and upgrade rates; the increased time, cost and complexity that may be required to successfully target larger customers; our ability to scale our operations and increase productivity to support our existing and growing customer base; our ability to successfully manage our growth and any future acquisitions of businesses, solutions or technologies; the timing of future acquisitions of businesses, solutions or technologies and new product launches; the impact of uncertain domestic and worldwide economic conditions, including the resulting effect on residential mortgage volumes; changes in government regulation affecting Ellie Mae Network participants or our business, and potential structural changes in the U.S. residential mortgage industry; the attraction and retention of qualified employees and key personnel; our ability to compete effectively in a highly competitive market and adapt to technological changes; our ability to enhance the features and functionality of our Encompass software and the Ellie Mae Network; our ability to protect our intellectual property, including our proprietary Encompass software; costs associated with defending intellectual property infringement and other claims; our ability to maintain effective internal controls and the risk of natural and man-made catastrophic interruptions to our business. We undertake no obligation to revise or update any forward-looking statements to reflect any event or circumstance that arises after the date of this report, or to conform such statements to actual results or changes in our expectations.

This discussion should be read in conjunction with the condensed consolidated financial statements and notes presented in this Quarterly Report on Form 10-Q and the consolidated financial statements and notes in our Annual Report on Form 10-K for the year ended December 31, 2013, or 2013 Form 10-K.

Overview

We are a leading provider of innovative on-demand software solutions and services for the residential mortgage industry in the United States. Our end-to-end Encompass mortgage management solution provides one system of record that allows banks, credit unions and mortgage lenders to originate and fund mortgages and improve compliance, loan quality and efficiency.

Mortgage originators use our Encompass software, a comprehensive operating system that handles key business and management functions involved in running a mortgage origination business. Mortgage originators use Encompass as a single tool for loan processing, marketing, customer communication and to interact electronically with lenders, investors and service providers over the Ellie Mae Network. Our software also enables enforcement of rules and business practices designed to ensure loan quality, adherence to processing standards and regulatory compliance.

We also offer Encompass users a variety of other on-demand software services, including: Encompass Docs Solution, which automatically prepares the disclosure and closing documents necessary to fund a mortgage; Encompass

CenterWise, a bundled offering of electronic document management, or EDM, and websites used for customer relationship management; TQL, which offers a suite of fraud detection, valuation, validation and risk analysis services using streamlined workflows and processing rules; Encompass Compliance Service, which automatically checks for compliance with federal, state and local regulations throughout the origination process; tax transcript services which provide income verification capability to our customers; Encompass Product and Pricing Service, which allows Encompass users to compare loans offered by different lenders and investors to determine appropriate mortgage programs available to a particular borrower, Encompass Flood Service, which allows Encompass users to order and transfer flood zone certifications and Encompass CRM, which offers a suite of sales and marketing tools that allows users to manage contacts, leads and marketing campaigns. By the nature of our on-demand service, even with our robust security monitoring and detection systems, we cannot guarantee that our security measures will prevent security breaches and we may

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need to expend significant resources to protect against and remedy any potential security breaches and their consequences.

The Ellie Mae Network electronically connects the approximately 95,000 mortgage professionals using Encompass to the broad array of mortgage lenders, investors and third-party service providers integral to the origination and funding of residential mortgages. During the mortgage origination process, mortgage originators may order various services through the Ellie Mae Network, including credit reports, product eligibility and pricing services, automated underwriting services, appraisals, title reports, insurance, flood certifications and flood insurance, compliance reviews, fraud detection, document preparation and verification of income, identity and employment. Mortgage originators can also initiate secure data transmission to and from lenders and investors.

We were formed as a California corporation in 1997 and reincorporated in Delaware in November 2009. From inception through 2000, we developed consumer-facing websites and initial versions of our network. We launched our first transaction platform in late 2000, the present version of which is the Ellie Mae Network.

Our revenues consist of on-demand and on-premise revenues. On-demand revenues are generated primarily from software subscriptions we host that customers access through the Internet, including customers who pay fees based on the number of loans they fund, or success basis, subject to monthly base fees, which we refer to as Success-Based Pricing, and related professional services such as consulting, implementation and training services. On-demand revenues also include software services that are sold transactionally and Ellie Mae Network transaction fees paid by lender-investors, service providers and certain government-sponsored entities participating on the Ellie Mae Network. On-premise revenues are generated from customer-hosted software licenses and related professional services and maintenance services.

Our on-demand revenues generally track the seasonality of the residential mortgage industry, typically, but not always, with increased activity in the second and third quarters and reduced activity in the first and fourth quarters as home buyers tend to purchase their homes during the spring and summer in order to move to a new home before the start of the school year. Mortgage volumes are also impacted by other factors such as interest rate fluctuations, home sale activity and general economic conditions, which can lead to departures from the typical seasonal pattern. For example, increases in mortgage interest rates could reduce the volume of new mortgages originated and, in particular, the volume of mortgage refinancings. We currently estimate that approximately 30% to 40% of our revenues have some sensitivity to volume.

We are investing aggressively in initiatives that we believe will help us continue to grow our business, improve our products and services and strengthen our competitive advantage while bringing sustainable, long-term value to our customers. During 2013 and the first quarter of 2014, we accelerated our investments in our sales and client services capabilities, in research and development and in technology infrastructure to support our user additions and overall business growth. These investments included expanding our talent across the organization by hiring additional personnel, especially for our customer acquisition, client services and implementation teams and our research and development teams; developing next-generation products and enhancements; purchasing computer equipment; upgrading our telephony systems and building out new office facilities.

On March 31, 2014, we experienced an outage of our Encompass services, which prevented our customers from being able to complete loan transactions until the system was restored on April 1, 2014. In responding to this outage, we engaged forensics experts and other consultants, and we expect to incur significant forensics and consulting fees in the second quarter of 2014. In addition, we have decided to accelerate our investments to bolster our infrastructure and enhance our system capacity, reliability and security, which costs we expect will be incurred throughout the remainder of 2014.

In addition to our internal initiatives, our business strategy has evolved to address recent industry trends, including:

- expected lower lending volume;
- increased quality standards imposed by regulators, lenders and investors;
- increased regulation affecting lenders and investors;
- greater focus by our customers on operational efficiencies; and
- customers adopting multi-channel strategies

We are responding to these trends as follows:

Expected lower lending volume. Mortgage lending volume is expected to be lower in 2014 than in 2013, as forecasted by Fannie Mae, Freddie Mac and the Mortgage Bankers Association. Since late 2009, we have focused our marketing and sales efforts on our on-demand SaaS Encompass offering, and particularly our SaaS Encompass Success-Based Pricing model, in contrast to our on-premise license model. In our on-demand SaaS Encompass offering, the customer does not pay the significant up-front licensing fee associated with our license model, which we believe is particularly attractive in the present climate of the residential mortgage origination market. Our SaaS Encompass Success-Based Pricing model builds on this value proposition by aligning customers' payments for our software solutions with their own receipts of revenues. Our focus on our SaaS Encompass offering is important in light of lower lending volumes because we typically generate greater revenues per user through our on-demand SaaS Encompass offering than through our on-premise license offering.

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We are also focusing on increasing use of our Ellie Mae Network offerings and our other services, which were introduced from late 2009 through late 2011. These offerings include our TQL program, Encompass Compliance Service, Encompass Product and Pricing Service, Encompass Docs Solution, Encompass 4506-T Service and Encompass CRM. During the three months ended March 31, 2014 and 2013, Encompass users employed the Ellie Mae Network to process on average approximately five transactions per loan file. By continuing to enhance our service offerings and encouraging providers of settlement services to deliver their services electronically through the Ellie Mae Network, we will continue to build value for our customers while increasing the number of transactions for which the Ellie Mae Network is used.

Increased quality standards imposed by regulators, lenders and investors. Encompass is designed to automate and streamline the process of originating mortgages to, among other things, satisfy increased quality requirements of investors. Relevant features of Encompass include enabling customers' management to impose processing rules and formats, and providing milestone and process reminders, automated population of forms with accurate data, and accurate and automated transmission of loan files and data from originators to investors and lenders. Our TQL program is designed to further enhance the quality, compliance and saleability of loans that are originated through Encompass. Additionally, TQL is intended to reduce the opportunities for errors in the process of transferring information from originator to investor and give investors confidence in the accuracy and regulatory compliance of the information that is underlying loan files.

In response to the increased quality standards and compliance mandates affecting the industry, we expect an increased number of mortgage lenders to assess new platform options and replace their legacy systems. We have increased the size of our customer acquisition, implementation and support teams by approximately 55% from 154 employees on December 31, 2012 to 239 employees on March 31, 2014 in order to address anticipated demand for our software solutions.

