

3D SYSTEMS CORP  
Form 10-Q/A  
February 09, 2007

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q/A**

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

For the quarterly period ended March 31, 2006

OR

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

Commission File No. 0-22250

**3D SYSTEMS CORPORATION**

(Exact Name of Registrant as Specified in Its Charter)

**DELAWARE**  
(State or Other Jurisdiction of  
Incorporation or Organization)  
**333 THREE D SYSTEMS CIRCLE**  
**ROCK HILL, SOUTH CAROLINA**  
(Address of Principal Executive Offices)

**95-4431352**  
(I.R.S. Employer  
Identification No.)  
**29730**  
(Zip Code)

**(803) 326-3900**

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

**APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY  
PROCEEDINGS DURING THE PRECEDING FIVE YEARS:**

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes  No

**APPLICABLE ONLY TO CORPORATE ISSUERS:**

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

**Shares of Common Stock, par value \$0.001, outstanding as of April 28, 2006: 15,514,527**

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3D SYSTEMS CORPORATION

TABLE OF CONTENTS

PART I.	FINANCIAL INFORMATION		
	<u>Explanatory Statement Regarding Restatement</u>		i
	ITEM 1.	Financial Statements (Unaudited)	1
		<u>Condensed Consolidated Balance Sheets March 31, 2006 and December 31, 2005 (Restated)</u>	1
		<u>Condensed Consolidated Statements of Operations Three Months Ended March 31, 2006 and March 31, 2005 (Restated)</u>	2
		<u>Condensed Consolidated Statements of Cash Flows Three Months Ended March 31, 2006 and March 31, 2005 (Restated)</u>	3
		<u>Condensed Consolidated Statements of Comprehensive Income (Loss) Three Months Ended March 31, 2006 and March 31, 2005 (Restated)</u>	5
		<u>Notes to Condensed Consolidated Financial Statements (Restated) March 31, 2006</u>	6
	ITEM 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	45
	ITEM 3.	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	77
	ITEM 4.	<u>Controls and Procedures</u>	78
PART II.	OTHER INFORMATION		
	ITEM 1.	<u>Legal Proceedings</u>	83
	ITEM 1A.	<u>Risk Factors</u>	83
	ITEM 6.	<u>Exhibits</u>	85
<u>SIGNATURES</u>			86

**PART I**

**EXPLANATORY STATEMENT REGARDING RESTATEMENT**

**Restatement of Condensed Consolidated Financial Statements**

On November 3, 2006, we announced that management and the Audit Committee of our Board of Directors had determined, based on information presented by our management in connection with the preparation of our financial statements for the third quarter of 2006, that our financial statements included in our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2006 and June 30, 2006 contained errors. As a result, the Audit Committee concluded that those financial statements should be restated and that investors should not rely upon those financial statements without taking into account the anticipated adjustments described in our Current Report on Form 8-K filed on November 3, 2006 and the press release filed as an exhibit thereto. The adjustments described in that Form 8-K and related press release are reflected in our Quarterly Report on Form 10-Q for the quarter ended September 30, 2006 and in the restated financial statements included in this Form 10-Q/A.

We also announced on November 3, 2006 that we were assessing whether our financial statements for prior periods contained errors and as a result should be restated. On December 14, 2006, we announced that management and the Audit Committee had completed our assessment of the prior-period financial statements and that, based on information presented by our management, the financial statements included in our Annual Reports on Form 10-K for the 2004 and 2005 calendar years also contained errors and should be restated. In evaluating the need to restate those periods, we also took into consideration adjustments that had been identified previously as not being material to those periods and have included those adjustments in the restated amounts for the applicable 2005 and 2004 periods.

We identified the errors in the first and second quarter 2006 financial statements primarily as a result of our efforts to remediate the material weaknesses that we previously identified and disclosed in our second quarter 2006 Form 10-Q as well as through our ongoing efforts:

- (a) to implement our new ERP system;
- (b) to reconcile the records in our new ERP system and those in our legacy systems; and
- (c) to test our internal controls in the context of the new ERP system environment.

As part of these efforts, management:

- (i) has carried out a comprehensive account reconciliation initiative to test and verify the accuracy and integrity of information recorded by, and data imported and input from our legacy accounting system into, the new ERP system;
- (ii) is continuing to train employees in the use of the new ERP system and our established system of internal controls; and
- (iii) is continuing to promote strict adherence to those established internal controls.

We have also performed physical inventory counts and undertaken and completed a variety of other confirmatory procedures. See Part I, Item 4, Controls and Procedures.

This Quarterly Report on Form 10-Q/A includes the restated financial information for each period affected by the restatement through March 31, 2006. That information is also included in the Quarterly Report on Form 10-Q/A for the quarterly period ended June 30, 2006 and in the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 that we have filed with the Securities and Exchange Commission. Such restated financial information will also be included in our Annual Report on Form 10-K for the year ended December 31, 2006.

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The following table shows the impact of the correction of all errors on income (loss) available to common stockholders on a pretax basis for the full years ended December 31, 2004 and 2005 and for each calendar quarter thereafter through March 31, 2006. It also shows the cumulative impact of prior-period errors on the accumulated deficit in earnings at December 31, 2003, which errors were not material either individually or in the aggregate. The tax effect of the correction of these errors on each restated period was either minimal or nil.

	Accumulated Deficit in Earnings December 31, 2003 (Amounts in \$000s)	Effect of Restatement on Income (Loss) Available to Common Stockholders						Year Ended December 31, 2005	Quarter Ended March 31, 2006
		Year Ended December 31, 2004	Quarter Ended March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005	December 31, 2005		
Previously reported	\$ (47,442)	\$ 1,027	\$ 783	\$ 855	\$ 749	\$ 6,017	\$ 8,404	\$ (1,244)	
Adjustments:									
Credit memos		10	(19 )	(79 )	(164 )	(101 )	(363 )	(251 )	
Royalty income/expense		253	5	(17 )	(17 )	(293 )	(322 )	13	
Recognition of warranty and training revenue	32	220	11	(246 )	13	33	(189 )	121	
Stock issuance costs						211	211		
Prepaid materials reconciliation				(29 )	(4 )	(64 )	(97 )	(201 )	
Depreciation of fixed assets		(4 )	(19 )	(37 )	(42 )	(63 )	(161 )	(106 )	
Accrual for professional services						(15 )	(15 )	(247 )	
Inventory usage						22	22		
Other		(20 )	20	44	(2 )	(16 )	46	(86 )	
Tax provision	(191 )					191	191	53	
Total adjustments:	(159 )	459	(2 )	(364 )	(216 )	(95 )	(677 )	(704 )	
Restated	\$ (47,601)	\$ 1,486	\$ 781	\$ 491	\$ 533	\$ 5,922	\$ 7,727	\$ (1,948)	
Net income (loss) available to common stockholders per share diluted (as previously reported)		\$ 0.07	\$ 0.05	\$ 0.05	\$ 0.05	\$ 0.32	\$ 0.53	\$ (0.08 )	
Effect of restatement		0.04	(0.00 )	(0.02 )	(0.02 )	(0.00 )	(0.05 )	(0.05 )	
Net income (loss) available to common stockholders per share diluted (restated)		\$ 0.11	\$ 0.05	\$ 0.03	\$ 0.03	\$ 0.32	\$ 0.48	\$ (0.13 )	

As shown in this table, the errors that affect income (loss) available to common stockholders in each restated period primarily include:

- \$0.6 million in the aggregate of errors related to credit memoranda issued to customers, of which \$0.3 million was attributable to the first quarter of 2006, \$0.4 million was attributable to the 2005 periods and a nominal credit was attributable to 2004.
- \$0.3 million in the aggregate of errors related to the reconciliation of prepaid materials accounts from sub-ledger to general ledger, substantially all of which was attributable to the first quarter of 2006, and \$0.1 million of which was attributable to the 2005 periods.
- \$0.3 million in the aggregate of errors related to additional depreciation expense for items placed in service that had not been removed from construction-in-progress ( CIP ) accounts prior to the restatement, of which \$0.1 million was attributable to the first quarter of 2006, \$0.2 million was attributable to the 2005 periods and a nominal amount was attributable to 2004.
- \$0.3 million in the aggregate of errors in related to accrued professional services, which was primarily attributable to the first quarter of 2006.
- \$0.2 million in the aggregate of errors related to state and foreign income taxes, of which \$0.1 million was attributable to the first quarter of 2006 and \$0.2 million was attributable to the 2005 periods.

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The aggregate effect of these adjustments was to:

- increase net loss by \$0.7 million, or 56.6%, from \$1.2 million as originally reported to \$1.9 million as restated for the quarter ended March 31, 2006;

ii

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- decrease net income by \$0.7 million, or 8.1%, from \$8.4 million as originally reported to \$7.7 million as restated for the year ended December 31, 2005;
- for the respective quarters of 2005:
- decrease net income by 0.2% with net income of \$0.8 million both as originally reported and as restated for the quarter ended March 31, 2005;
- decrease net income by \$0.4 million or 42.6% and from \$0.9 million as originally reported to \$0.5 million as restated for the quarter ended June 30, 2005;
- decrease net income by \$0.2 million or 28.8% with net income of \$0.7 million as originally reported to \$0.5 million as restated for the quarter ended September 30, 2005; and
- decrease net income by \$0.1 million or 1.6% and from \$6.0 million as originally reported to \$5.9 million as restated for the quarter ended December 31, 2005; and
- increase net income by \$0.5 million, or 44.7%, for the year ended December 31, 2004 from \$1.0 million as originally reported to \$1.5 million as restated.

On a per share basis, the aggregate effect of these adjustments was to:

- increase diluted net loss per share by \$0.05 from \$0.08 to \$0.13 for the quarter ended March 31, 2006;
- decrease diluted net income per share by \$0.05 from \$0.53 as originally reported to \$0.48 as restated for the year ended December 31, 2005;
- for the respective quarters of 2005:
- there was no change to diluted net income per share for the quarter ended March 31, 2005;
- decrease diluted net income per share by \$0.02 from \$0.05 as originally reported to \$0.03 as restated for the quarter ended June 30, 2005;
- decrease diluted net income per share by \$0.02 from \$0.05 as originally reported to \$0.03 as restated for the quarter ended September 30, 2005;
- there was no change to diluted net income per share for the quarter ended December 31, 2005;
- the sum of diluted net income per share for the four 2005 quarters does not equal the diluted net income per share for the year ended December 31, 2005 due to changes in the weighted average shares outstanding at the end of each quarterly period, which were not affected by the restatement;
- increase diluted net income per share by \$0.04 from \$0.07 as originally reported to \$0.11 as restated for the year ended December 31, 2004.

Compared to the amounts originally reported, the restatement resulted in a \$0.2 million increase in cash and cash equivalents at March 31, 2006 that arose from the reclassification of certain unrestricted deposits previously erroneously recorded in prepaid expenses and other current assets.

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The restatement also resulted in a \$0.3 million increase in cash and cash equivalents at March 31, 2005, a \$0.2 million increase in cash and cash equivalents at June 30, 2005, September 30, 2005 and December 31, 2005 and a \$0.2 million increase in cash and cash equivalents at December 31, 2004 primarily as a result of the reclassification of certain amounts previously erroneously recorded as prepaid expenses and other current assets, as discussed above. See Note 2 to the Condensed Consolidated Financial Statements.

iii

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The restatement also resulted in a \$0.2 million reduction to the ending retained earnings balance at December 31, 2003 for errors related to prior periods that we believe are immaterial individually and in the aggregate.

As a result of the errors mentioned above, we have restated:

- our historical consolidated balance sheets as of December 31, 2004, the last calendar day for each quarter in 2005, including December 31, 2005, and the first two quarters in 2006;
- our consolidated statements of operations for the years ended December 31, 2004 and 2005, each quarter ended in 2005 and the first two quarters in 2006; and
- our consolidated statements of cash flows for the year ended December 31, 2004, the three, six and nine months ended March 31, 2005, June 30, 2005 and September 30, 2005, respectively, and for the year ended December 31, 2005, and the three and six months ended March 31, 2006 and June 30, 2006, respectively.

The restated consolidated financial information is set forth in Note 2 to the Condensed Consolidated Financial Statements below and is further discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations.

As disclosed in the Form 10-Q filed with respect to the period ended June 30, 2006, management determined that control deficiencies existed relating to the design and implementation of controls regarding our procedures for (a) reconciling and compiling the financial records and (b) processing and safeguarding of inventory that constituted, either individually or in the aggregate, material weaknesses in our internal control over financial reporting. In the course of our efforts to remediate those deficiencies and these weaknesses, we determined the existence of the errors discussed above, which led to the determination to carry out the restatement discussed above. We also identified additional control deficiencies with respect to the third quarter of 2006 that we believe, taken together with the material weaknesses that we previously disclosed in the second-quarter Form 10-Q, constitute individually or in the aggregate additional material weaknesses with respect to those matters. These additional deficiencies relate to (a) a deficiency in the invoicing and processing of accounts receivable and the application of customer payments and (b) deficiencies in the timeliness and accuracy of our period-end financial statement closing process and the monitoring of our accounting function and oversight of financial controls. We have taken steps to remediate certain of these deficiencies, and we are taking steps to remediate the others. See Part I, Item 4, Controls and Procedures, of this Form 10-Q/A for additional information.

As used in this Form 10-Q/A, the terms we, us, our and the Company refer to 3D Systems Corporation and our consolidated subsidiaries, and all dollar amounts other than per share amounts are in thousands, unless otherwise noted.

## Item 1. Financial Statements

**3D SYSTEMS CORPORATION**  
**Condensed Consolidated Balance Sheets**  
**March 31, 2006 and December 31, 2005**  
(in thousands, except par value)  
(unaudited)

	March 31, 2006 Restated	December 31, 2005 Restated
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 26,614	\$ 24,328
Accounts receivable, net of allowance for doubtful accounts of \$1,059 (2006) and \$990 (2005)	29,317	32,766
Inventories, net of reserves of \$1,158 (2006) and \$1,317 (2005)	16,344	14,810
Deferred tax assets, net	2,500	2,500
Prepaid expenses and other current assets	9,384	9,275
Total current assets	84,159	83,679
Property and equipment, net	13,324	11,992
Intangible assets, net	7,949	8,577
Goodwill	44,843	44,747
Restricted cash	1,200	1,200
Other assets, net	837	985
	\$ 152,312	\$ 151,180
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$ 217	\$ 207
Accounts payable	12,525	11,684
Accrued liabilities	12,486	12,316
Customer deposits	1,353	1,945
Deferred revenue	14,079	13,725
Total current liabilities	40,660	39,877
Long-term debt, less current portion	3,456	3,568
Convertible subordinated debentures	22,604	22,604
Other liabilities	1,024	1,001
	67,744	67,050
Authorized 5,000 preferred shares; Series B convertible redeemable preferred stock, authorized 2,670 shares, issued and outstanding 2,617 (2006 and 2005), mandatory redemption in 2013 (aggregate liquidation value of \$16,355)	15,257	15,242
Stockholders' equity:		
Common stock, \$0.001 par value, authorized 60,000 shares; issued and outstanding 15,638 (2006) and 15,302 (2005)	16	15
Additional paid-in capital	106,810	106,530
Deferred Compensation		(1,461 )
Treasury stock, at cost; 17 shares at March 31, 2006 and 12 shares at December 31, 2005	(17 )	(12 )
Accumulated deficit in earnings	(36,711 )	(35,175 )
Accumulated other comprehensive income (loss)	(787 )	(1,009 )
Total stockholders' equity	69,311	68,888
	\$ 152,312	\$ 151,180

See accompanying notes to condensed consolidated financial statements.

**3D SYSTEMS CORPORATION****Condensed Consolidated Statements of Operations**

Three Months Ended March 31, 2006 and March 31, 2005

(in thousands, except per share amounts)

(unaudited)

	<b>March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
<b>Revenue:</b>		
Products	\$ 24,252	\$ 20,238
Services	9,391	10,186
Total revenue	33,643	30,424
<b>Cost of sales:</b>		
Products	13,010	10,275
Services	7,028	7,131
Total cost of sales	20,038	17,406
Gross profit	13,605	13,018
<b>Operating expenses:</b>		
Selling, general and administrative	10,057	8,710
Research and development	3,257	2,675
Severance and restructuring	1,638	
Total operating expenses	14,952	11,385
Income (loss) from operations	(1,347 )	1,633
Interest and other expense, net	167	346
Income (loss) before provision for income taxes	(1,514 )	1,287
Provision for income taxes	23	94
Net income (loss)	(1,537 )	1,193
Preferred stock dividends	411	412
Income (loss) available to common stockholders	\$ (1,948 )	\$ 781
Net income (loss) available to common stockholders per share basic	\$ (0.13 )	\$ 0.05
Net income (loss) available to common stockholders per share diluted	\$ (0.13 )	\$ 0.05

See accompanying notes to condensed consolidated financial statements.

**3D SYSTEMS CORPORATION**  
**Condensed Consolidated Statements of Cash Flows**  
**Three Months Ended March 31, 2006 and March 31, 2005**  
**(in thousands)**  
**(unaudited)**

	<b>March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
Cash flows from operating activities:		
Net income (loss)	\$ (1,537 )	\$ 1,193
Adjustments to reconcile net income to net cash used in operating activities:		
Provision for deferred income taxes	23	94
Depreciation and amortization	1,619	1,568
Bad debt provision (benefit)	60	(39 )
Adjustments to inventory reserves	(170 )	(97 )
Stock-based compensation expense	452	75
Loss (gain) on disposition of property and equipment	2	1
Changes in operating accounts:		
Accounts receivable	3,650	1,723
Lease receivables	20	68
Inventories	(1,930 )	635
Prepaid expenses and other current assets	25	(2,233 )
Other assets	183	(105 )
Accounts payable	815	(74 )
Accrued liabilities	(476 )	(2,863 )
Customer deposits	(594 )	(26 )
Deferred revenue	277	516
Other liabilities	1	(132 )
Net cash provided by operating activities	2,420	304
Cash flows from investing activities:		
Purchases of property and equipment	(1,584 )	(677 )
Additions to licenses and patents	(159 )	(132 )
Proceeds from the sale of property and equipment	150	
Software development costs	(130 )	(222 )
Net cash used in investing activities	(1,723 )	(1,031 )
Cash flows from financing activities:		
Stock option, stock purchase plan and restricted stock proceeds	1,687	1,115
Repayment of long-term debt	(102 )	(89 )
Payments under obligation to former 3D Systems SA stockholders		(219 )
Payment of accrued liquidated damages		(36 )
Net cash provided by financing activities	1,585	771
Effect of exchange rate changes on cash	4	253
Net increase in cash and cash equivalents	2,286	297
Cash and cash equivalents at the beginning of the period	24,328	26,505
Cash and cash equivalents at the end of the period	\$ 26,614	\$ 26,802

See accompanying notes to condensed consolidated financial statements.

**3D SYSTEMS CORPORATION****Condensed Consolidated Statements of Cash Flows (Continued)****Three Months Ended March 31, 2006 and March 31, 2005****(in thousands)****(unaudited)**

	<b>March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
<b>Supplemental Cash Flow Information</b>		
Interest payments	30	61
Income tax payments	312	602
Non-cash items		
Conversion of 6% convertible subordinated debentures		100
Conversion of Series B convertible preferred stock		26
Accrued dividends on preferred stock	387	387
Transfer of equipment from inventory to property and equipment, net(a)	694	545
Transfer of equipment to inventory from property and equipment, net(b)	30	307

(a) Inventory is transferred from inventory to property and equipment, net at cost when the Company requires additional machines for training, demonstration or short-term rentals.

(b) In general, an asset is transferred from property and equipment, net into inventory at its net book value when the Company has identified a potential sale for a used machine. The machine is removed from inventory upon recognition of the sale.

See accompanying notes to condensed consolidated financial statements.

**3D SYSTEMS CORPORATION**

**Condensed Consolidated Statements of Comprehensive Income (Loss)**

**Three Months Ended March 31, 2006 (Restated) and March 31, 2005**

**(in thousands)**

**(unaudited)**

	<b>March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
Net income (loss)	\$ (1,537 )	\$ 1,193
Foreign currency translation	222	(301 )
Comprehensive income (loss)	\$ (1,315 )	\$ 892

See accompanying notes to condensed consolidated financial statements.

5

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**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

**(1) Basis of Presentation**

The accompanying condensed consolidated financial statements include the accounts of 3D Systems Corporation and its subsidiaries (collectively, the Company). All significant intercompany transactions and balances have been eliminated in consolidation. The condensed consolidated financial statements were prepared in accordance with generally accepted accounting principles (GAAP) and the rules and regulations of the Securities and Exchange Commission (SEC) applicable to interim reporting. Accordingly, they omit certain footnotes and other financial information that are required for complete financial statements. In management's opinion, after giving effect to the restatement presented in Note 2, all adjustments considered necessary for a fair presentation of the condensed consolidated financial position as of March 31, 2006 and the condensed consolidated results of operations and the condensed consolidated statement of cash flows for the three months ended March 31, 2006 and March 31, 2005 have been included.

The financial information contained in the condensed consolidated financial statements for the first three months of 2006 and the 2005 periods set forth herein have been restated, as described in Note 2 below.

The results set forth in the condensed consolidated statement of operations for the three months ended March 31, 2006 are not necessarily indicative of the results to be expected for the full year.

The condensed consolidated balance sheet at December 31, 2005 has been derived from the Company's annual historical financial statements, as adjusted for the restatement set forth in Note 2, at that date but omits certain of the information and footnotes required by GAAP for complete financial statements.

Certain amounts in the 2005 condensed consolidated financial statements, as restated, have been reclassified in order to conform with the 2006 presentations.

The Company is responsible for the unaudited condensed consolidated financial statements included in this document. As these are condensed financial statements, they should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 and the information set forth in Note 2.

**(2) Financial Statement Restatement**

On November 3, 2006, the Company announced that management and the Audit Committee of the Board of Directors had determined, based on information presented by management in connection with the preparation of the Company's financial statements for the third quarter of 2006, that its financial statements included in its Quarterly Reports on Form 10-Q for the quarters ended March 31, 2006 and June 30, 2006 contained errors and should be restated.

The Company also announced at that time that it was assessing whether its financial statements for prior periods should be restated. On December 14, 2006, the Company announced that management and the Audit Committee had completed their assessment of the prior-period financial statements and that, based on information presented by management, the Company's financial statements included in its

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

Annual Reports on Form 10-K for the 2004 and 2005 calendar years also contained errors and should be restated. In evaluating the need to restate those periods, the Company also took into consideration adjustments that had been identified previously as not being material to those periods, and those adjustments are included in the restated amounts for the applicable 2005 and 2004 periods.

The Company has identified and evaluated the errors noted in its prior-period financial statements and has corrected those errors through adjustments reflected in the restated historical consolidated financial statements in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 154 ( SFAS No. 154 ), Accounting Changes and Error Corrections. The Company also assessed on a quarterly basis the materiality of prior-period misstatements that were previously identified but not corrected because they were originally considered to be immaterial. As a result of the Company's analysis of errors identified during the third quarter of 2006 that were attributable to prior periods as well as previously unadjusted amounts attributable to prior periods, the Company concluded that the prior-period impact was material in the second and fourth quarters of 2005 as well as for the years ended December 31, 2005 and 2004. Therefore, the restated financial information set forth herein reflects adjustments to correct or record all such previously unadjusted amounts.

At the end of the second quarter of 2006, the Company first identified and disclosed control deficiencies in its procedures for (a) reconciling and compiling its financial records for the second quarter of 2006 and (b) processing and safeguarding inventory for the period ended June 30, 2006 that it concluded constituted, individually or in the aggregate, material weaknesses.

With respect to the Company's procedures for compiling and reconciling its financial records for the second quarter of 2006, the Company determined that the material weaknesses primarily arose as a result of the following contributing factors:

- inexperience and lack of training of personnel with respect to the closing procedures required under the Company's new enterprise resource management ( ERP ) system;
- unfamiliarity with the reports generated by its new ERP system such that their utility in compiling and reconciling financial data was not fully recognized in connection with the quarter-end closing process;
- the combination of starting up its new ERP system, addressing problems with supply chain and order processing and fulfillment activities, and conflicting demands on its employees' time;
- human errors in entering, completing and correcting product and vendor data in the ERP system; and
- difficulties in consolidating European financial information and in the U.S. consolidation process.

With respect to inventory accounting matters, the Company determined that the material weaknesses relating to that matter primarily resulted from three fundamental sources:

- insufficient planning and execution of the conversion from the Company's legacy systems to its new ERP system;



**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

- errors or corruption in the data migrated from its legacy accounting systems to its new ERP system; and
- data that was missing from, and errors in inputting data into, its new ERP system.

The Company also noted that such inventory accounting matters also arose out of the significant operational difficulties that the Company encountered in taking, processing and filling orders on its new ERP system during the second quarter of 2006 both directly and through certain of its third-party suppliers to end users, including a logistics and warehousing firm that the Company employed beginning in the second quarter of 2006.

As the Company prepared its financial statements for the period ended September 30, 2006, it discovered errors in its financial statements for the periods ended March 31, 2006 and June 30, 2006 and for prior periods that are discussed below in this Note 2 and that led to the restatement of its financial statements set forth herein. The Company identified these errors primarily as a result of its efforts to remediate the material weaknesses that it disclosed with respect to the second quarter of 2006 and through its efforts to implement its new ERP system, to reconcile the records in its new ERP system with those in its legacy systems, and to test its internal controls in the context of its new ERP system environment.

