ADVANCED PHOTONIX INC
Form 10QSB/A
March 22, 2005

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

FORM 10-QSB/A

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 26, 2004

OR

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

Commission file no. 1-11056

ADVANCED PHOTONIX, INC.

Incorporated pursuant to the Laws of Delaware

IRS Employer Identification No. 33-0325826

1240 Avenida Acaso, Camarillo, CA 93012

(805) 987-0146

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 [X] No [ ]

On February 9, 2005, 13,512,631 shares of Class A Common Stock, $.001 par value, and 31,691 shares of Class B Common Stock, $.001 par value, were outstanding.

ADVANCED PHOTONIX, INC.
QUARTERLY REPORT ON FORM 10-QSB/A
For the quarterly period ended December 26, 2004

INTRODUCTORY NOTE

This Amendment No. 1 on Form 10-QSB/A to the Quarterly Report on Form

10-QSB of Advanced Photonix, Inc. (the Company) for the quarterly period ended December 26, 2004 is being filed to (a) restate the Company's Consolidated Balance Sheet and Statement of Cash Flows (Unaudited) and (b) revise related and other disclosures included in the quarterly report on Form 10-QSB.

The restatement of the Balance Sheet primarily involves a reclassification of specific cash accounts and other accrued liabilities: Previously, $2,800,000 was shown on the balance sheet as short term investments; due to the highly liquid and short-term nature of these funds, this amount has been reclassified as cash equivalents. $2,500,000 of restricted cash was included in the total cash balance; this amount has been reclassified and presented as a separate line item on the balance sheet. Customer deposits were previously included in Other current liabilities; this amount has been reclassified and presented as a separate line item under Current Liabilities.

The Statement of Cash Flows has been restated to reflect the related changes in short-term investments and restricted cash, as well as a reclassification of the cash acquired through acquisition from an operating activity to a financing activity. Accordingly, management's discussion regarding Liquidity and Capital Resources has been revised to reflect the changes made.

Additionally, Note 4 to the Consolidated Financial Statements has been revised to provide additional detail on the terms relating to the restricted cash account and the disclosure under Item 3. Controls and Procedures has been revised to more accurately describe management's process for evaluating the Company's disclosure controls and procedures.

This Amendment No. 1 amends Parts I and II of the Quarterly Report on Form 10-QSB for the quarterly period ended December 26, 2004. This Amendment No. 1 continues to reflect circumstances as of the date of the original filing of the Quarterly Report on Form 10-QSB and the Company has not updated the disclosures contained therein to reflect events that occurred at a later date, except for items relating to the restatement and disclosures regarding the restricted cash account.

ADVANCED PHOTONIX, INC.

INDEX

3

ADVANCED PHOTONIX, INC.

CONSOLIDATED BALANCE SHEET
AT DECEMBER 26, 2004
(UNAUDITED)

ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	$ 3,234,000
Restricted cash	2,500,000
Accounts receivable, less allowance of $44,000	2,846,000
Inventories, net of reserve of $1,061,000	3,327,000
Prepaid expenses and other current assets	630,000
Total Current Assets	12,537,000
EQUIPMENT AND LEASEHOLD IMPROVEMENTS, at cost	5,091,000
Less accumulated depreciation and amortization	(3,620,000
Total Equipment and Leasehold Improvements	1,471,000
OTHER ASSETS	
Goodwill, net of accumulated amortization of $353,000	2,421,000
Patents, net of accumulated amortization of $50,000	14,000
Prepaid capital finance expenses, net of current portion and accumulated amortization of $30,000	326,000
Customer list of acquired company, net of current portion	490,000
Other	85,000
Total Other Assets	3,336,000
TOTAL ASSETS	$ 17,344,000

See notes to consolidated financial statements.

4

ADVANCED PHOTONIX, INC.