Increased regulation affecting lenders and investors. Regulatory reforms have significantly increased the complexity and importance of regulatory compliance. We devote considerable resources to continually upgrading software to help customers address regulatory changes. We offer Encompass Compliance Service, which automatically checks loan files for compliance with the myriad of federal, state and local regulations and alerts users to possible violations of these regulations. In addition, we have a staff of attorneys and work with compliance experts who help assure that documents prepared using our software and the processes recommended by the Encompass workflow comply with applicable rules and regulations. We believe we are well-positioned to help our customers meet additional requirements from the Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank Act, that became effective in January 2014. Our Ability-to-Repay, or ATR, / Qualified Mortgage, or QM, functionality is designed to allow our customers to document their compliance with the Consumer Financial Protection Bureau, or CFPB's ATR/QM Final Rule that applies to the majority of residential mortgage loan originations in the United States. We believe we are also well-positioned to help our customers meet future Dodd-Frank Act requirements as they are published and become effective.

Greater focus on operational efficiencies. Mortgage originators experienced an approximately 39% increase in total production costs per loan between 2009 and 2012[1], and an approximately 24% increase in total production costs per loan from the fourth quarter of 2012 to the fourth quarter of 2013.[2, 3] We expect this trend to continue due to continued increased regulation and heightened quality standards. By automating many of the functions of mortgage origination, we enable our users to comply with regulations and process quality loans more efficiently and effectively. This reduces the cost of originating a loan and lowers the risk of buy back demands from investors resulting from poorly originated or documented loans and/or loans that fail to comply with applicable regulations.

With an eye towards providing customers with ever-greater tools to enhance efficiency, we will continue to develop new service offerings through the Ellie Mae Network and pursue adoption of our services through initiatives such as our TQL program. By integrating and expanding our current and new services, we will provide a more comprehensive benefit to our users.

In addition to providing efficiency-enhancing solutions, delivery of our Encompass software in an on-demand SaaS environment provides customers with the added benefits of lower up front implementation costs and reduced need for an infrastructure of servers, storage and network devices as well as providing access to the most current release of an application, periodic upgrades and regulatory updates.

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1 Mortgage Bankers Association, Annual Mortgage Bankers Performance Report 2012 Data, Net Loan Production Income and Expense, $ per loan, Copyright June 2013.

2 Mortgage Bankers Association, Independent Mortgage Banker Profits Reach New Lows in the Fourth Quarter of 2013, March 26, 2014

3 Mortgage Bankers Association, MBA: Despite Higher Volumes, Independent Mortgage Banker Per-Loan Profits Decrease in the Fourth Quarter as the Cost to Originate Rises, April 22, 2013

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Customers adopting multi-channel strategies. Customers are developing multi-channel strategies beyond a single retail, correspondent or wholesale channel in order to grow their businesses. The requirements of these different channels vary and in order to maintain a single operating system, customers must use a robust system with customizable functionality. We continually address the changing needs of our customers by developing and enhancing tools to allow for simplified regulatory compliance, increased availability of information, and enhanced system functionality and performance.

Acquisition Strategy

Our industry is highly fragmented, and we believe there are strategic opportunities available to acquire competing software companies or software providers that offer related mortgage origination functionality that will complement and increase the attractiveness of Encompass. For example, in January 2014, we acquired substantially all the assets of ARG Interactive, LLC (dba MortgageCEO), or MortgageCEO, a SaaS company specializing in customer relationship management and marketing solutions for the residential mortgage industry. We intend to continue pursuing additional strategic acquisitions.

Operating Metrics

We use certain operational metrics to evaluate our business, determine allocation of our resources and make decisions regarding corporate strategy. We focus on these metrics to determine our success in leveraging our user base to increase our revenues and to gauge the degree of our market penetration.

These metrics are defined below.

Contracted revenues. Contracted revenues are those revenues that are fixed by the terms of a contract and are not affected by fluctuations in mortgage origination volume. These revenues consist of the base fee portion of success-based SaaS Encompass revenues, monthly per-user subscription SaaS Encompass revenues, professional services revenues, on-premise revenues, and subscription revenues paid for products other than Encompass.

SaaS Encompass revenues. SaaS Encompass revenues are those revenues earned from the customer’s usage of the SaaS version of Encompass. These revenues consist of success-based SaaS Encompass revenues and subscription-based SaaS Encompass revenues.

Active Encompass users. An active Encompass user is a mortgage origination professional who has used Encompass at least once within a 90-day period preceding the measurement date. An Encompass user is a mortgage origination professional working at an Encompass mortgage lender, such as a mortgage bank, commercial bank, thrift or credit union, which sources and funds loans and generally sells these funded loans to investors; or a mortgage brokerage, which typically processes and submits loan files to a mortgage lender or mega lender that funds the loan.

Contracted SaaS users. A contracted SaaS user is a mortgage origination professional who has a license to use SaaS Encompass and has an obligation to pay for this license, but who is not necessarily an active user.

Active SaaS Encompass users. An active SaaS Encompass user is a mortgage origination professional who has used the SaaS Encompass system at least once within a 90-day period preceding the measurement date.

Average active Encompass users. Average active Encompass users during a period is calculated by averaging the monthly active Encompass users during a period.

Average active SaaS Encompass users. Average active SaaS Encompass users during a period is calculated by averaging the monthly active SaaS Encompass users during a period.

Revenue per average active Encompass user. Revenue per average active Encompass user is calculated by dividing total revenues by average active Encompass users during the period.

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The following table shows these operating metrics as of and for the three months ended March 31, 2014 and 2013:

	Three Months ended March 31,			
	2014		2013	
Revenues (in thousands):				
Total revenues	$32,178		$30,855	
Total contracted revenues	$22,541		$15,836	
Total SaaS Encompass revenues	$19,129		$16,482	
Users at end of period:				
Contracted SaaS users	99,089		68,882	
Active Encompass users	94,971		80,710	
Active SaaS Encompass users	67,416		48,121	
Active SaaS Encompass users as a percentage of active Encompass users	71	%	60	%
Active SaaS Encompass users as a percentage of contracted SaaS users	68	%	70	%
Average users during period:				
Active Encompass users	93,702		78,242	
Active SaaS Encompass users	66,160		45,868	
Active SaaS Encompass users as a percentage of active Encompass users	71	%	59	%
Revenue per average user during period:				
Revenue per average active Encompass user	$343		$394	

Basis of Presentation

General

Our consolidated financial statements include the accounts of Ellie Mae, Inc. and our wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated upon consolidation.

Revenue Recognition

We generate revenue primarily from transaction-based fees and fees for software and related services. Our software can be accessed either through a company-hosted subscription or a customer-hosted license. Accordingly, our revenues are described as on-demand and on-premise revenues. Sales taxes assessed by governmental authorities are excluded from revenue.

In the Notes to our condensed consolidated financial statements on our Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, we included all revenues from professional services in on-premise revenues in our disclosure related to revenues by type. For the quarter ended March 31, 2014, we included professional services revenues in either on-demand revenues or on-premise revenues as determined by the related service or software license revenue. We have retrospectively reclassified our disclosure of on-demand and on-premise revenues for the three months ended March 31, 2013 in order to conform to the current presentation.

On-demand Revenues

On-demand revenues are revenues generated from company-hosted software subscriptions that customers access through the Internet, revenues from a small number of customers that have opted to self-host a portion of the software but pay fees based on a per closed loan, or success, basis subject to monthly base fees, which we refer to as Success-Based Pricing, and related professional services which include consulting, implementation and training services. On-demand revenues are also comprised of software services sold transactionally and Ellie Mae Network transaction fees.

On-premise Revenues

On-premise revenues are revenues generated from maintenance services, sales of customer-hosted software licenses (except for customer-hosted Success-Based Pricing revenues, which are included in on-demand revenues described above), and related professional services which include consulting, implementation and training services.