In connection with the identification of these errors and the preparation of the Company's third-quarter financial statements, it identified additional control deficiencies that it believes, taken together with the material weaknesses that it previously disclosed with respect to the second quarter of 2006, constitute individually or in the aggregate material weaknesses with respect to those matters. These additional deficiencies relate to (a) a deficiency in the invoicing and processing of accounts receivable and the application of customer payments and (b) deficiencies in the timeliness and accuracy of its period-end financial statement closing process and the monitoring of its accounting function and oversight of financial controls.

With respect to the deficiency in the Company's procedures for the processing of and accounting for accounts receivable and the application of customer payments, the Company determined that this material weakness resulted in the following errors in the Company's financial statements:

- The Company experienced errors in the invoicing and recording of customer billings, in the application of customer payments and in the reconciliation of customer accounts. These matters required the Company to issue and record credit memoranda for the benefit of customers for product returns, pricing adjustments, changes to service contracts, freight-related matters and other similar matters that are discussed elsewhere in this Note 2. The Company also identified cash that it had received but which had not been applied to customer accounts or the related accounts receivable.
- Some customer contracts had not been fully integrated and reflected in its new ERP system.
- Certain tax-exempt customers were charged sales tax in error and certain customers were inadvertently not billed for sales tax on their purchases.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

With respect to the deficiency in the timeliness and accuracy of the Company's period-end financial statement closing process and the monitoring of its accounting function and oversight of financial controls, it determined that this material weakness primarily arose as a result of the following contributing factors:

- The combination of its relocation to Rock Hill, South Carolina, and the difficulties that it encountered in implementing its new ERP system;
- The loss of certain experienced accounting and other personnel who did not relocate to Rock Hill;
- Inexperience and lack of training of newly hired personnel with respect to its existing system of internal controls and the closing procedures required under its new ERP system;
- Unfamiliarity with the reports generated by its new ERP system such that their utility in compiling and reconciling financial data was not fully recognized in connection with the quarter-end closing process;
- The combination of starting up its new ERP system, addressing problems with supply chain and order processing and fulfillment activities, and conflicting demands on its employees' time;
- Human errors in entering, completing and correcting product and vendor data in the ERP system; and
- Contrary to its policies and procedures, a lack of consistent and effective review and supervision of account reconciliations and data entries at various levels of its accounting organization to confirm, analyze and reconcile account balances that adversely affected its financial reporting and disclosure controls.

The material weaknesses described in this Note 2, combined with the time needed to complete the Company's assessment of the need to restate its financial statements, rendered it unable to complete its financial statements for the periods ended September 30, 2006 on a timely basis and also necessitated significant additional resources and efforts to complete its third-quarter financial statements.

The Company also undertook a review of the potential effect of the financial statement errors that it discovered on prior periods. As discussed elsewhere in this Note 2, on November 3, 2006, it announced that management and the Audit Committee of its Board of Directors had determined, based on information presented by its management in connection with the preparation of its financial statements for the third quarter of 2006, that its financial statements as of and for the quarters ended March 31, 2006 and June 30, 2006 should be restated as a result of the errors in them that the Company had discovered, and on December 14, 2006, it announced that management and the Audit Committee had completed their assessment of the Company's prior-period financial statements and that, based on information presented by management, the Company's financial statements as of and for the years ended December 31, 2004 and 2005 also contained errors and should be restated. As discussed elsewhere in this Note 2, in evaluating the need to restate those periods, the Company also took into consideration audit adjustments that had been identified previously as not being material to those periods, and it has included those adjustments in the restated amounts for the applicable 2005 and 2004 periods.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

The restatement of the errors and previously unrecorded audit adjustments that the Company identified included the following:

- Errors in the invoicing and recording of customer billings, in the application of customer payments and in the reconciliation of customer accounts that were corrected by the issuance and recording of credit memoranda for the benefit of customers for product returns, pricing adjustments, changes to service contracts, freight-related matters and other similar matters.
- Errors related to the timing of recognition of royalty income and expense.
- Errors related to the timing of the recognition of warranty and training revenue.
- Errors related to securities issuance costs that arose as a result of expensing such costs rather than applying such costs against the net proceeds of sale of the related securities.
- Errors related to prepaid materials that arose from the incomplete reconciliation of such accounts between the sub-ledger and the general ledger for the affected periods.
- Errors related to the failure to record depreciation expense for assets that had been placed in service but which remained recorded in the Company's construction-in-progress ( CIP ) accounts.
- Errors related to the timing of expenses for certain unrelated third party professional services.
- Errors related to accounts payable that arose from the incomplete reconciliation of such accounts between the sub-ledger and the general ledger for each applicable period.
- Errors related to inventory usage that arose from variances identified between actual and recorded inventory values following the Company's conducting physical inventory counts to test the accuracy of the recorded inventory data.
- Errors related to hedging activities for foreign currency transactions that arose from mechanical errors in accumulating spreadsheet data as well as the recording of net unrealized losses on foreign exchange hedges that had previously been excluded from the consolidated statement of operations.
- Errors related to foreign income tax expense that relate to a previously identified adjustment related to periods prior to 2004 but that was not deemed material to those periods.

The deficiencies and errors described above were identified during the Company's preparation of its financial statements and in reviewing the effectiveness of the design and operation of its disclosure controls and procedures as of and for the period ended September 30, 2006. The Company performed additional detailed transaction reviews and control activities in connection with reconciling and compiling its financial records. Such procedures were undertaken in order to confirm that the Company's financial statements for the three months and nine months ended September 30, 2006 were free of material errors.



**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

As a result of this effort, the Company identified several reconciliation issues and accounting shortcomings, including:

- Some accounts had not been adequately reconciled in accordance with the Company's policies and procedures.
- Certain accounts contained unreconciled differences that had not been timely resolved in accordance with the Company's policies and procedures, including credits for the benefit of customers and cash that had not been applied to customer accounts or the related accounts receivable.
- Certain fixed assets that had been placed in service remained recorded in construction-in-progress ( CIP ) resulting in a failure to depreciate those items beginning when they were placed in service.
- Some service contracts had not been fully integrated and reflected in the Company's new ERP system.
- Certain tax-exempt customers were charged sales tax in error and certain customers were inadvertently not billed for sales tax on their purchases.

The Company also identified variances in recorded versus actual inventory values. The Company conducted physical inventory counts during the third quarter of 2006 to test the accuracy of the recorded inventory data. As a result, the Company identified variances between the inventory data in the Company's records compared to the inventory values determined through the physical counts. The Company determined that the discrepancy in recorded versus actual third quarter inventory values resulted from:

- Errors or corruption in the data migrated from the Company's legacy accounting systems to the new ERP system implemented in the second quarter of 2006;
- Errors in processing, shipping and properly recording orders by the Company's third party logistics and warehousing provider; and
- Failure to properly record certain orders that were shipped directly from the Company's third-party suppliers to the end users.

As a result, the Company concluded that the variances within the cost of sales account should be written off in order to fairly state the inventory value in the consolidated financial statements.

The following table shows the impact of the correction of all errors on income (loss) available to common stockholders for the full year ended December 31, 2004, for each calendar quarter in 2005, for the full year ended December 31, 2005 and for the first quarter of 2006, as well as the cumulative impact of prior-period errors on retained earnings at December 31, 2003. The tax effect of the correction of these errors on each restated period was either minimal or nil.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

	Accumulated Deficit in Earnings December 31, 2003	Effect of Restatement on Income (Loss) Available to Common Stockholders						
		Year Ended December 31, 2004	Quarter Ended March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005	Year Ended December 31, 2005	Quarter Ended March 31, 2006
	(amounts in \$000s)							
Previously reported	\$ (47,442)	\$ 1,027	\$ 783	\$ 855	\$ 749	\$ 6,017	\$ 8,404	\$ (1,244)
Adjustments:								
Credit memos		10	(19 )	(79 )	(164 )	(101 )	(363 )	(251 )
Royalty income/expense		253	5	(17 )	(17 )	(293 )	(322 )	13
Recognition of warranty and training revenue	32	220	11	(246 )	13	33	(189 )	121
Stock issuance costs						211	211	
Prepaid materials reconciliation				(29 )	(4 )	(64 )	(97 )	(201 )
Depreciation of fixed assets		(4 )	(19 )	(37 )	(42 )	(63 )	(161 )	(106 )
Accrual for professional services						(15 )	(15 )	(247 )
Inventory usage						22	22	
Other		(20 )	20	44	(2 )	(16 )	46	(86 )
Tax provision	(191 )					191	191	53
Total adjustments:	(159 )	459	(2 )	(364 )	(216 )	(95 )	(677 )	(704 )
Restated	\$ (47,601)	\$ 1,486	\$ 781	\$ 491	\$ 533	\$ 5,922	\$ 7,727	\$ (1,948)
Net income (loss) available to common stockholders per share diluted (as previously reported)		\$ 0.07	\$ 0.05	\$ 0.05	\$ 0.05	\$ 0.32	\$ 0.53	\$ (0.08 )
Effect of restatement		0.04	(0.00 )	(0.02 )	(0.02 )	(0.00 )	(0.05 )	(0.05 )
Net income (loss) available to common stockholders per share diluted (restated)		\$ 0.11	\$ 0.05	\$ 0.03	\$ 0.03	\$ 0.32	\$ 0.48	\$ (0.13 )

As shown in this table, the errors affecting income (loss) available to the common stockholders reflected in the restated financial information primarily include:

- \$(604) in the aggregate of errors related to credit memoranda issued to customers, of which \$(251) was attributable to the first quarter of 2006, \$(363) was attributable to the 2005 periods (mainly the third and fourth quarters of 2005) and a \$10 credit was attributable to 2004;

Such credit memoranda were issued to customers mainly for product returns or pricing adjustments as well as for changes to service contracts and freight-related matters. Error corrections related to credit memoranda were posted to revenue or the related cost of sales in the period to which they related in carrying out the restatement;

- \$(56) in the aggregate of errors related to the timing of recognition of royalty income and expense, of which \$13 was attributable to the first quarter of 2006, \$(322) of expense was attributable to the 2005 periods (mainly the fourth quarter of 2005) and \$253 was attributable to 2004;

These errors arose from the timing of the recording of and misclassification of such revenue and cost of sales;

- \$152 in the aggregate of errors related to the recognition of warranty and training revenue, of which \$121 was attributable to the first quarter of 2006, \$(189) was attributable to the 2005 periods (mainly the second quarter of 2005) and \$220 was attributable to 2004;

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These errors arose from the incorrect timing of recording such revenue to the appropriate period;

- \$211 of errors related to securities issuance costs, all which was attributable to the fourth quarter of 2005;

12

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**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

These errors arose because such costs were originally expensed rather than charged to additional paid-in capital and applied against the net proceeds of sale of the related securities;

- \$244 in the aggregate of errors related to tax adjustments, of which \$191 related to foreign income tax provisions related to the fourth quarter of 2005, and \$53 related to the net consolidated tax effect of the restatement adjustments for the first quarter of 2006;

These errors relate to an amount previously identified that related to periods prior to 2004 which was originally not deemed material to those periods. Such adjustments have been included in the restated amounts herein for the applicable period;

- \$(298) in the aggregate of errors related to prepaid materials, of which \$(201) was attributable to the first quarter of 2006 and \$(97) was attributable to the 2005 periods;

These errors arose from the incomplete reconciliation of prepaid materials between the sub-ledger and the general ledger for each period;

- \$(271) in the aggregate of errors related to depreciation expense, of which \$(106) was attributable to the first quarter of 2006, \$(161) was attributable to the 2005 periods and \$(4) was attributable to 2004;

These errors related to depreciation expense for assets placed in service but which remained recorded in the Company's CIP accounts;

- \$(262) of errors related to accrued professional services, of which \$(247) was attributable to the first quarter of 2006 and \$(15) was attributable to 2005 periods;

These errors arose from the correction of the treatment of previously incurred accounting fees;

- \$22 of errors related to inventory, which was attributable to the fourth quarter of 2005;

These errors arose from variances identified between actual and recorded inventory values as a result of the Company's conduct of physical inventory counts to test the accuracy of the recorded inventory data; and

- \$(60) in the aggregate of errors for other adjustments related to cost of sales, selling, general and administrative expenses, other income and expense and taxes, of which \$(86) was attributable to the first quarter of 2006, \$46 was attributable to the 2005 periods and \$(20) was attributable to 2004.



**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The impact of these adjustments on the consolidated statements of operations for the years ended December 31, 2004 and 2005 is as follows:

Consolidated Statement of Operations	2004 Year Ended			2005 Year Ended		
	As Previously Reported December 31 (amounts in \$000s)	Restatement Adjustments	Restated	As Previously Reported December 31	Restatement Adjustments	Restated
Revenue:						
Products	\$ 83,976	\$ 231	\$ 84,207	\$ 100,396	\$ (615 )	\$ 99,781
Services	41,403		41,403	39,274	23	39,297
Total revenue	125,379	231	125,610	139,670	(592 )	139,078
Cost of sales:						
Products	43,898	(234 )	43,664	49,973	359	50,332
Services	25,390		25,390	26,567	17	26,584
Total cost of sales	69,288	(234 )	69,054	76,540	376	76,916
Gross profit	56,091	465	56,556	63,130	(968 )	62,162
Operating expenses:						
Selling, general and administrative	39,411	4	39,415	40,382	(38 )	40,344
Research and development	10,474		10,474	12,176		12,176
Severance and restructuring	605		605	1,227		1,227
Total operating expenses	50,490	4	50,494	53,785	(38 )	53,747
Income from operations	5,601	461	6,062	9,345	(930 )	8,415
Interest and other expense, net	1,979	2	1,981	762	(62 )	700
Income before provision for (benefit from) income taxes	3,622	459	4,081	8,583	(868 )	7,715
Provision for (benefit from) income taxes	1,061		1,061	(1,500 )	(191 )	(1,691 )
Net income	2,561	459	3,020	10,083	(677 )	9,406
Preferred stock dividends	1,534		1,534	1,679		1,679
Income available to common shareholders	\$ 1,027	\$ 459	\$ 1,486	\$ 8,404	\$ (677 )	\$ 7,727
Net income available to common stockholders per share basic	\$ 0.08	\$ 0.03	\$ 0.11	\$ 0.56	\$ (0.04 )	\$ 0.52
Net income available to common stockholders per share diluted	\$ 0.07	\$ 0.04	\$ 0.11	\$ 0.53	\$ (0.05 )	\$ 0.48

The changes to the consolidated statements of operations reflected in the table above include:

- For the year ended December 31, 2004, the changes arising from the restatement primarily relate to the following:
- Revenue increased by \$231, or 0.2%, for the year. The increase in revenue primarily relates to a \$220 adjustment of amortization for warranty and training revenue.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

- Cost of sales decreased by \$234, or 0.3%. This decrease primarily relates to a \$254 adjustment of royalty expense that was overstated in 2004 and understated in 2005.
- As a result of these changes, net income increased by \$459, or 44.7%.
- For the year ended December 31, 2005, the changes arising from the restatement are discussed following the next table.

15

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## 3D SYSTEMS CORPORATION

## Notes to Condensed Consolidated Financial Statements (Restated) (Continued)

For the Three Months Ended March 31, 2006 and 2005

(amounts in thousands, except per share data)

(unaudited)

The impact on the condensed consolidated statements of operations each quarterly period in 2005 as a result of the restatement is as follows:

Statement of Operations	2005 Quarter Ended			As Previously			Restatement			As Previously			Restatement		
	As Previously Reported March 31	Restatement Adjustments	Restated	As Previously Reported June 30	Restatement Adjustments	Restated	As Previously Reported September 30	Restatement Adjustments	Restated	As Previously Reported December 31	Restatement Adjustments	Restated			
Revenue:															
Products	\$ 20,246	\$ (8)	\$ 20,238	\$ 22,657	\$ (304)	\$ 22,353	\$ 23,005	\$ (131)	\$ 22,874	\$ 34,488	\$ (172)	\$ 34,316			
Services	10,186		10,186	10,112	(21)	10,091	9,319	(20)	9,299	9,657	64	9,721			
Total revenue	30,432	(8)	30,424	32,769	(325)	32,444	32,324	(151)	32,173	44,145	(108)	44,037			
Cost of sales:															
Products	10,298	(23)	10,275	12,231	46	12,277	10,909	21	10,930	16,535	315	16,850			
Services	7,129	2	7,131	6,193	4	6,197	6,562	6	6,568	6,683	5	6,688			
Total cost of sales	17,427	(21)	17,406	18,424	50	18,474	17,471	27	17,498	23,218	320	23,538			
Gross profit	13,005	13	13,018	14,345	(375)	13,970	14,853	(178)	14,675	20,927	(428)	20,499			
Operating expenses:															
Selling, general and administrative	8,696	14	8,710	9,900	37	9,937	9,917	43	9,960	11,869	(132)	11,737			
Research and development	2,675		2,675	2,701		2,701	3,429		3,429	3,371		3,371			
Severance and restructuring				7		7	42		42	1,178		1,178			
Total operating expenses	11,371	14	11,385	12,608	37	12,645	13,388	43	13,431	16,418	(132)	16,286			
Income from operations	1,634	(1)	1,633	1,737	(412)	1,325	1,465	(221)	1,244	4,509	(296)	4,213			
Interest and other expense, net	345	1	346	185	(48)	137	204	(5)	199	28	(10)	18			
Income before provision for (benefit from) income taxes	1,289	(2)	1,287	1,552	(364)	1,188	1,261	(216)	1,045	4,481	(286)	4,195			
Provision for (benefit from) income taxes	94		94	253		253	100		100	(1,947)	(191)	(2,138)			
Net income	1,195	(2)	1,193	1,299	(364)	935	1,161	(216)	945	6,428	(95)	6,333			
Preferred stock dividends	412		412	444		444	412		412	411		411			
Income available to common shareholders	\$ 783	\$ (2)	\$ 781	\$ 855	\$ (364)	\$ 491	\$ 749	(216)	\$ 533	\$ 6,017	\$ (95)	\$ 5,922			
Net income available to common stockholders per share basic	\$ 0.05	\$	\$ 0.05	\$ 0.06	\$ (0.03)	\$ 0.03	\$ 0.05	\$ (0.01)	\$ 0.04	\$ 0.40	\$ (0.01)	\$ 0.39			
Net income available to common stockholders per share diluted	\$ 0.05	\$	\$ 0.05	\$ 0.05	\$ (0.02)	\$ 0.03	\$ 0.05	\$ (0.02)	\$ 0.03	\$ 0.32	\$	\$ 0.32			

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

(amounts in thousands, except per share data)

(unaudited)

The following is a summary of the changes to the consolidated statements of operations reflected in the table above.

- For the year ended December 31, 2005, the changes arising from the restatement primarily relate to the following:
  - Revenue decreased by \$8 for the first quarter of 2005, by \$325 (1.0%) for the second quarter, by \$151 (0.5%) for the third quarter and by \$108 (0.2%) for the quarter ended December 31, 2005. The decreases in revenue during the third and fourth quarters of 2005 primarily relate to adjustments for credit memoranda as discussed above that were applicable to those periods. These amounted to \$153 in the third quarter and \$80 in the fourth quarter. The decrease in revenue during the second quarter primarily relates to a \$246 adjustment related to amortization for warranty and training revenue and \$79 of adjustments for credit memoranda for customers that were applicable to that period.
  - Cost of sales increased by \$320 (1.4%) for the fourth quarter and changed nominally in the other quarters. The increase in cost of sales during the fourth quarter primarily relates to a \$293 adjustment for royalties that had been incorrectly expensed in 2004.
  - Operating expenses decreased by \$132 (0.8%) during the fourth quarter, increased by \$37 (0.3%) and \$43 (0.3%) for the second and third quarters, respectively, and increased nominally for the first quarter. The decrease during the fourth quarter primarily relates to an adjustment for stock issuance costs of \$211, partially offset by additional depreciation being recorded for assets placed into service of \$63. The second-quarter and third-quarter increases totaling \$80 primarily relate to additional depreciation being recorded for assets placed in service.
  - The nominal changes to interest and other expense, net relate to an increase in interest income in the affected quarters.
  - The income tax benefit recorded in the fourth quarter relates to the correction of a foreign tax provision in 2005 which was applicable to prior periods.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The impact on the condensed consolidated statement of operations for the first quarter of 2006 as a result of the restatement is as follows:

	<b>2006 Quarter Ended As Previously Reported March 31</b>	<b>Restatement Adjustments</b>	<b>Restated</b>
<b>Consolidated Statement of Operations</b>			
<b>Revenue:</b>			
Products	\$ 24,216	\$ 36	\$ 24,252
Services	9,311	80	9,391
Total revenue	33,527	116	33,643
<b>Cost of sales:</b>			
Products	12,526	484	13,010
Services	6,986	42	7,028
Total cost of sales	19,512	526	20,038
Gross profit	14,015	(410 )	13,605
<b>Operating expenses:</b>			
Selling, general and administrative	9,763	294	10,057
Research and development	3,257		3,257
Severance and restructuring	1,638		1,638
Total operating expenses	14,658	294	14,952
Loss from operations	(643 )	(704 )	(1,347 )
Interest and other expense, net	114	53	167
Loss before provision for (benefit from) income taxes	(757 )	(757 )	(1,514 )
Provision for (benefit from) income taxes	76	(53 )	23
Net loss	(833 )	(704 )	(1,537 )
Preferred stock dividends	411		411
Loss available to common shareholders	\$ (1,244 )	\$ (704 )	\$ (1,948 )
Net loss available to common stockholders per share basic	\$ (0.08 )	\$ (0.05 )	\$ (0.13 )
Net loss available to common stockholders per share diluted	\$ (0.08 )	\$ (0.05 )	\$ (0.13 )

A summary of the changes to the condensed consolidated statement of operations reflected in the table above include:

- For the first quarter of 2006, the changes arising from the restatement primarily relate to the following:
- Revenue increased \$116, or 0.3%, for the quarter ended March 31, 2006. The increase in revenue for the first quarter primarily relates to \$121 of adjustments related to the recognition of warranty and training revenue, \$59 of adjustments related to royalty income and \$160 of other adjustments, partially offset by \$224 of adjustments for credit memoranda that were applicable to the first quarter.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

- Cost of sales increased by \$526, or 2.7%, for the quarter ended March 31, 2006. The first-quarter increase in cost of sales primarily relates to a \$201 reconciliation adjustment related to prepaid materials and \$207 of other adjustments
- Operating expenses increased by \$294, or 2.0%, for the quarter ended March 31, 2006. The first-quarter increase in operating expenses primarily relates to a \$248 adjustment to record an increase in professional fees and a \$106 adjustment to record additional depreciation expense for items placed in service that had not been removed from CIP accounts prior to the restatement.
- Interest and other expense, net increased by \$53, or 46.5%, for the quarter ended March 31, 2006. The first-quarter increase relates to adjustments to record interest income in the correct period.
- The change in the income tax provision during the first quarter represents an adjustment to the state and foreign income tax provision due to computational errors in tax provision calculations.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

**The impact of the restatement on the condensed consolidated balance sheets as of December 31, 2004 and as of each quarter end in 2005 is as follows:**

Consolidated Balance Sheet	2004			2005		
	As Previously Reported December 31 (amounts in \$000s)	Restatement Adjustments	Restated	As Previously Reported March 31	Restatement Adjustments	Restated
<b>ASSETS</b>						
Current assets:						
Cash and cash equivalents	\$ 26,276	\$ 229	\$ 26,505	\$ 26,507	\$ 295	\$ 26,802
Accounts receivable	22,209	(13 )	22,196	19,871	18	19,889
Inventories	9,512	(18 )	9,494	8,505		8,505
Prepaid expenses and other current assets	5,278	(50 )	5,228	7,735	(295 )	7,440
Deposits	229	(229 )				
Total current assets	63,504	(81 )	63,423	62,618	18	62,636
Property and equipment, net	9,500	71	9,571	9,737	(29 )	9,708
Intangible assets, net	10,224	584	10,808	10,247		10,247
Goodwill	45,135		45,135	44,978		44,978
Restricted cash	1,200		1,200	1,200		1,200
Lease receivable	365		365			
Other assets, net	1,568	(584 )	984	1,423		1,423
	\$ 131,496	\$ (10 )	\$ 131,486	\$ 130,203	\$ (11 )	\$ 130,192
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>						
Current liabilities:						
Current portion of long-term debt	\$ 180	\$ 6	\$ 186	\$ 190	\$ 6	\$ 196
Accounts payable	6,937	35	6,972	6,848		6,848
Accrued liabilities	13,447	(112 )	13,335	10,570	(65 )	10,505
Customer deposits	819		819	793		793
Deferred revenue	13,797	(225 )	13,572	13,991	(236 )	13,755
Total current liabilities	35,180	(296 )	34,884	32,392	(295 )	32,097
Long-term debt, less current portion	3,745	36	3,781	3,645	29	3,674
Convertible subordinated debentures	22,704		22,704	22,604		22,604
Other liabilities	1,607	(50 )	1,557	1,457	(43 )	1,414
	63,236	(310 )	62,926	60,098	(309 )	59,789
Preferred stock	15,196		15,196	15,195		15,195
Stockholders' equity:						
Common stock	14		14	15		15
Additional paid-in capital	97,859	(59 )	97,800	99,714	(59 )	99,655
Deferred compensation	(45 )		(45 )	(949 )		(949 )
Treasury stock, at cost; 8 shares at December 31, 2004 and March 31, 2005	(68 )	59	(9 )	(68 )	59	(9 )
Accumulated deficit in earnings	(44,881 )	300	(44,581 )	(43,686 )	298	(43,388 )
Accumulated other comprehensive income (loss)	185		185	(116 )		(116 )
Total stockholders' equity	53,064	300	53,364	54,910	298	55,208
	\$ 131,496	\$ (10 )	\$ 131,486	\$ 130,203	\$ (11 )	\$ 130,192