CONSOLIDATED BALANCE SHEET
AT DECEMBER 26, 2004
(UNAUDITED)

LIABILITIES AND STOCKHOLDERS' EQUITY	
CURRENT LIABILITIES	
Line of credit	$ 77,000
Accounts payable	687,000
Accrued salaries, wages and benefits	488,000
Current portion of capital lease payable	11,000
Customer deposits	305,000
Other accrued liabilities	215,000
Total Current Liabilities	1,783,000
LONG TERM DEBT	
Convertible note payable, net of discount of $141,000	4,859,000
Capital lease payable, net of current portion	5,000
Total Long Term Debt	4,864,000
COMMITMENTS AND CONTINGENCIES	
Class A redeemable convertible preferred stock, $.001 par value; 780,000 shares authorized; 40,000 shares issued and outstanding	32,000
SHAREHOLDERS' EQUITY	
Preferred stock, $.001 par value; 10,000,000 shares authorized; 780,000 shares designated Class a redeemable convertible; no shares issued and outstanding other than Class A redeemable convertible	--
Class A common stock, $.001 par value; 50,000,000 shares authorized; 13,512,631 shares issued and outstanding	13,000
Class B common stock, $.001 par value; 4,420,113 shares authorized; 31,691 shares issued and outstanding	--
Additional paid-in capital	27,995,000
Accumulated Deficit	(17,343,000
Total Shareholders' Equity	10,665,000
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 17,344,000

See notes to consolidated financial statements.

ADVANCED PHOTONIX, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended		
	December 26, 2004	December 28, 2003	December
SALES	$3,852,000	$2,933,000	$10,
Cost of goods sold	2,832,000	1,895,000	7,
GROSS PROFIT	1,020,000	1,038,000	3,
Research and development expenses	33,000	32,000	
Marketing and sales expenses	278,000	188,000	
General and administrative expenses	592,000	568,000	1,
INCOME (LOSS) FROM OPERATIONS	117,000	250,000	
OTHER INCOME			
Interest income	17,000	5,000	
Interest expense	(63,000)	(7,000)	
Other, net	(36,000)	8,000	
TOTAL OTHER INCOME (EXPENSE)	(82,000)	6,000	
NET INCOME (LOSS)	$ 35,000	$ 256,000	$
Basic Earnings Per Share	$ .00	$ .02	
Diluted Earnings Per Share	$ .00	$ .02	
Weighted Average Number of Common Shares Outstanding	13,437,000	13,458,000	13,

See notes to consolidated financial statements.

ADVANCED PHOTONIX, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

For the nine month period ended	December 26,
CASH FLOWS FROM OPERATING ACTIVITIES	
Net Income	$ 642,00
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation	269,00
Amortization	89,00
Disposal of fixed assets	53,00
Changes in operating assets and liabilities:	
Accounts receivable	(165,00
Inventories	(680,00
Prepaid expenses and other current assets	(240,00
Other assets	(400,00
Accounts payable and accrued expenses	266,00
Net cash provided by (used by) operating activities	(166,00
CASH FLOWS FROM INVESTING ACTIVITIES	
Capital expenditures	(150,00
Short term investments	1,700,00
Increase in restricted cash	(2,500,00
Cash acquired through acquisition of Photonic Detectors, Inc.	44,00
Purchase of outstanding shares of Photonic Detectors, Inc. common stock	(1,094,00
Net cash used by investing activities	(2,000,00
CASH FLOWS FROM FINANCING ACTIVITIES	
Proceeds from private placement of convertible note	5,000,00
Proceeds from exercise of stock options	1,00
Repayment of Line of Credit	(900,00
Net cash provided by (used by) financing activities	4,101,00
NET INCREASE (DECREASE) IN CASH & CASH EQUIVALENTS	1,935,00
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	1,299,00
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 3,234,00

See notes to consolidated financial statements.