Cost of Revenues and Operating Expenses
Cost of Revenues
Our cost of revenues consists primarily of: salaries and benefits, including stock-based compensation expense, expenses for document preparation, income verification and compliance services, customer support, data centers, depreciation on computer equipment used in supporting the Ellie Mae Network, SaaS Encompass and Encompass CenterWise offerings, amortization of acquired intangible assets such as developed technology and trade names, professional services associated with implementation of our software, and allocated facilities costs. We expect that our cost of revenues will continue to increase in absolute dollars as our revenues increase, as we make additional and accelerated investments to bolster our infrastructure and enhance our system capacity, reliability and security, as we pursue additional strategic acquisitions and as we continue to hire additional personnel in our implementation and customer support departments to support new customers. Additionally, we expect cost of revenues to increase as a result of forensic and consulting fees incurred in the second quarter of 2014 in response to the service outage.
Sales and Marketing
Our sales and marketing expenses consist primarily of: salaries, benefits and incentive compensation, including stock-based compensation expense and commissions; allocated facilities costs; expenses for trade shows, public relations and other promotional and marketing activities; expenses for travel and entertainment; and amortization of acquired intangible assets such as customer relationships. We expect that our sales and marketing expense will continue to increase as we continue to hire additional sales personnel in order to address anticipated demand for our software solutions as we expect an increased number of mortgage lenders to assess new platform options and replace their legacy systems. We also intend to increase marketing activities focused on SaaS Encompass, our Ellie Mae Network offerings and our other Encompass services. We will continue to see increased amortization of intangible assets as we pursue additional strategic acquisitions.
Research and Development
Our research and development expenses consist primarily of: salaries and benefits, including bonuses and stock-based compensation expense; fees to contractors engaged in the development and support of the Ellie Mae Network, Encompass software and other products; and allocated facilities costs. We expect that our research and development expenses will continue to increase in absolute dollars as we continue to invest in our products and services and related next-generation enhancements, including hiring additional engineering and product development personnel.
General and Administrative
Our general and administrative expenses consist primarily of: salaries and benefits, including bonuses and stock-based compensation expense for employees involved in finance, accounting, human resources, administrative and legal roles, consulting, legal, accounting and other professional services by third-party providers, and allocated facilities costs. We expect general and administrative expenses to continue to increase in absolute dollars primarily due to greater amounts of stock compensation expense relating to awards granted to attract and retain the employees needed to continue to grow our business.
Other Income, Net
Other income, net consists of interest income earned on investments, cash accounts and notes receivable, offset by investment discount amortization and imputed interest expense related to our acquisition holdback payments and interest expense paid on equipment and software leases.
Income Taxes
On a quarterly basis, we evaluate our expected income tax expense or benefit based on our year-to-date operations, and we record an adjustment in the current quarter. The net tax provision is the result of the mix of profits earned by us and our subsidiaries in tax jurisdictions with a broad range of income tax rates. We are required to estimate deferred tax assets and liabilities based on the differences between the financial reporting and tax bases of assets and liabilities measured using the enacted tax rates that will be in effect when the differences are expected to reverse. In general, deferred tax assets represent future tax benefits to be received when certain expenses previously recognized in our consolidated statements of operations become deductible expenses under applicable income tax laws or loss or credit carry forwards are utilized. Accordingly, realization of our deferred tax assets is dependent on future taxable income against which these deductions, losses and credits can be utilized. We use management judgment to assess the

likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not more likely than not, we must establish a valuation allowance to reduce the deferred tax assets to the amount that is more likely than not to be realized.

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Critical Accounting Policies and Estimates

There have been no material changes during the three months ended March 31, 2014 to our critical accounting policies and estimates previously disclosed in our 2013 Form 10-K.

Results of Operations

The following tables set forth our results of operations for the periods presented and as a percentage of our revenues for those periods. The period-to-period comparison of financial results is not necessarily indicative of future results.

	Three Months ended March 31,	
	2014	2013
	(in thousands)	
Revenues	$32,178	$30,855
Cost of revenues (1)	9,200	7,611
Gross profit	22,978	23,244
Operating expenses:		
Sales and marketing (1)	6,095	4,903
Research and development (1)	6,815	5,548
General and administrative (1)	8,993	7,586
Total operating expenses	21,903	18,037
Income from operations	1,075	5,207
Other income, net	100	121
Income before income taxes	1,175	5,328
Income tax provision	393	1,415
Net income	$782	$3,913

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(1) Stock-based compensation included in the above line items:

	Three Months ended March 31,	
	2014	2013
	(in thousands)	
Cost of revenues	$238	$99
Sales and marketing	333	136
Research and development	736	685
General and administrative	2,003	2,453
	$3,310	$3,373

	Three Months ended March 31,			
	2014		2013	
Revenues	100.0	%	100.0	%
Cost of revenues	28.6		24.7	
Gross margin	71.4		75.3	
Operating expenses:				
Sales and marketing	18.9		15.9	
Research and development	21.2		18.0	
General and administrative	27.9		24.6	
Total operating expenses	68.0		58.5	
Income from operations	3.4		16.8	
Other income, net	0.3		0.4	
Income before income taxes	3.7		17.2	

Income tax provision	1.2		4.6	
Net income	2.5	%	12.6	%

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Comparison of the Three Months Ended March 31, 2014 and 2013

Revenues

The following table sets forth our revenues by type for the periods presented:

	Three Months ended March 31,	
	2014	2013
	(dollars in thousands)	
Revenue by type:		
On-demand	$30,146	$27,951
On-premise	2,032	2,904
Total	$32,178	$30,855

	Three Months ended March 31,			
	2014		2013	
Revenue by type:				
On-demand	93.7	%	90.6	%
On-premise	6.3	%	9.4	%
Total	100.0	%	100.0	%

Total revenues increased $1.3 million, or 4.3%, for the three months ended March 31, 2014 as compared to the same period of 2013.

On-demand revenues increased by $2.2 million, consisting primarily of a $2.6 million increase in SaaS Encompass revenues, of which $2.2 million related to our Success-Based Pricing model. SaaS Encompass revenues increased as a result of the addition of new SaaS Encompass users and as a result of upgrades of existing customers to our SaaS platform. The number of average active SaaS Encompass users increased by 44.2% from 45,868 for the three months ended March 31, 2013 to 66,160 for the three months ended March 31, 2014.

The revenue increase from additional users was offset by a reduction in revenue generated from closed loan volume, which was driven by customers delaying the implementation of Encompass as they focused on preparing for ATR/QM rules, as well as an overall estimated 50% decline in mortgage origination volume for the three months ended March 31, 2014 compared to the same period of 2013.

Also contributing to the increase in on-demand revenues was a $0.8 million increase in revenues from professional services, primarily driven by training and implementation services provided to new customers and customers that converted from on-demand users to SaaS Encompass Success-Based Pricing users. Partially offsetting the increase in on-demand revenues was a $1.3 million decrease in revenues from our standalone Encompass Docs Solution for the three months ended March 31, 2014 compared to the same period of 2013, primarily as a result of the conversion of customers from standalone solutions to SaaS Encompass and partially from two standalone solutions subscription customers having gone out of business during the third quarter of 2013.

On-premise revenues decreased by $0.9 million for the three months ended March 31, 2014 compared to the same period of 2013, primarily due to a $0.8 million decrease in software license and maintenance fees and a $0.1 million decrease in revenues from professional services as our on-premise customers converted to SaaS Encompass Success-Based Pricing users.

Revenue per average active Encompass user decreased from $394 for the three months ended March 31, 2013 to $343 for three months ended March 31, 2014, caused primarily by a decline in closed loan volume and longer implementation cycles for some of the larger customers that were added in 2013. Contracted revenues, which are not sensitive to volume, increased from $15.8 million for the three months ended March 31, 2013 to $22.5 million for the three months ended March 31, 2014, driven by an increase in monthly base fees due to an increase in contracted SaaS users.

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Gross Profit

	Three Months ended March 31,	
	2014	2013
	(dollars in thousands)	
Gross profit	$22,978	$23,244
Gross margin	71.4 %	75.3 %

Gross profit decreased by $0.3 million and gross margin percentage decreased by 3.9 percentage points during the three months ended March 31, 2014 as compared to the same period of 2013 as revenues increased by $1.3 million and cost of revenues increased by $1.6 million. The increase in cost of revenues was due to a $1.6 million increase in fixed salary and employee benefit costs associated with headcount added to our professional services and customer support organizations in anticipation of continued increasing demand for our software solutions.

Sales and Marketing

	Three Months ended March 31,	
	2014	2013
	(dollars in thousands)	
Sales and marketing	$6,095	$4,903
Sales and marketing as % of revenues	18.9 %	15.9 %

Sales and marketing expenses increased by $1.2 million, or 24.3%, for the three months ended March 31, 2014 as compared to the same period of 2013. This increase was primarily due to a $1.1 million increase in salaries and employee benefits related to increased headcount as we continued to grow our sales and marketing departments in an effort to increase our market share and address anticipated demand for our software solutions.

Research and Development

	Three Months ended March 31,	
	2014	2013
	(dollars in thousands)	
Research and development	$6,815	$5,548
Research and development as % of revenues	21.2 %	18.0 %

Research and development expenses increased by $1.3 million, or 22.8%, in the three months ended March 31, 2014 compared to the same period of 2013. The increase was primarily due to a $1.2 million increase in salaries and employee benefits related to increased headcount as we continue to invest in our products and services.