## 3D SYSTEMS CORPORATION

## Notes to Condensed Consolidated Financial Statements (Restated) (Continued)

## For the Three Months Ended March 31, 2006 and 2005

(amounts in thousands, except per share data)

(unaudited)

Consolidated Balance Sheet	2005			As Previously Reported			Restatement		
	As Previously Reported June 30 (amounts in \$000s)	Restatement Adjustment	Restated	As Previously Reported September 30	Restatement Adjustment	Restated	As Previously Reported December 31	Restatement Adjustment	Restated
<b>ASSETS</b>									
Current assets:									
Cash and cash equivalents	\$ 28,121	\$ 243	\$ 28,364	\$ 25,991	\$ 242	\$ 26,233	\$ 24,112	\$ 216	\$ 24,328
Accounts receivable	19,294	(61 )	19,233	21,631	(225 )	21,406	33,172	(406 )	32,766
Inventories	9,319		9,319	13,417		13,417	13,960	850	14,810
Prepaid expenses and other current assets	8,979	(224 )	8,755	10,195	(221 )	9,974	9,307	(32 )	9,275
Deposits							216	(216 )	
Deferred tax assets							2,500		2,500
Total current assets	65,713	(42 )	65,671	71,234	(204 )	71,030	83,267	412	83,679
Property and equipment, net	9,256	(67 )	9,189	10,449	(110 )	10,339	12,166	(174 )	11,992
Intangible assets, net	9,655		9,655	9,201		9,201	7,990	587	8,577
Goodwill	44,795		44,795	44,790		44,790	44,747		44,747
Restricted cash	1,200		1,200	1,200		1,200	1,200		1,200
Other assets, net	1,164		1,164	852		852	1,572	(587 )	985
	\$ 131,783	\$ (109)	\$ 131,674	\$ 137,726	\$ (314)	\$ 137,412	\$ 150,942	\$ 238	\$ 151,180
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>									
Current liabilities:									
Current portion of long-term debt	\$ 190	\$ 6	\$ 196	\$ 200	\$ 6	\$ 206	\$ 200	\$ 7	\$ 207
Accounts payable	5,153		5,153	7,866		7,866	10,949	735	11,684
Accrued liabilities	9,025	(45 )	8,980	9,996	(24 )	9,972	12,174	142	12,316
Customer deposits	927		927	2,040		2,040	1,945		1,945
Deferred revenue	12,275	10	12,285	12,008		12,008	13,768	(43 )	13,725
Total current liabilities	27,570	(29 )	27,541	32,110	(18 )	32,092	39,036	841	39,877
Long-term debt, less current portion	3,645	27	3,672	3,545	26	3,571	3,545	23	3,568
Convertible subordinated debentures	22,604		22,604	22,604		22,604	22,604		22,604
Other liabilities	1,063	(41 )	1,022	1,018	(40 )	978	1,039	(38 )	1,001
	54,882	(43 )	54,839	59,277	(32 )	59,245	66,224	826	67,050
Preferred stock	15,211		15,211	15,226		15,226	15,242		15,242
Stockholders equity:									
Common stock	15		15	15		15	15		15
Additional paid-in capital	106,697	(59 )	106,638	107,041	(62 )	106,979	106,883	(353 )	106,530
Deferred compensation	(1,774 )		(1,774 )	(1,647 )		(1,647 )	(1,461 )		(1,461 )
Treasury stock, at cost; 8 shares at June 30, 2005, 10 shares at September 30, 2005 and 12 shares at December 31, 2005	(68 )	59	(9 )	(71 )	62	(9 )	(154 )	142	(12 )
Accumulated deficit in earnings	(42,387 )	(66 )	(42,453 )	(41,226 )	(282 )	(41,508 )	(34,798 )	(377 )	(35,175 )
Accumulated other comprehensive income (loss)	(793 )		(793 )	(889 )		(889 )	(1,009 )		(1,009 )
Total stockholders equity	61,690	(66 )	61,624	63,223	(282 )	62,941	69,476	(588 )	68,888
	\$ 131,783	\$ (109)	\$ 131,674	\$ 137,726	\$ (314)	\$ 137,412	\$ 150,942	\$ 238	\$ 151,180



**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

The changes to the consolidated balance sheets reflected in the table above as a result of the restatement are summarized below.

- As of December 31, 2004, the changes arising from the restatement primarily relate to the following:
  - Cash and cash equivalents increased by \$229, or 0.9%, as a result of a reclassification of deposits in the balance sheet to correct an error in recording unrestricted cash in deposits.
  - Intangible assets, net increased by \$584, or 5.7%, as a result of a reclassification of certain other assets in the balance sheet to conform to the current presentation.
  - Accrued liabilities decreased by \$112, or 0.8%, as of December 31, 2004. This decrease relates to a \$253 adjustment of the royalty expense which was overstated in 2004 and understated in 2005, offset in part by a \$191 adjustment to increase the foreign tax liability.
  - Deferred revenue decreased by \$225, or 1.6%, as of December 31, 2004. This decrease relates to a \$225 adjustment of amortization for warranty and training revenue.
  - Treasury stock increased by \$59, or 86.8%, as of December 31, 2004 as the result of a correction of an error for the incorrect recording of treasury stock at fair value in lieu of cost.
  - Other changes to the consolidated balance sheet line items at December 31, 2004 were not material, individually or in the aggregate. Such changes include miscellaneous adjustments to inventory, additional depreciation expense for items placed in service which had not been depreciated prior to restatement and miscellaneous reconciliation adjustments.
- As of each quarter end in 2005, the changes arising from the restatement primarily relate to the following:
  - Primarily as a result of reclassifications of amounts in the balance sheet, the following changes were noted:
    - Cash and cash equivalents increased by \$295, or 1.1%, as of March 31, 2005 creating a decrease of \$295 in prepaid expenses and other current assets as a result of a previous error in recording unrestricted cash in prepaid expenses and other current assets. Prepaid expenses and other current assets decreased, in total, by \$295, or 3.8% as of March 31, 2005.
    - Cash and cash equivalents increased by \$243, or 0.9%, as of June 30, 2005 while prepaid expenses and other current assets decreased, in total, by \$224, or 2.5%, as of June 30, 2005.
    - Cash and cash equivalents increased by \$242, or 0.9%, as of September 30, 2005 while prepaid expenses and other current assets decreased, in total, by \$221, or 2.2%, as of September 30, 2005.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

(amounts in thousands, except per share data)

(unaudited)

- Cash and cash equivalents increased by \$216, or 0.9%, as of December 31, 2005 while deposits decreased by \$216, or 100%, as of December 31, 2005. Intangible assets increased \$587, or 7.3%, and other assets decreased \$587, or 37.3% as of December 31, 2005.
- The increase in accounts receivable as of March 31, 2005 primarily relates to an adjustment for recognition of warranty and training revenue while the decreases in accounts receivable as of June 30, 2005, September 30, 2005 and December 31, 2005 primarily relate to adjustments for credit memoranda discussed above that were applicable to each period.
- Inventory increased by \$850 (6.1%) as of December 31, 2005 only. The increase in inventory as of December 31, 2005 primarily relates to the \$716 accrual for inventory in transit at year end where title had transferred.
- Property and equipment, net decreased by \$174 or 1.4% as of December 31, 2005 for depreciation associated with assets placed into service in that period.
- Accounts payable increased \$735, or 6.7%, as of December 31, 2005 primarily to reflect the \$716 liability associated with the in-transit inventory recorded.
- Deferred revenue decreased by \$236 (1.7%) as of March 31, 2005 and changed by nominal amounts as of the last day of the second and fourth quarters. The first-quarter decrease in deferred revenue relates to a \$236 adjustment to recognition of warranty and training revenue.
- Additional paid-in capital decreased by \$59 (0.1%) as of March 31, 2005 and June 30, 2005, decreased by \$62 (0.1%) as of September 30, 2005 and decreased by \$353 (0.3%) as of December 31, 2005. The decrease at each date was the result of a correction of an error for the incorrect recording of treasury stock at fair value in lieu of cost. Additionally, at December 31, 2005, the decrease included a \$211 adjustment for the issuance of securities which were charged to additional paid-in capital as discussed above. This change for the issuance of securities will be reflected in all future balance sheet restatements contained herein.
- Treasury stock increased by \$59 (86.8%) as of March 31, 2005 and June 30, 2005, increased by \$62 (87.3%) as of September 30, 2005 and increased by \$142 (92.2%) as of December 31, 2005 as the result of a correction of an error in recording treasury stock as discussed above.
- Other changes to the balance sheet line items for the 2005 periods were not material, individually or in the aggregate. Such changes include miscellaneous adjustments to inventory, additional depreciation expense for items placed in service which had not been depreciated prior to restatement.

The segment information contained in Note 24 to the Company's Consolidated Financial Statements included in Form 10-K for the year ended December 31, 2005 contains a table of assets allocated by

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

geographic region that has been restated as of December 31, 2005 to reflect the corrections to the allocation of assets by geographic region as well as the effect of the adjustments to the December 31, 2005 balance sheet discussed above. The corrections were required due to previous calculation errors in compiling the appropriate data by geographic region.

	<b>December 31, 2005 (As Previously Reported)</b>	<b>Restatement Adjustments</b>	<b>December 31, 2005 (restated)</b>
<b>Assets:</b>			
North America	\$ 102,891	\$ (26,026 )	\$ 76,865
Germany	29,624	(15,268 )	14,356
Other Europe	42,770	13,004	55,774
Asia	20,426		20,426
Subtotal	195,711	(28,290 )	167,421
Inter-company elimination	(44,770 )	28,529	(16,241 )
Total assets	\$ 150,941	\$ 239	\$ 151,180

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The impact of the restatement on the condensed consolidated balance sheet as of March 31, 2006 is as follows:

<b>Consolidated Balance Sheet</b>	<b>2006 As Previously Reported March 31 (amounts in \$000s)</b>	<b>Restatement Adjustments</b>	<b>Restated</b>
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$ 26,398	\$ 216	\$ 26,614
Accounts receivable	29,735	(418 )	29,317
Inventories	16,410	(66 )	16,344
Deferred tax assets	2,500		2,500
Prepaid expenses and other current assets	9,910	(526 )	9,384
Asset held for sale			
Total current assets	84,953	(794 )	84,159
Property and equipment, net	13,605	(281 )	13,324
Intangible assets, net	7,949		7,949
Goodwill	44,843		44,843
Restricted cash, long-term	1,200		1,200
Other assets, net	837		837
	\$ 153,387	\$ (1,075 )	\$ 152,312
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>			
Current liabilities:			
Current portion of long-term debt	\$ 210	7	\$ 217
Accounts payable	12,525		12,525
Accrued liabilities	12,143	343	12,486
Customer deposits	1,353		1,353
Deferred revenue	14,198	(119 )	14,079
Total current liabilities	40,429	231	40,660
Long-term debt, less current portion	3,435	21	3,456
Convertible subordinated debentures	22,604		22,604
Other liabilities	1,060	(36 )	1,024
	67,528	216	67,744
Preferred stock	15,257		15,257
Stockholders' equity:			
Common stock	16		16
Additional paid-in capital	111,344	(4,534 )	106,810
Deferred compensation	(4,127 )	4,127	
Treasury stock, at cost; 17 shares at March 31, 2006	(213 )	196	(17 )
Accumulated deficit in earnings	(35,631 )	(1,080 )	(36,711 )
Accumulated other comprehensive income (loss)	(787 )		(787 )
Total stockholders' equity	70,602	(1,291 )	69,311
	\$ 153,387	\$ (1,075 )	\$ 152,312

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

The changes to the balance sheet reflected in the table above as a result of the restatement are summarized below.

- As of March 31, 2006, the changes arising from the restatement primarily relate to the following:
  - Cash and cash equivalents increased by \$216, or 0.8%, as of March 31, 2006. As noted below within prepaid expenses and other current assets, this increase relates to the reclassification of certain cash amounts in the balance sheet.
  - Accounts receivable decreased by \$418, or 1.4%, as of March 31, 2006. The decrease primarily relates to adjustments for credit memoranda as discussed above.
  - Prepaid expenses and other current assets decreased by \$526, or 5.3%, as of March 31, 2006. The decrease primarily relates to \$201 of reconciliation adjustments related to prepaid materials and a \$216 adjustment related to the reclassification of certain amounts held on deposit to cash and cash equivalents.
  - Inventories decreased by \$66, or 0.4%, as of March 31, 2006. The decrease in the first quarter related to an adjustment for credit memoranda as discussed above.
  - Property and equipment decreased by \$281, or 2.1%, as March 31, 2006. The first-quarter decrease relates primarily to adjustments to record additional depreciation expense for items placed in service that had not been removed from CIP accounts prior to the restatement.
  - Accrued liabilities increased by \$343, or 2.8%, as of March 31, 2006. The first-quarter increase primarily relates to a \$207 adjustment for professional fees for the 2005 financial statement audit partially offset by a tax credit of \$53.
  - Additional paid-in capital decreased \$404 as of March 31, 2006 to reflect \$211 of the stock issuance costs incurred in 2005 as discussed above and \$193 as the result of a correction of an error for the incorrect recording of treasury stock at fair value in lieu of cost.
  - Other changes to the balance sheet line items were not material, individually or in the aggregate. Such changes included a balance-sheet reclassification for unrestricted cash, miscellaneous adjustments to inventory, adjustments to amortization for warranty and training revenue and an adjustment to correct the processing of payments received for restricted stock.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The impact of the restatement on the consolidated statement of cash flows for the year ended December 31, 2004 is as follows:

<b>Consolidated Statement of Cash Flows</b>	<b>Year Ended As Previously Reported December 31, 2004 (amounts in \$000s)</b>	<b>Restatement Adjustments</b>	<b>Restated</b>
Cash flows from operating activities:			
Net income	\$ 2,561	\$ 459	\$ 3,020
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	6,956		6,956
Bad debt benefit	(216 )		(216 )
Adjustments for inventory reserve	(310 )		(310 )
Stock-based compensation	634		634
Non-cash payment of interest on employee note with Common Stock	(4 )		(4 )
Loss on disposition of property and equipment	231		231
Changes in operating accounts:			
Deposits	338	(338 )	
Accounts receivable	1,537	13	1,550
Lease receivable	21		21
Inventories	(189 )	(60 )	(249 )
Prepaid expenses and other current assets	(2,908 )	50	(2,858 )
Other assets	316		316
Accounts payable	(448 )	35	(413 )
Accrued liabilities	(2,849 )	(304 )	(3,153 )
Customer deposits	48		48
Deferred revenue	(2,340 )	(193 )	(2,533 )
Other liabilities	(450 )	(2 )	(452 )
Net cash provided by operating activities	2,928	(340 )	2,588
Cash flows used in investing activities:			
Purchases of property and equipment	(781 )		(781 )
Additions to license and patent costs	(417 )		(417 )
Software development costs	(737 )		(737 )
Net cash used in investing activities	(1,935 )		(1,935 )
Cash flows from financing activities:			
Stock options, stock purchase plan and restricted stock proceeds	4,898	1	4,899
Repayment of long-term debt	(165 )		(165 )
Payments under obligation to former stockholders of 3D Systems S.A.	(852 )		(852 )
Payment of preferred stock dividends	(1,420 )		(1,420 )
Payment of accrued liquidated damages	(837 )		(837 )
Stock issuance costs	(428 )		(428 )
Payment to OptoForm minority shareholder	(49 )		(49 )
Net cash provided by financing activities	1,147	1	1,148
Effect of exchange rate changes on cash	182	14	196
Net increase in cash and cash equivalents	2,322	(325 )	1,997
Cash and cash equivalents, beginning of period	23,954	554	24,508
Cash and cash equivalents, end of period	\$ 26,276	\$ 229	\$ 26,505

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The changes for the year ended December 31, 2004 displayed in the table above are the result of the restatement adjustments previously described in this Note 2.

The impact of the restatement on the condensed consolidated statements of cash flows for the three, six, nine and twelve month periods ended March 31, 2005, June 30, 2005, September 30, 2005 and December 31, 2005, respectively, is as follows:

Consolidated Statement of Cash Flows	Three Months Ended			Six Months Ended		
	As Previously Reported	Restatement Adjustments	Restated	As Previously Reported	Restatement Adjustments	Restated
	March 31, 2005			June 30, 2005		
	(amounts in \$000s)					
Cash flows from operating activities:						
Net income	\$ 1,195	\$ (2 )	\$ 1,193	\$ 2,494	\$ (366)	\$ 2,128
Adjustments to reconcile net income to net cash provided by (used in) operating activities:						
Provision for deferred income taxes		94	94		347	347
Depreciation and amortization	1,549	19	1,568	3,122	55	3,177
Bad debt provision (benefit)	(39 )		(39 )	(122 )		(122 )
Adjustments for inventory reserve	(97 )		(97 )	(694 )		(694 )
Stock-based compensation	75		75	551		551
Loss (gain) on disposition of property and equipment	1		1	38		38
Changes in operating accounts:						
Deposits	(78 )	78		(40 )	40	
Accounts receivable	1,754	(31 )	1,723	1,699	48	1,747
Lease receivable	68		68	200		200
Inventories	653	(18 )	635	(240 )	(8 )	(248 )
Prepaid expenses and other current assets	(2,183 )	(50 )	(2,233 )	(3,566 )	(69 )	(3,635 )
Other assets	(105 )		(105 )	54		54
Accounts payable	(40 )	(34 )	(74 )	(1,682 )	(35 )	(1,717 )
Accrued liabilities	(2,818 )	(45 )	(2,863 )	(3,459 )	(279 )	(3,738 )
Customer deposits	(26 )		(26 )	109		109
Deferred revenue	494	22	516	(930 )	235	(695 )
Other liabilities	(91 )	(41 )	(132 )	(419 )	(7 )	(426 )
Net cash provided by (used in) operating activities	312	(8 )	304	(2,885 )	(39 )	(2,924 )
Cash flows used in investing activities:						
Purchases of property and equipment	(764 )	87	(677 )	(788 )	79	(709 )
Proceeds on disposition of property and equipment						
Additions to license and patent costs	(132 )		(132 )	(238 )		(238 )
Software development costs	(222 )		(222 )	(444 )		(444 )
Net cash used in investing activities	(1,118 )	87	(1,031 )	(1,470 )	79	(1,391 )
Cash flows from financing activities:						
Stock options, stock purchase plan and restricted stock proceeds	1,115		1,115	7,240		7,240
Repayment of long-term debt	(90 )	1	(89 )	(90 )	2	(88 )
Payments under obligation to former stockholders of 3D Systems S.A.	(219 )		(219 )	(439 )		(439 )
Payment of preferred stock dividends				(785 )		(785 )
Stock issuance costs				(103 )		(103 )
Payment of accrued liquidated damages	(36 )		(36 )	(36 )		(36 )
Net cash provided by financing activities	770	1	771	5,787	2	5,789
Effect of exchange rate changes on cash	267	(14 )	253	413	(28 )	385
Net increase (decrease) in cash and cash equivalents	231	66	297	1,845	14	1,859
Cash and cash equivalents, beginning of period	26,276	229	26,505	26,276	229	26,505
Cash and cash equivalents, end of period	\$ 26,507	\$ 295	\$ 26,802	\$ 28,121	\$ 243	\$ 28,364





**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

Consolidated Statement of Cash Flows	Nine Months Ended		Restated	Year Ended		
	As Previously Reported	Restatement Adjustments		As Previously Reported	Restatement Adjustments	Restated
	September 30, 2005			December 31, 2005		
	(amounts in \$000s)					
Cash flows from operating activities:						
Net income	\$ 3,655	\$ (582)	\$ 3,073	\$ 10,083	\$ (677)	\$ 9,406
Adjustments to reconcile net income to net cash provided by (used in) operating activities:						
Deferred income taxes, net of valuation allowance				(2,500 )		(2,500 )
Depreciation and amortization	4,715	97	4,812	5,764	162	5,926
Bad debt provision (benefit)	16		16	(48 )		(48 )
Adjustments for inventory reserve	(720 )		(720 )	(733 )		(733 )
Stock-based compensation	699		699	941		941
Loss (gain) on disposition of property and equipment	(54 )		(54 )	(262 )		(262 )
Changes in operating accounts:						
Deposits	(39 )	39		(13 )	13	
Accounts receivable	(909 )	212	(697 )	(13,008 )	393	(12,615 )
Lease receivable	344		344	448		448
Inventories	(5,189 )	(17 )	(5,206 )	(7,907 )	(868 )	(8,775 )
Prepaid expenses and other current assets	(4,839 )	(71 )	(4,910 )	(4,207 )	(18 )	(4,225 )
Other assets	229		229	69	(90 )	(21 )
Accounts payable	1,044	(35 )	1,009	4,211	700	4,911
Accrued liabilities	(2,599 )	92	(2,507 )	(148 )	255	107
Customer deposits	1,228		1,228	1,157		1,157
Deferred revenue	(1,131 )	225	(906 )	763	182	945
Other liabilities	(460 )	(6 )	(466 )	(418 )	(7 )	(425 )
Net cash provided by (used in) operating activities	(4,010 )	(46 )	(4,056 )	(5,808 )	45	(5,763 )
Cash flows used in investing activities:						
Purchases of property and equipment	(1,873 )	87	(1,786 )	(2,603 )	87	(2,516 )
Proceeds on disposition of property and equipment	98		98	727		727
Additions to license and patent costs	(504 )		(504 )	(372 )		(372 )
Software development costs	(635 )		(635 )	(598 )	90	(508 )
Net cash used in investing activities	(2,914 )	87	(2,827 )	(2,846 )	177	(2,669 )
Cash flows from financing activities:						
Stock options, stock purchase plan and restricted stock proceeds	8,020		8,020	8,135		8,135
Repayment of long-term debt	(180 )	3	(177 )	(180 )	3	(177 )
Payments under obligation to former stockholders of 3D Systems S.A.	(585 )		(585 )	(585 )		(585 )
Payment of preferred stock dividends	(785 )		(785 )	(1,617 )		(1,617 )
Stock issuance costs	(211 )		(211 )		(211 )	(211 )
Payment of accrued liquidated damages	(36 )		(36 )	(36 )		(36 )
Net cash provided by financing activities	6,223	3	6,226	5,717	(208 )	5,509
Effect of exchange rate changes on cash	416	(31 )	385	773	(27 )	746
Net increase (decrease) in cash and cash equivalents	(285 )	13	(272 )	(2,164 )	(13 )	(2,177 )
Cash and cash equivalents, beginning of period	26,276	229	26,505	26,276	229	26,505
Cash and cash equivalents, end of period	\$ 25,991	\$ 242	\$ 26,233	\$ 24,112	\$ 216	\$ 24,328

The changes for each period displayed in the table above are the result of the restatement adjustments previously described in this Note 2.



**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The impact of the restatement on the condensed consolidated statement of cash flows for the three-month period ended March 31, 2006 is as follows:

<b>Consolidated Statement of Cash Flows</b>	<b>Three Months Ended</b>		
	<b>As Previously Reported March 31, 2006 (amounts in \$000s)</b>	<b>Restatement Adjustments</b>	<b>Restated</b>
<b>Cash flows from operating activities:</b>			
Net loss	\$ (833 )	\$ (704 )	\$ (1,537 )
<b>Adjustments to reconcile net loss to net cash provided by (used in) operating activities:</b>			
Provision for deferred income taxes		23	23
Depreciation and amortization	1,514	105	1,619
Bad debt provision (benefit)	60		60
Adjustments to inventory reserves		(170 )	(170 )
Stock-based compensation	452		452
Loss (gain) on disposition of property and equipment	2		2
<b>Changes in operating accounts:</b>			
Accounts receivable	3,639	11	3,650
Lease receivable		20	20
Inventories	(2,352 )	422	(1,930 )
Prepaid expenses and other current assets	(395 )	420	25
Other assets	93	90	183
Accounts payable	1,550	(735 )	815
Accrued liabilities	(495 )	19	(476 )
Customer deposits	(594 )		(594 )
Deferred revenue	353	(76 )	277
Other liabilities	(2 )	3	1
Net cash provided by (used in) operating activities	2,992	(572 )	2,420
<b>Cash flows used in investing activities:</b>			
Purchases of property and equipment	(2,184 )	600	(1,584 )
Proceeds on disposition of property and equipment	150		150
Additions to license and patent costs	(159 )		(159 )
Software development costs	(40 )	(90 )	(130 )
Net cash used in investing activities	(2,233 )	510	(1,723 )
<b>Cash flows from financing activities:</b>			
Stock options, stock purchase plan and restricted stock proceeds	1,687		1,687
Repayment of long-term debt	(100 )	(2 )	(102 )
Net cash provided by financing activities	1,587	(2 )	1,585
Effect of exchange rate changes on cash	(60 )	64	4
Net increase (decrease) in cash and cash equivalents	2,286		2,286
Cash and cash equivalents, beginning of period	24,112	216	24,328
Cash and cash equivalents, end of period	\$ 26,398	\$ 216	\$ 26,614

The changes for the period displayed in the table above are the result of the restatement adjustments previously described in this Note 2.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005**

(amounts in thousands, except per share data)

(unaudited)

**(3) Inventories**

Components of inventories, net are as follows:

	<b>March 31, 2006 Restated</b>	<b>December 31, 2005 Restated</b>
Raw materials	\$ 2,645	\$ 207
Inventory held by assemblers	680	417
Work in process	94	55
Finished goods	12,925	14,131
	<b>\$ 16,344</b>	<b>\$ 14,810</b>

Inventory held by assemblers at March 31, 2006 and December 31, 2005 represented inventory sold to those assemblers and accounted for in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 49, Accounting for Product Financing Arrangements, issued by the Financial Accounting Standards Board ( FASB ). See Note 4.