ADVANCED PHOTONIX, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS - Continued
(UNAUDITED)

For the nine month period ended	December 26,
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION	
Cash paid for interest	$ 70,000
Cash paid for taxes	19,000

ADVANCED PHOTONIX, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 26, 2004

(UNAUDITED)

NOTE 1 - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts of Advanced Photonix, Inc. ("the Company") and the Company's wholly owned subsidiaries, Silicon Sensors Inc. ("SSI"), Texas Optoelectronics, Inc. ("TOI") and Photonic Detectors, Inc. ("PDI"). (See Note 3). These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-QSB and Article 10 of Regulation S-X and Regulation S-B. All significant intercompany accounts and transactions have been eliminated in consolidation. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation have been included. Operating results for the nine month period ended December 26, 2004 are not necessarily indicative of the results that may be expected for the fiscal year ending March 27, 2005. For further information, refer to the financial statements and notes thereto included in the Advanced Photonix, Inc.

Annual Report on Form 10-KSB for the fiscal year ended March 28, 2004.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cash and Cash Equivalents: The Company considers all highly liquid investments, with an original maturity of three months or less when purchased, to be cash equivalents.

Operating Segment Information: The Company predominantly operates in one industry segment: light and radiation detection devices. Substantially all of the Company's assets and employees are located at the Company's facilities in Camarillo, California and Dodgeville, Wisconsin. In addition, the assets and employees located at the Photonic Detectors, Inc. facility in Simi Valley, California (see Note 3) are currently in the process of being evaluated for transfer to either the Camarillo or Dodgeville site. It is expected that the transfer of business from Simi Valley into the other California and Wisconsin facilities will be completed by March 31, 2005.

For the nine month period ended December 26, 2004, sales to foreign countries amounted to approximately 16% of total revenues, with sales to the United Kingdom representing the largest portion at 7%. For the same nine month period in the prior year, export sales represented approximately 10% of total revenues, including sales to the United Kingdom amounting to 4% of total revenues.

Shipping and Handling Costs: The Company's policy is to classify shipping and handling costs as a component of Costs of Goods Sold in the Statement of Operations.

9

NOTE 2 - Continued

Net Income (Loss) Per Share: Net income (loss) per share is based on the weighted average number of common shares outstanding. Such weighted average shares were approximately 13,433,000 at December 26, 2004 and 13,441,000 at December 28, 2003. Net income (loss) per share calculations are in accordance with Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings per Share" (SFAS 128). Accordingly, "basic" net income (loss) per share is computed by dividing net income (loss) by the weighted average number of shares outstanding for the year. The impact of Statement 128 on the calculation of earnings per share is as follows:

BASIC	Nine Months Ended December 26, 2004	Nine Months Ende December 28, 200
Average Shares Outstanding	13,433,000	13,441,000
Net Income (Loss)	642,000	593,000
Basic Income (Loss) Per Share	$ 0.05	$ 0.04
DILUTED		
Average Shares Outstanding	13,433,000	13,441,000
Net Effect of Shares Issuable pursuant to terms of convertible note, based on a weighted average	708,000	--
Net Effect of Dilutive Stock Options		

and Warrants based on the treasury stock method using average market price	873,000	497,000
Total Shares	15,014,000	13,938,000
Net Income, adjusted for interest expense on convertible note (net of tax)	683,000	593,000
Diluted Earnings Per Share	$ 0.05	$ 0.04
Average Market Price of Common Stock	$ 2.27	$ 1.43
Ending Market Price of Common Stock	$ 1.76	$ 2.13

The following stock options granted to Company employees, directors, and former owners were excluded from the calculation of earnings per share in the financial statements because they were anti-dilutive for the periods reported:

Nine Months Ended December 26, 2004		Nine Months Ended December 28, 2003	
No. of Shares Underlying Options	Exercise Price Per Share	No. of Shares Underlying Options	Exercise Price Per Share
27,700	2.5000	80,000	1.8750
1,000	3.0940	28,400	2.5000
350,000	3.1875	1,000	3.0940
50,000	5.3440	350,000	3.1875
		50,000	5.3440
428,700		509,400	

NOTE 2 - Continued

Inventories: Inventories consist of the following:

	December 26, 2004
Raw materials	$ 3,156,000
Work in progress	1,008,000
Finished products	224,000
Total inventories	$ 4,388,000
Less reserve	(1,061,000)
Inventories, net	$ 3,327,000

NOTE 3 - ACQUISITION

On December 21, 2004, the Company purchased all of the issued and outstanding shares of common stock of PDI, a privately owned manufacturer of opto-electronic components and assemblies located in Simi Valley, California. The purchase price was 113,572 shares of API Class A Common Stock (issued at $1.82 per share) plus $1,075,000 in cash and the assumption of the Seller's trade accounts payable, accrued liabilities, and bank line of credit amounting to approximately $259,000. The Company incurred $19,000 of expenses in connection with this acquisition. The Company has plans to close the Simi Valley location and integrate its business into the Camarillo, California and Dodgeville, Wisconsin facilities. In connection with the transaction, the Company recorded a $612,000 intangible asset ("Customer List") which it will amortize over a 5 year period, beginning January 2005. A summary of the assets and liabilities acquired at fair market value is as follows:

Assets Acquired	
Cash	$ 44,000
Accounts receivable	239,000
Inventories	423,000
Prepaid & other current assets	3,000
Furniture and equipment	239,000
Customer list	612,000
Total Assets Acquired	$ 1,560,000
Liabilities Assumed	
Accounts payable	$ (159,000)
Accrued salaries & benefits	(22,000)
Bank line of credit	(78,000)
Total liabilities assumed	$ (259,000)
Total Purchase Price	$ 1,301,000

NOTE 4 - NOTE PAYABLE & RESTRICTED CASH

On October 12, 2004, the Company entered into a definitive agreement for the private placement to three institutional investors of $5 million aggregate principal amount of its senior convertible notes. The notes are convertible at the option of the holder under certain circumstances into shares of the Company's Class A Common Stock at an initial conversion price of $1.9393 per share, subject to adjustment. The notes pay interest at an annual rate of prime plus 1% and will mature on September 30, 2007. $2.5 million of the purchase price for the notes is being held in a cash collateral account subject to release upon satisfaction of certain conditions specified in the purchase agreement. The original conditions of release provided for $1,250,000 to be eligible for release if the Company had entered into a definitive agreement for a permitted acquisition on or before January 31, 2005. Subsequently, any balance remaining in the cash collateral account, up to the full $2,500,000, would be released upon the Company's consummation of a permitted acquisition on or before March 31, 2005. The original terms were modified by letters of agreement between API and the investors dated March 9, 2005. The modified terms provide for

$1,250,000 to be released upon entry into a definitive agreement for a permitted acquisition on or before March 11, 2005 and for the remaining funds to be released upon the consummation of that acquisition on or before May 1, 2005. A "permitted acquisition" is defined in the Securities Purchase Agreement as the purchase by the Company of an entity with (1) EBITDA of not less than $750,000 during the twelve months immediately preceeding the acquisition and (2) revenues of not less than $4,000,000 during the twelve months immediately preceeding the acquisition. Since Photonic Detectors, Inc. did not qualify as a "permitted acquisition" no funds were released as a result of completing that transaction. The original Securities Purchase Agreement was filed with the Securities and Exchange Commission on October 12, 2004.