General and Administrative

	Three Months ended March 31,	
	2014	2013
	(dollars in thousands)	
General and administrative	$8,993	$7,586
General and administrative as % of revenues	27.9 %	24.6 %

General and administrative expenses increased by $1.4 million, or 18.5%, in the three months ended March 31, 2014 as compared to the same period of 2013. This increase was primarily due to a $1.0 million increase in salaries and employee benefits related to increased headcount and a $0.3 million increase in technology expenses relating to licenses and support for software used to manage our business, offset by a $0.5 million decrease in stock-based compensation expense primarily resulting from a decrease in expense relating to Performance Awards for which expense is recognized on an accelerated basis.

Other Income, Net

Other income, net includes imputed interest expense related to our acquisition holdback and capital lease obligations and interest income from notes receivable and investments. The amounts were not significant in the three months ended March 31, 2014 and 2013.

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Income Taxes

Income tax provision was $0.4 million for the three months ended March 31, 2014, compared to $1.4 million for the three months ended March 31, 2013. The decrease in income tax provision was primarily due to the decrease of pretax income from $5.3 million for the three months ended March 31, 2013 to $1.2 million for the three months ended March 31, 2014.

Liquidity and Capital Resources

As of March 31, 2014, we had cash, cash equivalents and short-term investments of $75.3 million and long-term investments of $58.0 million. Cash and cash equivalents consist of cash and money market accounts. Both short and long-term investments consist of corporate bonds and obligations, certificates of deposit, municipal obligations, U.S. government notes and U.S. government agency securities.

We believe that our existing cash, cash equivalents and short-term investments will be sufficient to fund capital expenditures, operating expenses and other cash requirements for at least the next 12 months. We may enter into acquisitions in the future, which could require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

The following table sets forth our statement of cash flows data for the periods presented:

	Three Months ended March 31,		Net
	2014	2013	Change
	(in thousands)		
Net cash provided by operating activities	$2,123	$9,220	$(7,097)
Net cash used in investing activities	(11,644)	(29,036)	17,392
Net cash provided by financing activities	2,482	1,618	864
Net decrease in cash and cash equivalents	$(7,039)	$(18,198)	$11,159

Operating Activities

Cash provided by operating activities decreased by $7.1 million from $9.2 million in 2013 to $2.1 million in 2014. In the consolidated statements of cash flows, cash provided by operating activities is presented as net income adjusted for non-cash expense items and changes in operating assets and liabilities. Net income decreased by $3.1 million for the three months ended March 31, 2014 as compared to the same period of 2013. The net contribution of non-cash expense items to cash provided by operating activities increased by $0.4 million for the three months ended March 31, 2014 as compared to the same period of 2013. The net contribution of changes in operating assets and liabilities to cash provided by operating activities decreased by $4.4 million for the three months ended March 31, 2013 as compared to the same period of 2013.

The increase in the net contribution of non-cash expense items was primarily due to a $0.3 million charge from deferred taxes in 2012 that we did not incur during 2013.

Changes in operating assets and liabilities resulted in a net decrease of $4.4 million to cash provided by operating activities in the three months ended March 31, 2014 as compared to the same period in 2013. Our net accounts receivable balance fluctuates from period to period, depending on the timing of sales and billing activity, cash collections and changes to our allowance for doubtful accounts. The change in prepaid expenses and other current assets was primarily due to the timing of the payment for computer software licenses. The change in deposits and other assets was due to deferred commission expenses and timing of the payment for software licenses. The change in accounts payable and accrued and other liabilities was due to the timing of additional liabilities and payments in general, and does not reflect any significant change in the nature of accrued liabilities. The change in deferred revenue is the result of timing differences in the recognition of revenues from professional services, which are deferred until the projects are completed.

Investing Activities

Our primary investing activities have consisted of purchases and maturities of investments, purchases of property and equipment specifically related to the build out of our data centers, as well as payments for acquisitions. Purchases of property and equipment may vary from period to period due to the timing of the expansion of our operations and certain software development projects subject to capitalization. We plan to continue to invest in technology hardware and software to support our growth and corporate infrastructure. Additionally, consistent with our acquisition strategy, we intend to continue pursuing additional strategic acquisitions.

Cash used in investing activities of $11.6 million for the three months ended March 31, 2014 was primarily the result of $4.6 million in net purchases of investments, $2.5 million for purchases of property and equipment mainly for our data centers and $4.5 million cash paid for the acquisition of MortgageCEO.

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Cash used in investing activities of $29.0 million for the three months ended March 31, 2013 was the result of $27.7 million in net purchases of short-term investments and $1.3 million for purchases of property and equipment mainly for our data centers.

Financing Activities

Financing activities have consisted primarily of cash provided from the exercise of stock options, excess tax benefits from employee exercises of stock options and payments related to capital lease obligations.

Cash provided by financing activities of $2.5 million for the three months ended March 31, 2014 consisted primarily of $2.6 million in proceeds from the exercise of stock options and $0.4 million in excess tax benefits from employee exercises of stock options, offset by payments on capital leases of $0.5 million.

Cash provided by financing activities of $1.6 million for the three months ended March 31, 2013 consisted primarily of $1.4 million in proceeds from the exercise of stock options, and $0.2 million in excess tax benefits from employee exercises of stock options.

Off Balance Sheet Arrangements

As of March 31, 2014, we had no off-balance sheet arrangements and operating leases were the only financing arrangements not reported on our consolidated financial statements.

ITEM 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We believe that there have been no significant changes in our market risk exposures for the three months ended March 31, 2014, as compared with those discussed in our 2013 Form 10-K.

ITEM 4—CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2014. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of March 31, 2014, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II—OTHER INFORMATION

ITEM 1—LEGAL PROCEEDINGS

For a description of the material legal proceedings, please see Note 8 of the Notes to Condensed Consolidated Financial Statements.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below and the other information in this report. If any of the following risks materialize, our business could be materially harmed, and our financial condition and results of operations could be materially and adversely affected. The risks described below are not the only ones facing us. Additional risks not currently known to us or that we currently believe are immaterial may also impair our business, results of operations, financial condition and liquidity.

We experienced a system outage in March 2014 that prevented our customers from being able to complete loan transactions during the outage period. This system interruption and future system interruptions that impair access to the Ellie Mae Network or SaaS Encompass could damage our reputation and brand and may substantially harm our business.

The satisfactory performance, reliability and availability of SaaS Encompass, the Ellie Mae Network, our website, our services, including our Encompass Compliance Service, and our network infrastructure are critical to our reputation and our ability to attract and retain Ellie Mae Network participants and Encompass users. Because our service is complex and incorporates a variety of hardware and proprietary and third-party software, our service may have errors or defects that could result in unanticipated downtime for our subscribers. Internet-based services frequently contain undetected errors when first introduced or when new versions or enhancements are released, and we have from time to time found defects in our service and new errors in our service may be detected in the future. In addition, our customers may use our service in unanticipated ways that may cause a disruption in service for other customers attempting to access their data.

Moreover, we have experienced and may in the future continue to experience temporary system interruptions, either to the Ellie Mae Network or to SaaS Encompass hosting locations, for a variety of reasons, including network failures, power failures, software errors, problems with Encompass and other third-party firmware updates, as well as an overwhelming number of Ellie Mae Network participants and Encompass users trying to access our network during periods of strong demand. For example, on March 31, 2014, we experienced an outage of our Encompass services which prevented our customers from being able to complete loan transactions until the system was restored on April 1, 2014. Since our customers use our service for important aspects of their business, any errors, defects, disruptions in service or other performance problems could result in negative publicity, damage our reputation and brand, reduce our revenue, increase our operating expenses, negatively impact our ability to run our business, hinder our ability to enroll new customers and cause us to lose current customers, all of which could substantially harm our business and operating results.

In addition, our two primary data centers, located in Santa Clara, California and Chicago, Illinois, are hosted by a third-party service provider over which we have little control. We depend on this third-party service provider to provide continuous and uninterrupted access to the Ellie Mae Network and SaaS Encompass. If for any reason our relationship with this third party were to end, it would require a significant amount of time to transition the hosting of our data centers to a new third-party service provider. Since we are dependent on third parties for the implementation and maintenance of certain aspects of our systems and because some of the causes of system interruptions may be outside of our control, we may not be able to remedy such interruptions in a timely manner, if at all.

Our future performance will be highly dependent on our ability to continue to attract SaaS Encompass customers and to grow revenues from new on-demand services.