**(4) Outsourcing of Assembly and Refurbishment Activities**

During 2004, the Company engaged selected design and manufacturing companies to assemble its equipment portfolio and discontinued its equipment assembly activities at its Grand Junction, Colorado facility. This included its InVision® 3-D printing equipment, its Viper SLA® systems and certain other equipment items, the refurbishment of used equipment systems, and the assembly of field service kits for sale by the Company to its customers.

The Company agreed to sell to those third parties components of its raw materials inventory related to those systems. Such sales were recorded in the financial statements as a product financing arrangement under SFAS No. 49. Pursuant to SFAS No. 49, as of March 31, 2006 and December 31, 2005, the Company's consolidated balance sheets included a non-trade receivable of \$1,047 and \$1,051, respectively, classified in prepaid expenses and other current assets reflecting the book value of the inventory sold to the assemblers for which the Company had not received payment. At March 31, 2006 and December 31, 2005, \$680 and \$417, respectively, remained in inventory with a corresponding amount included in accrued liabilities representing the Company's non-contractual obligation to purchase assembled systems and refurbished parts produced from such inventory. Under these arrangements, the Company generally purchases assembled systems from the assemblers following the Company's receipt of an order from a customer or as needed from the assembler to repair a component or to service equipment. Under certain circumstances, the Company anticipates that it may purchase assembled systems from the assemblers prior to the receipt of an order from a customer. At March 31, 2006 and December 31, 2005, the Company had made \$4,885 and \$5,271, respectively, of progress payments to assemblers for systems forecasted to be required for resale to customers after such dates. These progress payments were recorded in prepaid expenses and other current assets in the consolidated balance sheets.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)****(5) Property and Equipment, net**

Property and equipment is summarized as follows:

	<b>March 31, 2006 Restated</b>	<b>December 31, 2005 Restated</b>	<b>Useful Life (in years)</b>
Land	\$ 436	\$ 436	
Building	4,202	4,202	30
Machinery and equipment	21,227	21,603	3-5
Office furniture and equipment	3,013	3,022	5
Leasehold improvements	3,504	3,534	Life of Lease
Rental equipment	877	910	5
Construction in progress	5,496	3,785	N/A
	38,755	37,492	
Less: Accumulated depreciation	(25,431 )	(25,500 )	
	\$ 13,324	\$ 11,992	

Depreciation expense for the three months ended March 31, 2006 and March 31, 2005 was \$736 and \$653 on a restated basis, respectively. Leasehold improvements are amortized on a straight-line basis over the shorter of (i) their estimated useful lives and (ii) the estimated or contractual life of the related lease. The Company has accelerated amortization of the leasehold improvements related to the Valencia facility as a result of its plan to vacate the facility in September 2006. Such accelerated amortization amounted to \$20 in the first quarter of 2006.

The Company ceased operations at its Grand Junction, Colorado facility on April 28, 2006. The facility was listed for sale during the first quarter of 2006 at an amount in excess of its net book value. Effective on May 1, 2006, approximately \$3,454 in net assets on a restated basis associated with the facility were reclassified on the Company's consolidated balance sheet from long-term assets to current assets, where they will be recorded as assets held for sale. Following such reclassification, the Company ceased to record depreciation expense related to this facility, which amounted to \$570 per year. The Company expects to realize an amount from the disposition of these assets in excess of their net book value and in excess of the remaining balance of the industrial development bonds used to finance the facility. See Note 8.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)****(6) Intangible Assets****(a) Licenses and Patent Costs**

Licenses and patent costs are summarized as follows:

	<b>March 31, 2006 Restated</b>	<b>December 31, 2005 Restated</b>	<b>Weighted average useful life (in years)</b>
Licenses, at cost	\$ 2,333	\$ 2,333	fully amortized
Patent costs	18,393	18,226	7.7
	20,726	20,559	
Less: Accumulated amortization	(15,376 )	(15,034 )	
	\$ 5,350	\$ 5,525	

For the three months ended March 31, 2006 and March 31, 2005, the Company capitalized \$167 and \$132, respectively, of costs to acquire, develop and extend patents in the United States and certain other countries. The Company amortized \$342 and \$336 of previously capitalized patent costs for the three months ended March 31, 2006 and March 31, 2005, respectively.

**(b) Acquired Technology**

Acquired technology is summarized as follows:

	<b>March 31, 2006 Restated</b>	<b>December 31, 2005 Restated</b>
Acquired technology	\$ 10,172	\$ 10,148
Less: Accumulated amortization	(8,087 )	(7,683 )
	\$ 2,085	\$ 2,465

The remaining unamortized acquired technology was purchased in 2001 in connection with the DTM acquisition and assigned a useful life of six years, extending to 2007. In the first quarters of 2006 and 2005, the Company amortized \$404 and \$379, respectively, of acquired technology. The Company expects the total amortization expense with respect to remaining unamortized acquired technology to be \$1,596 in 2006 and \$1,008 in 2007, at which time these costs will be fully amortized.

**(c) Other Intangible Assets**

The Company had \$514 and \$587 of other net intangible assets as of March 31, 2006 and December 31, 2005, respectively. Amortization expense related to such intangible assets for the three months ended March 31, 2006 and March 31, 2005 was \$165 and \$200, respectively.

**(7) Hedging Activities and Derivative Instruments**

The Company and its subsidiaries conduct business in various countries using both its functional currencies and other currencies to effect cross-border transactions. As a result, the Company and its



**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

subsidiaries are subject to the risk that fluctuations in foreign exchange rates between the dates that those transactions are entered into and their respective settlement dates will result in a foreign exchange gain or loss. When practicable, the Company endeavors to match assets and liabilities in the same currency on its balance sheet and those of its subsidiaries in order to reduce these risks. The Company also, when it considers it to be appropriate, enters into foreign currency contracts to hedge exposures arising from those transactions. The Company has not adopted hedge accounting under SFAS No. 133, Accounting for Derivatives and Hedging Activities, as amended by SFAS No. 137 and SFAS No. 138, and all gains and losses (realized or unrealized) are recognized in cost of sales in the Condensed Consolidated Statements of Operations. The Company has entered into forward contracts to purchase and to sell foreign currencies. The purchase contracts related primarily to the purchases of inventory agreed to be made from suppliers denominated in Swiss francs. The foreign currency sales contracts were denominated in euros, pound sterling and Japanese yen and were entered into to hedge intercompany purchase obligations of the Company's subsidiaries. The respective notional amounts of the forward currency contracts outstanding as of March 31, 2006 aggregated Swiss francs 611 (equivalent to \$473 at settlement date), euros 500 (equivalent to \$597 at settlement date), pounds sterling 300 (equivalent to \$524 at settlement date) and Japanese yen 210,000 (equivalent to \$1,792 at settlement date).

During 2005, the Company entered into a range-forward arrangement with a large, creditworthy financial institution to hedge certain other currency-rate exposures in Japanese yen. This arrangement established a collar around a range of exchange rates between 106.0 and 113.5 Japanese yen to the U.S. Dollar to hedge 95,000 Japanese yen (approximate equivalent range of \$896 to \$837) of inter-company payments from the Company's Japanese subsidiary. Both the put and call options entered into under the hedge arrangement were for the same monetary amount and maturity date.

The dollar equivalent of the foreign currency contracts and related fair values as of March 31, 2006 and December 31, 2005 were as follows:

	Foreign Currency Option Contracts		Foreign Currency Purchase Contracts		Foreign Currency Sales Contracts	
	March 31, 2006 Restated	December 31, 2005 Restated	March 31, 2006 Restated	December 31, 2005 Restated	March 31, 2006 Restated	December 31, 2005 Restated
Notional amount	\$	\$ 837	\$ 473	\$ 1,269	\$ 2,912	\$ 4,624
Fair value		866	469	1,258	2,917	4,519
Net unrealized gain (loss)	\$	\$ 29	\$ (4 )	\$ (11 )	\$ (5 )	\$ 105

The net fair value of all of these contracts at March 31, 2006 and December 31, 2005 reflected unrealized gains (losses) of \$(9) and \$123, respectively. These foreign currency contracts expire at various dates between April 4, 2006 and April 20, 2006.

Changes in the fair value of derivatives are recorded in cost of sales in the consolidated statements of operations. Depending on their fair value at the end of the reporting period, derivatives are recorded either in prepaid expenses and other current assets or in accrued liabilities in the consolidated balance sheets.

The total impact of foreign currency related items on the consolidated statement of operations was a gain of \$78 and \$499 for the quarters ended March 31, 2006 and March 31, 2005, respectively.



**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

The Company is exposed to credit risk if the counterparties to such transactions are unable to perform their obligations. However, the Company seeks to minimize such risk by entering into transactions with counterparties that are believed to be creditworthy financial institutions.

**(8) Borrowings**

Total outstanding borrowings were as follows:

	March 31, 2006 Restated	December 31, 2005 Restated
Line of credit	\$	\$
Industrial development revenue bonds:		
Current portion of long-term debt	\$ 210	\$ 200
Long-term debt, less current portion	3,435	3,545
Total	\$ 3,645	\$ 3,745
Subordinated debt:		
6% convertible subordinated debentures	\$ 22,604	\$ 22,604
Installment note:		
Current portion of installment note	\$ 7	\$ 7
Installment note, less current portion	21	23
Total	\$ 28	\$ 30
Total current portion of debt	\$ 217	\$ 207
Total long-term portion of debt	26,060	26,172
Total debt	\$ 26,277	\$ 26,379

*Silicon Valley Bank loan and security agreement*

The Company maintains a loan and security agreement with Silicon Valley Bank that, as amended, is scheduled to expire on July 1, 2007. This credit facility provides that the Company and certain of its subsidiaries may borrow up to \$15,000 of revolving loans and includes sub-limits for letter of credit and foreign exchange facilities. The credit facility is secured by a first lien in favor of Silicon Valley Bank on certain of the Company's assets, including domestic accounts receivable, inventory and certain fixed assets. Interest accrues on outstanding borrowings at either the Bank's prime rate in effect from time to time or at a LIBOR rate plus 2.25%. The Company is obligated to pay, on a quarterly basis, a commitment fee equal to 0.375% per annum of the unused amount of the facility.

The facility, as amended, imposes certain limitations on the Company's activities, including limitations on the incurrence of debt and other liens, limitations on the disposition of assets, limitations on the making of certain investments and limitations on the payment of dividends on the Company's Common Stock. The facility also requires the Company to maintain (a) a quick ratio (as defined in the credit facility) of at least 1.00 as of the end of each calendar quarter and (b) a ratio of total liabilities less subordinated debt to

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

tangible net worth (as each such term is defined in the credit facility) of not more than 2.00 as of December 31, 2005 and at the end of each calendar quarter thereafter. The credit facility also requires that the Company maintain, on a trailing four-quarter basis, EBITDA (as defined in the credit facility) in an amount not less than \$18 million for certain periods ending on or before December 31, 2005 and, as amended effective March 30, 2006, not less than \$15 million for each period ending on or after March 31, 2006. The Company believes that it was in compliance with these requirements at March 31, 2006, both prior to and after giving effect to the restatement herein. Additionally, the Company believes that it was in compliance with these financial covenants at December 31, 2005, except for the minimum EBITDA covenant, which non-compliance the Bank agreed to waive.

At March 31, 2006 and December 31, 2005, respectively, the Company had \$357 and \$1,659 of foreign exchange forward contracts outstanding with Silicon Valley Bank. No borrowings or letters of credit were outstanding under this facility at either March 31, 2006 or December 31, 2005. See Note 7.

*Industrial development bonds*

The Company's Grand Junction, Colorado facility was financed by industrial development bonds in the original aggregate principal amount of \$4,900. At March 31, 2006, the outstanding principal amount of these bonds was \$3,645. Interest on the bonds accrues at a variable rate of interest and is payable monthly. The interest rate at March 31, 2006 was 3.2%. Principal payments are due in semi-annual installments through August 2016. The Company has made all required payments of principal and interest on these bonds. The bonds are collateralized by, among other things, a first mortgage on the facility, a security interest in certain equipment and an irrevocable letter of credit issued by Wells Fargo Bank, N.A. pursuant to the terms of a reimbursement agreement between the Company and Wells Fargo. The Company is required to pay an annual letter of credit fee equal to 1% of the stated amount of the letter of credit.

This letter of credit is in turn collateralized by \$1,200 of restricted cash that Wells Fargo holds. Effective November 9, 2005, the Company entered into an amendment to the reimbursement agreement with Wells Fargo pursuant to which such funds will be held in a non-interest-bearing account at Wells Fargo, and Wells Fargo will have a security interest in that account as partial security for the performance of the Company's obligations under the reimbursement agreement. Under that amendment, the Company also has the right to substitute a standby letter of credit issued by a bank acceptable to Wells Fargo as collateral in place of the funds held in that account.

The reimbursement agreement, as amended, contains financial covenants that require, among other things, that the Company maintain a minimum tangible net worth (as defined in the reimbursement agreement) of \$23.0 million plus 50% of net income from July 1, 2001 forward and a fixed-charge coverage ratio (as defined in the reimbursement agreement) of no less than 1.25. The Company is required to demonstrate its compliance with these financial covenants as of the end of each calendar quarter. As of March 31, 2006 and December 31, 2005, both prior to and after giving effect to the restatement contained herein, the Company was in compliance with these financial covenants.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

As discussed above, the Company ceased operations at the Grand Junction facility on April 28, 2006 and intends subsequently to sell it. At the time the Company sells the facility, it expects to either pay off these bonds or, with the approval of Wells Fargo, have them assumed by a qualified buyer.

*6% Convertible Subordinated Debentures*

In the fourth quarter of 2003, the Company privately placed \$22,704 of 6% convertible subordinated debentures with institutional and accredited investors. The net proceeds from the issuance of these debentures, after deducting capitalized issuance costs of \$578, amounted to \$22,126. The capitalized issuance costs are being amortized to interest expense over the 10-year life of the debentures. The 6% convertible subordinated debentures bear interest at the rate of 6% per year payable semi-annually in arrears in cash on May 31 and November 30 of each year. They are convertible into shares of Common Stock at the option of the holders at any time prior to maturity at \$10.18 per share, subject to customary anti-dilution adjustments. The Company has the right to redeem the debentures, in whole or in part, commencing on November 24, 2006 at a price equal to 100% of the then outstanding principal amount of the debentures being redeemed, together with all accrued and unpaid interest and other amounts due in respect of the debentures. The aggregate principal amount of these debentures then outstanding matures on November 30, 2013. If the Company undergoes a change in control (as defined), the holders may require the Company to redeem the debentures at 100% of their then outstanding principal amount, together with all accrued and unpaid interest and other amounts due in respect of the debentures. At March 31, 2006, they were convertible into an aggregate of 2,220 shares of Common Stock.

The debentures are subordinated in right of payment to senior indebtedness (as defined). At the time the debentures were issued, the Company granted registration rights to the purchasers of the debentures pursuant to which, subject to certain terms and conditions, the Company agreed to file a registration statement to register for resale under the Securities Act of 1933, as amended (the Securities Act), the shares of Common Stock into which the debentures are convertible. The conditions to the Company's obligation to file such registration statement have not yet been satisfied, and no such registration statement is currently pending. The Company is not subject to any penalties under the terms of such registration rights if it fails to comply with its obligation to file such registration statement once the conditions to such filing have been satisfied.

*Installment Loans*

The installment debt relates to an auto loan for a term of 72 months at \$0.7 per month for a motor vehicle that the Company purchased in December 2003 for the use of the Company's chief executive officer as provided for in his employment agreement entered into in 2003. The implicit rate is 8% per annum.

**(9) Convertible Preferred Stock**

On May 5, 2003, the Company privately placed 2,634 shares of Series B Convertible Preferred Stock at a price of \$6.00 per share with institutional and accredited investors. Net proceeds were \$15,167 after deducting \$637 of offering expenses. The offering expenses were recorded as a reduction to the face value

37

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**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

of the redeemable preferred stock and are being accreted as dividends over ten years. The Series B Convertible Preferred Stock accrues dividends, on a cumulative basis, at \$0.60 per share each year while it remains outstanding. Prior to May 6, 2004, the cumulative dividend rate was \$0.48 per share per year. The Series B Convertible Preferred Stock is senior to the Company's Common Stock and any other stock that ranks junior to the Series B Convertible Preferred Stock. Dividends are payable semi-annually, when, as and if declared by the Board of Directors, on May 5 and November 5 of each year while these shares remain outstanding. In addition, the Series B Convertible Preferred Stock votes equally with the Company's Common Stock and is convertible at any time at the option of the holders on a share-for-share basis. The Series B Convertible Preferred Stock is redeemable at the Company's option at any time after May 5, 2006. The Company must redeem any shares of Series B Convertible Preferred Stock that remain outstanding on May 5, 2013. The redemption price in either case is \$6.00 per share plus any accrued and unpaid dividends. At March 31, 2006, 2,617 shares of Series B Convertible Stock were issued and outstanding.

**(10) Stock-based Compensation Plans**

The Company maintains stock-based compensation plans that are described more fully in Note 18, "Stockholders' Equity," to the Consolidated Financial Statements for the year ended December 31, 2005, filed with the Company's Annual Report on Form 10-K.

The Company adopted SFAS No. 123R effective January 1, 2006 and began recording compensation expense for previously issued options that vest subsequent to that date. Compensation expense for the three months ended March 31, 2006 for options that vested during the quarter was \$179. Compensation expense is included in selling, general and administrative expenses on the Condensed Consolidated Statements of Operations. The Company used a Black-Scholes option pricing model to determine the fair value of the unvested options at March 31, 2006. The compensation expense reflects a reduction in expense for an annualized 6.25% forfeiture rate and also reflects a stock price volatility rate of 0.41. No stock options have been granted since 2004.

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

Prior to January 1, 2006, the Company applied the intrinsic-value-based method of accounting prescribed by APB Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations to account for stock options previously issued under its stock option plans. These interpretations include FASB Interpretation No. 44, Accounting for Certain Transactions Involving Stock Compensation, an interpretation of APB Opinion No. 25, issued in March 2000. Under this method, compensation expense is generally recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. Prior to January 1, 2006, the Company applied the disclosure only provisions of SFAS No. 123, Accounting for Stock-Based Compensation, and SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure, which was released in December 2002 as an amendment to SFAS No. 123. These statements established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. The Company has elected to apply SFAS No. 123R prospectively only. The following pro forma net income and net income per share information is presented for 2005 only as if the Company had commenced applying SFAS No. 123R in 2005 for stock-based compensation awarded under its stock-based compensation plans using the fair value method. Under the fair value method, the estimated fair value of stock-based incentive awards is charged against income on a straight-line basis over the vesting period.

	<b>Three Months Ended March 31, 2005 Restated</b>
Net income available to common stockholders as restated	\$ 781
Deduct: Stock-based employee compensation expense determined under the fair value method for all awards	427
Pro forma net income	\$ 354
Basic net income available to common stockholders per share:	
As restated	\$ 0.05
Pro forma	\$ 0.02
Diluted net income available to common stockholders per share:	
As restated	\$ 0.05
Pro forma	\$ 0.02

During the first quarter of 2006 and 2005, the Company made restricted stock awards covering 141 and 55 shares, respectively and net of repurchases, of Common Stock to certain employees, including executive officers, pursuant to the Company's 2004 Incentive Stock Plan. Shares of restricted Common Stock awarded under that Plan are issued for a purchase price of \$1.00 per share and are subject to forfeiture for a period of three years following their date of grant in the event that the recipient leaves the employ of the Company other than as a result of death or disability. The Company records deferred compensation in stockholders' equity with respect to such awards in an amount equal to the difference between the fair market value of the Common Stock covered by each award on the date of grant less the amount payable by each recipient. For the quarters ended March 31, 2006 and 2005, the Company

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

recorded \$2,765 and \$941, respectively, of deferred compensation expense and \$188 and \$32, respectively, of amortization expense related to deferred compensation with respect to restricted stock awards. In both years, certain of such awards were made in lieu of, or as an alternative to, cash bonuses that had previously been accrued with respect to 2005 or 2004, as the case may be. As a result, the Company reduced its accrual for 2005 cash-based bonuses by a net amount of \$256 in the first quarter of 2006 and, for 2004, reduced its accrual for cash-based bonuses by a net amount of \$256 in the first quarter of 2005.

**(11) Computation of Net Income (Loss) Per Share**

The following is a reconciliation of the numerator and denominator of the basic and diluted net income (loss) per share computations:

	<b>Three Months Ended March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
<b>Numerator:</b>		
Net income (loss) available to common stockholders numerator for dilutive net income (loss) per share	\$ (1,948 )	\$ 781
<b>Denominator:</b>		
Denominator for basic net income (loss) per share weighted average shares	15,366	14,575
Add:		
Effect of dilutive securities:		
Stock options and restricted stock		1,238
Preferred stock		
6% convertible subordinated debentures		
Denominator for diluted net income (loss) per share weighted average shares	15,366	15,813

For the three months ended March 31, 2006, 2,617 shares of Common Stock issuable upon the conversion of the Series B Convertible Preferred Stock, 2,220 shares issuable upon conversion of convertible debentures and 835 shares issuable upon the exercise of stock options were excluded from the calculation of diluted net loss per share because their effects would have been anti-dilutive, that is, they would have reduced net loss per share.

For the quarter ended March 31, 2005, 2,618 shares of Common Stock issuable upon conversion of the Series B Convertible Preferred Stock and 2,225 shares issuable upon conversion of convertible debentures were excluded from the calculation of diluted net income (loss) per share because their effects would have been anti-dilutive, that is, they would have increased net income per share available to the common stockholders.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

**(12) Income Taxes**

The Company used a 1.5% effective income tax rate to determine its income tax provision for the first quarter of 2006, which reflected the effect of the utilization of foreign net operating loss carry-forwards in certain tax jurisdictions.

During the fourth quarter of 2005, the Company reduced its valuation allowance for its deferred tax assets by \$2.5 million and recorded a net deferred tax asset on its consolidated balance sheet as a result of its determination that it was more likely than not that it would be able to utilize a portion of its deferred tax assets attributable to U.S. taxes in 2006 in light of the improvement in the Company's operations and management's expectation of future taxable income. Utilization of that tax asset depends on future taxable income of the Company.

As of March 31, 2006, except for the \$2.5 million net deferred tax asset described above, the Company maintained a full valuation allowance on all of its deferred tax assets, including net operating loss carry-forwards, in various tax jurisdictions. The Company intends to continue to assess the valuation allowance periodically under the standards of SFAS No. 109, Accounting for Income Taxes.

For a discussion of other tax matters relating to the Company, please see Note 23 to the Consolidated Financial Statements that are set forth in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

**(13) Segment Information**

The Company operates in one reportable business segment in which it develops, manufactures and markets worldwide rapid 3-D printing, prototyping and manufacturing systems designed to reduce the time it takes to produce three-dimensional objects. The Company conducts its business through operations in the United States, sales and service offices in the European Community (France, Germany, the United Kingdom and Italy) and Asia (Japan and Hong Kong), and a research and production facility in Switzerland. Revenue from unaffiliated customers attributed to Germany includes sales by the Company's German unit to customers in countries other than Germany. The Company has historically disclosed summarized financial information for the geographic areas of operations as if they were segments in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information.

41

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**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

Such summarized financial information concerning the Company's geographical operations is shown in the following tables:

	<b>Three Months Ended March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
<b>Revenue from unaffiliated customers:</b>		
North America	\$ 18,394	\$ 14,245
Germany	4,699	5,156
Other Europe	6,413	5,991
Asia	4,137	5,032
Total	\$ 33,643	\$ 30,424

All revenue between geographic areas is recorded at transfer prices which are above cost and provide for an allocation of profit between entities.

