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SIMTEK CORP
Form 10-Q
November 14, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

- Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarter ended September 30, 2006
OR
 Transition report pursuant to section 13 or 15 (d) of the Securities Exchange Act of 1934

Commission file number 0-19027

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

Delaware
(State or other jurisdiction
of incorporation or organization)

84-1057605
(I.R.S. Employer Identification No.)

4250 Buckingham Drive, Suite 100,
Colorado Springs, Colorado 80907
(Address of principal executive offices) (Zip Code)

(719) 531-9444

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

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

The total number of shares of Common Stock issued and outstanding as of November 8, 2006 was 8,120,606.

SIMTEK CORPORATION

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For the Quarter Ended September 30, 2006

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ASSETS		September 30, 2006
-----		-----
		(Unaudited)
CURRENT ASSETS:		
Cash and cash equivalents	\$	3,653
Restricted investments		1,775
Accounts receivable - trade, net		5,051
Inventory, net		5,394
Prepaid expenses and other current assets		401
Deposits		-

Total current assets		16,274
EQUIPMENT AND FURNITURE, net		1,128
DEFERRED FINANCING COSTS AND DEBT ISSUANCE COSTS		127
GOODWILL		992
NON-COMPETITION AGREEMENT		7,571
OTHER ASSETS		41

TOTAL ASSETS	\$	26,133
		=====
LIABILITES AND SHAREHOLDERS' EQUITY		

CURRENT LIABILITIES:		
Accounts payable	\$	3,287
Accrued expenses		1,237
Accrued vacation payable		200
Accrued wages		230
Obligation under capital leases		-
Line of credit		917
Debentures, current		480

Total current liabilities		6,351
DEBENTURES, NET OF CURRENT		2,220

Total liabilities		8,571
Temporary equity, 8,028,170 shares of common stock, \$0.0001 par value, subject to penalties under registration rights agreements, net of financing costs of \$708		14,847
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY:		
Preferred stock, \$.0001 par value; 200,000 shares authorized, none issued		-
Common stock, \$.0001 par value; 30,000,000 shares authorized, 8,005,903 and 8,006,903 shares issued and outstanding at September 30, 2006 and 7,817,082 and 7,818,082 shares issued and outstanding at December 31, 2005, excluding temporary equity		1
Additional paid-in capital		51,430
Treasury stock, at cost; 1,000 shares		(1)
Accumulated deficit		(48,795)
Accumulated other comprehensive income:		
Cumulative translation adjustment		80

Total shareholders' equity		2,715

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TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY \$ 26,133
=====

The accompanying notes are an integral part of these financial statements

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SIMTEK CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(Amounts in thousands, except share and per share amounts)

	Three Months Ended September 30,		Nine Sep
	2006	2005	2006
REVENUE:			
Product sales, net	\$ 8,251	\$ 2,412	\$ 19,436
Royalty revenue	--	--	1,518
Total revenue	8,251	2,412	20,954
Cost of sales	4,979	1,807	13,016
GROSS PROFIT	3,272	605	7,938
OPERATING EXPENSES:			
Research and development costs	1,351	1,572	4,578
Sales and marketing	1,250	321	3,233
General and administrative	838	412	2,595
Total operating expenses	3,439	2,305	10,406
LOSS FROM CONTINUING OPERATIONS	(167)	(1,700)	(2,468)
OTHER INCOME (EXPENSE):			
Interest income	36	45	112
Interest expense	(113)	(63)	(247)
Exchange rate variance	(7)	--	(4)
Other income (expense)	2	--	2
Total other expense	(82)	(18)	(137)
LOSS FROM CONTINUING OPERATIONS BEFORE PROVISION FOR INCOME TAXES	(249)	(1,718)	(2,605)
Provision for income taxes	--	--	--
LOSS FROM CONTINUING OPERATIONS	(249)	(1,718)	(2,605)
INCOME FROM DISCONTINUED OPERATIONS (including gain on disposal of \$1,689)	--	1,701	--
NET LOSS	\$ (249)	\$ (17)	\$ (2,605)

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	=====	=====	=====
NET LOSS PER COMMON SHARE:			
Basic and diluted			
Loss from continuing operations	\$ (.02)	\$ (.24)	\$ (.18)
Income (Loss) from discontinued operations	(.00)	.24	(.00)
	-----	-----	-----
Total	\$ (.02)	\$ (.00)	\$ (.18)
	=====	=====	=====
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:			
Basic and diluted	14,966,916	7,073,599	14,791,191
	=====	=====	=====

The accompanying notes are an integral part of these financial statements

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SIMTEK CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(Amounts in thousands)

	Nine Months Ended
	----- 2006 -----
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net loss	\$(2,605)
Income from discontinued operations	--
Adjustments to reconcile net loss to net cash used in operating activities:	
Activities:	
Depreciation and amortization	361
Expense related to stock options	417
Issuance of common stock per compensation agreements	53
Expense related to issuance of warrants	--
Gain from discontinued operations	--
Amortization of non-competition agreement	1,339
Net change in allowance accounts	577
Deferred financing fees	37
Changes in assets and liabilities:	
(Increase) decrease in:	
Accounts receivable	(3,687)
Inventory	(3,799)
Prepaid expenses and other	282
Increase (decrease) in:	
Accounts payable	461
Accrued expenses	996

Net cash used in operating activities of continuing operations	(5,568)
Net cash provided by operating activities of discontinued operations	--

Net cash used in operating activities	(5,568)
CASH FLOWS FROM INVESTING ACTIVITIES:	

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Purchase of equipment and furniture, net	(914)
Proceeds from discontinued operations, net	--
Purchase of certain assets from ZMD	(116)

Net cash provided by (used in) investing activities of continuing operations	(1,030)
Net cash used in investing activities of discontinued operations	--

Net cash provided by (used in) investing activities	(1,030)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Payments on capital lease obligation	(13)
Receipts from restricted cash	200
Funds received from December 2005 equity financing, net	1,874
Warrants issued for license rights	1,478
Equity financing, net	--
Transfer to restricted investment	--
Proceeds from sale of common stock	--
Payments from restricted investment	306
Funds received from September 2006 equity financing, net	4,515
Exercise of stock options	78

Net cash provided by financing activities	8,438

Effect of exchange rate changes on cash	47

NET CHANGE IN CASH AND CASH EQUIVALENTS	1,887
CASH AND CASH EQUIVALENTS, beginning of period	1,766

CASH AND CASH EQUIVALENTS, end of period	\$ 3,653
	=====
Cash Paid for interest	\$ 222
	=====
Warrants issued for debt issuance cost	\$ 53
	=====
Conversion of debentures	\$ 300
	=====

The accompanying notes are an integral part of these financial statements.

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SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The consolidated financial statements include the accounts of Simtek and its wholly owned subsidiaries. Intercompany accounts and transactions have been eliminated. The financial statements included herein are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally made in the registrant's annual Form 10-K filing. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Annual Report and Form 10-K and Annual Report and Form 10-K/A for Simtek Corporation ("Simtek" or the "Company") filed on April 7, 2006 and April 28, 2006, respectively for fiscal year 2005.