To maintain or increase our revenues, we must increase the number of users of our software and percentage of our software users who choose our on-demand SaaS Encompass offering, from which we generate greater revenues than from our on-premise license offering. We cannot guarantee our Success-Based Pricing strategy will continue to be successful. If it is not successful, or if we are unable to identify an alternate strategy and successfully increase the number of SaaS Encompass customers, our business may be materially adversely affected.

Our success will also depend, to a large extent, on the willingness of mortgage lenders to continue to accept the SaaS model for delivering software applications that they view as critical to the success of their business. Our success will substantially depend on our ability to convince enterprises using on-premise enterprise software solutions to invest significant personnel and financial resources to migrate to our SaaS offering. It is difficult to predict customer adoption rates and demand for our services, the future growth rate and size of the SaaS market or the entry of competitive applications. The growth of the SaaS market depends on a number of factors, including the cost, performance and perceived value associated with SaaS offerings, as well as the ability of

SaaS companies to address security and privacy concerns. If other SaaS providers experience security incidents, loss of customer data, disruptions in delivery or other problems, the market for SaaS applications as a whole, including our own products and services, may be negatively affected. If there is a reduction in demand for SaaS caused by technological challenges, weakening economic conditions, security or privacy concerns, competing technologies and products, decreases in corporate spending or otherwise, it could result in decreased revenues and our business could be adversely affected.

In order to grow our business, we must expand the use of settlement services on, and increase the number of transactions effected through, the Ellie Mae Network.

To grow our base of Ellie Mae Network participants, we and settlement service providers must continue to enhance the features and functionality of offerings to them. In addition, increasing the number of settlement service transactions effected through the Ellie Mae Network will depend, in part, on settlement service providers enhancing their technical capabilities, which is largely beyond our control.

We must also convince a variety of potential Ellie Mae Network participants, including mortgage lenders, originators, settlement service providers and mega lenders, of the benefits of electronic origination and network participation as compared to traditional mortgage origination methods including paper, facsimile, courier, mail and email.

We cannot guarantee that our Ellie Mae Network and other service offerings will achieve market acceptance. In the event these efforts are not successful, our business and growth prospects would be adversely affected.

Our failure to protect the confidential information of our Encompass users, our Ellie Mae Network participants and their respective customers could damage our reputation and brand and substantially harm our business.

Certain confidential information relating to certain of our Encompass users, our Ellie Mae Network participants and their respective customers resides on our third-party hosted data center servers and is transmitted over our network. We rely on encryption and authentication technology licensed from third parties to effect secure transmission of confidential information, including personal information and credit card numbers. These security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers, service provider error, malfeasance or otherwise. These servers may also be vulnerable to computer viruses, break-ins and similar disruptions from unauthorized tampering with our computer systems, which could result in someone obtaining unauthorized access to our customers' data or our data, including our intellectual property and other confidential business information, or our IT systems. Because the techniques used to obtain unauthorized access to, or to sabotage, systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. The possession and use of personal information in conducting our business subject us to legislative and regulatory burdens that may require notification to customers of a security breach, restrict our use of personal information and hinder our ability to acquire new customers or market to existing customers.

We cannot guarantee that our security measures will prevent security breaches. Any such compromise of our security could damage our reputation and brand and expose us to a risk of loss or litigation and potential liability, which would substantially harm our business and operating results. We may need to expend significant resources to protect against and remedy any potential security breaches and their consequences.

We cannot accurately predict subscription renewal or upgrade rates and the impact these rates may have on our future revenues and operating results.

Our customers have no obligation to renew their subscriptions for our service after the expiration of their initial subscription period, which ranges from one to five years. They may also choose to renew their subscriptions at lower levels. In addition, in the first year of a subscription, customers often purchase a higher level of professional services than they do in renewal years. As a result, our ability to grow is dependent in part on customers purchasing additional subscriptions and services after the initial subscription term. We cannot accurately predict renewal rates given our varied customer base and the number of multi-year subscription contracts. Our customers' renewal rates may decline or fluctuate because of several factors, including their satisfaction or dissatisfaction with our services, the prices of our services, the prices of services offered by our competitors or reductions in our customers' spending levels due to the macroeconomic environment or other factors. If our customers do not renew their subscriptions for our services, renew on less favorable terms or do not purchase additional subscriptions or services, our revenues may grow more slowly than expected or decline and our profitability and gross margin may be harmed.

Mortgage lending volume was lower in 2013 than in 2012, and it is expected to be lower in 2014 than in 2013 due to various factors which could adversely affect our business.

Mortgage lending volume was lower in 2013 than in 2012, and it is expected to be lower in 2014 than in 2013. Factors that adversely impact mortgage lending volumes include increasing mortgage interest rates, reduced consumer and investor demand

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for mortgages, more stringent underwriting guidelines, decreased liquidity in the secondary mortgage market, high levels of unemployment, high levels of consumer debt, lower consumer confidence, changes in tax and other regulatory policies, the number of existing mortgages eligible for refinancing and other macroeconomic factors.

In addition, mortgage interest rates were at historic lows and recently have been rising. Mortgage interest rates are influenced by a number of factors, including monetary policy. The Federal Reserve Bank may raise the federal funds rate, which would likely cause mortgage interest rates to rise. Increases in mortgage interest rates could reduce the volume of new mortgages originated, in particular the volume of mortgage refinancings. Additionally, because the ratio of applications to closed loans typically is greater with refinancings than with purchase loans, a continued decrease in refinancings would result in fewer mortgage applications per funded loan. Since we generate some Ellie Mae Network revenues during the application process, regardless of whether the loan is eventually funded, this may continue to negatively impact our transaction based revenue.

We currently estimate that approximately 30% to 40% of our revenues have some sensitivity to volume. The forecasted lower levels in residential mortgage loan volume in 2015 as compared to 2014 levels will require us to increase our user base and/or our revenues per loan processed by our customers in order to maintain our financial performance. Any additional decrease in residential mortgage volumes would heighten our need to increase these revenue drivers. We cannot guarantee we will be successful in these efforts, which could materially adversely affect our business.

A significant decline in mortgage origination volume, such as the significant drop in mortgage volume anticipated in 2014, could also negatively impact our customers, resulting in a reduction of their Encompass users, consolidation with other lenders or cessation of operations. If any of these occurs, it could materially adversely affect our business.

We expect a number of factors to cause our operating results to fluctuate on a quarterly and annual basis, which may make it difficult to predict our future performance.

Our revenues and operating results have in the past varied and could in the future vary significantly from quarter-to-quarter and year-to-year because of a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be indicative of future operating results. In addition to other risk factors discussed in this section, factors that may contribute to the variability of our quarterly and annual results include:

- the number of Encompass users;
- the volume of mortgages originated by Encompass users, especially users on our Success-Based Pricing model;
- transaction volume on the Ellie Mae Network;
- fluctuations in mortgage lending volume;
- the relative mix of purchase and refinance volume handled by Encompass users;
- the level of demand for our services;
- the timing of the introduction and acceptance of Ellie Mae Network offerings and new on-demand services;
- costs associated with defending intellectual property infringement and other claims; and
- changes in government regulation affecting Ellie Mae Network participants or our business.

Due to these and other factors, our future results may not reach our internal projections. In addition, our operating results in future periods may not meet the expectations of investors or public market analysts who follow our company, which could cause our stock price to decline rapidly and significantly. The results of any prior quarterly or annual periods should not be relied upon as indications of our future operating performance.

Since part of our sales efforts are targeted at larger customers, our sales cycle may become longer and more expensive, we may encounter pricing pressure and implementation and customization challenges, and we may have to delay revenue recognition for some complex transactions, all of which could harm our business and operating results.

Part of our business strategy is to target larger mortgage lenders that handle greater volumes of loans. As we target more of our sales efforts at larger customers, we could face greater costs, longer sales cycles and less predictability in completing some of our sales. In this market, the customer's decision to use our products and services may be an enterprise-wide decision and, if so, this type of sale could require us to provide greater levels of education regarding the use and benefits of our products and services. In addition, larger customers may demand more customization, implementation services and features. As a result of these factors, these sales opportunities may require us to devote greater sales support and professional services resources to individual customers, driving up costs and time required to complete sales and diverting our own sales and professional services resources to a smaller number of larger transactions, while potentially requiring us to delay revenue recognition on some of these transactions until the technical or implementation requirements have been met.

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Supporting our existing and growing customer base could strain our personnel resources, and if we are unable to scale our operations and increase productivity, we may not be able to successfully implement our business plan.