	<b>Three Months Ended March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
<b>Revenue from or transfers between geographic areas:</b>		
North America	\$ 8,793	\$ 9,248
Germany	1,011	726
Other Europe	865	1,351
Asia		
Total	\$ 10,669	\$ 11,325

	<b>Three Months Ended March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
<b>Income (loss) from operations:</b>		
North America	\$ (536 )	\$ 2,111
Germany	449	(242 )
Other Europe	(1,356 )	78
Asia	484	255
Subtotal	(959 )	2,202
Inter-company elimination	(388 )	(569 )
Total	\$ (1,347 )	\$ 1,633

**3D SYSTEMS CORPORATION****Notes to Condensed Consolidated Financial Statements (Restated) (Continued)****For the Three Months Ended March 31, 2006 and 2005****(amounts in thousands, except per share data)****(unaudited)**

	<b>March 31, 2006 Restated</b>	<b>December 31, 2005 Restated</b>
Assets:		
North America	\$ 89,146	\$ 76,865
Germany	13,913	14,356
Other Europe	53,699	55,774
Asia	12,700	20,426
Subtotal	169,458	167,421
Inter-company elimination	(17,146 )	(16,241 )
Total assets	\$ 152,312	\$ 151,180

The Company's revenue from unaffiliated customers by type is as follows:

	<b>Three Months Ended</b>	
	<b>March 31, 2006 Restated</b>	<b>March 31, 2005 Restated</b>
Systems and other products	\$ 12,379	\$ 10,145
Materials	11,873	10,093
Services	9,391	10,186
Total sales	\$ 33,643	\$ 30,424

**(14) Commitments and Contingencies***Rock Hill Facility Lease Agreement*

On February 8, 2006, the Company entered into a Lease Agreement with KDC-Carolina Investments 3, LP pursuant to which KDC agreed to construct and to lease to the Company an approximately 80 square foot building in Rock Hill, South Carolina in connection with the relocation of the Company's headquarters from Valencia, California, and the transfer of certain operations of its Grand Junction, Colorado facility, to Rock Hill. Under the terms of this Lease, KDC will lease the building to the Company for an initial 15-year term following completion.

After its initial term, the Lease provides the Company with the option to renew the Lease for two additional five-year terms as well as the right to cause KDC, subject to certain terms and conditions, to expand the leased premises during the term of the Lease, in which case the term of the Lease would be extended. The Lease is a triple net lease and provides for the payment of base rent of approximately \$707 in each of full calendar years one through five, \$750 in each of calendar years nine through ten and \$794 in each of calendar years eleven through fifteen. Under the terms of the Lease, the Company will be obligated to pay all taxes, insurance, utilities and other operating costs with respect to the leased premises. The Lease also grants the Company the right to purchase the leased premises and undeveloped land surrounding the leased premises on terms and conditions described more particularly in the Lease.

**3D SYSTEMS CORPORATION**

**Notes to Condensed Consolidated Financial Statements (Restated) (Continued)**

**For the Three Months Ended March 31, 2006 and 2005**

**(amounts in thousands, except per share data)**

**(unaudited)**

*Symyx Agreement*

Effective April 1, 2006, the Company entered into an agreement with Symyx Technologies, Inc. under which the Company and Symyx will work together to discover and commercialize advanced materials for use in the Company's rapid prototyping and rapid manufacturing solutions. Under this agreement, the Company will fund up to \$2,400 of research over a two-year period to enable Symyx to develop new materials formulations that the Company would commercialize for rapid prototyping and rapid manufacturing applications.

*Certain Legal Matters*

On May 6, 2003, the Company received a subpoena from the U.S. Department of Justice to provide certain documents to a grand jury investigating antitrust and related issues within its industry. The Company understands that the issues being investigated include issues involving the consent decree that the Company entered into and that was filed on August 16, 2001 with respect to the Company's acquisition of DTM Corporation and the requirement of that consent decree that the Company issue a broad intellectual property license with respect to certain patents and copyrights to another entity already manufacturing rapid prototyping industrial equipment. The Company complied with the requirement of that consent decree for the grant of that license in 2002. In connection with that investigation, the grand jury has taken testimony from various individuals, including certain of its current and former employees and executives. The Company was advised that it is not a target of the grand jury investigation, and the Company has not been informed that this status has changed. The Company has furnished documents required by the subpoena and is otherwise complying with the subpoena.

The Company is involved in various legal matters incidental to its business. The Company's management believes, after consulting with counsel, that the disposition of these other legal matters will not have a material effect on the Company's consolidated results of operations or consolidated financial position.

## **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

This discussion should be read in conjunction with the Condensed Consolidated Financial Statements and the notes thereto included in Item 1 of this Quarterly Report on Form 10-Q/A.

We are subject to a number of risks and uncertainties that may affect our future performance, as discussed in greater detail in the sections entitled "Forward-Looking Statements" and "Cautionary Statements and Risk Factors" at the end of this Item 2 and Item 1A of Part II of this Quarterly Report on Form 10-Q/A.

### **Business Overview**

We design, develop, manufacture, market and service rapid 3-D printing, prototyping and manufacturing systems and related products and materials and provide customer services that enable complex three-dimensional objects to be produced directly from computer data without tooling, greatly reducing the time and cost required to produce prototypes or customized production parts. Our consolidated revenue is derived primarily from the sale of our systems, the sale of the related materials used by the systems to produce solid objects and the provision of services to our customers.

### **Restatement of Financial Statements**

On November 3, 2006, we announced that management and the Audit Committee of our Board of Directors had determined, based on information presented by our management in connection with the preparation of our financial statements for the third quarter of 2006, that our financial statements included in our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2006 and June 30, 2006 contained errors. As a result, the Audit Committee concluded that those financial statements should be restated and that investors should not rely upon those financial statements without taking into account the effects of the restated financial information that is included in this Form 10-Q/A.

We also announced at that time that we were assessing whether our financial statements for prior periods should be restated. On December 14, 2006, we announced that management and the Audit Committee had completed our assessment of the prior-period financial statements and that, based on information presented by our management, the financial statements included in our Annual Reports on Form 10-K for the 2004 and 2005 calendar years also contained errors and should be restated. In evaluating the need to restate those periods, we also took into consideration audit adjustments that had been identified previously as not being material to our financial statements for those periods and have included those adjustments in the restated amounts for the applicable 2005 and 2004 periods.

We have identified and evaluated the errors noted in our prior-period financial statements and have corrected those errors through adjustments reflected in the restated historical consolidated financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 154 (SFAS No. 154), Accounting Changes and Error Corrections. We also assessed on a quarterly basis the materiality of prior-period misstatements that were previously identified but not corrected because they were originally considered to be immaterial. As a result of our analysis of adjustments identified during the third quarter of 2006 which were attributable to prior periods as well as previously unadjusted amounts attributable to prior periods, we concluded the prior-period impact was material in the second and fourth quarters of 2005 as well as for the year ended December 31, 2004. Therefore, the restated financial information reflects adjustments to correct or record all such previously unadjusted amounts.

This Quarterly Report on Form 10-Q/A includes all of the restated financial information for each period ended March 31, 2006 and earlier affected by the restatement. Such restated financial information will also be included in our Annual Report on Form 10-K for the year ended December 31, 2006.

We identified the errors in the 2006 financial statements primarily as a result of our efforts to remediate the material weaknesses that we previously identified and disclosed with respect to our second quarter 2006 financial statements as well as through our ongoing efforts to:

- (a) implement our new ERP system;
- (b) reconcile the records in our new ERP system and those in our legacy systems; and
- (c) test our internal controls in the context of the new ERP system environment.

As part of these efforts, management:

- (i) has carried out a comprehensive account reconciliation initiative to test and verify the accuracy and integrity of information recorded by, and data imported and input from our legacy accounting system into, the new ERP system;
- (ii) is continuing to train employees in the use of the new ERP system and our established system of internal controls; and
- (iii) is continuing to promote adherence to those internal controls.

We have also performed physical inventory counts and a variety of other confirmatory procedures. See Part I, Item 4, Controls and Procedures.

The following table shows the impact of the correction of all errors on income (loss) available to common stockholders for the full years ended December 31, 2004 and 2005 and for each calendar quarter in 2005 and 2006 through March 31, 2006 as well as the cumulative impact of prior-period adjustments on retained earnings at December 31, 2003. The tax effect of the correction of these errors on each restated period was either nominal or nil.

Table 1

	Accumulated Deficit in Earnings December 31, 2003 (dollars in \$000s)	Effect of Restatement on Income (Loss) Available to Common Stockholders						Year Ended December 31, 2005	Quarter Ended March 31, 2006
		Year Ended December 31, 2004	Quarter Ended March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005	December 31, 2005		
Previously reported	\$ (47,442)	\$ 1,027	\$ 783	\$ 855	\$ 749	\$ 6,017	\$ 8,404	\$ (1,244)	
Adjustments:									
Credit memos		10	(19 )	(79 )	(164 )	(101 )	(363 )	(251 )	
Royalty income/expense		253	5	(17 )	(17 )	(293 )	(322 )	13	
Recognition of warranty and training revenue	32	220	11	(246 )	13	33	(189 )	121	
Stock issuance costs						211	211		
Prepaid materials reconciliation				(29 )	(4 )	(64 )	(97 )	(201 )	
Depreciation of fixed assets		(4 )	(19 )	(37 )	(42 )	(63 )	(161 )	(106 )	
Accrual for professional services						(15 )	(15 )	(247 )	
Inventory usage						22	22		
Other		(20 )	20	44	(2 )	(16 )	46	(86 )	
Tax provision	(191 )					191	191	53	
Total adjustments:	(159 )	459	(2 )	(364 )	(216 )	(95 )	(677 )	(704 )	
Restated	\$ (47,601)	\$ 1,486	\$ 781	\$ 491	\$ 533	\$ 5,922	\$ 7,727	\$ (1,948)	
Net income (loss) available to common stockholders per share diluted (as previously reported)		\$ 0.07	\$ 0.05	\$ 0.05	\$ 0.05	\$ 0.32	\$ 0.53	\$ (0.08 )	
Effect of restatement		0.04	(0.00 )	(0.02 )	(0.02 )	(0.00 )	(0.05 )	(0.05 )	
Net income (loss) available to common stockholders per share diluted (restated)		\$ 0.11	\$ 0.05	\$ 0.03	\$ 0.03	\$ 0.32	\$ 0.48	\$ (0.13 )	

As shown in this table, the adjustments for errors reflected in the restated financial information primarily include:

- \$0.6 million in the aggregate of errors related to credit memoranda issued to customers, of which \$0.3 million was attributable to the first quarter of 2006, \$0.4 million was attributable to the 2005 periods and a nominal credit was attributable to 2004.
- \$0.3 million in the aggregate of errors related to the reconciliation of prepaid materials accounts from sub-ledger to general ledger, substantially all of which was attributable to the first quarter of 2006, and \$0.1 million of which was attributable to the 2005 periods.
- \$0.3 million in the aggregate of errors related to additional depreciation expense for items placed in service that had not been removed from construction-in-progress ( CIP ) accounts prior to the restatement, of which \$0.1 million was attributable to the first quarter of 2006, \$0.2 million was attributable to the 2005 periods and a nominal amount was attributable to 2004.
- \$0.3 million in the aggregate of errors in related to accrued professional services, which was primarily attributable to the first quarter of 2006.
- \$0.2 million in the aggregate of errors related to state and foreign income taxes, of which \$0.1 million was attributable to the first quarter of 2006 and \$0.2 million was attributable to the 2005 periods.

See Note 2 to the Condensed Consolidated Financial Statements for a detailed discussion of these errors.

The aggregate effect of these adjustments was to:

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- increase net loss by \$0.7 million, or 56.6%, from \$1.2 million as originally reported to \$1.9 million as restated for the quarter ended March 31, 2006;
- decrease net income by \$0.7 million, or 8.1%, from \$8.4 million as originally reported to \$7.7 million as restated for the year ended December 31, 2005, and for the respective quarters of 2005 to
- nominally decrease net income for the quarter ended March 31, 2005;

47

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- decrease net income by \$0.4 million or 42.6% and from \$0.9 million as originally reported to \$0.5 million as restated for the quarter ended June 30, 2005;
- decrease net income by \$0.2 million or 28.8% and from \$0.7 million as originally reported to \$0.5 million as restated for the quarter ended September 30, 2005; and
- decrease net income by \$0.1 million or 1.6% and from \$6.0 million as originally reported to \$5.9 million as restated for the quarter ended December 31, 2005; and
- increase net income by \$0.5 million, or 44.7%, for the year ended December 31, 2004 from \$1.0 million as originally reported to \$1.5 million as restated.

On a per share basis, the aggregate effect of these adjustments was to:

- increase diluted net loss per share by \$0.05 from \$0.08 as originally reported to \$0.13 as restated for the quarter ended March 31, 2006;
- decrease diluted net income per share by \$0.05 from \$0.53 as originally reported to \$0.48 as restated for the year ended December 31, 2005;
- for the respective quarters of 2005:
  - there was no change to diluted net income per share of \$0.05 for the quarter ended March 31, 2005;
  - diluted net income per share decreased by \$0.02 from \$0.05 as originally reported to \$0.03 as restated for the quarter ended June 30, 2005;
  - diluted net income per share decreased by \$0.02 from \$0.05 as originally reported to \$0.03 as restated for the quarter ended September 30, 2005; and
  - there was no change to diluted net income per share for the quarter ended December 31, 2005;
- the sum of diluted net income per share for the 2005 quarters does not equal the diluted net income per share for the year ended December 31, 2005 as the quarterly calculations of weighted average shares outstanding are made independently based on the shares applicable to each period, which were not affected by the restatement;
- increase diluted net income per share by \$0.04 from \$0.07 as originally reported to \$0.11 as restated for the year ended December 31, 2004.

Compared to the amounts originally reported, the restatement resulted in a \$0.2 million increase in cash and cash equivalents at March 31, 2006 that arose from the reclassification of certain unrestricted deposits previously erroneously recorded in prepaid expenses and other current assets.

The restatement also resulted in a \$0.3 million increase in cash and cash equivalents at March 31, 2005, a \$0.2 million increase in cash and cash equivalents at June 30, 2005, September 30, 2005 and December 31, 2005 and a \$0.2 million increase in cash and cash equivalents at December 31, 2004 primarily as a result of the reclassification of certain amounts previously erroneously recorded as prepaid expenses and other current assets, as discussed above. See Note 2 to the Condensed Consolidated Financial Statements.





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The restatement also resulted in a \$0.2 million reduction to the ending retained earnings balance on December 31, 2003 for errors related to prior periods.

Refer to Note 2 to the Condensed Consolidated Financial Statements and the discussion below for further information with respect to the causes and the effect of the restatement of our Consolidated Financial Statements.

### *Impact of Restatement on 2006 Condensed Consolidated Financial Statements*

As a result of the errors that we identified in connection with our financial statements for the third quarter of 2006, we have restated our consolidated statement of operations, consolidated balance sheet and the consolidated statement of cash flows for the three-month period ended March 31, 2006. The effect of these restatements is discussed below.

*Condensed Consolidated Statement of Operations.* The effect of the errors that we identified on our statement of operations for the first quarter of 2006 are shown in Table 2.

**Table 2**

Changes in Consolidated Statement of Operations	March 31, 2006 (amounts in \$000s)
Revenue	\$ 116
Cost of sales	526
Gross profit	(410 )
Operating expenses	294
Operating loss	(704 )
Interest and other expense, net	53
Loss before income taxes	(757 )
Income tax provision (benefit)	(53 )
Net loss	\$ (704 )

As shown in Table 2, the changes in the first quarter of 2006 relate primarily to the following items:

- Revenue increased \$0.1 million, or 0.2%, for the quarter ended March 31, 2006. The increase in revenue during the first quarter primarily relates to \$121 of adjustments related to the recognition of warranty and training revenue, \$59 of adjustments related to royalty income and \$160 of other adjustments, partially offset by \$224 of adjustments for credit memoranda that were applicable to the first quarter.
- Cost of sales increased by \$0.5 million, or 2.7%, for the quarter ended March 31, 2006. The first-quarter increase in cost of sales primarily relates to a \$0.2 million reconciliation adjustment related to prepaid materials and \$0.2 million of other adjustments, each as discussed in Note 2.
- Operating expenses increased by \$0.3 million, or 2.0%, for the quarter ended March 31, 2006. The first-quarter increase in operating expenses primarily relates to a \$0.2 million adjustment to record an increase in professional fees and a \$0.1 million adjustment to record additional depreciation expense for items placed in service that had not been removed from CIP accounts prior to the restatement.
- Interest and other expense, net increased by \$0.1 million, or 46.5%, for the quarter ended March 31, 2006. The increase relates to \$0.1 million of adjustments to record interest income in the correct periods.

- The changes in the income tax provision during the first quarter represents an adjustment to the foreign income tax provision accrual discussed in Note 2.

*Condensed Consolidated Balance Sheet.* The identified errors impacted the balance sheet line items at March 31, 2006 as follows:

**Table 3**

Changes in Consolidated Balance Sheet	March 31, 2006 (amounts in \$000s)
<b>Current Assets:</b>	
Cash	\$ 216
Accounts receivable	(418 )
Inventory	(66 )
Prepaid expenses and other current assets	(526 )
Total current assets	\$ (794 )
<b>Other Assets:</b>	
Property and equipment	\$ (281 )
<b>Current Liabilities:</b>	
Current portion of long-term debt	\$ 7
Accrued liabilities	343
Deferred revenue	(119 )
Total current liabilities	\$ 231
<b>Other Liabilities:</b>	
Long-term debt, less current portion	\$ 21
Other liabilities	(36 )
Total other liabilities	\$ (15 )
Stockholders' Equity	\$ (1,291 )

The changes for the period relate primarily to the following:

- Cash and cash equivalents increased by \$0.2 million, or 0.8%, as of March 31, 2006. As noted below within the description of prepaid expenses and other current assets, these increases relate to the reclassification of amounts in the balance sheet.
- Accounts receivable decreased by \$0.4 million, or 1.4%, as of March 31, 2006. The decrease primarily relates to adjustments for credit memoranda for customers as discussed above.
- Prepaid expenses and other current assets decreased by \$0.5 million, or 5.3%, as of March 31, 2006. The decrease in prepaid expenses and other current assets primarily relates to \$0.2 million of reconciliation adjustments related to prepaid materials and a \$0.2 million adjustment related to the reclassification of certain amounts held on deposit to cash and cash equivalents.
- Property and equipment decreased by \$0.3 million, or 2.1%, as March 31, 2006. The decrease in property and equipment relates primarily to adjustments to record additional depreciation expense for items placed in service that had not been removed from CIP accounts prior to the restatement.
- Accrued liabilities increased by \$0.3 million, or 2.8%, as of March 31, 2006. The increase primarily relates to a \$0.2 million adjustment for professional fees for the 2005 financial statement audit partially offset by a tax credit of \$0.1 million.



- Additional paid-in capital decreased \$0.4 million as of March 31, 2006 to reflect a charge for stock issuance costs in 2005 as discussed above and for the correction of an error in recording treasury stock as previously discussed.

Other changes to the balance sheet line items were not material, individually or in the aggregate. Such changes included a balance-sheet reclassification for unrestricted cash, miscellaneous adjustments to inventory, adjustments to amortization for warranty and training revenue and an adjustment to correct the processing of payments received for restricted stock.

*Consolidated Statements of Cash Flows.* As a result of the restatement, cash and cash equivalents increased by \$0.2 million as of March 31, 2006. This increase was the result of a reclassification of unrestricted cash on the balance sheet as discussed above. Table 4 shows the impact that the errors corrected by the restatement had on the statement of cash flow.

**Table 4**

Changes in Consolidated Statement of Cash Flows	Three months ended March 31, 2006 (amounts in \$000s)
Net loss	\$ (704 )
Non-cash operating items	(42 )
Changes to operating accounts	174
Net cash provided by (used in) operating activities	(572 )
Cash provided by (used in) investing activities	510
Cash provided by financing activities	(2 )
Effects of exchange rate changes on cash	64
Net increase (decrease) in cash and cash equivalents	
Cash and cash equivalents, beginning of period	216
Cash and cash equivalents, end of period	\$ 216

For the three months ended March 31, 2006, on a restated basis:

- The \$0.6 million decrease in net cash provided by operating activities primarily relates to the \$0.7 million increase in net loss arising from the restatement, the \$0.7 million decrease in accounts payable, the \$0.1 million decrease in deferred revenue, and a nominal decrease in non-cash items that was offset by \$1.0 million of cash provided by changes to operating accounts not mentioned above, including primarily changes to inventories, prepaid expenses and other current assets and other assets that occurred for the reasons discussed above.
- The \$0.5 million increase in net cash provided by investing activities relates to the decrease in fixed asset purchases during the period offset in part by an increase in software development costs during the period as a result of the restatement adjustments.

*Impact of Restatement on 2005 Consolidated Financial Statements*

As a result of the errors that we identified at the end of the third quarter of 2006 and our evaluation of the impact on 2005 of the audit adjustments for periods prior to 2006 that we had previously considered to be nonmaterial, we have restated our consolidated financial statements for each calendar quarter in 2005 and for the year ended December 31, 2005. As discussed above, for the year ended December 31, 2005, on a restated basis:

- Total revenue decreased by \$0.6 million or 0.4% from \$139.7 million to \$139.1 million;
- Total cost of sales increased by \$0.4 million or 0.5% from \$76.5 million to \$76.9 million;



- Total operating expenses decreased nominally;
- Income from operations decreased by \$0.9 million or 10.0% from \$9.3 million to \$8.4 million; and
- Income available to common stockholders decreased by \$0.7 million or 8.1% from \$8.4 million to \$7.7 million.

The effects of that restatement on the 2005 quarterly periods are discussed below.

*Condensed Consolidated Statements of Operations.* Table 5 shows the effect of the restatement on the 2005 quarterly statements of operations line items.

**Table 5**

Changes in Consolidated Statement of Operations	2005 Quarter Ended		September 30	December 31
	March 31	June 30		
	(amounts in \$000s)			
Revenue	\$ (8 )	\$ (325 )	\$ (151 )	\$ (108 )
Cost of sales	(21 )	50	27	320
Gross profit	13	(375 )	(178 )	(428 )
Operating expenses	14	37	43	(132 )
Operating income	(1 )	(412 )	(221 )	(296 )
Interest and other expense, net	1	(48 )	(5 )	(10 )
Income before income taxes	(2 )	(364 )	(216 )	(286 )
Income tax provision (benefit)				(191 )
Net income	\$ (2 )	\$ (364 )	\$ (216 )	\$ (95 )

The changes in each period primarily relate to the following:

- Revenue decreased nominally for the first quarter of 2005, by \$0.3 million (1.0%) for the second quarter, by \$0.2 million (0.5%) for the third quarter and by \$0.1 million (0.2%) for the quarter ended December 31, 2005. The decreases in revenue during the third and fourth quarters primarily relate to adjustments for credit memoranda for customers discussed above. These amounted to \$0.2 million in the third quarter and \$0.1 million in the fourth quarter. The decrease in revenue during the second quarter primarily relates to a \$0.2 million adjustment related to amortization for warranty and training revenue and \$0.1 million of adjustments for credit memoranda for customers discussed above.
- Cost of sales increased by \$0.3 million (1.4%) for the fourth quarter and changed nominally in the other quarters. The increase in cost of sales during the fourth quarter primarily relates to the correction of the recognition of royalty expense.
- Operating expenses decreased by \$0.1 million (0.8%) during the fourth quarter, and increased nominally for the first, second and third quarters. The decrease in the fourth quarter is the result of corrections made to capitalize stock issuance costs as a reduction of additional paid-in capital, offset in part by a combination of additional depreciation being recorded for assets placed in service and accrual of professional fees. The first-quarter, second-quarter and third-quarter increases primarily relate to additional depreciation being recorded for assets placed in service.

- The nominal changes to interest and other expense, net relate to an increase in interest income in the affected quarters.
- The income tax benefit recorded in the fourth quarter relates to the correction of a foreign tax provision in 2005 which was applicable to prior periods.

*Condensed Consolidated Balance Sheets.* Table 6 shows the impact of the restatement of our 2005 financial statements on the 2005 quarterly balance sheet line items.

**Table 6**

Changes in Consolidated Balance Sheet	2005			
	March 31	June 30	September 30	December 31
	(amounts in \$000s)			
<b>Current Assets:</b>				
Cash	\$ 295	\$ 243	\$ 242	\$ 216
Accounts receivable	18	(61 )	(225 )	(406 )
Inventory				850
Prepaid expenses and other current assets	(295 )	(224 )	(221 )	(32 )
Deposits				(216 )
Total current assets	\$ 18	\$ (42 )	\$ (204 )	\$ 412
<b>Other Assets:</b>				
Property and equipment	\$ (29 )	\$ (67 )	\$ (110 )	\$ (174 )
Intangible assets, net				587
Other assets, net				(587 )
Total other assets	\$ (29 )	\$ (67 )	\$ (110 )	\$ (174 )
<b>Current Liabilities:</b>				
Current portion of long-term debt	\$ 6	\$ 6	\$ 6	\$ 7
Accounts payable				735
Accrued liabilities	(65 )	(45 )	(24 )	142
Deferred revenue	(236 )	10		(43 )
Total current liabilities	\$ (295 )	\$ (29 )	\$ (18 )	\$ 841
<b>Other Liabilities:</b>				
Long-term debt, less current portion	\$ 29	\$ 27	\$ 26	\$ 23
Other liabilities	(43 )	(41 )	(40 )	(38 )
Total other liabilities	\$ (14 )	\$ (14 )	\$ (14 )	\$ (15 )
Stockholders' Equity	\$ 298	\$ (66 )	\$ (282 )	\$ (588 )

The changes in each period primarily relate to the following:

- The increases in cash and cash equivalents in each period relate to the reclassification of unrestricted deposits from prepaid expenses and other current assets or deposits in the balance sheet to cash and cash equivalents in order to conform to the current presentation.
- The increase in accounts receivable as of March 31, 2005 primarily relates to an adjustment for recognition of warranty and training revenue while the decreases in accounts receivable as of June 30, 2005, September 30, 2005 and December 31, 2005 primarily relate to adjustments for credit memoranda for customers discussed above that were applicable to each period.