In connection with the transaction, the Company had issued to the investors five-year warrants to purchase 850,822 shares of the Company's Class A Common Stock at an exercise price of $2.1156 per share, subject to adjustment. The Company has agreed to register the shares of common stock issuable upon conversion of the notes and upon exercise of the warrants for resale under the Securities Act of 1933. The investors have the option for a period of one year following effectiveness of the registration statement to acquire an additional $5 million aggregate principal amount of the notes with an initial conversion price of $2.1156 per share and five-year warrants to purchase an additional 850,822 shares of common stock. The original terms of the warrants issued and, the additional warrants to be issued, in the private placement to the investors were also modified on March 9, 2005 to reduce the exercise price from $2.1156 per share of Class A Common Stock of API to $1.78 per share. Similarly, on March 9, 2005, the terms of the notes issued in connection with the private placement (the "Notes") were modified to (i) provide that the interest rate shall not be less than 6.5% at any time and (ii) increase the amount of "Permitted Indebtedness" (as such term is defined in the Notes) from $3 million to $6 million and (iii) decrease the amount of "Permitted Acquisition Indebtedness" (as such term is defined in the Notes) from $6 million to $3 million. In addition, the investors in the private placement have agreed to subordinate, pursuant to a form of subordination agreement in form and substance reasonable satisfactory to them, (i) the principal and interest payments on the Notes to the "Permitted Bank Debt" (as such term is defined in the letters of agreement) and (ii) their liens on the Company's assets to any lien granted by the Company as security for the "Permitted Bank Debt".

In accordance with APB 14, the Company has recorded a discount to the note of $141,000 to account for the fair value associated with the note's detachable warrants. Upon any exercise of the conversion feature, the notes will then be converted from debt to equity. A copy of the original agreement and all related documents were filed with the Securities and Exchange Commission on October 12, 2004 on Form 8-K, and the foregoing summary is qualified in its entirety by reference thereto.

12

NOTE 5 - NEW ACCOUNTING PRONOUNCEMENTS

In December 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation 46(r), ("FIN 46(r)") "Consolidation of Variable Interest Entities". The pronouncement amends Accounting Research Bulletin 51 to set standards to require financial statement consolidation of certain variable interest entities that meet specific characteristics if the company has a controlling financial interest. This interpretation shall be applied to all variable interest entities by the end of the first reporting period ending after December 15, 2004, for enterprises that are small business issuers. The Company adopted this Interpretation on October 1, 2004.

In December 2004, the FASB issued Statement No. 123(R), ("FAS 123(R)") "Share-Based Payment". This statement replaces FASB Statement No. 123, "Accounting for Stock-Based Compensation", and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees". FAS 123(R) covers a wide range of share-based compensation, including stock options, and requires that the compensation cost relating to share-based transactions be measured at fair value and recognized in the financial statements. Public entities filing as small business issuers will be required to apply Statement 123(R) in the first interim or annual reporting period beginning after December 15, 2005. The Company will adopt this statement in January 2006.

In November 2004, the FASB issued FASB Statement No. 151, "Inventory Costs - An amendment of ARB No. 43, Chapter 4". Statement 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs and spoilage should be expensed as incurred and not included in overhead. Further, Statement 151 requires that allocation of fixed production overheads to conversion costs should be based on normal capacity of the production facilities. The provisions in Statement 151 are effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Companies must apply the standard prospectively. The Company will adopt this standard on April 1, 2006.

In December 2004, the FASB issued FASB Statement No. 153, "Exchanges of Nonmonetary Assets" which is an amendment of APB Opinion No. 29. The amendments made by the Statement are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replaces it with a broader exception for exchanges of nonmonetary assets that do not have "commercial substance." Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. The provisions in Statement 153 are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Early application is permitted and companies must apply the standard prospectively. The Company will adopt this statement on October 1, 2005.

The Company does not believe that either of these accounting pronouncements will have a material impact on its financial position or results of operations.

13

Item 2. Management's Discussion and Analysis

Application of Critical Accounting Policies

Application of our accounting policies requires management to make certain judgments and estimates about the amounts reflected in the financial statements. Management uses historical experience and all available information to make these estimates and judgments, although differing amounts could be reported if there are changes in the assumptions and estimates. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventory allowances, impairment costs, depreciation and amortization, warranty costs, taxes and contingencies. Management has identified the following accounting policies as critical to an understanding of our financial statements and/or as areas most dependent on management's judgment and estimates.

Revenue Recognition
In accordance with Staff Accounting Bulletin No. 404, we recognize revenue from the sale of products when the products are shipped to the customer. Revenues from the sale of services consist of non-recurring engineering charges, which are recognized when the services have been rendered. Historically, sales returns have amounted to less than 1% of net income and all sales are recorded net of sales returns and discounts.