We continue to experience significant growth in our customer base, which has placed a strain on our management and administrative, operational and financial infrastructure. We anticipate that additional investments in our implementation capabilities and research and development and general and administrative spending will be required to scale our operations and increase productivity, address the needs of our customers, further develop and enhance our products and services and scale with the overall growth of our company.

In addition, professional services, such as implementation services, are a key aspect of on-boarding new customers. The implementation process is complicated and we will need to scale our capabilities in this area to meet future revenue targets. If a customer is not satisfied with the quality of work performed by us or with the type of services or solutions delivered, then we could incur additional costs to address the situation, the profitability of that work might be impaired, and the customer's dissatisfaction with our products and services could damage our ability to obtain additional work from that customer. In addition, negative publicity related to our customer relationships, regardless of its accuracy, may further damage our business by affecting our ability to compete for new business with current and prospective customers.

Continued growth may place significant demands on our management and our infrastructure and require significant expenditures and resources.

Our growth has placed and may continue to place significant demands on our management and our administrative, operational and financial infrastructure. As our operations grow in size, scope and complexity, we will need to improve and upgrade our systems and infrastructure, including our data centers and financial reporting systems. These upgrades and improvements are necessary in order to offer an increasing number of customers enhanced solutions, features and functionality and to ensure continued adequate controls over financial reporting.

In addition, the expansion of our systems and infrastructure will require us to commit substantial financial, operational and technical resources in advance of any anticipated increase in the volume of business, with no assurance that the volume of business will actually increase. Continued growth could also strain our ability to maintain reliable service levels for our customers, develop and improve our operational, financial and management controls, enhance our reporting systems and procedures and recruit, train and retain highly skilled personnel.

Managing our growth will require significant expenditures and allocation of valuable management resources. We have been aggressively hiring talent in all areas of our business, which has significantly increased our expenses. If we fail to achieve the necessary level of efficiency in our organization as it grows, our business would be harmed. We are also in the process of upgrading and/or replacing various software systems including our new enterprise resource planning, or ERP, system, which we began using during the fourth quarter of 2013. The implementation of an ERP system entails certain risks, including difficulties with changes in business processes that could disrupt our company's operations, such as our ability to process orders, provide services and customer support, fulfill contractual obligations and aggregate financial and operational data, and the ERP providers to deliver the functionality we require and in a timely manner. Unanticipated problems impacting the implementation of these systems could significantly increase the expenditures and resources allocated to this project, divert the attention of management and harm our business. If the implementations of these new applications are delayed, or if we encounter unforeseen problem with our new systems or in migrating away from our existing applications and systems, our operations and our ability to manage our business could be negatively impacted.

Integrating future acquisitions could disrupt our business, harm our financial condition and operating results or dilute or adversely affect the price of our common stock.

Our success will depend in part on our ability to expand our solutions and services and to grow our business in response to changing technologies, customer demands and competitive pressures. In some circumstances, we may pursue growth through the acquisition of complementary businesses, solutions or technologies rather than through internal development. For example, in January 2014, we acquired substantially all the assets of MortgageCEO, a SaaS company specializing in customer relationship management and marketing solutions for the residential mortgage industry.

The identification of suitable acquisition candidates can be difficult, time-consuming and costly, and we may not be able to complete acquisitions successfully. Moreover, if such acquisitions require us to seek additional debt or equity financing, we may not be able to obtain such financing on terms favorable to us or at all. Acquisitions and investments involve numerous risks which may have a negative impact on our results of operations, including:

- write-offs of acquired assets or investments;
- potential financial and credit risks associated with acquired customers;

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- unknown liabilities associated with the acquired businesses;
- unanticipated expenses related to acquired technology and its integration into existing technology;
- depreciation and amortization of amounts related to acquired intangible assets, fixed assets and deferred compensation; and
- adverse tax consequences of any such acquisitions.

Even if we successfully complete an acquisition, we may not be able to assimilate and integrate effectively the acquired business, technologies, solutions, assets, personnel or operations, particularly if key personnel of an acquired company decide not to work for us. We may encounter difficulty in incorporating acquired technologies into our service and maintaining the quality standards that are consistent with our brand and reputation. In addition, we may issue debt or equity securities to complete an acquisition, which could dilute our stockholders' ownership and adversely affect the price of our common stock.

Events similar to the extreme turmoil in the residential mortgage industry that occurred from 2007 to 2009 could adversely affect our business.

From 2007 to 2009, the worldwide credit market was severely disrupted by the global financial crisis due to the precipitous rise of sub-prime mortgage delinquencies and resulting failure of securities backed by mortgages, including these sub-prime mortgages. This crisis resulted in extreme turmoil in the residential mortgage industry and caused many mortgage originators and other mortgage industry participants to go out of business. If the residential mortgage industry were to experience another similar disruptive event, our business could be materially adversely affected.

The residential mortgage industry is heavily regulated and changes in current legislation or new legislation could adversely affect our business.

Changes in the regulations that govern our customers could adversely affect our business.

The U.S. mortgage industry is heavily regulated. Federal and state governments and agencies could enact legislation or other policies that could negatively impact the business of our Encompass users and other Ellie Mae Network participants. Any changes to existing laws or regulations or adoption of new laws or regulations that increase restrictions on the residential mortgage industry may decrease residential mortgage volume or otherwise limit the ability of our Encompass users and Ellie Mae Network participants to operate their businesses, resulting in decreased usage of our solutions.

Changes in current legislation or new legislation may increase our costs by requiring us to update our products and services.

Changes to existing laws or regulations or adoption of new laws or regulations relating to the residential mortgage industry could require us to incur significant costs to update our products and services. Our Encompass Compliance Service analyzes mortgage loan data for compliance with consumer protection laws and institutionally mandated compliance policies and must continually be updated to incorporate changes to such laws and policies. The Dodd-Frank Act has caused and will continue to cause us to make similar updates to Encompass, Encompass Product and Pricing Service, Encompass Docs Solution, TQL and the Ellie Mae Network to address, among other things, regulations that protect consumers against unfair, deceptive and abusive practices by lenders. For example, additional tools and product updates were recently required to address the Ability-to-Repay, or ATR, / Qualified Mortgage, or QM, and Federal and State High Cost rules effective in January 2014. These additions and updates have caused us to incur significant expense, and future updates will likely similarly cause us to incur significant expense.

Potential structural changes in the U.S. residential mortgage industry, in particular plans to diminish the role of Fannie Mae and Freddie Mac, could disrupt the residential mortgage market and have a material adverse effect on our business.

Fannie Mae and Freddie Mac play a very important role in providing liquidity, stability and affordability in the current U.S. residential mortgage market. In particular, they participate in the secondary mortgage market by purchasing mortgage loans and mortgage-related securities for investment and by issuing guaranteed mortgage-related securities. In February 2011, the Obama administration delivered a report to Congress which proposed the winding down of Fannie Mae and Freddie Mac and shrinking the federal government's role in the housing market. This proposal includes the withdrawal of government guarantees currently available for certain residential loans and increasing the down payment requirements for borrowers, both of which could reduce mortgage lending volume. In February 2012, the Federal Housing Finance Agency sent Congress a strategic plan to wind down Fannie Mae and Freddie Mac over the next several years. This proposal includes building a new infrastructure for the secondary mortgage market, continuing to shrink Fannie Mae's and Freddie Mac's operations by eliminating the direct funding of mortgages and shifting mortgage credit risk to private investors and maintaining foreclosure prevention activities and credit availability. In August 2012, the U.S. Department of the Treasury announced it would require Fannie Mae and Freddie Mac to reduce their investment portfolios more quickly, at an annual rate of 15% versus the previous rate of 10%. In June 2013, the U.S. Senate