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In the opinion of management, the unaudited financial statements reflect all adjustments of a normal recurring nature necessary to present a fair statement of the results of operations for the respective interim periods. The year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. Results of operations for the interim periods are not necessarily indicative of the results of operations for the full fiscal year.

On October 5, 2006, Simtek completed a 1 for 10 reverse stock split. All share and per share amounts have been restated to reflect the effect of the reverse stock split as if it had occurred as of the balance sheet date or as of the beginning of each fiscal period presented. In addition, on October 5, 2006, Simtek converted from a Colorado corporation to a Delaware corporation. This reincorporation had no effect on the consolidated financial statements.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standard 123(R) "Share-Based Payment" ("SFAS 123(R)") using the modified prospective transition method. In addition, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 "Share-Based Payment" ("SAB 107") in March, 2005, which provides supplemental SFAS 123(R) application guidance based on the views of the SEC. Under the modified prospective transition method, compensation cost recognized in the three and nine month periods ending September 30, 2006 includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, and (b) compensation cost for all share-based payments granted beginning January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). In accordance with the modified prospective transition method, results for prior periods have not been restated.

The adoption of SFAS 123(R) resulted in stock compensation expense for the three months and nine months ended September 30, 2006 of \$139,000 and \$417,000, respectively to loss from continuing operations and loss before income taxes. The Company did not recognize a tax benefit from the stock compensation expense because the Company considers it is more likely than not that the related deferred tax assets, which have been reduced by a full valuation allowance, will not be realized. The following table summarizes the effects of the share-based compensation resulting from the application of SFAS No. 123(R) to options granted under the Company's stock option plan.

SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Three Months
Ended
September 30, 2006

Nin
Septe

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(In thousands except per share amounts)

Research and development	\$	43
Sales and marketing		20
General and administrative		76

Share-based compensation effect on loss from continuing operations before provision for income taxes	\$	139
Provision for income taxes		-

Net share-based compensation effects on net loss	\$	139
		=====
Share-based compensation effects on basic and diluted loss per common share	\$.01
		=====
Share-based compensation effects on cash flow from operations	\$	139
		=====

The Black-Scholes option-pricing model was used to estimate the option fair values. The option-pricing model requires a number of assumptions, of which the most significant are expected stock price volatility and the expected option term (the amount of time from the grant date until the options are exercised or expire). Expected volatility was calculated based upon actual historical stock price movements over the most recent periods ending September 30, 2006 equal to the expected option term. In accordance with SFAS No. 123(R), the Company adjusts share-based compensation on a quarterly basis for changes to the estimate of expected forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate for all expense amortization after January 1, 2006 is recognized in the period the forfeiture estimate is changed. The effect of forfeiture adjustments in the three and nine months ended September 30, 2006 was insignificant. The expected option term was calculated using the "simplified" method permitted by SAB 107.

SFAS 123(R) requires tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options ("excess tax benefits") to be classified and reported as both an operating cash outflow and a financing cash inflow upon adoption of SFAS 123(R). As discussed in Note 7 - Taxes from the Company's report on Form 10-K for the period ending December 31, 2005, as a result of the Company's net operating losses, the excess tax benefits that would otherwise be available to reduce income taxes payable have the effect of increasing the Company's net operating loss carry forwards. Accordingly, because the Company is not able to realize these excess tax benefits, such benefits have not been recognized in the condensed statement of cash flow for the nine months ended September 30, 2006.

Pro-Forma Stock Compensation Expense for the three and nine months Ended September 30, 2005

Prior to January 1, 2006, as permitted under the SFAS No. 123, Accounting for Stock-Based Compensation, the Company accounted for its stock-based compensation in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees. As such, compensation expense was recorded on the date of grant if the current market price of the underlying stock exceeded the exercise price. Certain pro forma net loss and EPS disclosures for employee stock option grants are included below as if the fair value method as defined in SFAS No. 123 had been applied. Transactions in equity instruments with non-employees for goods or services are accounted for by the fair value method. Had compensation cost been determined based on the fair value at the grant dates for awards under employee stock based

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compensation plans consistent with the fair value method for the three and nine months ending September 30, 2005, the Company's net loss and net loss per share would have been increased to the pro forma amounts indicated below.

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SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	Three Months Ended September 30,	En
	2005	

(In thousands except per share amounts)		
Net loss as reported	\$ (17)	\$
Add: Stock based compensation included in reported		
Net loss	-	
Deduct: Fair value of stock based compensation	(363)	
Proforma net loss	\$ (380)	\$
	\$ (380)	\$
Net loss as reported - basic and diluted	\$ (.00)	\$
Proforma net loss - basic and diluted	\$ (.01)	\$

In accordance with the modified prospective transition method of SFAS 123(R), the prior comparative quarterly results have not been restated.

Stock Options as of the three and nine month periods ended September 30, 2006

The Company adopted a Non-Qualified Stock Option Plan in 1994, as amended, that authorizes 2,060,000 non-qualified stock options that may be granted to directors, employees, and consultants. The plan permits the issuance of non-statutory options and provides for a minimum exercise price equal to 100% of the fair market value of the Company's common stock on the date of grant. The maximum term of options granted under the plan are 10 years and options granted to employees expire three months after the termination of employment. In 2004, the Non-Qualified Stock Option Plan was extended for 10 more years.

The following table summarizes stock options outstanding and changes during the nine months ended September 30, 2006:

	Outstanding Opt	

Number of Shares	-----	Wegted Average Exercise Price

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Options outstanding at January 1, 2006.....	796,937	\$6.20
Granted.....	428,585	3.46
Exercised.....	(40,583)	(1.89)
Cancelled or forfeited.....	(31,678)	(9.46)
Options outstanding at September 30, 2006.....	1,153,261	\$5.21
Options exercisable at September 30, 2006.....	568,095	\$6.34

(1) Represents the difference between the exercise price and the value of Simtek stock at the time of exercise.

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SIMTEK CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Stock options outstanding and currently exercisable at September 30, 2006 are as follows:

Exercise Price	Outstanding			Exercisable	
	Number Outstanding	Remaining Contractual Life in Months	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$1.40-\$3.50	369,426	48	\$ 2.94	110,197	\$ 2.41
\$3.65-\$6.00	456,189	58	\$ 4.48	191,147	\$ 4.48
\$6.20-\$9.00	222,912	54	\$ 6.57	162,017	\$ 6.56
\$11.25-\$15.00	82,234	28	\$ 12.37	82,234	\$ 12.37

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\$15.30-\$19.00	22,500 -----	55	\$ 17.77	22,500 -----	\$ 17.77
	1,153,261 =====			568,095 =====	

Total estimated unrecognized compensation cost from unvested stock options as of September 30, 2006 was approximately \$1.5 million, which is expected to be recognized over the next four years.

The weighted average per share fair value of stock options granted during the three months ending September 30, 2006 and 2005 were \$3.00 and \$2.30, respectively. The weighted average per share fair value stock options granted during the nine months ending September 30, 2006 and 2005 were \$2.30 and \$3.70, respectively. The fair value was estimated as of the grant date using the Black-Scholes option pricing model with the following assumptions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Volatility	79.38%	85.28%	80.22%	84.22%
Expected option term	5 years	4 years	4.80 years	4.80 years
Risk-free interest rate	5.33%	4.00%	5.02%	3.80%
Expected dividend yield	0%	0%	0%	0%

Modifications of Stock Options Granted

In May 2005, the Company accelerated vesting of certain unvested and out-of-the-money stock options previously awarded to employees and officers. Because the price of the Company's common stock was \$5.70 on the day of acceleration, the options, which are exercisable at \$6.20 and above, had no economic value on the date of acceleration. As a result of the acceleration, options to purchase approximately 170,000 shares of Simtek common stock are now exercisable. Options held by non-employee directors were excluded from the vesting acceleration.