Impairment of Long-Lived Assets
We continually review the recoverability of the carrying value of long-lived assets using the methodology prescribed in Statement of Financial Accounting Standards (SFAS) 144, "Accounting for the Impairment and Disposal of Long-Lived Assets." We also review long-lived assets and the related intangible assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Upon such an occurrence, recoverability of these assets is determined by comparing the forecasted undiscounted net cash flows to which the assets relate, to the carrying amount. If the asset is determined to be unable to recover its carrying value, then intangible assets, if any, are written down first, followed by the other long-lived assets to fair value. Fair value is determined based on discounted cash flows, appraised values or management's estimates, depending on the nature of the assets.

Deferred Tax Asset Valuation Allowance
We record a deferred tax asset in jurisdictions where we generate a loss for income tax purposes. Due to our history of operating losses, we have recorded a full valuation allowance against these deferred tax assets in accordance with SFAS 109, "Accounting for Income Taxes," because, in management's judgment, the deferred tax assets may not be realized in the foreseeable future.

Inventories
Our inventories are stated at standard cost (which approximates the first-in, first-out method) or market. Slow moving and obsolete inventories are analyzed quarterly. To calculate a reserve for obsolescence, we begin with a review of our slow moving inventory. Any inventory which has not moved within the past 24 months is reserved for at 100% of book value; inventory which has not moved within the past 12 months is reserved for at 40%. The percentages applied to the reserve calculation are based on historical usage analyses. In addition, any residual inventory which is customer specific and remaining on hand at the time

14

of contract completion is reserved for at the standard unit cost. The complete list of slow moving and obsolete inventory is then reviewed by the production, engineering and/or purchasing departments to identify items that can be utilized in the near future. These items are then excluded from the analysis and the remaining amount of slow-moving and obsolete inventory is then reserved for. Additionally, non-cancelable open purchase orders for parts we are obligated to purchase where demand has been reduced may be reserved. Reserves for open purchase orders where the market price is lower than the purchase order price are also established. If a product which had previously been reserved for is subsequently sold, the amount of reserve specific to that item is then reversed.

Accounts Receivable and Allowance for Doubtful Accounts
The Allowance for Doubtful Accounts is established by analyzing each account that has a balance over 90 days past due. Each account is individually assigned a probability of collection. The total amount determined to be uncollectible in the 90-days-past-due category is then reserved fully. The percentage of this reserve to the 90-days-past-due total is then established as a guideline and

applied to the rest of the non-current accounts receivable balance where appropriate. When other circumstances suggest that a receivable may not be collectible, it is immediately reserved for, even if the receivable is not yet in the 90-days-past-due category.

RESULTS OF OPERATIONS

The Company's net sales for the third quarter (Q3 05) and nine month period (YTD 05) ended December 26, 2004, were $3.85 million and $10.81 million, respectively. As compared to the third quarter of the prior year ("Q3 04"), net sales increased by 31%, while year to date net sales increased by 22% over the same nine month period of the prior year (YTD 04).

As has been the case throughout most of the current fiscal year, the increase in net sales for both the quarter and year to date periods is largely attributable to increases in revenues to the medical and industrial sensing markets, which have increased by 48% and 38%, respectively, over the same quarter of the previous year. Year to date, sales to the medical markets, which represent 16% of total sales, have increased 32% over the prior year and sales to the industrial sensing markets, representing 42% of total sales, have increased by 26% over the same nine-month period of the previous year. In addition, sales to the military aerospace markets continue to grow and currently represent 35% of total year to date revenues. As the acquisition of Photonic Detectors, Inc. (PDI) was not completed until the end of the fiscal quarter, none of the sales increases are attributable to revenues generated as a result of acquisition. We continue to expect sales to increase in fiscal 2005 as compared to fiscal 2004; however our shipment schedules and thus recognition of revenues are primarily dependent on customer defined delivery schedules. As such, our quarter-to-quarter comparisons often vary for revenue and market composition, due to fluctuations in customer delivery schedules which are beyond our control.