- Inventory increased by \$0.9 million (6.1%) as of December 31, 2005 and nominally at each of the other balance sheet dates. The increase in inventory as of December 31, 2005 primarily relates to an increase in the accrual for inventory in transit from our suppliers where title had passed at year end.
- As noted above, the decreases in prepaid expenses and other current assets as of March 31, 2005, June 30, 2005 and September 30, 2005 primarily relate to the reclassification of amounts from prepaid expenses and other current assets to cash and cash equivalents in order to conform to the current presentation.
- As noted above, the decrease in deposits as of December 31, 2005 relates to the reclassification of amounts from deposits to cash and cash equivalents in order to conform to the current presentation.
- Intangible assets, net increased by \$0.6 million, or 7.3%, as of December 31, 2005 and was unchanged in the other periods. Other assets, net decreased by \$0.6 million, or 37.3%, as of December 31, 2005 and was unchanged in the other periods. These changes were the result of a reclassification of amounts between the two line items on the balance sheet.
- Accrued liabilities decreased by \$0.1 million, or 0.6%, at March 31, 2005, nominally by 0.5%, at June 30, 2005, nominally by 0.2% at September 30, 2005 and increased by \$0.1 million, or 1.2%, at December 31, 2005. The fourth quarter was impacted by \$0.2 million of adjustments, related to the reclassification of securities registration costs.
- Deferred revenue decreased by \$0.2 million (1.7%) as of March 31, 2005 and changed by nominal amounts as of the last day of the second and fourth quarters. The first-quarter decrease in deferred revenue relates to a \$0.2 million adjustment to recognition of warranty and training revenue.

Other changes to the balance sheet line items for the 2005 periods were not material, individually or in the aggregate. Such changes include miscellaneous adjustments to inventory, additional depreciation expense for items placed in service which had not been depreciated prior to restatement and miscellaneous reconciliation adjustments.

*Condensed Consolidated Statements of Cash Flows.* The restatement of our 2005 financial statements resulted in increases in cash and cash equivalents of \$0.3 million as of March 31, 2005 and \$0.2 million as of June 30, 2005, September 30, 2005 and December 31, 2005, respectively. These increases were the result of reclassifications within the balance sheet to conform to current presentation. Table 7 sets forth the impact of the restatement on our 2005 quarterly statements of cash flow.

Table 7

Changes in Consolidated Statement of Cash Flows	Three months ended March 31, 2005 (amounts in \$000s)	Six months ended June 30, 2005	Nine months ended September 30, 2005	Year ended December 31, 2005
Net income	\$ (2 )	\$ (366 )	\$ (582 )	\$ (677 )
Non-cash operating items	113	402	97	162
Changes to operating accounts	(119 )	(75 )	439	560
Net cash provided by (used in) operating activities	(8 )	(39 )	(46 )	45
Cash provided by (used in) investing activities	87	79	87	177
Cash provided by financing activities	1	2	3	(208 )
Effects of exchange rate changes on cash	(14 )	(28 )	(31 )	(27 )
Net increase (decrease) in cash and cash equivalents	66	14	13	(13 )
Cash and cash equivalents, beginning of period	229	229	229	229
Cash and cash equivalents, end of period	\$ 295	\$ 243	\$ 242	\$ 216

The changes in each period primarily relate to the following:

For the year ended December 31, 2005, on a restated basis:

- The nominal increase in net cash provided by operating activities for the year primarily relates to the \$0.7 million reduction in net income for the year that was more than offset by cash generated from \$0.6 million of changes to operating accounts and a \$0.2 million increase in depreciation and other non-cash items. The changes in operating accounts were primarily due to changes in accounts receivable, inventories, accounts payable, accrued liabilities and deferred revenue.
- The \$0.2 million decrease in net cash used in investing activities for the year relates to the \$0.1 million reduction in purchases of property and equipment and the \$0.1 million reduction in software development costs.
- The increase in net cash provided by operating activities and decrease in net cash used in investing activities was offset by a \$0.2 million decrease in net cash provided by financing activities resulting from a decrease in securities issuance costs included in those cash flows.

For the nine months ended September 30, 2005, the \$0.6 million decline in net income arising from the restatement was more than offset by an increase in non-cash items and changes in operating accounts, and a decrease in net cash used in investing activities.

Similarly, for the six months ended June 30, 2005, the \$0.4 million decline in net income and the \$0.1 million decrease in changes to operating accounts arising from the restatement was more than offset by an increase in non-cash items and a decrease in net cash used in investing activities.

For the three months ended March 31, 2005, the nominal decrease in net income and the \$0.1 million decrease in changes to operating accounts arising from the restatement was offset by an increase in non-cash items and a decrease in net cash used in investing activities.

*Impact of the Restatement on 2004 Consolidated Financial Statements*

As a result of the errors that we identified at the end of the third quarter of 2006 and our evaluation of the impact on our 2004 consolidated financial statements of the audit adjustments for periods prior to 2006 that we had previously considered to be nonmaterial, we have restated our consolidated financial statements for the year ended December 31, 2004.

*Condensed Consolidated Statement of Operations.* Table 8 shows the effect of the restatement on our consolidated statement of operations for the year ended December 31, 2004.

**Table 8**

<b>Changes in Consolidated Statement of Operations</b>	<b>December 31, 2004</b> (amounts in \$000s)
Revenue	\$ 231
Cost of sales	(234 )
Gross profit	465
Operating expenses	4
Operating income	461
Interest and other expense, net	2
Income before income taxes	459
Net income	\$ 459

The changes in our operating results in 2004 arising out of the restatement primarily relate to the following:

- Revenue increased by \$0.2 million, or 0.2%, for the year. The increase in revenue primarily relates to a \$0.2 million adjustment of amortization for warranty and training revenue.
- Cost of sales decreased by \$0.2 million, or 0.5%. This decrease primarily relates to a \$0.3 million adjustment of royalty expense which was overstated in 2004 and understated in 2005.
- As a result of these changes, net income increased by \$0.5 million, or 44.7%.

*Consolidated Balance Sheet.* Table 9 shows the impact of the restatement of our 2004 consolidated balance sheet line items.

**Table 9**

Changes in Consolidated Balance Sheet	December 31, 2004 (amounts in \$000s)
<b>Current Assets:</b>	
Cash	\$ 229
Accounts receivable	(13 )
Inventory	(18 )
Prepaid expenses and other current assets	(50 )
Deposits	(229 )
Total current assets	\$ (81 )
<b>Other Assets:</b>	
Property and equipment	\$ 71
Intangible assets, net	584
Other assets, net	(584 )
Total other assets	\$ 71
<b>Current Liabilities:</b>	
Current portion of long-term debt	\$ 6
Accounts payable	35
Accrued liabilities	(112 )
Deferred revenue	(225 )
Total current liabilities	\$ (296 )
<b>Other Liabilities:</b>	
Long-term debt, less current portion	\$ 36
Other liabilities	(50 )
Total other liabilities	\$ (14 )
Stockholders' Equity	\$ 300

The changes in the December 31, 2004 consolidated balance sheet primarily relate to the following:

- The increase in cash and cash equivalents relates to the reclassification of amounts from deposits in the balance sheet to cash and cash equivalents as discussed above.
- As noted above, the decrease in deposits as of December 31, 2004 relates to the reclassification of amounts from deposits to cash and cash equivalents in order to conform to the current presentation.
- Intangible assets, net increased by \$0.6 million as a result of a reclassification of certain other assets on the balance sheet.
- Accrued liabilities decreased by \$0.1 million, or 0.8%, as of December 31, 2004. This decrease relates to a \$0.3 million adjustment of the royalty expense which was overstated in 2004 and understated in 2005 offset in part by a \$0.2 million adjustment to increase the foreign tax liability.
- Deferred revenue decreased by \$0.2 million, or 1.6%, as of December 31, 2004. This decrease relates to a \$0.2 million adjustment of amortization for warranty and training revenue.

- Stockholders' equity increased by \$0.3 million, or 0.6%, as of December 31, 2004. This increase arose from the \$0.5 million increase in net income for the year ended December 31, 2004 as a result of the restatement adjustments and was partially offset by the cumulative effect of restatement adjustments prior to 2004.

Other changes to the consolidated balance sheet line items at December 31, 2004 were not material, individually or in the aggregate. Such changes included miscellaneous adjustments to inventory, additional depreciation expense for items placed in service which had not been removed from CIP accounts prior to restatement and miscellaneous reconciliation adjustments.

*Consolidated Statement of Cash Flows.* The restatement of our financial statements for the year ended December 31, 2004 resulted in a \$0.2 million increase in cash and cash equivalents as of December 31, 2004. This increase was the result of a reclassification within the balance sheet to conform to current presentation.. Table 10 sets forth the impact of the restatement on our consolidated statement of cash flow at December 31, 2004.

**Table 10**

Changes in Consolidated Statement of Cash Flows	Year ended December 31, 2004 (amounts in \$000s)
Net income	\$ 459
Changes to operating accounts	(799 )
Net cash provided by operating activities	(340 )
Cash provided by financing activities	1
Effects of exchange rate changes on cash	14
Net increase (decrease) in cash and cash equivalents	(325 )
Cash and cash equivalents, beginning of period	554
Cash and cash equivalents, end of period	\$ 229

As shown in Table 10, as a result of the restatement, cash provided by operating activities decreased \$0.3 million for the year ended December 31, 2004. The \$0.5 million increase in net income arising from the restatement was more than offset by restated changes to operating accounts. These items primarily included a \$0.3 million increase in deposits, a \$0.3 million decrease in accrued liabilities and a \$0.2 million decrease in deferred revenue.

The restatement did not affect cash used in investing activities and nominally affected cash provided by financing activities for the year ended December 31, 2004.

### Recent Developments

During the first quarter of 2006, we were engaged in several major projects that we expect to create long-term benefits. These include:

- Our planned relocation to Rock Hill, South Carolina;
- The implementation of an Oracle® enterprise resource planning (ERP) system;
- Establishment of an internal, centralized shared service center in Europe;
- Completion of the transfer of our InVision® materials production line to our Marly, Switzerland facility; and
- The outsourcing of our spare-parts supply activities to United Parcel Service, Inc.



During the first quarter of 2006, we also announced a strategic collaboration with Materialise, one of the industry's leaders in software development for rapid prototyping and manufacturing, to distribute jointly their Magics product line worldwide.

After the end of the first quarter, we also announced that we have entered into an agreement with Symyx Technologies, Inc. under which we and Symyx will work together to discover and commercialize advanced materials for use in our rapid prototyping and rapid manufacturing solutions. As we move forward with this research and development project, we will fund up to \$2.4 million of research by Symyx over a two-year period, and we expect Symyx to develop new materials formulations that should broaden the range of materials that we expect to make available to our customers for specialized rapid prototyping applications as well as rapid manufacturing applications.

With respect to our relocation project, during the first quarter of 2006, we opened an interim facility in Rock Hill, South Carolina, began to hire employees to replace departing employees, replicated functions in Rock Hill that were previously being performed at our Valencia and Grand Junction facilities and entered into a lease, which we have previously disclosed, for the construction of our new headquarters and research and development facility in Rock Hill. We also began work on exiting and disposing of our Valencia and Grand Junction facilities. The costs associated with these activities, which were generally in line with our previously announced expectations, adversely affected our profitability in the first quarter of 2006, and we expect that they will continue to hurt our profitability for the remainder of 2006.

Our Oracle®-based ERP system implementation is a project that we currently expect to involve a \$4 million investment in transactional automation and analysis tools and technology. During the first quarter of 2006, this program included hiring new staff in Rock Hill for training and testing of the new system while existing staff continued to perform those functions in Valencia using our legacy system. Consequently, we incurred duplicate staffing costs and incurred additional costs for some temporary staffing as a result of the combined effects of relocation and new-system start-up work. Operation of the new system began in the U.S. on May 1, 2006, and implementation in Europe and the Asia-Pacific region is planned for later in the second quarter of 2006. We expect this project to further improve our business processes and control environment.

During the first quarter of 2006, we established and began staffing a centralized European shared service center to provide order entry, invoicing, collection and other financial administration services for our operations throughout Europe. We expect this center to become operational in conjunction with our Oracle® ERP implementation in Europe, at which time we expect duplicative staffing costs in Europe relating to this center to be eliminated.

In preparation for the closure of our Grand Junction, Colorado facility, the manufacturing line for our InVision® material was moved from that facility to our facility in Marly, Switzerland, where it commenced operation in the first quarter of 2006. We also completed the outsourcing of our systems refurbishment activities previously conducted in Grand Junction during the first quarter of 2006. As we have previously disclosed, we outsourced our systems assembly operations from Grand Junction to third parties during 2004 and 2005. After the end of the first quarter of 2006, we outsourced the logistics and warehousing of our spare parts inventory in the U.S. to United Parcel Service, Inc., and we also plan to outsource those activities to UPS in Europe. As a result, the Grand Junction facility has been increasingly under-utilized, although a substantial portion of the overhead costs associated with that facility have continued. Operations ceased at that facility April 28, 2006. Consequently, we expect its subsequent carrying costs to decline and \$0.1 million of depreciation and amortization expense per quarter with respect to it to be curtailed with its reclassification as of May 1, 2006 to property held for sale. See Note 5 to the Condensed Consolidated Financial Statements.

Following on the heels of our rapid growth and record revenue in the fourth quarter of 2005 and the first quarter of 2006, we have experienced some growing pains as our initial success in placing new Sinterstation® Pro, Viper Pro and 3-D Printing systems has stretched our field engineering resources. We have found that these new, sophisticated, advanced systems, with their broader range of capabilities, require more extensive commissioning and training to achieve operating stability and operating potential. As a result of the high volume of sales of these systems that we have experienced in the past two quarters and the need to work closely with our customers to provide more extended customer training support and installation activities than the traditional services provided with our legacy systems, we have experienced field service resource constraints that have led to delayed start-up of some systems. We believe that the additional costs and foregone service revenue associated with these growth challenges adversely affected our revenue growth and profitability during the first quarter of 2006 as we have devoted substantial resources to meeting the needs of our customers. We believe that these are normal by-products of our growth, and we are working to address these issues.

Since the beginning of 2006, we have announced several new products including:

- a 30% faster model of our InVision® LD 3-D printer;
- a new dental lab system, the InVision® DP (Dental Professional), which is capable of producing castable wax-ups for dental copings and bridges;
- a new suite of software, 3DView®, 3DManage and 3DPrint , for our stereolithography systems, selective laser sintering systems and InVision 3-D printers that we expect to provide numerous productivity and cost-saving benefits to our customers;
- Accura® 60 Plastic, a new stereolithography material that simulates the look and feel of molded polycarbonate; and
- new VisiJet® LD100 materials in two new colors, red and blue.

None of these new products had a material impact on our operating results for the first quarter of 2006.

## Results of Operations

Table 11 below sets forth, for the periods indicated, revenue and percentages of revenue by class of product and service.

**Table 11**

	Three months ended March 31 2006 Restated (dollars in thousands)			2005 Restated		
Systems and other products	\$ 12,379	36.8 %		\$ 10,145	33.3 %	
Materials	11,873	35.3		10,093	33.2	
Services	9,391	27.9		10,186	33.5	
Consolidated revenue	\$ 33,643	100.0 %		\$ 30,424	100.0 %	

### *Consolidated revenue*

The principal factors affecting our consolidated revenue in the first three months of 2006 compared to the 2005 quarter were increases in new product revenue, the combined positive effect of changes in product mix and average selling prices, and the adverse effect of foreign currency translation. Revenue from legacy products continued to decline in the first quarter of 2006, consistent with its past trend. As used in this management's discussion and analysis, the combined effect of changes in product mix and average selling prices, sometimes referred to as price and mix, relates to changes in product-line revenue that are not able to be specifically related to changes in unit volume or foreign currency



translation. Among these changes are changes in the product mix among our systems as the trend toward smaller, more economical systems that has affected our business for the past several years has continued and the influence of new products has grown.

60

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For the first quarter of 2006, our consolidated revenue increased 10.6% to \$33.6 million on a restated basis from \$30.4 million for the first quarter of 2005. This increase was primarily due to higher sales of new products and the combined effect of changes in product mix and average selling prices, partially offset by lower volume of core products and services and the unfavorable effect of foreign currency translation. Sales of new products and services introduced since the latter part of 2003 increased by \$5.3 million to \$11.3 million in the first quarter of 2006 on a restated basis, approximately one-third of revenue for the quarter. New systems and materials introduced since the latter part of 2003 that contributed to our higher revenue in the first quarter of 2006 included our new Sinterstation® Pro SLS® systems, our new Viper Pro SLA® system, our 3-D Printers and various materials.

The components of the change in revenue by class of product and service for the first quarter of 2006 as restated are shown in Table 12, together with the corresponding percentage of that change compared to the restated 2005 level of revenue for that product or service.

**Table 12 (Restated)**

	Systems and Other Products (dollars in thousands)		Materials		Services		Net Change in Consolidated Revenue	
Volume Core products and services	\$ (2,096 )	(20.7 )%	\$ (167 )	(1.7 )%	\$ (583 )	(5.7 )%	\$ (2,846 )	(9.4 )%
Volume New products	3,616	35.6	1,547	15.3	152	1.5	5,315	17.5
Price/mix	1,091	10.8	977	9.7			2,068	6.8
Foreign currency translation	(377 )	(3.7 )	(577 )	(5.7 )	(364 )	(3.6 )	(1,318 )	(4.3 )
Net change in consolidated revenue	\$ 2,234	22.0 %	\$ 1,780	17.6 %	\$ (795 )	(7.8 )%	\$ 3,219	10.6 %

As set forth in Tables 11 and 12:

- Revenue from systems and other products increased 22.0% to \$12.4 million in the first quarter of 2006 from \$10.2 million in the first quarter of 2005. Revenue from systems and other products represented 36.8% and 33.3% of consolidated revenue for the first quarter of 2006 and 2005, respectively.

On a restated basis, the increase in revenue from systems and other products was primarily due to a \$3.6 million increase in volume of sales of our newer systems, including our Viper Pro and Sinterstation® Pro systems and the favorable combined effect of price and mix. This increase was partially offset by a \$2.1 million decline in legacy product sales, and the unfavorable effect of foreign currency translation.

- Revenue from materials increased 17.6% to \$11.9 million for the first quarter of 2006 from \$10.1 million for the first quarter of 2005. Revenue from materials represented 35.3% and 33.2% of consolidated revenue for the first quarter of 2006 and 2005, respectively.

On a restated basis, the increase in revenue from materials was primarily due to \$1.5 million arising from higher unit sales of new products and the \$1.0 million favorable combined effect of price and mix, which partially reflected the benefits of promotional efforts in prior periods. These increases were partially offset by the \$0.6 million unfavorable effect of foreign currency translation and a \$0.2 million decline in core materials unit volume.

- Revenue from services decreased 7.8% to \$9.4 million for the first quarter of 2006 from \$10.2 million for the first quarter of 2005. Revenue from services represented 27.9 % and 33.5% of consolidated revenue for the first quarter of 2006 and 2005, respectively.

On a restated basis, the decrease in revenue from services was principally due to a \$0.6 million decline in service revenue primarily related to core products, which included reduced sales of

upgrades following our decision to cease offering upgrades for older legacy systems and foregone ordinary time and material field service revenue as a result of resource constraints in connection with the growth challenges discussed above. We have also increased the reliability of certain of the replacement parts that we are now selling as part of our service business. As a result, these parts have longer service lives, are being replaced less frequently and their sales have declined. Revenue from services was also negatively affected by a \$0.4 million unfavorable effect of foreign currency translation. These decreases in service revenue were partially offset by a \$0.2 million increase in service revenue related to new systems.

Backlog has historically not been a significant factor in our business, reflecting our relatively short production and delivery lead times. We had approximately \$2.8 million of booked orders outstanding at March 31, 2006, primarily for systems, all of which we expect to ship in 2006, reflecting the shipment during the first quarter of 2006 of a substantial portion of the \$6.8 million of booked orders that we had outstanding at December 31, 2005. We believe that the level of booked orders at March 31, 2006 remains higher than our historical experience.

Systems orders and sales tend to fluctuate on a quarterly basis as a result of a number of factors, including the types of systems ordered by customers, customer acceptance of newly introduced products, the timing of product orders and shipments, global economic conditions and fluctuations in foreign exchange rates. Our customers generally purchase our systems as capital equipment items, and their purchasing decisions may have a long lead-time. Due to the relatively high list price of certain systems and the overall low unit volume of sales in any particular period, the acceleration or delay of orders and shipments of a small number of systems from one period to another can significantly affect revenue reported for our systems sales for the period involved. Revenue reported for systems sales in any particular period is also affected by revenue recognition rules prescribed by generally accepted accounting principles. However, as noted above, production and delivery of our systems is generally not characterized by long lead times, and backlog is therefore generally not a material factor in our business.

#### *Revenue by geographic region*

As discussed more fully below, our operations in the U.S. contributed substantially all of our higher revenue in the first quarter of 2006 both as restated and as originally reported. Revenue from European operations was essentially flat, and revenue from Asia-Pacific operations declined by \$0.9 million, compared to that in the first quarter of 2005. Revenue by geographic area in which we operate is shown in Table 13.

**Table 13**

	<b>Three months ended</b>			<b>March 31, 2005</b>		
	<b>March 31, 2006</b>			<b>Restated</b>		
	<b>Restated</b>			<b>Restated</b>		
	<b>(dollars in thousands)</b>					
U.S. operations	\$ 18,394	54.7	%	\$ 14,245	46.8	%
European operations	11,112	33.0		11,147	36.6	
Asia-Pacific operations	4,137	12.3		5,032	16.6	
Total revenue	\$ 33,643	100.0	%	\$ 30,424	100.0	%

The components of the changes in revenue by geographic region for the first quarter of 2006 are shown in Table 14, together with the corresponding percentage of that change compared to the level of revenue for the corresponding restated 2005 period for that geographic area.

**Table 14 (Restated)**

	U.S. (dollars in thousands)		Europe		Asia-Pacific		Net Change in Consolidated Revenue	
Volume	\$ 3,013	21.2 %	\$ 683	6.1 %	\$ (561 )	(11.1 )%	\$ 3,135	10.3 %
Price/mix	1,136	8.0	271	2.4	(5 )	(0.1 )	1,402	4.6
Foreign currency translation			(989 )	(8.9 )	(329 )	(6.5 )	(1,318 )	(4.3 )
Net change in consolidated revenue	\$ 4,149	29.2 %	\$ (35 )	(0.4 )%	\$ (895 )	(17.7 )%	\$ 3,219	10.6 %

On a consolidated geographic basis, our \$3.2 million increase in revenue in the first quarter of 2006 resulted from \$3.1 million of higher volume and \$1.4 million from the favorable combined effect of price and mix, each of which was generated by our U.S. and European operations, partially offset by the \$1.3 million unfavorable effect of foreign currency translation, arising from both Europe and the Asia-Pacific region.

As set forth in Tables 13 and 14:

- Revenue from U.S. operations increased by 29.2% to \$18.4 million for the first quarter of 2006 from \$14.3 million for the first quarter of 2005. Our U.S. operations revenue growth arose from higher volumes of both systems and materials and the favorable combined effect of price and mix. The increased revenue in the U.S. reflects the favorable effects of our previously restructured sales force, sales to new customers and to a broader range of applications, and benefits of promotional efforts for materials in prior periods. Revenue from U.S. operations represented 54.7% and 46.8% of consolidated revenue for the first quarters of 2006 and 2005, respectively.
- Revenue from operations outside the U.S. decreased by \$0.9 million in the first quarter of 2006 and decreased to 45.3% of consolidated revenue for the first quarter of 2006 from 53.2% of consolidated revenue for the first quarter of 2005, reflecting the effect of the higher growth in revenue in the U.S. and the unfavorable effect of foreign currency translation. The \$1.3 million unfavorable effect of foreign currency translation had the effect of reducing the first-quarter revenue contribution from our operations outside the U.S. by 4.3 percentage points from what would have otherwise been 49.6% of revenue at constant exchange rates.
- Revenue from European operations was \$11.1 million for both the first quarter of 2006 and the first quarter of 2005. The positive effects in Europe of increased revenue from new product sales and the favorable effects of price and mix were more than offset by the unfavorable effect of foreign currency translation. The unfavorable effect of foreign currency translation more than offset what would have otherwise been an 8.6% increase in European revenue in the first quarter of 2006 at constant exchange rates. European revenue represented 33.0% and 36.6% of consolidated revenue for the first quarters of 2006 and 2005, respectively.
- Revenue from Asia-Pacific operations decreased 17.8% to \$4.1 million for the first quarter of 2006 from \$5.0 million for the first quarter of 2005. This decrease in revenue resulted primarily from quarterly fluctuations in sales of large systems and the effect of the growth challenges mentioned above. Asia-Pacific revenue represented 12.3% and 16.6% of consolidated revenue for the first quarters of 2006 and 2005, respectively.