Non-competition Agreement

In December 2005, the Company entered into a non-competition agreement with Zentrum Mikroelektronik Dresden AG ("ZMD") as part of the acquisition of ZMD's nvSRAM product line. The Company assigned a value of \$8,910,000 to the non-competition agreement in December 2005. The value assigned to the

non-competition agreement is being amortized on a straight-line basis over its

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five-year life. The Company recorded an expense for the amortization of approximately \$1,339,000 to sales and marketing for the nine months ended September 30, 2006.

Goodwill

Goodwill represents the excess of the total amount paid to ZMD for the nvSRAM assets acquired on December 30, 2005 and the fair value assigned to specific assets. This amount will not be amortized, but will be reviewed for impairment on a periodic basis. As of September 30, 2006 no impairment of value has been recorded.

Accumulated other comprehensive income (loss)

The functional currency for Simtek GmbH is the local currency, the Euro. Assets and liabilities for this foreign subsidiary are translated at the exchange rate in effect at the balance sheet date, and income and expenses are translated at average exchange rates prevailing during the period. Translation gains or losses are included within shareholders' equity as part of accumulated other comprehensive income (loss). As of September 30, 2006, the Company recorded approximately \$80,000 in comprehensive income.

2. Liquidity

During the three and nine months ended September 30, 2006 and the twelve months ended December 31, 2005, the Company incurred net losses from continuing operations of approximately \$249,000, \$2,605,000 and \$7,490,000, respectively and has an accumulated deficit of \$48,795,000 as of September 30, 2006. The Company was also not in compliance with its debentures throughout 2005 and the first nine months of 2006, but was successful in obtaining waivers through October 1, 2007 from the debenture holders. The Company has working capital of approximately \$9,923,000 as of September 30, 2006.

The Company operates in a volatile industry, whereby its average selling prices and product costs are influenced by competitive factors. Furthermore, the Company continues to incur significant research and development costs for product development. These factors create pressures on sales, costs, earnings and cash flows, which will impact liquidity.

On September 21, 2006, the Company raised gross proceeds of \$4,555,000 in a private placement. The Company issued 1,153,171 shares of our common stock at a per share price of \$3.95 and 172,981 warrants to purchase common stock. The warrants have a per share exercise price of \$5.40 and a five-year term. The Company anticipates using the proceeds for general working capital and to produce silicon wafers to support revenue growth. The shares have been included in the Consolidated Balance Sheet as Temporary Equity, because of the potential penalties associated with the Registration Rights Agreement.

3. Recent Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes ("FIN 48"). The interpretation clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. Specifically, the pronouncement prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The interpretation also provides guidance on the related derecognition, classification, interest and penalties, accounting for interim periods, disclosure and transition of uncertain tax positions. The

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interpretation is effective for fiscal years beginning after December 15, 2006. The adoption of FIN 48 is expected to have an immaterial impact on the Company's consolidated financial position, results of operations or cash flows.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" ("FAS 157"). This Statement defines fair value as used in numerous accounting pronouncements, establishes a

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SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

framework for measuring fair value in generally accepted accounting principles and expands disclosure related to the use of fair value measures in financial statements. The Statement is to be effective for the Company's financial statements issued in 2008; however, earlier application is encouraged. The Company is currently evaluating the timing of adoption and the impact that adoption might have on its financial position or results of operations.

In September 2006, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 108 ("SAB 108"). Due to diversity in practice among registrants, SAB 108 expresses SEC staff views regarding the process by which misstatements in financial statements are evaluated for purposes of determining whether financial statement restatement is necessary. SAB 108 is effective for fiscal years ending after November 15, 2006, and early application is encouraged. The Company does not believe SAB 108 will have a material impact on its financial position or results from operations.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments ("SFAS 155"), which amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS 155 simplifies the accounting for certain derivatives embedded in other financial instruments by allowing them to be accounted for as a whole if the holder elects to account for the whole instrument on a fair value basis. The statement also clarifies and amends certain other provisions of SFAS No. 133 and SFAS No. 140. SFAS 155 is effective for all financial instruments acquired, issued, or subject to a remeasurement event occurring in fiscal years beginning after September 15, 2006. We do not expect the adoption of SFAS 155 to have an impact on our results of operations or financial condition.

4. Revenue Recognition

Revenue Recognition - Product sales revenue is recognized when a valid purchase order has been received with a fixed price and the products are shipped to customers FOB origin (Colorado Springs, Colorado or Dresden, Germany), including distributors. Based on historic business with the majority of the Company's customers and, in the case of new customers, the Company is reasonably assured that collectibility on our shipments will occur. Customers receive a one-year product warranty and sales to distributors are subject to a limited product exchange program and a price protection in the event of changes in the Company's product price. The Company provides a reserve for possible product returns, product price protection and warranty costs at the time the sale is recognized. The Company has a detailed procedure to ensure that its estimates for reserves are reasonable and reliable. The reserve for product returns is

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based on the actual inventory value of the Company's semiconductor products held by its distributors. The Company's distributors are permitted to rotate up to 5% of their stock every six months with the stipulation that they must submit a replacement order of equal dollar value to the stock that they are returning. The reserve for price protection is used when the Company authorizes special pricing to one of its distributors for a specific customer. To date, the estimates have not been materially different from the credits the Company has issued under these reserves.

Revenue from royalties related to non-refundable prepaid royalty payments is recognized upon receipt. Revenue from royalties related to sales of products by license partners is recognized upon the notification to us of shipment of product from the Company's technology license partners to direct customers.

5. Inventories

The Company records inventory using the lower of cost (first-in, first-out) or market. Inventory at September 30, 2006 and December 31, 2005 included:

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SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	September 30, 2006	December 31, 2005
(In thousands)		
Raw Materials	\$ 51	\$ 33
Work in progress	4,011	1,096
Finished Goods	1,932	1,056
	-----	-----
	5,994	2,185
Less reserves for excess inventory	(600)	(117)
	-----	-----
	\$ 5,394	\$ 2,068
	=====	=====

6. Line of Credit

On June 2, 2006, the Company secured a \$3.6 million revolving line of credit by entering into an Account Purchase Agreement (the "Agreement") with Wells Fargo Bank, National Association ("Wells Fargo"). Pursuant to the Agreement, the Company may sell up to \$3.6 million of eligible accounts receivable to Wells Fargo. Advances are limited to 80% of the eligible receivables. The amount actually collected on any receivable by Wells Fargo that is beyond the advance will be forwarded to the Company, less certain discounts and fees retained by Wells Fargo (including a minimum fee of \$7,500 per month for the term of the Agreement). To secure the Company's obligations under the Agreement, the Company granted Wells Fargo a security interest in certain of the Company's property. The Agreement has a term of two years, but may be terminated at any time by the Company upon 60 days' written notice. As of September 30, 2006, the Company had financed receivables with Wells Fargo for approximately \$917,000.