COSTS AND EXPENSES

Cost of product sales increased by $937,000 (49%) during Q3 05 and by $1.44 million (25%) during YTD 05 as compared to the same periods of the prior year. Stated as a percentage of net sales, cost of goods sold, increased 9 percentage points to 74% for Q3 05, as compared to 65% in Q3 04. Year over year, cost of sales increased only slightly, to 67%, as compared to 66% in the previous year. As a result, gross margin decreased to 26% for the quarter and to 33% year to date, as compared to 35% and 34% for the comparable periods of the prior year. The reduction in margins for the quarter is the direct result of manufacturing issues, including machinery failures and other production yield issues, encountered during the quarter. Machinery and production failures which resulted in low product yields and large amounts of scrapped materials accounted for approximately 50% of the variance and occurred primarily during the latter half of the quarter. The remaining variance was due to the recognition of manufacturing costs (materials, labor and overhead) associated with work in progress jobs which were determined to be no longer current. We regard both the quarterly and year to date gross margins to be lower than expected and, assuming no additional mechanical or production failures, we anticipate that year end gross margins will improve slightly, by one to two percentage points over the current year to date margin.

Research and development (R&D) costs remained flat at $33,000 in Q3 05 as compared to $32,000 in Q3 04 (an increase of 3%). Year to date, research and development costs have decreased by $77,000 or 41% as compared to YTD 04. Throughout the year, management has continued to focus R&D expenditures on those projects which offer higher commercial potential per each dollar spent and the current level of expense approximates our expectations for both the quarter and year to date periods. During the remainder of the fiscal year, we expect R&D expenses to remain at or above the same level. At this time, we do not anticipate any major fluctuations in R&D activity; however the possibility exists that certain customer project parameters may change which would cause an increase in R&D expenses for any given period.

Marketing and sales expenses increased by $90,000 (48%) to $278,000 in the third quarter of 2005 compared to Q3 04 and by $173,000 (24%) to $888,000 year to date, as compared to YTD 04. Stated as a percentage of sales, marketing and sales expenses represent 7% and 8% for the quarter and year to date periods, respectively. The increase over the prior year for both comparative periods remains primarily due to expansion of the sales department during the year, resulting in increased salaries, commissions, travel and other employee related expenses as well as increases in advertising and marketing expenses over the same periods of the prior year. In addition, marketing and sales expenses in the prior year were lower than expected due to a recovery of amounts previously recorded as bad debt expense. Although no significant bad debt expenses have been recorded in the current year, net expenses are higher as they do not reflect any credits as a result of bad debt recoveries. The Company expects that the current level of marketing and sales expenses, presented as a percentage of net sales, is a fair representation of what can be expected of the remainder of the year.

General and administrative (G&A) expenses increased by $24,000 (4%) to $592,000 in Q3 05 as compared to $568,000 in Q3 04. Year to date, general and administrative expenses increased by $321,000 (21%) to $1.865 million as compared to $1.544 million for YTD 04. The net increase for the quarter is primarily due to accumulated expenses associated with the private placement transaction which are being amortized over the term of the note (36 months). In addition to the capital finance expenses, the increases in year to date expenses are attributable to costs associated with the Company's ongoing acquisition investigation activities. As with the sales department, additional G&A personnel have been added during the year, resulting in increased salary and employee related expenses, as well as increased accruals of bonus expenses. Expressed as a percentage of net sales, G&A expenses represent 17% of year to date revenues, which we feel is indicative of what can be expected for the remainder of the fiscal year.

In addition to the above, net income for the quarter was impacted by interest expense of $63,000 and by losses on the disposal of fixed assets totaling $33,000. Both the manufacturing issues and loss on fixed asset disposals are considered by management to be one-time events, and are not expected to repeat during the remainder of the fiscal year. As such, net income was $35,000, or $0.00 per share, for Q3 05 and $642,000, or $0.05 per share, for YTD 05. During the same periods of the prior year, the Company reported net income of $256,000 ($0.02 per share) and $593,000 ($0.04 per share), respectively.