*Costs and margins*

Gross profit increased by \$0.6 million on a restated basis to \$13.6 million for the 2006 quarter from \$13.0 million for the first quarter of 2005 on a restated basis, but declined 2.4 percentage points to 40.4% of consolidated revenue for the 2006 quarter on a restated basis from 42.8% of consolidated revenue for the first quarter of 2005.

**Table 15**

	<b>Gross profit</b>		<b>March 31, 2005</b>	
	<b>Three months ended</b>		<b>Restated</b>	
	<b>Restated</b>	<b>%</b>	<b>Gross</b>	<b>%</b>
	<b>Profit</b>	<b>Revenue</b>	<b>Profit</b>	<b>Revenue</b>
	<b>(dollars in thousands)</b>			
Products	\$ 11,242	46.4 %	\$ 9,963	49.2 %
Services	2,363	25.2 %	3,055	30.0 %
Total	\$ 13,605	40.4 %	\$ 13,018	42.8 %

The \$0.6 million increase in gross profit in the first quarter of 2006 was due primarily to our overall higher revenue and the favorable combined effects of price and mix. The decrease in gross profit margin in the first quarter of 2006 reflected a decrease in both product and service margins.

Cost of sales, which is the principal influence on gross profit, increased 15.0% to \$20.0 million in the first quarter of 2006, both as originally presented and as restated, from \$17.4 million for the 2005 period. This increase was due primarily to our higher volume and to higher costs incurred as installation, service and training resources were stretched due to the growth challenges discussed above. This increase included travel and on-site costs to expedite installations as well as compensation to some customers for their additional costs during extended installation periods as well as additional costs reflected in our first-quarter restatement. As a percentage of consolidated revenue, cost of sales increased to 59.6% of revenue, on a restated basis, in the 2006 quarter compared to 57.2%, on a restated basis, in the 2005 period.

Gross profit margin for products decreased to 46.4% of consolidated product revenue, on a restated basis, in the first quarter of 2006 from 49.2% of consolidated product revenue, on a restated basis, in the first quarter of 2005. The decrease in product margins in the first quarter of 2006 was due primarily to additional costs incurred to deal with the challenges of growth in systems sales discussed above, short-term incremental overhead costs associated with transitioning operations out of our Grand Junction facility, and to a lesser extent the effect of the correction of errors related to the first quarter of 2006 that affected product cost of sales. Product margins benefited from expanded sales of materials to new customers as a result of promotional efforts in prior periods.

Gross profit margin for services decreased to 25.2% of consolidated service revenue, on a restated basis, for the first quarter of 2006 from 30% of consolidated service revenue, on a restated basis, for the first quarter of 2005. Service margins in the first quarter of 2006 were adversely affected by lower sales of upgrades for older legacy systems, certain of which we have previously announced that we would no longer support, and by the strains on resources related to installation, service and training that resulted in foregone service income from time and material service activities.

*Operating expenses*

As shown in Table 16, on a restated basis, total operating expenses increased by \$3.6 million or 31.3% to \$15.0 million in the first quarter of 2006 compared to \$11.4 million in the first quarter of 2005. The increase in the first quarter of 2006 was primarily due to:

- \$1.6 million of severance and restructuring costs, which were generally in line with our previously announced expectations;
- \$1.3 million higher selling, general and administrative expenses, including \$0.2 million arising primarily from additional depreciation expense recorded as a restatement item as discussed in Note 2 to the Condensed Consolidated Financial Statements (Restated); and
- \$0.6 million of higher research and development expenses, which are discussed in greater detail below.

Operating expenses in the first quarter of 2006 increased to 44.5% of revenue in that quarter compared to 37.4% of revenue in the first quarter of 2005. Approximately half of that increase related to the severance and restructuring costs referred to above.

**Table 16**

	Three months ended March 31, 2006 Restated		March 31, 2005 Restated	
	Amount (dollars in thousands)	% Revenue	Amount	% Revenue
Selling, general and administrative expenses	\$ 10,057	29.9 %	\$ 8,710	28.6 %
Research and development expenses	3,257	9.7	2,675	8.8
Severance and restructuring costs	1,638	4.9		
Total	\$ 14,952	44.5 %	\$ 11,385	37.4 %

*Selling, general and administrative expenses*

For the first quarter of 2006, selling, general and administrative expenses increased 15.5% to \$10.1 million from \$8.7 million in the first quarter of 2005. This \$1.4 million increase was due primarily to:

- \$0.4 million of higher expenses associated with our higher level of revenue, including \$0.2 million of higher commission expenses;
- a \$0.2 million increase in equity compensation expense arising from our adoption on January 1, 2006 of SFAS No. 123R (see Note 10 to the Condensed Consolidated Financial Statements (Restated));
- \$0.2 million arising primarily from additional depreciation expense recorded in the restatement of our statement of operations for the first quarter of 2006; and
- a variety of other expenses, including expenses associated with the growth challenges discussed above.

As previously disclosed, beginning on January 1, 2006, we began to expense previously issued equity awards for which service has not been rendered as required by Statement of Financial Accounting Standards ( SFAS ) No. 123R, which relates to the expensing of stock options and certain other equity compensation. During the first quarter of 2006, we modestly lowered our most recently disclosed estimates of these expenses because of forfeitures during the first quarter of 2006. As of March 31, 2006, we estimate our maximum expense for existing stock options as a result of the adoption of SFAS No. 123R to be approximately \$1.1 million, of which \$0.4 million (including the \$0.2 million recognized in the first quarter) would be recognized for 2006 and the remainder would be recognized for 2007. This projected expense will change if any stock options are granted, which we do not expect to occur, or cancelled prior to the respective reporting periods.

*Research and development expenses*

Research and development expenses for the first quarter of 2006 increased by 21.8% to \$3.3 million compared to \$2.7 million for the 2005 quarter, reflecting our continued high levels of new product development work. We anticipate that research and development expenses for 2006 will be in the range of \$12.0 to \$14.0 million due to increased activity with selected projects, including our recently announced agreement with Symyx Technologies, Inc., which is discussed above.

*Severance and restructuring costs*

Severance and other restructuring costs amounted to \$1.6 million in the first quarter of 2006. There were no such costs in the first quarter of 2005. These costs related primarily to costs incurred in connection with our planned relocation to Rock Hill, South Carolina, and they primarily included personnel, relocation and recruiting costs.

We estimate that, during 2006 and including the costs we incurred in the first quarter, the total pretax costs to complete this relocation and consolidation should be in the range of \$6.4 million to \$8.1 million. This amount includes estimated cash expenditures for moving costs and other costs related to personnel, relocation and recruiting and up to \$1.7 million of facility exit costs. These estimated 2006 costs do not include an estimated \$0.2 million of non-cash costs related to accelerated amortization and asset impairments that we expect to incur. Included in the range of facility exit costs is an estimate of costs that may be incurred if we encounter delays in disposing of the Grand Junction facility, which we own and closed at the end of April 2006, and the Valencia facility, which we lease.

In addition to other significant operational and strategic improvements that we expect to achieve from our relocation project, we project that we should realize facilities and operating-cost savings in excess of \$2.5 million per year beginning in 2007, the first full year of planned operations in the Charlotte area. We also believe that South Carolina will provide a favorable business climate, significant investment and tax benefits and a sustained lower cost of doing business. We believe these savings should provide a substantial return on the anticipated investment in up-front moving and other costs, and we expect them to translate into long-term improvements in profitability.

Except for the costs incurred through the first quarter of 2006, all of the foregoing cost estimates and anticipated savings relating to our relocation project are provided solely as estimates. There can be no assurance that our estimates will not change as we proceed with this project, that actual expenditures will not differ from our estimates, or that anticipated savings and efficiencies will be realized.

*Income (loss) from operations*

Notwithstanding our higher consolidated revenue, as a result of the growth challenges and our higher operating costs and expenses discussed above that more than offset our higher gross profit, on a restated

basis, we recorded a \$1.3 million loss from operations, as restated, in the first quarter of 2006 compared to \$1.6 million of income from operations, as restated, for the 2005 period.

Depreciation and amortization included in operating income was \$1.6 million for both the three months ended March 31, 2006 and the three months ended March 31, 2005. We expect annual depreciation and amortization to be in the range of \$6.0 to \$7.0 million in 2006.

*Interest and other expense, net*

Interest and other expense, net, which consists primarily of interest income and interest expense, was \$0.2 million for the first quarter of 2006 compared to \$0.3 million for the first quarter of 2005 as \$0.2 million of investment income from our continuing high level of cash and cash equivalents and higher interest rates for invested funds in the first quarter of 2006 partially offset interest expense from our \$26.3 million of outstanding debt.

*Provisions for(benefit of) income taxes*

Income taxes were not material in any of the periods included in this Form 10-Q-A.

*Net income (loss) and net income (loss) available to common stockholders*

Reflecting our \$1.3 million of restated operating loss in the first quarter and the other factors discussed above, we recorded a \$1.5 million net loss for the first quarter of 2006 compared to \$1.2 million of net income in the 2005 quarter.

Net loss available to common stockholders for the first quarter of 2006 was \$1.9 million, as restated, after giving effect to accrued dividends and accretion of preferred stock issuance costs with respect to our Series B Convertible Preferred Stock. On a per share basis, basic and diluted net loss per share available to the common stockholders in the first quarter was \$0.13 on a restated basis.

Net income available to common stockholders for the first quarter of 2005 was \$0.8 million, as restated, after giving effect to accrued dividends and accretion of preferred stock issuance costs with respect to the Series B Convertible Preferred Stock. On a per share basis, basic and diluted income per share available to the common stockholders in the first quarter of 2005 was \$0.05. The dilutive effect of outstanding stock options was included in diluted income per share in the 2005 period.

**Liquidity and Capital Resources**

Our principal sources of liquidity during the first quarter of 2006 were cash flow from operations and net proceeds from the exercise of stock options.

*Working capital*

Our net working capital was \$43.5 million on a restated basis at March 31, 2006 reflecting a \$0.3 million decrease from the \$43.8 million of net working capital at December 31, 2005 on a restated basis. See Note 2 to the Condensed Consolidated Financial Statements (Restated).

The decrease in net working capital in the first quarter of 2006, as restated, resulted primarily from the following items:

- a \$1.5 million increase in inventories
- a \$2.3 million increase in cash and cash equivalents; and
- a \$0.6 million reduction in customer deposits;



that was more than offset by:

- a \$3.4 million decrease in accounts receivable, net
- a \$0.8 million increase in accounts payable;
- a \$0.4 million increase in deferred revenue
- a \$0.2 million increase in accrued liabilities; and

For additional information regarding our restated net working capital at March 31, 2006 and the effect of the restatement on the amount originally reported in the Original 10-Q, please see Note 2 to the Condensed Consolidated Financial Statements (Restated).

Components of inventories were as follows:

**Table 17**

	<b>March 31, 2006 Restated (dollars in thousands)</b>	<b>December 31, 2005 Restated</b>
Raw materials	\$ 2,645	\$ 207
Inventory held by assemblers	680	417
Work in process	94	55
Finished goods	12,925	14,131
	<b>\$ 16,344</b>	<b>\$ 14,810</b>

The higher level of inventory at March 31, 2006 arose from \$2.4 million of higher raw materials inventory incurred to support our higher level of sales and modest increases in inventory held by assemblers and work in process, partially offset by a modest decline in finished goods inventory.

The \$1.5 million increase in inventory shown in Table 17 and on the restated consolidated balance sheets resulted from the cash-flow-related \$1.6 million increase in net inventory set forth on the consolidated statement of cash flows and a \$0.1 million increase from the unfavorable effect of foreign currency translation.

For additional information regarding the value of inventory at March 31, 2006 and the effect of the restatement on the amount reported in the Original 10-Q, please see Note 2 to the Condensed Consolidated Financial Statements (Restated).

In connection with the outsourcing activities that we have entered into with our third-party assemblers, we sold to them components of our raw materials inventory related to those systems. We recorded those sales in our financial statements as a product financing arrangement under SFAS No. 49, Accounting for Product Financing Arrangements. At March 31, 2006, \$0.7 million of the inventory sold to assemblers remained in inventory, and we had a corresponding accrued liability representing our non-contractual obligation to repurchase assembled systems and refurbished parts produced from such inventory. At March 31, 2006, inventory held by assemblers and our corresponding accrued liability had increased from \$0.4 million at December 31, 2005 to \$0.7 million.

In view of the outsourcing of substantially all of our equipment assembly and refurbishment activities, a majority of our inventories now relate to finished goods, including principally systems, materials and service parts, as our third-party assemblers have taken over supply-chain responsibility for the assembly of systems. Since our third-party assemblers have assumed supply-chain responsibility, we generally no longer hold in inventory most parts for production of our systems, which has also resulted in an overall reduction of work-in-process inventory. Consequently, in calculating inventory reserves, we now direct our attention



to spare parts in inventory that we expect to be used over the expected life cycles of the related systems and to our ability to sell items that are recorded in finished goods inventory, a large portion of which are new systems.

Our prepaid expenses and other current assets also include amounts attributable to our arrangements with our outsource suppliers, which amounts affect our working capital. The components of prepaid expenses and other current assets were as follows:

**Table 18**

	<b>March 31, 2006 Restated (dollars in thousands)</b>	<b>December 31, 2005 Restated</b>
Progress payments to assemblers	\$ 4,885	\$ 5,271
Non-trade receivables	1,047	1,051
Other	3,452	2,953
Total	\$ 9,384	\$ 9,275

The non-trade receivables shown in Table 18 together with inventory held by assemblers shown in Table 17, and a related accrued liability in an amount that corresponds to the book value of inventory held by assemblers included in accrued liabilities on our balance sheet relate to the accounting for our outsourcing arrangements pursuant to SFAS No. 49. On a restated basis, the non-trade receivables were \$1.0 million at March 31, 2006, as compared to \$1.1 million at December 31, 2005. These non-trade receivables relate to parts that our third-party assemblers purchased from us to complete the assembly of systems.

As is shown in Table 19 below, the \$2.3 million increase in cash and cash equivalents arose from \$2.4 million of cash generated by operating activities and \$1.6 million of cash generated by financing activities in the first quarter of 2006, partially offset by \$1.7 million of cash used in investing activities. See the discussion of cash flow immediately below for a discussion of the factors that affected these items of cash flow.

The \$1.0 million decrease in customer deposits related primarily to shipments during the first quarter of orders placed prior to December 31, 2005.

The decrease in accounts receivable, net resulted from changes in our revenue and collections from period to period and, as restated, included the recordation of \$0.2 million of previously unrecorded credit memoranda in favor of trade customers for product returns and pricing issues and correction of customer sales tax charges. As previously disclosed, accounts receivable outstanding at December 31, 2005 included amounts attributable to the timing of new systems shipments late in the fourth quarter of 2005. While we collected a substantial portion of these accounts receivable during the first quarter of 2006, we also experienced some delays in payment during the quarter, some of which arose from the growth challenges discussed above. As a result, days sales outstanding (DSO) increased to 78 days at March 31, 2006 compared to 68 days at December 31, 2005. Accounts receivable more than 90 days past due were 8.4% of receivables at March 31, 2006 compared to 5.1% of receivables at December 31, 2005. Although this is a departure from the prior trends of these measures, we believe that it is a short-term change that is not indicative of an adverse trend.

The changes in the first quarter of 2006 in accounts payable, deferred revenue and the other items of working capital not discussed above arose in the ordinary course of business. Differences not discussed above between the amounts of working capital item changes in the cash flow statement and the amount of balance sheet changes for those items are primarily the result of foreign currency translation adjustments.

#### *Cash flow*

Table 19 summarizes the cash provided by or used in operating activities, investing activities and financing activities, as well as the effect of changes in foreign exchange rates on cash, for the first three months of 2006 and 2005. The restatement of our condensed consolidated financial statements had no significant effect on our cash flow from operations for the quarter ended March 31, 2006, and our cash and cash equivalents increased by \$2.3 million for that period.

**Table 19**

	<b>Three months ended March 31, 2006 Restated (dollars in thousands)</b>	<b>March 31, 2005 Restated</b>
Cash provided by operating activities	\$ 2,420	\$ 304
Cash used in investing activities	(1,723 )	(1,031 )
Cash provided by financing activities	1,585	771
Effect of exchange rate changes on cash	4	253
Net increase in cash and cash equivalents	\$ 2,286	\$ 297

#### *Cash flow from operations*

Notwithstanding our net loss for the period, our operations provided \$2.4 million of net cash on a restated basis in the first three months of 2006. This cash was generated primarily by the changes in operating accounts and non-cash items discussed below:

- \$3.7 million net decrease of accounts receivable;
- \$1.9 million in non-cash items;
- a \$0.8 million increase in accounts payable;
- a \$0.3 million increase in deferred revenues; and
- a \$0.2 million increase arising from other operating accounts, partially offset by
- a \$1.9 million increase in inventories;

- a \$0.6 million decrease in customer deposits; and
- a \$0.5 million decrease in accrued liabilities.

The principal reasons for these changes are discussed in *Working capital* above.

Our operations provided \$0.3 million of net cash in the first three months of 2005. Such cash was generated by our \$1.2 million of net income, partially offset by the \$1.5 million combined net effect of non-cash items, including depreciation and amortization, and changes in operating assets and operating liabilities in the ordinary course of business. Such non-cash items and changes in operating assets and operating liabilities included:

- \$1.6 million of non-cash items, including depreciation and amortization;
- a \$1.7 million decrease in accounts receivable, net;
- a \$0.6 million decrease in inventories, net; and
- a \$0.5 million increase in deferred revenue,

partially offset by a net reduction in cash resulting from

- a \$2.2 million decrease in prepaid expenses and other current assets;
- a \$2.9 million decrease in accrued liabilities; and
- a \$0.3 million net decrease arising from other operating accounts.

#### *Cash used for investing activities*

We used \$1.7 million of net cash for investing activities in the first three months of 2006 compared to \$1.0 million in the first three months of 2005. In the 2006 period, we also recognized \$0.2 million of cash from the net proceeds of sale of property and equipment. In each period, the principal uses of cash for investment purposes were for capital expenditures, patent and license rights and software development costs. The increase in the 2006 period was due to higher levels of capital expenditures in the 2006 period compared to the 2005 quarter.

Capital expenditures were \$1.6 million in the first quarter of 2006 compared to \$0.7 million in the first quarter of 2005 primarily for information technology systems and hardware related to the implementation of our Oracle® ERP system and for capital expenditures related to our corporate headquarters relocation project. As of the end of the first quarter of 2006, we expect our capital expenditures in 2006 to be in the range of \$5 million to \$6 million, of which approximately \$2.1 million, which does not include the developer's cost for construction of the new facility that we have agreed to lease, relates to our relocation project.

#### *Cash provided by financing activities*

Net cash provided by financing activities in the first three months of 2006 increased to \$1.6 million from \$0.8 million in the first three months of 2005. In each period, such cash was provided primarily by the net proceeds of stock option exercises and was offset partially by scheduled payments of principal on our outstanding industrial development bonds and payments of other obligations.

#### *Liquidity*

As discussed above, our principal sources of liquidity for the first quarter of 2006 were cash flow from operations and net proceeds from the exercise of stock options. As noted above, our unrestricted cash and cash equivalents increased by \$2.3 million to \$26.6 million at March 31, 2006 from \$24.3 million at



December 31, 2005 due to \$4.0 million of cash provided by operating and financing activities, partially offset by \$1.7 million of cash used in investing activities.

#### *Outstanding debt*

Our outstanding debt at March 31, 2006 and December 31, 2005 was as follows:

**Table 20**

	<b>March 31, 2006 Restated (dollars in thousands)</b>	<b>December 31, 2005 Restated</b>
Line of credit	\$	\$
Industrial development revenue bonds:		
Current portion of long-term debt	\$ 210	\$ 200
Long-term debt, less current portion	3,435	3,545
Total	\$ 3,645	\$ 3,745
Subordinated debt:		
6% convertible subordinated debentures	\$ 22,604	\$ 22,604
Installment note:		
Current portion of installment note	\$ 7	\$ 7
Installment note, less current portion	21	23
Total	\$ 28	\$ 30
Total current portion of debt	\$ 217	\$ 207
Total long-term portion of debt	26,060	26,172
Total debt	\$ 26,277	\$ 26,379

At March 31, 2006, the carrying value of our total debt had declined by \$0.1 million primarily as a result of scheduled principal payments during the first three months of 2006 on our floating-rate industrial development bonds. At March 31, 2006, \$0.2 million of principal payments were due under those bonds during the next twelve months. No principal payments are required to be made under our 6% convertible subordinated debentures until their maturity in November 2013. As discussed below, no borrowings were outstanding under our line of credit at March 31, 2006 or December 31, 2005.

#### *Silicon Valley Bank loan and security agreement*

We maintain a loan and security agreement with Silicon Valley Bank that is scheduled to expire on July 1, 2007. This credit facility, as amended, provides that we and certain of our subsidiaries may borrow up to \$15.0 million of revolving loans and includes sub-limits for letter of credit and foreign exchange facilities. The credit facility is secured by a first lien in favor of Silicon Valley Bank on certain of our assets, including domestic accounts receivable, inventory and certain fixed assets. Interest accrues on outstanding borrowings at either the Bank's prime rate in effect from time to time or at a LIBOR rate plus 2.25%. We are obligated to pay, on a quarterly basis, a commitment fee equal to 0.375% per annum of the unused amount of the facility.

The facility, as amended, imposes certain limitations on our activities, including limitations on the incurrence of debt and other liens, limitations on the disposition of assets, limitations on the making of certain investments and limitations on the payment of dividends on our Common Stock. The facility also requires us to maintain (a) a quick ratio (as defined in the credit facility) of at least 1.00 as of the end of each calendar quarter and (b) a ratio of total liabilities less subordinated debt to tangible net worth (as each such term is defined in the credit facility) of not more than 2.00 as of December 31, 2005 and at the

end of each calendar quarter thereafter. The credit facility also requires that we maintain, on a trailing four-quarter basis, EBITDA (as defined in the credit facility) in an amount not less than \$18 million for certain periods ending on or before December 31, 2005 and, as amended effective March 30, 2006, not less than \$15 million for each period ending on or after March 31, 2006. We believe that we were in compliance with these requirements at March 31, 2006, both prior to and after giving effect to the restatement herein. Additionally, we believe that we were in compliance with these financial covenants at December 31, 2005, except for the minimum EBITDA covenant, which non-compliance the Bank agreed to waive.

At March 31, 2006 and December 31, 2005, respectively, we had \$0.4 million and \$1.7 million of foreign exchange forward contracts outstanding with Silicon Valley Bank. No borrowings or letters of credit were outstanding under this facility at either March 31, 2006 or December 31, 2005, and we do not currently expect to borrow under this credit facility due to our current cash position and our currently anticipated future cash flow. However, we expect this credit facility to provide us with additional liquidity as we grow and that the credit facility will allow us to better manage our foreign exchange exposure. See Note 7 to the Condensed Consolidated Financial Statements (Restated).

#### *Industrial development bonds*

Our Grand Junction, Colorado facility was financed by industrial development bonds in the original aggregate principal amount of \$4.9 million. At March 31, 2006, the outstanding principal amount of these bonds was \$3.6 million. Interest on the bonds accrues at a variable rate of interest and is payable monthly. The interest rate at March 31, 2006 was 3.2%. Principal payments are due in semi-annual installments through August 2016. We have made all required payments of principal and interest on these bonds. The bonds are collateralized by, among other things, a first mortgage on the facility, a security interest in certain equipment and an irrevocable letter of credit issued by Wells Fargo Bank, N.A. pursuant to the terms of a reimbursement agreement between us and Wells Fargo. We are required to pay an annual letter of credit fee equal to 1% of the stated amount of the letter of credit.

This letter of credit is in turn collateralized by \$1.2 million of restricted cash that Wells Fargo holds in an interest-bearing account. Wells Fargo has a security interest in that account as partial security for the performance of our obligations under the reimbursement agreement. We have the right, which we have not exercised, to substitute a standby letter of credit issued by a bank acceptable to Wells Fargo as collateral in place of the funds held in that account.

The reimbursement agreement, as amended, contains financial covenants that require, among other things, that we maintain a minimum tangible net worth (as defined in the reimbursement agreement) of \$23.0 million plus 50% of net income from July 1, 2001 forward and a fixed-charge coverage ratio (as defined in the reimbursement agreement) of no less than 1.25. We are required to demonstrate our compliance with these financial covenants as of the end of each calendar quarter. We believe that we were in compliance with these financial covenants as of March 31, 2006 both prior to and after giving effect to the restatement contained herein and December 31, 2005.

As discussed above, we ceased operations at our Grand Junction facility at the end of April 2006, we have listed it for sale, and we intend subsequently to sell it. At the time we sell the facility, we expect to either pay off these bonds or, with the approval of Wells Fargo, have them assumed by a qualified buyer. See Note 5 to the Condensed Consolidated Financial Statements.



*6% convertible subordinated debentures*

The 6% convertible subordinated debentures bear interest at the rate of 6% per year payable semi-annually in arrears in cash on May 31 and November 30 of each year. They are convertible into shares of Common Stock at the option of the holders at any time prior to maturity at \$10.18 per share, subject to customary anti-dilution adjustments. They are currently convertible into approximately 2.2 million shares of Common Stock.