7. Convertible Debentures

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On July 1, 2002, the Company received funding of \$3,000,000 in a financing transaction with Renaissance Capital Growth & Income Fund III, Inc., Renaissance US Growth Investment Trust PLC and US Special Opportunities Trust PLC. RENN Capital Group, Inc. is the agent for the RENN investment funds. One of the Company's directors holds the position of Senior Vice President of RENN Capital Group. The \$3,000,000 funding consists of convertible debentures with a 7-year term at a 7.5% per annum interest rate. Each fund equally invested \$1,000,000. The holder of the debenture shall have the right, at any time, to convert all, or in multiples of \$100,000, any part of the Debenture into fully paid and nonassessable shares of Simtek Corporation common stock. The debentures were originally convertible into Simtek common stock at \$3.12 per share, which was in excess of the market price per share on July 1, 2002. At March 31, 2006, the Company was not in compliance with two of the covenants set forth in the loan agreement. In order to obtain a waiver for the covenants, the Company issued the debenture holders a total of 5,000 warrants for receipt of the waiver. Through September 30, 2006, the Company was not in compliance with two of the covenants set forth in the loan agreement. These covenants relate to the interest coverage ratio and debt to equity ratio. On November 10, 2006, the Company received a waiver for the two covenants through October 1, 2007. However, significant variances in future actual operations from the Company's current estimates could result in the reclassification of this note to current liabilities. The Convertible Debentures allows for an adjustment in the conversion price, if the Company issues Common Stock in connection with an equity financing, where the sale price is less than the conversion price of \$3.12. This occurred in December 2005 in connection with the common stock sale of \$11,000,000 at a price of \$1.60 per share. Pursuant to the terms of the 2002 convertible debentures, the Company agreed with the RENN Capital Group that the conversion price would be reduced to \$2.20 per share. Based on the conversion rate of \$2.20 per share, each RENN investment fund is entitled to 409,091 shares upon conversion.

On June 28, 2005, the Company received a waiver from the debenture holders extending until July 1, 2006 the commencement date for principal payments of the \$3 million aggregate principal amount. The original terms of the debentures required the Company to make monthly principal payments of \$10 per \$1,000 of the then remaining principal amount, beginning on June 28, 2005. The Company will

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SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

still be required to make interest payments. Under the terms of the waiver, monthly principal payments of \$13.33 per \$1,000 of the then remaining outstanding principal amount were to commence on July 1, 2006. The final maturity date remains as June 28, 2009. As consideration for the extension, the Company has issued to the debenture holders warrants to purchase 20,000 shares of Simtek common stock at \$5.00 per share, a premium to the market price on the date of the waiver. The Company estimated the value of the warrants at the time of grant, using the Black Scholes option-pricing model, to be approximately \$62,000. The Company recognized \$12,000 as additional interest expense for the nine months ending September 30, 2006. On July 24, 2006, each of the debenture holders converted \$100,000 of the amount due into 45,455 shares of the Company's common stock in lieu of the Company making the principal payment it was required to make on July 1, 2006.

8. Non-Refundable Prepaid Royalties

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On March 24, 2006, the Company entered into a License and Development Agreement with Cypress pursuant to which, among other things, Cypress agreed to license certain intellectual property from the Company to develop and manufacture standard, custom and embedded nvSRAM products and Cypress has agreed to pay to the Company \$4,000,000 in non-refundable pre-paid royalties of which \$2 million was paid upon signing of the agreement and \$1 million was paid on June 30, 2006 and \$1 million will be paid on December 31, 2006. In addition, the Company licensed rights to use certain intellectual property from Cypress for use in its products. As part of the License and Development Agreement, the Company agreed to issue Cypress warrants to purchase 2 million shares of the Company's common stock for \$7.50 per share. The warrants have a ten year life. The warrants will be issued upon receipt of each of the prepaid royalty amounts. As of September 30, 2006, the Company had received \$3,000,000 from Cypress in pre-paid royalties, in exchange for which the Company has issued warrants to purchase 1.5 million shares of common stock. The value of the warrants issued of \$1,482,000 was determined by an independent valuation firm and has been recorded as an increase in additional paid in capital. The net balance of the non-refundable prepaid royalties of \$1,035,000 for the March 31, 2006 payment and \$483,000 for the June 30, 2006 payment were recognized as revenue at the time the payments were received.

9. Geographic Concentration

Sales of the Company's semiconductor products by location for the three month and nine month periods ended September 30, 2006 and 2005 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
United States	29%	29%	23%	27%
Europe	23%	20%	27%	19%
Far East	41%	43%	42%	44%
All Others	7%	8%	8%	10%
	-----	-----	-----	-----
	100%	100%	100%	100%
	=====	=====	=====	=====

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SIMTEK CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

10. Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) net of tax is as follows:

	Foreign Currency Translation Adjustment
Balance at January 1, 2006	\$ -
Current period change	80

Balance September 30, 2006	\$ 80

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11. Discontinued Operation

On August 30, 2005, the Company, along with the Company's wholly-owned subsidiary, Q-DOT, Inc. ("Q-DOT"), entered into an Asset Purchase Agreement with Hittite Microwave Corporation ("Hittite") and a wholly-owned subsidiary of Hittite, HMC Acquisition Corporation ("HMC Acquisition"), whereby substantially all of the assets of Q-DOT were sold to HMC Acquisition in exchange for a cash payment of approximately \$2.2 million. The Company realized a net gain of approximately \$1,689,000. In addition, Hittite assumed certain future obligations of Q-DOT, including obligations related to Q-DOT's real estate lease and certain software license agreements. Incident to the Asset Purchase Agreement, the parties also entered an Escrow Agreement, whereby \$200,000 of the purchase price was placed in escrow for one year to secure certain indemnification obligations of Simtek and Q-DOT. In addition, the parties entered into a Confidentiality, Non-Disclosure and Restrictive Covenant Agreement, whereby, among other things, Simtek and Q-DOT agreed not to compete against Hittite and HMC Acquisition for a period of four years with respect to certain businesses relating to Q-DOT's operations. On September 1, 2006, the Company received the \$200,000 that was placed in the escrow account.

In accordance with SFAS No. 144, the consolidated financial statements of the Company have been recast to present this business as a discontinued operation. Accordingly, the revenues, the costs and expenses and assets and liabilities of the discontinued operation have been excluded from the respective captions in the accompanying Consolidated Statements of Operations and Consolidated Balance Sheets. In addition, certain of the Notes to the Consolidated Financial Statements have been recast for all periods to reflect the discontinuance of this operation.