16

LIQUIDITY AND CAPITAL RESOURCES

On December 21, 2004, the Company purchased the business and all of the outstanding stock of Photonic Detectors, Inc., a privately owned manufacturer of optoelectronic components and assemblies, located in Simi Valley, California. In connection with the transaction, the Company acquired certain net assets, including $44,000 cash, and assumed certain outstanding liabilities of Photonic Detectors, Inc. $1,050,000 net cash was expended for the transaction, which included the agreed purchase price of $1,075,000, plus additional expenses incurred of $19,000, less the $44,000 cash received.

At December 26, 2004 , the Company had cash and cash equivalents of $3.2 million and working capital of $10.8 million. The Company's cash and cash equivalents increased by $1.9 million during the nine months ended December 26, 2004, including $1.7 million transferred from short-term investments into cash. $5.0 million was obtained through private placement of a convertible note, of which $2.5 million was placed in a restricted cash collateral account subject to release upon satisfaction of certain conditions (See Note 4 to the Consolidated Financial Statements), and the balance was available for working capital and other requirements. Cash used by operating activities totaled $166,000, which included significant outlays for capital finance expenses and other prepaid expenses. $900,000 was used to pay off the Company's credit line balance and $150,000 was used for capital expenditures required primarily for necessary computer and manufacturing equipment upgrades or replacements.

The Company is exposed to interest rate risk for marketable securities. Due to anticipated cash needs and continually declining interest rates available to the Company pursuant to its investment policy, the Company was able to achieve the best yields on liquid money market and income fund accounts and thus transferred the majority of its available cash reserves from longer term investment instruments to such short term accounts during the past year. At December 26, 2004, the Company held $2.8 million in highly liquid income and money fund accounts which carry an average interest rate of 1.3%. Due to the short-term nature of these funds, the full $2.8 million is considered to be a cash equivalent. During the remainder of 2005, the Company will continue to monitor available interest rates and will attempt to utilize the best possible avenues of investment for its excess liquid assets.

Item 3. Controls and Procedures

Our Chief Executive Officer, President, and Chief Financial Officer (the "Certifying Officers") are responsible for establishing and maintaining disclosure controls and procedures for the Company. The Certifying Officers have designed such disclosure controls and procedures to ensure that material information is made known to them, particularly during the period in which this report was prepared. The Certifying Officers have evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by the quarterly report and believe that the Company's disclosure controls and procedures are effective based on the required evaluation. There were no changes in internal controls over financial reporting or in other factors during the period reported that have materially affected, or that are reasonably likely to materially affect, internal controls over financial reporting. Subsequent to the date of their evaluation, there have been no significant changes in internal controls over financial reporting which are likely to materially affect internal controls over financial reporting for future periods.

FORWARD LOOKING STATEMENTS

The information contained herein includes forward looking statements that are based on assumptions that management believes to be reasonable but are subject to inherent uncertainties and risks including, but not limited to, risks associated with the integration of newly acquired businesses, unforeseen technological obstacles which may prevent or slow the development and/or manufacture of new products, limited (or slower than anticipated) customer acceptance of new products which have been and are being developed by the Company, the availability of other competing technologies and a decline in the general demand for optoelectronic products.

PART II OTHER INFORMATION

Items 1-5
None.

Item 6 Exhibits and Reports on Form 8-K
(a) Exhibits

31.1	Certification of the Registrant's Chairman, Chief Executive Officer, Chief Financial Officer and Director pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.3	Certification of the Registrant's President pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

18

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.

Advanced Photonix, Inc.
(Registrant)

Date: March 22, 2005

/s/ Richard Kurtz

Richard Kurtz
Chief Executive Officer, Chairman,
Chief Financial Officer and Director

/s/ Paul Ludwig

Paul Ludwig
President

19