introduced a bill to wind down Fannie Mae and Freddie Mac over five years. This legislation would replace Fannie Mae and Freddie Mac with a new Federal Mortgage Insurance Corporation that would continue to guarantee mortgages, but only after private capital absorbs the first 10% of any losses. In July 2013, the U.S. House of Representatives also unveiled draft legislation to similarly wind down Fannie Mae and Freddie Mac over a five year period. The effects of these proposals, the passage of either of these bills into law or any significant structural change to the U.S. residential mortgage industry may cause significant disruption to the residential mortgage market. If we are unable to react effectively and quickly to changes in the residential mortgage industry, our business could be harmed.
We may be limited in the way in which we market our business or generate revenue by U.S. federal law prohibiting referral fees in real estate transactions, and if we are found to be in violation of such laws we would be subject to significant liability.
RESPA generally prohibits the payment or receipt of fees or any other thing of value for the referral of business related to a residential real estate settlement service and prohibits fee shares or splits or unearned fees in connection with the provision of such services. Encompass software and services and the Ellie Mae Network were designed with payment methods that are not currently prohibited by the restrictions under RESPA. Nonetheless, RESPA may restrict our ability to enter into marketing and distribution arrangements with third parties for existing or newly developed products and services, particularly to the extent that such arrangements may be characterized as involving payments for the referral of residential real estate settlement service business. Additionally, any amendments to RESPA or court opinions interpreting the provisions of RESPA that result in restrictions on our current payment methods, or any determination that our payment methods have been and currently are subject to the restrictions under RESPA, could have a material adverse effect on our business. If we were found to be in violation of RESPA rules, we would be exposed to significant potential liability that could have a material adverse effect on our reputation and business.
We depend on key and highly skilled personnel to operate our business, and if we are unable to retain our current or hire additional personnel, our ability to develop and successfully market our business could be harmed.
We believe our future success will depend in large part upon our ability to attract and retain highly skilled managerial, technical, finance, creative and sales and marketing personnel. Moreover, we believe that our future success is highly dependent on the contributions of our named executive officers. All of our officers and other employees are at-will employees, which means they may terminate their employment relationship with us at any time, and their knowledge of our business and industry would be extremely difficult to replace. In addition, the loss of any key employees or the inability to attract or retain qualified personnel could delay the development and introduction of, and harm our ability to sell, our solutions and harm the market’s perception of us. Competition for qualified personnel is particularly intense in the San Francisco Bay Area, where our headquarters are located. Qualified individuals are in high demand, and we may incur significant costs to attract them. We may be unable to attract and retain suitably qualified individuals who are capable of meeting our growing sales, operational and managerial requirements, or may be required to pay increased compensation in order to do so. If we are unable to attract and retain the qualified personnel we need to succeed, our business will suffer.
Volatility or lack of performance in our stock price may also affect our ability to attract and retain our key employees. Our named executive officers are vested in a substantial amount of stock options and performance share awards. Employees may be more likely to leave us if the shares they own or the shares underlying their vested options have significantly appreciated in value relative to the original purchase prices of the shares or the exercise prices of the vested options, or if the exercise prices of the options that they hold are significantly above the market price of our common stock. If we are unable to retain our named executive officers or other key employees, our business will be harmed.
We operate in a highly competitive market, which could make it difficult for us to attract and retain Encompass users and Ellie Mae Network participants.
The mortgage origination software market is highly competitive. There are many software providers, such as: Byte Software Inc., a subsidiary of CBCInnovis; Calyx Technology, Inc.; Harland Financial Solutions, a subsidiary of Davis + Henderson Corporation; and PCLender.com, Inc., a subsidiary of Fidelity National Financial, Inc., that compete with us by offering loan origination software to mortgage originators. Some software providers, including Calyx Technology, Inc., also provide connectivity between their software users and lenders and service providers.

Other connectivity alternatives are provided by services such as RealEC Technologies, Inc., a subsidiary of Fidelity National Financial, Inc. We also compete with compliance and document preparation service providers that are much larger and more established than us. There is vigorous competition among providers of these services and we may not succeed in convincing potential customers using other services to switch to ours. Many service providers connect directly to mortgage originators without using any loan origination software. Some of our competitors also offer services on a per closed loan basis, which could adversely impact the effectiveness of our Success-Based Pricing strategy for increasing the number of SaaS Encompass customers. If we are unsuccessful in competing effectively by providing attractive functionality, customer service or value, we could lose existing Encompass users to our competitors and our ability to attract new Encompass users could be harmed.

We only offer our Encompass services to Encompass users. There are many other service providers that offer our Encompass users competing services, including borrower-facing websites, document preparation services, compliance services and EDM. We may be unsuccessful in continuing to differentiate our Encompass service offerings to the extent necessary to effectively compete in some or all of these markets.

The Ellie Mae Network is only available to mortgage originators using Encompass. The principal alternative to the use of the Ellie Mae Network by Encompass users remains traditional methods of exchanging data and documents among mortgage industry participants by email, facsimile, phone, courier and mail. In addition, mortgage originators may use standalone web browsers to go individually to each investor, lender or service provider’s website and then manually upload loan data or enter information into the website. Mortgage originators may continue to use these methods due to habit, personal business relationships or otherwise. The success of the Ellie Mae Network depends on our ability to achieve and offer access to both the critical mass of investors, lenders and service providers necessary to attract and retain mortgage originators using Encompass on the Ellie Mae Network and the critical mass of active mortgage originators necessary to attract and retain investors, lenders and service providers on our network.

Some of our actual and potential competitors have longer operating histories and significantly greater financial, technical, marketing and other resources than we do and, as a result, these companies may be able to respond more quickly to changes in regulations, new technologies or customer demands, or devote greater resources to the development, promotion and sale of their software and services than we can. In addition, we may face increased competition as a result of continuing industry consolidation, such as: Accenture's acquisition of Mortgage Cadence LLC in August 2013; Davis + Henderson Corporation’s acquisitions of Harland Financial Solutions in August 2013, Mortgagebot LLC in April 2011 and Avista Solutions, Inc. in May 2012; Lender Processing Services, Inc.’s acquisition of PCLender.com, Inc. in March 2011; Optimal Blue, Inc.’s acquisition of LoanSifter, Inc. in December 2013 and Fidelity National Financial, Inc.’s acquisition of Lender Processing Services, Inc. in January 2014. We expect the mortgage origination market to continue to attract new competitors and there can be no assurance that we will be able to compete successfully against current or future competitors or that competitive pressures we face will not materially adversely affect our business.

Failure to adapt to technological changes may render our technology obsolete or decrease the attractiveness of our solutions to our customers.

If new industry standards and practices emerge, or if competitors introduce new solutions embodying new services or technologies, Encompass and the Ellie Mae Network technology may become obsolete. Our future success will depend on our ability to:

- enhance our existing solutions;
- develop and potentially license new solutions and technologies that address the needs of our prospective customers; and
- respond to changes in industry standards and practices on a cost-effective and timely basis.

We must continue to enhance the features and functionality of Encompass, other Encompass services and the Ellie Mae Network. The effective performance, reliability and availability of Encompass, Encompass services and the Ellie Mae Network infrastructure are critical to our reputation and our ability to attract and retain Encompass users and Ellie Mae Network participants. If we do not continue to make investments in product development and, as a result, or due to other reasons, fail to attract new and retain existing mortgage originators, lenders, investors and service providers, we may lose existing Ellie Mae Network participants, which could significantly decrease the value of the Ellie Mae Network to all participants and materially adversely affect our business.

Failure to adequately protect our intellectual property could harm our business.

The protection of our intellectual property rights, including our proprietary Encompass software and Ellie Mae Network technology, is crucial to the success of our business. We rely on a combination of patent, copyright, trademark and trade secret law and contractual restrictions to protect our intellectual property. Our present and future patents may provide only limited protection for our technology and may not be sufficient to provide competitive advantage to us. Furthermore, we cannot guarantee any patents will be issued to us as a result of our patent applications. We also rely in part on confidentiality and invention assignment agreements with our employees, independent contractors and consultants. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our Ellie Mae Network and Encompass features and functionality or obtain and use information that we consider proprietary. Enforcing our proprietary rights is difficult and may not always be effective. We have registered “Ellie Mae” and “Encompass” and certain of our other trademarks as trademarks in the United States. Competitors may adopt service names similar to ours, thereby impeding our ability to build brand identity and possibly leading to customer confusion. In addition, there could be potential trade name or trademark infringement claims brought by owners of other registered trademarks or trademarks that incorporate variations of the terms Ellie Mae, Encompass or our other trademarks.

Litigation or proceedings before the U.S. Patent and Trademark Office or other governmental authorities and administrative bodies in the United States and abroad may be necessary in the future to enforce our intellectual property rights, protect our patent and copyright rights, trade secrets and domain names and determine the validity and scope of the proprietary rights of others. Our efforts to enforce or protect our proprietary rights may be ineffective and could result in substantial costs and diversion of resources and could harm our business.

Assertions that we infringe third-party intellectual property rights could result in significant costs and substantially harm our business.