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SIMTEK CORPORATION

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

The following discussion and analysis in this quarterly report on Form 10-Q is intended to provide greater details of the results of operations and financial condition of our Company. The following discussion should be read in conjunction with our condensed consolidated financial statements and notes thereto and other financial data included elsewhere herein. Certain statements under this caption constitute forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The reader should not place undue reliance on these forward looking statements for many reasons including those risks discussed in this document. In addition, when used in this quarterly report, the words "believes," "anticipates," "expects," "plans," "intends" and similar expressions are intended to identify forward-looking statements. Forward-looking statements and statements of expectations, plans and intent are subject to a number of risks and uncertainties. Actual results in the future could differ materially from those described in the forward-looking statements, as a result, among other things, of changes in technology, customer requirements and needs. We undertake no obligation to release publicly the results of any revisions to these forward-looking statements that may be made to reflect any future events or circumstances.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which require us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and the related disclosures. Our accounting policies are discussed in Note 1 of the Notes to Consolidated Financial Statements included in our 2005 Form 10-K. The estimates used by us are based upon our historical experiences combined with our understanding of current facts and circumstances. Certain of our accounting policies are considered critical as they are both important to the portrayal of our financial condition and the results of our operations and require significant or complex judgments on our part. We believe that the following represent the critical accounting policies of Simtek as described in Financial Reporting Release No. 60, Cautionary Advice Regarding Disclosure About Critical Accounting Policies, which was issued by the Securities and Exchange Commission: inventories; deferred income taxes; allowance for doubtful accounts; and, allowance for sales returns.

Product sales revenue is recognized when a valid purchase order has been received with a fixed price and the products are shipped to customers FOB origin (Colorado Springs, Colorado or Dresden, Germany), including distributors. Based on historic business with the majority of our customers and, in the case of new customers, we are reasonably assured that collectibility on our shipments will occur.

Revenue from royalties related to non-refundable prepaid royalty payments is recognized upon receipt. Revenue from royalties related to sales of products by license partners is recognized upon the notification to us of shipment of product from our technology license partners to direct customers and collectibility is reasonable assured.

The allowance for doubtful accounts reflects a reserve that reduces

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

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We record an allowance for sales returns as a net adjustment to customer accounts receivable. The allowance for sales returns consists of two separate segments, distributor stock rotation and distributor price reductions. When we record the allowance, the net method reduces customer accounts receivables and gross sales. Generally, we calculate the stock rotation portion of the allowance based upon actual reported distributor inventory levels. The contracts we have with certain of our distributors generally allow them to return to us 5% percent of their inventory every 6 months, in exchange for inventory that better meets their demands. At times, our distributors reduce the selling price of a specific device in order to meet competition related to a specific end customer program, which we support through a credit back to the distributor for that specific program. When this occurs, we record an allowance for potential credit that our distributors will be requesting. This allowance is based on approved pricing changes, inventory affected and historical data. We believe that our processes to adequately predict our allowance for sales returns are effective in quantifying our exposures due to industry or specific customer conditions.

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

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

We assess the impairment of long-lived assets when events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. Factors that we consider in deciding when to perform an impairment review include significant under-performance of the business in relation to

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expectations, significant negative industry or economic trends, and significant changes or planned changes in our use of the assets. Recoverability of assets that will continue to be used in our operations is measured by comparing the carrying amount of the assets to our estimate of the related future net cash flows. If the asset's carrying amount is not recoverable through the related cash flows, the asset is considered to be impaired. The impairment is measured by the difference between the asset's carrying amount and its fair value, based on the best information available, including market prices or discounted cash flows.

Goodwill represents the excess of the purchase price over the fair value of identifiable net tangible and intangible assets acquired in the acquisition of the nvSRAM assets from ZMD. Goodwill is required to be tested for impairment. This assessment requires estimates of future revenue, operating results and cash flows, as well as estimates of critical valuation inputs such as discount rates, terminal values and similar data. We will continue to perform periodic and annual impairment analyses of goodwill. As a result of such impairment analyses, impairment charges may be recorded and may have a material adverse impact on our financial position and operating results. Additionally, we may make strategic business decisions in future periods which impact the fair value of goodwill, which could result in significant impairment charges. There can be no assurance that future goodwill impairments will not occur.

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

SIMTEK CORPORATION

Overview

Total revenue for the three and nine months ended September 30, 2006 was \$8.3 million and \$21.0 million, respectively, including \$1.5 million of royalty revenue for the nine months ended September 30, 2006. Total unit shipments of our semiconductor memory products increased in both the three and nine month periods compared to the 2005 periods. Our net product revenue was \$8,251,000 and \$19,436,000 for the three and nine months ended September 30, 2006, respectively, up from \$2,412,000 and \$7,591,000 for the comparable periods of 2005, an approximate 242% and 156% increase, respectively. This increase was due primarily to increased product demand and the addition of revenue from customers previously serviced by ZMD prior to the acquisition of the nvSRAM product line from ZMD in December 2005.

Increased operating expenses had an impact on our profitability for the three and nine months ended September 30, 2006 compared to the three and nine months ended September 30, 2005. The increase in operating expenses includes non-cash charges of \$446,000 and \$1,339,000 for amortization of the non-compete

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agreement with ZMD and \$139,000 and \$417,000 for expenses related to employee stock options, for the three and nine months ended September 30, 2006, respectively. Operating expenses also included first-time operating expenses of \$580,000 and \$1,074,000 for our European subsidiary, Simtek GmbH, for the three and nine months ended September 30, 2006, respectively.

Simtek reported a net loss for the three months ended September 30, 2006 of \$249,000. However, excluding the amortization of the non-compete agreement with ZMD of \$446,000 and expense related to stock options of \$139,000, Simtek achieved a net profit of \$317,000 for the quarter. This non-GAAP measure of financial performance is important because it highlights the progress Simtek has made in improving its operating results. The non-GAAP results are also directly comparable to the third quarter of 2005 in which Simtek posted a loss from continuing operations of \$1,718,000.

Results of Operations:

Revenues

The following table sets forth our net revenues for semiconductor devices by product markets for the three and nine months ended September 30, 2006 and 2005 (in thousands):

	Three Months Ended September 30,			Nine Months E September 3	
	2006 ----	2005 ----	Variance -----	2006 ----	2005 ----
Commercial	\$ 7,754	\$ 2,171	\$ 5,583	\$17,736	\$ 6,387
High-end industrial and military	497	241	\$ 256	\$ 1,700	\$ 1,204
Total Semiconductor Revenue	\$ 8,251	\$ 2,412	\$ 5,839	\$19,436	\$ 7,591

Commercial revenues include revenue generated from our 0.8-micron products built from silicon wafers received from Chartered Semiconductor or purchased as finished units from ZMD, and from our 0.25-micron products built from silicon wafers received from Dongbu Electronics (DBE). Commercial revenues increased by \$5,583,000 and \$11,349,000 for the three and nine months ended September 30, 2006 as compared to the three and nine months ended September 30, 2005. As stated previously, this increase was due primarily to increased unit demand and the addition of revenue from customers previously serviced by ZMD prior to the acquisition of the nvSRAM product line from ZMD in December 2005.

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High-end industrial and military product revenues accounted for an increase of approximately \$256,000 and \$496,000 for the three and nine months ended September 30, 2006 as compared to the same period in 2005. The increase was due to the addition of new customer demand for our products and increased pricing to certain of our customers for industrial and military products.