We have the right to redeem the debentures, in whole or in part, commencing on November 24, 2006 at a price equal to 100% of the then outstanding principal amount of the debentures being redeemed, together with all accrued and unpaid interest and other amounts due in respect of the debentures. If we undergo a change in control (as defined), the holders may require us to redeem the debentures at 100% of their then outstanding principal amount, together with all accrued and unpaid interest and other amounts due in respect of the debentures.

The debentures are subordinated in right of payment to senior indebtedness (as defined). At the time the debentures were issued, we granted registration rights to the purchasers of the debentures pursuant to which, subject to certain terms and conditions, we agreed to file a registration statement to register for resale under the Securities Act of 1933, as amended (the Securities Act), the shares of Common Stock into which the debentures are convertible. The conditions to our obligation to file such registration statement have not yet been satisfied, and no such registration statement is currently pending.

*Derivative financial instruments*

As of March 31, 2006, we had entered into forward currency contracts related to our future liabilities for purchase orders issued to various suppliers and related to inter-company purchase obligations of our subsidiaries, and the notional amount of these contracts at their respective settlement dates amounted to \$3.4 million in the aggregate. These contracts are denominated in Swiss francs, euros, pounds sterling and Japanese yen. The respective notional amounts of the forward currency contracts outstanding as of March 31, 2006 aggregated Swiss francs 0.6 million (equivalent to \$0.5 million at settlement date), euros 0.5 million (equivalent to \$0.6 million at settlement date), pounds sterling 0.3 million (equivalent to \$0.5 million at settlement date) and Japanese yen 210 million (equivalent to \$1.8 million at settlement date).

See also Note 7 to the Condensed Consolidated Financial Statements (Restated) for additional information regarding these arrangements.

*Series B convertible preferred stock*

Our Series B Convertible Preferred Stock accrues dividends, on a cumulative basis, at \$0.60 per share each year while it remains outstanding. Prior to May 6, 2004, the cumulative dividend rate was \$0.48 per share per year.

The Series B Convertible Preferred Stock is senior to our Common Stock and any other stock that ranks junior to the Series B Convertible Preferred Stock. Dividends are payable in cash semi-annually, when, as and if declared by the Board of Directors, on May 5 and November 5 of each year while these shares remain outstanding. The Series B Convertible Preferred Stock votes equally with our Common Stock and is convertible at any time at the option of the holders on a share-for-share basis into approximately 2.6 million shares of Common Stock plus any accrued and unpaid dividends. Under certain circumstances, holders of these shares may receive upon conversion additional shares of Common Stock in respect of accrued and unpaid dividends.

The Series B Convertible Preferred Stock is redeemable at our option at any time after May 5, 2006. We must redeem any shares of Series B Convertible Preferred Stock that remain outstanding on May 5, 2013. The redemption price in either case is \$6.00 per share plus any accrued and unpaid dividends.

*Stockholders equity*

Stockholders equity increased 0.6% to \$69.3 million at March 31, 2006 from \$68.9 million at December 31, 2005. This increase resulted from the \$4.4 million increase in Common Stock and additional paid-in capital arising primarily from net proceeds from the exercise of stock options and the fair market value of restricted stock granted, partially offset by:

- a \$2.7 million net increase in deferred compensation arising from restricted stock awards; and
- our \$2.0 million net loss available to common stockholders.

**Critical Accounting Policies and Significant Estimates**

For a discussion of our critical accounting policies and estimates, refer to Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates in our Annual Report on Form 10-K for the year ended December 31, 2005.

**Forward-Looking Statements**

Certain statements made in this Form 10-Q/A that are not statements of historical or current facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from historical results or from any future results expressed or implied by such forward-looking statements.

In addition to statements that explicitly describe such risks and uncertainties, readers are urged to consider statements in future or conditional tenses or that include terms such as believes, belief, expects, estimates, intends, anticipates or plans to be uncertain and forward-looking. Forward-looking statements may include comments as to our beliefs and expectations as to future events and trends affecting our business. Forward-looking statements are based upon management's current expectations concerning future events and trends and are necessarily subject to uncertainties, many of which are outside of our control. The factors stated under the heading Cautionary Statements and Risk Factors set forth below and those described in Item 1A of Part II of this Form 10-Q/A and our other SEC reports, including our Form 10-K for the year ended December 31, 2005, as well as other factors, could cause actual results to differ materially from those reflected or predicted in forward-looking statements.

Any forward-looking statements are based on management's beliefs and assumptions, using information currently available to us. We assume no obligation, and do not intend, to update these forward-looking statements.

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from those reflected in or suggested by forward-looking statements. Any forward-looking statement you read in this Quarterly Report on Form 10-Q/A reflects our current views with respect to future events and is subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or individuals acting on our behalf are expressly qualified in their entirety by this paragraph. You should specifically consider the factors identified or referred to in this Form 10-Q/A and our other SEC reports, including our Form 10-K for the year ended December 31, 2005, which would cause actual results to differ from those referred to in forward-looking statements.

### Cautionary Statements and Risk Factors

We recognize that we are subject to a number of risks and uncertainties that may affect our future performance. The risks and uncertainties described below are not the only risks and uncertainties that we face. Additional risks and uncertainties not currently known to us or that we currently deem not to be material also may impair our business operations. If any of the following risks actually occur, our business, results of operations and financial condition could suffer. In that event the trading price of our Common Stock could decline, and you may lose all or part of your investment in our Common Stock. The risks discussed below also include forward-looking statements, and our actual results may differ substantially from those discussed in these forward-looking statements.

These risks include:

- our ability to identify and remedy all material errors in our financial statements for the first and second quarters of 2006, for the year ended December 31, 2005 and each of the quarters in that year and for the year ended December 31, 2004, and the related costs associated with identifying and remedying such errors;
- economic, political, business and market conditions in the geographic areas in which we conduct business;
- factors affecting the customers, industries and markets that use our materials and services;
- competitive factors;
- production capacity;
- raw materials availability and pricing;
- our ability to successfully consolidate operations from several locations into our new worldwide headquarters in Rock Hill, South Carolina and to achieve the cost-savings expected from such relocation and consolidation;
- our ability to complete a successful transition of our remaining supply chain and equipment refurbishment activities to our third-party equipment assemblers and others, the ability of those third parties to perform their assembly, refurbishment and supply chain activities in a satisfactory manner, and the risks to us of disruption in our supply of systems to our customers if such third parties fail to perform in a satisfactory manner;
- successful transition of all of our inventory management and distribution functions to a new third-party service provider and the risk that this third-party provider may not perform in a satisfactory manner;
- our ability to successfully transition and implement a new corporate-wide ERP system;
- our ability to successfully centralize and transition to a new shared service center which will centralize most administrative functions for all of our European subsidiaries;
- our success with new distribution agreements with suppliers of materials and other products;
- changes in energy-related expenses;

- changes in the value of foreign currencies against the U.S. dollar;
- changes in interest rates, credit availability or credit stature;
- the effect on us of new pronouncements by accounting authorities;
- our ability to hire, develop and retain talented employees worldwide;
- our ability to develop and commercialize successful new products;
- our success in entering new market places and acquiring and integrating new businesses;
- our access to financing and other sources of capital and our ability to generate cash flow from operations;
- our debt level;
- our compliance with financial covenants in financing documents;
- the outcome of litigation or other proceedings to which we are a party;
- the volatility of our stock price;
- the magnitude and timing of our capital expenditures;
- our ability to forecast our sales of systems and to manage our inventory efficiently;
- changes in our relationships with customers and suppliers;
- acts and effects of war or terrorism; and
- changes in domestic or foreign laws, rules or regulations, or governmental or agency actions.

For a more detailed discussion of such risks and uncertainties, see Management's Discussion and Analysis of Financial Condition and Results of Operations Cautionary Statements and Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2005, and the risk factors noted in our other SEC filings and in Item 1A, Risk Factors in Part II of this Form 10-Q/A.

Except as required by the federal securities laws, we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

For a discussion of market risks at December 31, 2005, refer to Item 7A, Quantitative and Qualitative Disclosures about Market Risk in our Annual Report on Form 10-K for the fiscal year ended December 31, 2005. During the first quarter of 2006, there were no material changes or developments that would materially alter the market risk assessment performed as of December 31, 2005, except as discussed in the following paragraphs.

We and our subsidiaries conduct business in various countries using both our functional currencies and other currencies to effect cross-border transactions. As a result, we and our subsidiaries are subject to the risk that fluctuations in foreign exchange rates between the dates that those transactions are entered into and their respective settlement dates will result in a foreign exchange gain or loss. When practicable, we endeavor to match assets and liabilities in the same currency on our balance sheet and those of our subsidiaries in order to reduce these risks. We also, when we consider it to be appropriate, enter into foreign currency contracts to hedge exposures arising from those transactions. At March 31, 2006, these contracts related primarily to purchases of inventory from suppliers that are denominated in Swiss francs, and to inter-company purchase obligations of our subsidiaries that are denominated in euros, pounds sterling and yen. The notional amount of these contracts at their

respective settlement dates amounted to \$3.4 million in the aggregate. The respective notional amounts of the forward currency contracts

77

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outstanding as of March 31, 2006 aggregated CHF 0.6 million (equivalent to \$0.5 million at settlement date), euros 0.5 million (equivalent to \$0.6 million at settlement date), pounds sterling 0.3 million (equivalent to \$0.5 million at settlement date), and yen 210 million (equivalent to \$1.8 million at settlement date).

During 2005, we entered into a range-forward arrangement with a large, creditworthy financial institution to hedge certain other currency-rate exposures in Japanese yen. This arrangement established a collar around a range of exchange rates between 106.0 and 113.5 yen to the U.S. Dollar to hedge 95 million yen (approximate equivalent range of \$0.9 million to \$0.8 million) of inter-company purchase obligations. Both the put and call options entered into under the hedge arrangement were for the same monetary amount and maturity date. The range-forward arrangement expired on February 6, 2006 without any additional arrangement being in place for any subsequent period.

We are exposed to credit risk if the counterparties to such transactions are unable to perform their obligations. However, we seek to minimize such risk by entering into transactions with counterparties that are creditworthy financial institutions.

#### **Item 4. Controls and Procedures**

##### *Evaluation of Disclosure Controls and Procedures*

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Principal Executive Officer and Principal Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the Exchange Act ). As disclosed in our original Form 10-Q filing for the period ended March 31, 2006, based on that evaluation, our Principal Executive Officer and Principal Financial Officer had previously concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act was recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. As discussed below, based on information subsequently obtained in connection with the preparation of our financial statements for the period ended September 30, 2006, our management, including our Principal Executive Officer and Principal Financial Officer, have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e)) were ineffective as of March 31, 2006.

A material weakness, as used throughout this section, is defined as a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects a company's ability to initiate, authorize, record, process or report external financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the annual or interim financial statements that is more than inconsequential will not be prevented or detected.

As we prepared our financial statements for the period ended September 30, 2006, we discovered errors in our financial statements for the periods ended March 31, 2006 and June 30, 2006 that are discussed below and in other parts of this Form 10-Q/A and that led to the restatement of our financial statements set forth in this Form 10-Q/A. We identified these errors primarily as a result of our efforts to remediate the material weaknesses that we disclosed in the Form 10-Q for the quarterly period ended June 30, 2006, and through our efforts to implement our new ERP system, to reconcile the records in our new ERP system with those in our legacy systems, and to test our internal controls in the context of our new ERP system environment.

In connection with the identification of these errors and the preparation of our third-quarter financial statements, we identified additional control deficiencies that, taken together with the material weaknesses that we previously disclosed in the Second Quarter 10-Q, constitute individually or in the aggregate additional material weaknesses with respect to those matters. These additional deficiencies relate to:

- (a) a deficiency in the processing of and accounting for accounts receivable and the application of customer payments; and
- (b) deficiencies in the timeliness and accuracy of our period-end financial statement closing process and the monitoring of our accounting function and oversight of financial controls.

With respect to the deficiency in our procedures for the processing of and accounting for accounts receivable and the application of customer payments, we determined that this control deficiency resulted in the following errors in our financial statements:

- We experienced errors in the invoicing and recording of customer billings, in the application of customer payments and in the reconciliation of customer accounts. These matters required us to issue and record credit memoranda for the benefit of customers for product returns, pricing adjustments, changes to service contracts, freight-related matters and other similar matters that are discussed elsewhere in this Item 4 and in this Form 10-Q/A. We also identified cash that we had received but which had not been applied to customer accounts or the related accounts receivable.
- Some customer contracts had not been fully integrated and reflected in our new ERP system.
- Certain tax-exempt customers were charged sales tax in error and certain customers were inadvertently not billed for sales tax on their purchases.

We also undertook a review of the potential effect of the financial statement errors that we discovered on prior periods. As discussed elsewhere in this Form 10-Q/A, on November 3, 2006, we announced that management and the Audit Committee of our Board of Directors had determined, based on information presented by our management in connection with the preparation of our financial statements for the third quarter of 2006, that our financial statements included in our Quarterly Reports on Form 10-Q as originally filed for the quarters ended March 31, 2006 and June 30, 2006 should be restated as a result of the errors in them that we had discovered, and on December 14, 2006, we announced that management and the Audit Committee had completed our assessment of our prior-period financial statements and that, based on information presented by our management, the financial statements included in our Annual Reports on Form 10-K for the 2004 and 2005 calendar years also contained errors and should be restated. As discussed elsewhere in this Form 10-Q/A, in evaluating the need to restate those periods, we also took into consideration audit adjustments that had been identified previously as not being material to those periods, and we have included those adjustments in the restated amounts for the applicable 2005 and 2004 periods.

Set forth below is a discussion of the reviews and procedures that we have conducted to identify the errors and control deficiencies that are discussed in this Item 4, the financial statement errors that we identified, the inventory accounting issues that we have identified, the factors contributing to the material weaknesses reported in this Form 10-Q/A, and corrective actions that we are taking to remedy the control deficiencies and material weaknesses reported in this Form 10-Q/A.

#### *Reviews and Procedures Conducted*

We identified most of the errors referred to above and the control deficiencies that contributed to them during the preparation of our financial statements for the three-month and nine-month periods ended September 30, 2006. Having identified these errors, we performed additional detailed transaction reviews and control activities in connection with reconciling and compiling our financial records. We undertook these procedures in order to confirm that our financial statements for the three months and

nine months ended September 30, 2006 were prepared in accordance with generally accepted accounting principles, fairly presented and were free of material errors.

In order to determine that we had identified and corrected all material errors, we performed additional detailed account reconciliations of all material line-item accounts reflected on our Condensed Consolidated Balance Sheet and Condensed Consolidated Statement of Operations as of and for the period ended September 30, 2006 in order to confirm the accuracy of, and to correct any inaccuracies in, those accounts. The accounts that we reconciled during this comprehensive additional account reconciliation process included:

- Cash;
- Trade accounts receivable;
- Trade receivable deposits, unapplied cash and unapplied credits;
- Accounts receivables other;
- Fixed assets;
- Inventory;
- Prepaid expenses;
- Accounts payable;
- Deferred revenue;
- Accrued liability accounts;
- Taxes, including sales and use taxes; and
- Various accrued liability accounts.

As a result of this comprehensive effort, we identified several reconciliation issues and accounting shortcomings, including:

- Some accounts had not been adequately reconciled in accordance with our policies and procedures.
- Certain accounts contained unreconciled differences that had not been timely resolved in accordance with our policies and procedures, including credits for the benefit of customers and cash that had not been applied to customer accounts or the related accounts receivable.

We also identified variances in recorded versus actual inventory values that are discussed below.

#### *Identification of Financial Statement Errors and Related Matters*

We have identified and evaluated the errors noted in our prior-period financial statements and have corrected those errors through adjustments reflected in the restated historical consolidated financial statements in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 154 ( SFAS No. 154 ), Accounting Changes and Error Corrections. We also assessed on a quarterly basis the materiality of prior-period misstatements that were previously identified but not corrected because they were originally considered to be immaterial. As a result of our analysis of adjustments identified during the third quarter of 2006 that were attributable to prior periods as well as previously unadjusted amounts attributable to prior periods, we concluded the prior-period impact was material in the second and fourth quarters of 2005 as well as for the year ended December 31, 2004. Therefore, the restated financial information reflects adjustments to correct or record all such previously unadjusted amounts.





The restatement of the errors and previous unrecorded audit adjustments that we identified included the following:

- Errors in the recording of customer billings, in the application of customer payments and in the reconciliation of customer accounts that were corrected by the issuance and recording credit memoranda for the benefit of customers for product returns, pricing adjustments, changes to service contracts, freight-related matters and other similar matters.
- Errors related to the timing of recognition of royalty income and expense.
- Errors related to the timing of the recognition of warranty and training revenue.
- Errors related to securities issuance costs that arose as a result of expensing such costs rather than applying such costs against the net proceeds of sale of the related securities.
- Errors related to prepaid materials that arose from the reconciliation of such accounts between the sub-ledger and the general ledger for the affected periods.
- Errors related to the failure to record depreciation expense for assets that had been placed in service but which remained recorded in the Company's in construction-in-progress accounts.
- Errors related to the timing of expenses for certain unrelated third party professional services.
- Errors related to the reconciliation of accounts payable that arose from the reconciliation of such accounts between the sub-ledger and the general ledger for each applicable period.
- Errors related to inventory shrinkage that arose from variances identified between actual and recorded inventory values following the Company's conducting physical inventory counts to test the accuracy of the recorded inventory data.
- Errors related to hedging activities on foreign currency transactions that arose from mechanical errors in accumulating spreadsheet data as well as the recording of unrealized gains and losses on foreign exchange hedges that had previously been excluded from the statement of operations.
- Prior-period adjustments related to inventory reserves that had previously been identified but which were not deemed material to that period.
- Errors related to foreign income tax expense that relate to a previously identified adjustment that related to periods prior to 2004 but that was not deemed material to those periods.

For a further discussion of these errors, see Note 2 to the Condensed Consolidated Financial Statements.

*Factors Contributing to Ineffectiveness/Material Weaknesses*

We have determined that the ineffectiveness of our disclosure controls and procedures at March 31, 2006 is primarily attributable to material weaknesses in our internal control over financial reporting as described with respect to the control deficiencies discussed above. Other factors that contributed to the control deficiencies discussed above include:

- Human error;
- Lack of training and experience of new personnel in our system of internal controls and the application of our policies and procedures; and

- Contrary to our policies and procedures, a lack of consistent and effective review and supervision of account reconciliations and data entries at various levels of our accounting organization to confirm, analyze and reconcile account balances that adversely affected our financial reporting and disclosure controls.

81

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The remedial measures we have implemented or are currently implementing are discussed in greater detail below.

*Effectiveness of Disclosure Controls and Procedures*

Based on the evaluation of our disclosure controls and procedures described above, and in light of the inventory variances and other issues identified with respect to the third quarter of 2006, our Principal Executive Officer and Principal Financial Officer concluded that our disclosure controls and procedures were not effective, based on the control deficiencies and material weaknesses as described above.

*Remediation Efforts*

We are continuing to work diligently to identify and remedy all sources of the problems with our inventory accounting procedures, our procedures for reconciling and compiling our financial records and the related matters described above, and we believe that we have identified the primary causes of and appropriate remedial actions for these problems. These are discussed above. While we continue to diligently implement appropriate corrective measures, we ultimately may be unable to achieve that goal despite our efforts, and the corrective actions that we implement may not fully remedy the material weaknesses that we have identified to date or prevent similar or other control deficiencies from having an adverse impact on our business and results of operations or our ability to timely make required SEC filings in the future.

At this time, we anticipate that certain of these control deficiencies may impact the fourth quarter and full year of 2006, despite our substantial remediation efforts, and may require us to undertake extraordinary measures to confirm the accuracy and reliability of our financial statements such as those we undertook in the second and third quarters of 2006.

*Corrective Actions*

In addition, of those corrective actions previously described in Item 4 of Part I of the Second Quarter 10-Q as originally filed, we believe we have substantially completed the following corrective actions:

*Credit Memoranda Remediation:*

- Implemented invoice processing changes and management review prior to submission to customer;
- Increased credit and collection efforts to include more timely contact with customers; and
- Implemented significant review of sales order entries to ensure correctness of items being sold, appropriate discounts, applicability of sales tax exemptions and payment terms.

There were no material changes in our internal control over financial reporting during the period covered by this Form 10-Q/A that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II

### Item 1. Legal Proceedings

On May 6, 2003, we received a subpoena from the U.S. Department of Justice to provide certain documents to a grand jury investigating antitrust and related issues within our industry. We understand that the issues being investigated include issues involving the consent decree that we entered into and that was filed on August 16, 2001 with respect to our acquisition of DTM Corporation and the requirement of that consent decree that we issue a broad intellectual property license with respect to certain patents and copyrights to another entity already manufacturing rapid prototyping industrial equipment. We complied with the requirement of that consent decree for the grant of that license in 2002. In connection with that investigation, the grand jury has taken testimony from various individuals, including certain of our current and former employees and executives. We were advised that we are not a target of the grand jury investigation, and we have not been informed that this status has changed. We have furnished documents required by the subpoena and are otherwise complying with the subpoena.

We are also involved in various other legal matters incidental to our business. Our management believes, after consulting with counsel, that the disposition of these other legal matters will not have a material effect on our consolidated results of operations or consolidated financial position.

### Item 1A. Risk Factors

In addition to the risk factors set forth in the section entitled "Cautionary Statements and Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2005, we have identified certain additional risk factors that are set forth in the section entitled "Cautionary Statements and Risk Factors" of this Quarterly Report on Form 10-Q/A, as follows:

**We face continuing risks in connection with the restatement that we have carried out to our financial statements for the first and second quarters of 2006, for the year ended December 31, 2005 and each of the quarters in that year and for the year ended December 31, 2004.**

These risks include:

- The risk that, notwithstanding our efforts to identify and remedy all material errors in those financial statements, we may discover other errors in those financial statements in the future.
- The risk that the cost of identifying and remedying those errors may be excessive.

**We face risks in connection with our efforts to transition our inventory management and distribution to a new third-party service provider.**

We are in the process of outsourcing the logistics and warehousing of our spare parts inventory to a third-party service provider. In transitioning these responsibilities to the third-party provider, we face a number of risks, including:

- The risk that the third-party service provider may not perform its logistics and warehousing tasks in a satisfactory manner;
- The risk of disruption in the supply of spare parts or other items to our customers if the third-party does not perform the logistics and warehousing services and as a result we are unable to maintain sufficient inventory or timely distribute spare parts or other items to meet our customers' demands; and
- The risk that we will not realize the anticipated financial and operational benefits we expect to receive from transitioning these services to a third party.

**We face risks in connection with our ability to successfully centralize the administrative functions for all of our European subsidiaries at a new shared service center.**

We are in the process of transitioning all of the administrative functions for our European subsidiaries to a centralized shared service center location. We face certain risks in connection with this undertaking, including:

- The risk that we may face unforeseen delays in centralizing the administrative functions of our European subsidiaries;
- The risk that the costs and disruptions associated with centralizing our European administrative functions may exceed the benefits and savings we expect to receive from creating the shared service center; and
- The risk that we may lose employees who are important to our business as a result of relocating and centralizing these administrative functions.

**We face risks in connection with changes in energy-related expenses.**

We and our suppliers depend on various energy products in manufacturing processes used to produce our products. Generally, we acquire energy products at market prices and do not use financial instruments to hedge prices. As a result, we are exposed to market risks related to changes in energy prices. In addition, many of the customers and industries to whom we market our systems and materials are directly or indirectly dependent upon the cost and availability of energy resources. Our business and profitability may be materially and adversely affected to the extent that our or our customers' energy-related expenses increase, both as a result of higher costs of producing, and potentially lower profit margins in selling, our products and materials and because increased energy costs may cause our customers to delay or reduce purchases of our systems and materials.

**We face risks in connection with the effect of new pronouncements by accounting authorities.**

From time to time, accounting authorities issue new rules and pronouncements that may have adverse effects on our reported results of operations or financial condition, may influence customers' ability and willingness to make capital expenditures such as purchases of our systems, or may otherwise have material adverse effects on our business and profitability.

**We face risks in connection with our success in acquiring and integrating new businesses.**

In the past, we have acquired other businesses and technologies as part of our growth and strategic plans. Although we do not currently plan to acquire new businesses, we may in the future make such acquisitions, and those acquisitions will be subject to certain risks, including risks that the costs of such acquisitions may be greater than anticipated and that the anticipated benefits of such acquisitions may be materially delayed or not realized.

**Item 6. Exhibits**

- 31.1 Certification of Principal Executive Officer filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 dated February 8, 2007.
- 31.2 Certification of Principal Financial Officer filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 dated February 8, 2007.
- 32.1 Certification of Principal Executive Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated February 8, 2007.
- 32.2 Certification of Principal Financial Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated February 8, 2007.

85

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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.

3D Systems Corporation

By:

/s/ FRED R. JONES

Fred R. Jones

*Vice President and Chief Financial Officer  
(Principal Financial Officer)*

*(Duly Authorized Officer)*

By:

/s/ WILLIAM J. TENNISON

William J. Tennison

*Vice President and Corporate Controller  
(Principal Accounting Officer)*

*(Duly Authorized Officer)*

Date: February 8, 2007