Other parties have asserted, and may in the future assert, that we have infringed their intellectual property rights. For example, on March 25, 2011, we were named a defendant in a patent infringement lawsuit filed by Industry Access Incorporated alleging that our Encompass loan management software system and related operations infringes a patent and on March 19, 2013, Industry Access filed a second patent infringement lawsuit against us alleging that our products and services infringe two additional patents. See Note 8 of the Notes to Condensed Consolidated Financial Statements. In addition, we generally agree to indemnify our customers against legal claims that our software products infringe intellectual property rights of third parties and, in the event of an infringement, to modify or replace the infringing product or, if those options are not reasonably possible, to refund the cost of the software, as pro-rated over a period of years. We cannot predict whether assertions of third-party intellectual property rights or claims arising from such assertions will substantially harm our business and operating results. If we are forced to defend against any infringement claims, whether they are with or without merit or are determined in our favor, we may face costly litigation and diversion of technical and management personnel. Furthermore, an adverse outcome of a dispute may require us to: pay damages, potentially including treble damages and attorneys' fees if the infringement were found to be willful; cease providing solutions that allegedly incorporate the intellectual property of others; expend additional development resources to redesign or re-engineer our solutions and products, if feasible; and enter into potentially unfavorable royalty or license agreements in order to obtain the right to use necessary technologies. We cannot be certain of the outcome of any litigation. Any royalty or licensing agreement, if required, may not be available to us on acceptable terms or at all. Our failure to obtain the necessary licenses or other rights could prevent the sale or distribution of some of our products and services and, therefore, could have a material adverse effect on our business.

Current or future litigation could substantially harm our business.

We have been and continue to be involved in legal proceedings, claims and other litigation. For more on legal proceedings, see Note 8 of the Notes to Condensed Consolidated Financial Statements.

We are also subject to various other legal proceedings and claims arising out of the ordinary course of business. While we do not expect the outcome of any such pending litigation to have a material adverse effect on our financial position, litigation is unpredictable and excessive verdicts, both in the form of monetary damages and injunctions, could occur. In the future, litigation could result in substantial costs and diversion of resources and we could incur judgments or enter into settlements of claims that could have a material adverse effect on our business.

If we fail to maintain proper and effective internal controls, our ability to produce accurate financial statements could be impaired, which could result in a loss of investor confidence in our financial reports, significant expenses to remediate any internal control deficiencies and ultimately have an adverse effect on the market price of our common stock.

As a publicly-traded company, we are subject to compliance with, among other regulations, Section 404 of the Sarbanes-Oxley Act of 2002, or SOX, which requires that we test our internal control over financial reporting and disclosure controls and procedures. Ensuring that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. Our compliance with SOX requires that we incur substantial expense and expend significant management time on compliance-related issues. If we fail to achieve and maintain an effective internal control environment, we could suffer material misstatements in our financial statements and fail to meet our reporting obligations, which would likely cause investors to lose confidence in our reported financial information. This could harm our operating results and lead to a decline in our stock price. Additionally, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to potential delisting from the New York Stock Exchange, regulatory investigations, civil or criminal sanctions and class action litigation.

As a third-party technology service provider of mission-critical products and services to many financial institutions that are regulated by one or more member agencies of the Federal Financial Institutions Examination Council, or FFIEC, we are subject to an IT examination by the member agencies of the FFIEC. As a result, the FFIEC conducts recurring IT Examinations in order

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to identify existing or potential risks associated with our operations that could adversely affect the financial institutions to whom we provide products and services, evaluate our risk management systems and controls and determine our compliance with applicable laws that affect the products and services we provide to financial institutions. In addition to examining areas such as our management of technology, data integrity, information confidentiality and service availability, the reviews also assess our financial stability. A sufficiently unfavorable review from the FFIEC could result in our financial institution customers not being allowed to use our technology products and services, which could have a material adverse effect on our business and financial condition.

If one or more U.S. states or local jurisdictions successfully assert that we should have collected or in the future should collect additional sales or use taxes on our fees, we could be subject to additional liability with respect to past or future sales, and the results of our operations could be adversely affected.

We do not collect state and local sales and use taxes in all jurisdictions in which our customers are located, based on our belief that such taxes are not applicable. Sales and use tax laws and rates vary by jurisdiction and such laws are subject to interpretation. Jurisdictions in which we do not collect sales and use taxes may assert that such taxes are applicable, which could result in the assessment of such taxes, interest and penalties, and we could be required to collect such taxes in the future. This additional sales and use tax liability could adversely affect the results of our operations.

Our business is subject to the risks of earthquakes, fires, floods and other natural catastrophic events and to interruption by man-made problems such as terrorism.

Our systems and operations are vulnerable to damage or interruption from earthquakes, fires, floods, power losses, telecommunications failures, terrorist attacks, acts of war and similar events. For example, a significant natural disaster, such as an earthquake, fire or flood, could have a material adverse impact on our business, operating results and financial condition, and our insurance coverage may be insufficient to compensate us for losses that may occur. Our corporate offices and one of the facilities we lease to house our computer and telecommunications equipment are located in the San Francisco Bay Area, a region known for seismic activity. In addition, acts of terrorism, which may be targeted at metropolitan areas with higher population density than rural areas, could cause disruptions in our or our customers' businesses or the economy as a whole. We may not have sufficient protection or recovery plans in certain circumstances, such as natural disasters affecting the San Francisco Bay Area, and our business interruption insurance may be insufficient to compensate us for losses that may occur.

Our stock price is volatile and purchasers of our common stock could incur substantial losses.

The trading price of our common stock may be subject to wide fluctuations in response to various factors, some of which are beyond our control. In addition to the factors discussed in this "Risk Factors" section and elsewhere in our filings with the Securities and Exchange Commission, these factors include:

- our operating performance and the operating performance of similar companies;
- the overall performance of the equity markets;
- the number of shares our common stock publicly owned and available for trading;
- threatened or actual litigation;
- changes in laws or regulations relating to our solutions;
- any major change in our board of directors or management;
- publication of research reports about us or our industry or positive or negative recommendations or withdrawal of research coverage by securities analysts;
- large volumes of sales of our shares of common stock by existing stockholders; and
- general political and economic conditions.

In addition, the stock market in general has experienced extreme price and volume fluctuations. Securities class action litigation has often been instituted against companies following periods of volatility in the overall market and in the market price of a company's securities. This litigation, if instituted against us, could result in very substantial costs, divert our management's attention and resources and harm our business.

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If securities or industry analysts discontinue publishing research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business. If one or more of the analysts who cover us downgrade our stock or publish inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, demand for our stock could decrease, which might cause our stock price and trading volume to decline.

Certain provisions in our charter documents and Delaware law could discourage takeover attempts and lead to management entrenchment.

Our amended and restated certificate of incorporation and amended and restated bylaws contain provisions that could have the effect of delaying or preventing changes in control or changes in our board of directors. These provisions include:

- a classified board of directors with three-year staggered terms, which may delay the ability of stockholders to change the membership of a majority of our board of directors;
- no cumulative voting in the election of directors, which limits the ability of minority stockholders to elect director candidates;
- the exclusive right of our board of directors to elect a director to fill a vacancy created by the expansion of the board of directors or the resignation, death or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors;
- the ability of our board of directors to determine to issue shares of preferred stock and to determine the price and other terms of those shares, including preferences and voting rights, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;
- a prohibition on stockholder action by written consent, which forces stockholder action to be taken at an annual or special meeting of our stockholders;
- the requirement that a special meeting of stockholders may be called only by the chairman of the board of directors, the chief executive officer, the president or the board of directors, which may delay the ability of our stockholders to force consideration of a proposal or to take action, including the removal of directors; and
- advance notice procedures that stockholders must comply with in order to nominate candidates to our board of directors or to propose matters to be acted upon at a stockholders' meeting, which may discourage or deter a potential acquirer from conducting a solicitation of proxies to elect the acquirer's own slate of directors or otherwise attempting to obtain control of us.

We are also subject to certain anti-takeover provisions under Delaware law. Under Delaware law, a corporation may not, in general, engage in a business combination with any holder of 15% or more of its capital stock unless the holder has held the stock for three years or, among other things, the board of directors has approved the transaction.

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ITEM 6—EXHIBITS

Exhibit Number	Description of Document
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document

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* Exhibits 32.1 and 32.2 are being furnished and shall not be deemed to be “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall such exhibits be deemed to be incorporated by reference in any registration statement or other document filed under the Securities Act of 1933, as amended, or the Exchange Act, except as otherwise specifically stated in such filing.

** XBRL information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933, as amended, and Section 18 of the Exchange Act, and is not subject to liability under those sections, is not part of any registration statement or prospectus to which it relates and is not incorporated or deemed to be incorporated by reference into any registration statement, prospectus or other document.

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SIGNATURES

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

	ELLIE MAE, INC.
Date: May 7, 2014	By: /s/ Edgar A. Luce Edgar A. Luce Executive Vice President, Finance and Administration and Chief Financial Officer (Principal Financial and Accounting Officer and duly authorized signatory)

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INDEX TO EXHIBITS

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