The following table sets forth the unit volumes for each period in thousands of units:

	Three Months Ended September 30,			Nine Months Ended September 30,	
	2006	2005	Variance	2006	2005
0.8 micron 256K devices	1,551	407	1,144	4,076	1,153
0.25 micron devices	178	37	141	269	73
Other devices	469	166	303	1,187	571
	-----	-----	-----	-----	-----
Total Units	2,198	610	1,588	5,532	1,797
	=====	=====	=====	=====	=====

One distributor and two direct customers accounted for approximately 36% and 28% of our revenue for the three and nine months ended September 30, 2006, respectively. Products sold to distributors are sold without material recourse. Distributors sell our products to various end customers. If this distributor was to terminate its relationship with us, we believe that there would not be a material impact on our product sales, as we believe that we would be able to service these various end customers through other distributors.

Cost of Sales and Gross Profit

We recorded cost of sales of \$4,979,000 and \$13,016,000 for the three and nine months ended September 30, 2006, respectively as compared to \$1,807,000 and \$5,490,000 for the comparable periods in 2005. The resulting product gross margin percentages for the three and nine months ended September 30, 2006 were 40% and 33%, respectively and 25% and 28% for the three and nine months ended September 30, 2005, respectively. The overall improvement in gross margin percentages is due to: (i) increased volume; (ii) higher overall average selling prices; and (iii) continued cost reductions in the 1 megabit device. We expect to see gross margins increase in the next several quarters, as average selling prices continue to increase, unit costs for all 0.25 micron devices continues to be reduced, and the benefits of moving final test operations offshore to more cost effective locations.

Research and Development

In order to maintain our growth, we must continue to invest in new product development and to increase the percentage of the overall nvRAM market that our products serve. In July 2006, we completed full qualification of the 1 megabit device with real time clock and the 0.25 micron 256 kilobit device both with and without the real time clock feature. Thus all of our 0.25 micron based products

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are fully qualified. We anticipate that we will continue to invest in the next several months in continued cost reductions, yield enhancements, and back end test efficiencies.

In May 2005, we began joint development of our next generation nvSRAM product family, in conjunction with Cypress, pursuant to the terms of the May 5, 2005 development agreement. This new product family will be based on Cypress' 0.13-micron "S8" process and we expect it will include memory densities up to and beyond 4-megabits. In the first half of 2006 we achieved our third major

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milestone under the development agreement, as scheduled. For the three and nine months ended September 30, 2006, we recognized expenses related to the Cypress development of \$0 and \$642,000, respectively. In 2005, the expense was \$564,000 and \$612,000 for the three and nine month periods, respectively.

As part of our strategic product development activities, on March 24, 2006, Simtek entered into a License and Development Agreement with Cypress which expands the agreement the two companies signed in May 2005. Under the terms of the new agreement:

- o Cypress will retain the right to include nvSRAM functionality on future programmable system-on-chip (PSoC(TM)) and customized integrated circuits originally granted in the May 2005 agreement, now with clearly defined royalty payments to Simtek for the use of its SONOS-based nvSRAM intellectual property;
- o Simtek is granted the right to use certain intellectual property of Cypress in developing future generation nvSRAM products, including the jointly developed 0.13u SONOS-based CMOS process, advanced SRAM intellectual property, design-related intellectual property, design-for-manufacturability know-how and other intellectual property related to Cypress' advanced CMOS manufacturing processes and procedures;
- o Simtek and Cypress agree to broad manufacturing support terms that will provide Simtek with a range of industry-leading manufacturing skills and know-how to enable cost-effective manufacturing of leading-edge SONOS nvSRAMs;
- o Simtek and Cypress will extend the deployment of Simtek's proprietary nvSRAM technology, and work to establish SONOS as the preferred technology for high reliability, high endurance, and scaleable non-volatile products at 65nm and below;
- o Simtek and Cypress will jointly develop and market a family of products utilizing Simtek's patented SONOS-based non-volatile technology for production using Cypress's advanced manufacturing processes.

Upon signing the agreement, Simtek received \$2 million from Cypress. Simtek

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also received an additional payment of \$1 million on June 30, 2006 and will receive an additional payment of \$1 million on December 31, 2006. The agreement also calls for Simtek to issue warrants to Cypress to purchase a total of 2 million shares of its common stock, 1 million of which were already issued upon the execution of the agreement, 500,000 of which were issued on June 30, 2006 upon the payment by Cypress of certain royalties and 500,000 of which are expected to be issued on December 31, 2006 upon the payment by Cypress of certain royalties. The warrants have, or will have, an exercise price of \$7.50 per share. Simtek believes that this new agreement will accelerate the timing of expanding nvSRAM adoption in new markets and shorten future product development cycle time. Please read Note 8 to the Condensed Consolidated Financial Statements for a discussion of the accounting treatment for the transactions related to this agreement.

Total research and development expenses were \$1,351,000 and \$4,578,000 for the three and nine months ended September 30, 2006, respectively, as compared to \$1,572,000 and \$4,697,000 for the three and nine months ended September 30, 2005, respectively.

The \$221,000 decrease for the three month period was primarily due to a decrease in product development costs of \$641,000 which included decreased costs related to the joint development with Cypress discussed previously. The decrease was offset by an increase in payroll related costs of \$252,000, including the engineering staff at Simtek GmbH and expenses related to stock options, equipment related expenses of \$148,000 and travel of \$17,000 for engineers traveling to and from Simtek GmbH. The decrease in product development costs was due to the timing of costs related to the joint development with Cypress

The \$119,000 decrease for the nine month period was primarily due to a decrease of \$768,000 for the charges related to the development of our .25

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micron product that we incurred in 2005 and a decrease of \$61,000 related to contract services. These decreases were partially offset by increases in payroll related costs of \$571,000, and travel of \$72,000.

General and Administration

Total general and administration expenses were \$838,000 and \$2,595,000 for the three and nine months ended September 30, 2006, respectively, as compared to \$412,000 and \$1,759,000, respectively, for the same periods in 2005.

The \$426,000 increase for the three month period was primarily due to increases in payroll related costs of \$80,000, accounting and legal expenses of \$215,000, contract services of \$14,000, travel of \$28,000 and other miscellaneous expenses of \$89,000. The increases in audit and legal expenses and contract services were primarily related to costs incurred for our securities related work. The increase in payroll related costs were related to increased headcount in both our Colorado Springs and Germany offices and expenses related to stock option grants.

The \$836,000 increase for the nine month period was primarily due to

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increases of \$498,000 in payroll related costs, \$363,000 in legal and audit fees, contract services of \$81,000, travel of \$103,000, bad debt expense of \$30,000 and other miscellaneous expenses of \$81,000. The increases were partially offset by a decrease of \$320,000 in one-time costs related to separation and employment agreements that were incurred in the first six months of 2005. The increases in legal and audit fees and contract services were primarily related to expenses related to our shareholder meeting, securities related work and the license agreement entered into with Cypress in March 2006. The increases in payroll and payroll overhead costs were due to increased headcount in both our Colorado Springs and Germany offices and for the expenses related to stock option grants.

Sales and Marketing

Total sales and marketing expenses were \$1,250,000 and \$3,233,000 for the three and nine months ended September 30, 2006, respectively, as compared to \$321,000 and \$1,164,000, respectively, for the same periods in 2005.

The increases for the three and nine month periods were due to the amortization of the non-compete agreement discussed in Note 1 to the Condensed Consolidated Financial Statements of \$446,000 and \$1,339,000, increase in payroll related costs of \$310,000 and \$523,000, respectively, and an increase in sales commissions of \$146,000 and \$181,000, respectively. The increase in payroll related costs were directly related to increased headcount and the increase in sales commissions was related to the higher revenue.

Loss from Continuing Operations

We recorded a net loss, from continuing operations, of \$249,000 and \$2,605,000 for the three and nine months ended September 30, 2006, respectively, as compared to \$1,718,000 and \$5,641,000 for the three and nine months ended September 30, 2005, respectively. The decreases of \$1,469,000 and \$3,036,000 for the three and nine month periods reflect the revenue and expense items discussed above.

Liquidity and Capital Resources

As of September 30, 2006, we had a net working capital of \$9,923,000 as compared to a net working capital of \$3,591,000 as of December 31, 2005.

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On September 21, 2006, we raised gross proceeds of \$4,555,000 in a private placement. We issued 1,153,171 shares of our common stock at a per share price of \$3.95 and 172,981 warrants to purchase common stock. The warrants have a per share exercise price of \$5.40 and a five-year term. We anticipate using the proceeds for general working capital and to produce silicon wafers to support

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revenue growth. The shares have been included in the Consolidated Balance Sheet as Temporary Equity, because of the potential penalties associated with the Registration Rights Agreement.

As discussed previously, on March 24, 2006, we entered into a License and Development Agreement with Cypress pursuant to which, among other things, Cypress has agreed to license certain intellectual property from us to develop and manufacture standard, custom, and embedded nvSRAM products. Cypress agreed to pay to Simtek royalties across all products they develop and sell which include intellectual property licensed from Simtek. We agreed to license from Cypress certain of their intellectual property for use in our design efforts. We agreed with Cypress to co-develop certain nvSRAM products and Cypress has agreed to pay us \$4 million in nonrefundable prepaid royalties, \$2 million of which was received at the time the contract was executed. On June 30, 2006, we received the second installment of \$1,000,000 and the remaining \$1 million is scheduled to be paid on December 31, 2006. In addition, we agreed with Cypress to work together to develop new products and processes. Please read Note 8 to the Condensed Consolidated Financial Statements for a discussion of the accounting treatment for the transactions related to this agreement.

Cash flows used in operating activities from continuing operations for the nine months ended September 30, 2006 were \$5,568,000 compared to \$2,939,000 in the same period in 2005, an increase of \$2,629,000. The net increase is primarily due to investment in working capital to support revenue growth. The key components of the cash (uses) and sources in working capital are as follows, in thousands of dollars:

	2006	2005	Change
	-----	-----	-----
Accounts receivable	\$(3,687)	\$ 1,447	\$(5,134)
		\$	
Inventory	\$(3,799)	\$ 575	\$(4,374)
Accounts payable	\$ 466	\$ (366)	\$ 832

The increase in working capital was partially off set by the reduction in net loss for the 2006 period of \$2.6 million from \$3.9 million in the 2005 period, the amortization of the non-compete agreement in 2006 of \$1.3 million and the \$1.7 million gain from discontinued operations in the 2005 period.

Cash flows used in investing activities from continuing operations increased for the nine months ended September 30, 2006 by approximately \$2,690,000 as compared to the same period in 2005. The increase was primarily the result of the purchase of equipment and furniture for our facility in Germany and test equipment for our research and development, which was offset by proceeds from discontinued operations of \$1.9 million recorded in the 2005 period.

The increase of \$7,071,000 in cash flows provided by financing activities from continuing operations was primarily due to the net proceeds from our September 2006 equity financing of \$4.55 million, the value assigned to the warrants issued to Cypress under the License and Development Agreement and receipt of funds related to the sale of common stock completed on December 30, 2005, for which some funds were received on January 3, 2006.

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Short-term liquidity.

Our unrestricted cash balance at September 30, 2006 was \$3,653,000.

Our future liquidity will depend on our revenue growth and our ability to generate cash flow from operations. Through December 31, 2006, we expect to spend approximately \$4,000,000, for operating expenses and working capital. We expect to meet these cash needs from cash generated by operations, the funds still due to us from Cypress under the Joint Development and License Agreement, and from our existing cash reserves and credit facility with Wells Fargo. Management believes that the current cash reserves and additional cash generated from operations will be sufficient to meet the cash flow needs for at least the next twelve months.

Long-term liquidity.

The Company has experienced significant revenue growth over the nine months ended September 30, 2006 and expects that growth trend to continue for the foreseeable future. With the improved financial results and current cash and credit reserves, management believes that it has sufficient capital to meet its operating cash requirements. However, should the company identify possible strategic opportunities, it may need to raise additional capital to exploit such opportunities. While the Company has no specific plans, management is constantly looking for new strategic product and technology opportunities that may provide significant revenue growth in the future.

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ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk represents the risk of loss that may impact our financial position, results of operations or cash flows due to adverse changes in financial and commodity market prices and rates. We are exposed to market risk in the areas of changes in United States interest rates and changes in foreign currency exchange rates as measured against the United States dollar. These exposures are directly related to our normal operating activities. We currently have no derivative financial instruments.

Interest payable on our convertible debentures is fixed at 7.5% over the term of the debentures. As such, changes in interest rates will not affect future expenses or cash flows.

We manage interest income by investing our excess cash in cash equivalents bearing variable interest rates, which are tied to various market indices. We do not believe that near-term changes in interest rates will result in a material effect on future earnings, fair values or cash flows.

We do not speculate in the foreign exchange market and do not manage exposures that arise in the normal course of business related to fluctuations in foreign currency exchange rates by entering into offsetting positions through the use of foreign exchange forward contracts.

Average selling prices of our products have not increased significantly as a result of inflation during the past several years, primarily due to intense competition within the semiconductor industry. The effect of inflation on our costs of production has been minimized through improvements in production efficiencies. We anticipate that these factors will continue to minimize the effects of any foreseeable inflation and other price pressures within the industry and markets in which we participate.

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ITEM 4 CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures.

Harold Blomquist, who serves as the Company's chief executive officer, and Brian Alleman, who serves as the Company's chief financial officer, after evaluating the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this quarterly report (the "Evaluation Date") concluded that as of the Evaluation Date, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported as specified in the SEC's rules and forms and to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is accumulated and communicated to our management to allow timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting.

There were no changes in the Company's internal control over financial reporting during the three months ended September 30, 2006, that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings -None

Item 1A. Risk Factors - The following new risk factors (each of which has been previously disclosed) represent material changes from the old risk factors set forth in Simtek's 10-K:

Old Risk Factor	New Risk Factor
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LIMITED OPERATING CAPITAL AND ABILITY TO RAISE ADDITIONAL MONEY MAY HARM OUR ABILITY TO DEVELOP AND MARKET PRODUCTS

We require significant capital for product development,

OUR LIMITED OPERATING CAPITAL AND ADDITIONAL MONEY MAY HARM OUR ABILITY TO DEVELOP AND MARKET OUR PRODUCTS AS WELL AS SUPPORT

To date, we have required si

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subcontracted production, and marketing. We have funded these needs from the sale of products, the sale of product and technology licenses, from royalties, as well as from the sale of our convertible debt and equity securities.

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

development, subcontracted production, and marketing. We have funded these from the sale of products, the sale of product and technology licenses and from the sale of our convertible debt securities.

In recent months, we have experienced revenue growth. In order to support this growth, we have ordered more silicon wafers than we can sell. The cash required for inventory purchases, has been greater than the cash generated from sales. Therefore, our cash requirements have been difficult to maintain. We may need more capital in the future to develop new products and market existing products. We cannot guarantee that we will be able to raise more capital on reasonable terms, if at all. If we cannot, then we may not be able to develop and market new products. The development, subcontracted production and marketing of existing products may also suffer, causing our financial position and stock price to deteriorate.

WE MAY BE UNABLE TO SUCCESSFULLY INTEGRATE THE ASSETS
ACQUIRED FROM ZMD ON DECEMBER 30, 2005

[Intentionally Omitted (i.e., risk factors)]

On December 30, 2005, we closed our acquisition from ZMD of certain intellectual property and assets related to ZMD's nvSRAM product line. We may be unable to integrate successfully into our operations the assets acquired from ZMD, including:

- o by a failure to gain customer agreement to purchase products from us or to qualify our designs or processes;
- o by a failure to coordinate international operations, relationships and facilities, which may be subject to additional constraints imposed by geographic distance, local laws and regulations; and
- o by a failure to implement and maintain uniform standards, internal controls, business processes, procedures, policies and information systems.

Our failure to meet any of these challenges could cause us to fail to realize any accretive benefits of the acquisition of the assets from ZMD and could seriously harm our results of operations.

SIMTEK CORPORATION

WE MAY BE UNABLE TO RETAIN AN EFFECTIVE FOCUS IN OUR
INDUSTRY OR RETAIN CUSTOMERS FOLLOWING THE ACQUISITION OF
ASSETS FROM ZMD

[Intentionally Omitted (i.e., risk factors)]

The challenges to us as a result of the acquisition of certain intellectual property and assets from ZMD on

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December 30, 2005 include:

- o communicating a strategic vision to the market regarding us and executing on that strategic vision;
- o implementing sales and marketing efforts to effectively communicate to customers our capabilities;
- o overcoming possible concerns of certain customers about not having two sources of supply for the products they previously purchased from both ZMD and us;
- o gaining acceptance from former ZMD customers for our designs, products or processes; and
- o overcoming any perceived adverse changes in business focus, including demonstrating to customers that the acquisition of certain assets from ZMD will not result in an adverse change in customer service standards or business focus and helping customers conduct business easily with us going forward.

The failure to meet any of these challenges could seriously hinder our plans for product development as well as business and market expansion following the acquisition of certain intellectual property and assets from ZMD.

[Intentionally Omitted (i.e., risk factor did not exist)]

The Registration Rights Agreement of the September 21, 2006 Securities Purchase Agreement amounting to \$4,555,000, whereby the investors therein would receive certain amounts of penalty shares if certain conditions followed or an effective Registration Statement was not maintained for the shares purchase. The penalties are 2% of the shares purchased under the warrants issued that a breach occurs. We cannot assure that we will be able to follow the required procedures to maintain such effective Registration Statement.

[Intentionally Omitted (i.e., risk factor did not exist)]

OUR CERTIFICATE OF INCORPORATION AND BYLAWS PROVIDE THAT WE WILL OPERATE AS AN ANTI-TAKEOVER PROTECTION COMPANY TO DISCOURAGE TAKEOVER ATTEMPTS AND TO MAINTAIN THE PRICE OF OUR COMMON STOCK.

We have opted to be governed, under the laws of the State of Delaware, by Section 203 of the Delaware General Corporation Law, which provides for certain business combination transactions with "interested stockholders" (generally, persons

15% or more of the corporation's outstanding common stock. Although we believe that Section 203 provides a significant barrier to a potential acquirer to negotiate with

Section 203 also might have the effect of reducing the ability of a potential acquirer to acquire the company for the company in which all stock is owned equally. In addition, Section 203 might cause us to reject a proposed business combination even though a potential acquirer might offer a significant premium for our common stock over the current market price. Section 203 would also discourage potential acquirers who are unwilling to comply with its provisions.

Because a proposed amendment to our charter of incorporation may not be submitted to the board without the approval of the board, we may be unable to remove any provisions in our charter that have anti-takeover effects or to change our board of directors, which in turn could have anti-takeover effects.

[Intentionally Omitted (i.e., risk factor did not exist)]

THE REVERSE SPLIT MAY NOT RESULT IN A SIGNIFICANTLY HIGHER STOCK PRICE AND MAY NOT LEAD TO AN IMPROVEMENT IN OUR (INCLUDING QUALIFICATION FOR LISTING ON THE NASDAQ CAPITAL MARKET) THAT WE INTENDED TO ACHIEVE BY SUCH REVERSE SPLIT

There can be no assurance that the reverse split will result in a capitalization of our common stock that will cause the price of all our common stock at the time of the reverse split to move back below the total market capitalization of our common stock. A reverse split, that the per share price of our common stock will not drop back below the price of our common stock before the reverse split or that the price of our common stock will increase to a price that is inverse to the one-for-ten reduction in the number of shares of our common stock outstanding before the reverse split.

The per share market price of our common stock may not be high enough to attract institutional investors or to satisfy the requirements of such investors and, consequently, the price of our common stock may not improve. The per share market price of our common stock may not be high enough to allow us to comply with the listing requirements of the NASDAQ Capital Market. Even if the per share price of our common stock is sufficiently high to meet the listing requirements, we cannot guarantee that we will be able to satisfy the other requirements for listing on the NASDAQ Capital Market or the American Stock Exchange. Other requirements include, among other things, a minimum number of shares that must be in the public float and a minimum number of round lot holders.

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SIMTEK CORPORATION

- Item 2. Unregistered Sales of Equity Securities and Use of Proceeds - None
- Item 3. Defaults upon Senior Securities - None
- Item 4. Submission of Matters to a Vote of Security Holders - None
- Item 5. Other Information - None
- Item 6. Exhibits
 - 10.1 Securities Purchase Agreement, dated as of September 21, 2006, by and between Simtek Corporation and each purchaser identified on the signature pages thereto (the "Purchasers"), incorporated by reference to the Company's Current Report on Form 8-K filed by the Company with the SEC on September 25, 2006.
 - 10.2 Securities Purchase Agreement, dated as of September 21, 2006, by and between Simtek Corporation and each Purchaser, incorporated by reference to the Company's Current Report on Form 8-K filed by the Company with the SEC on September 25, 2006.
 - 10.3 Form of Stock Purchase Warrant, dated as of September 21, 2006, by and between Simtek Corporation and each Purchaser, incorporated by reference to the Company's Current Report on Form 8-K filed by the Company with the SEC on September 25, 2006.
 - 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 of Principal Executive Officer
 - 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 of Principal Financial Officer
 - 32.1 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 of Principal Executive Officer
 - 32.2 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 of Principal Financial Officer

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SIMTEK CORPORATION

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.

SIMTEK CORPORATION
(Registrant)

November 14, 2006

By: /s/Harold Blomquist

HAROLD BLOMQUIST
Chief Executive Officer, President

November 14, 2006

By: /s/Brian Alleman

BRIAN ALLEMAN
Chief Financial Officer

