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

FORM 10-Q

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

For the quarterly period ended January 31, 2015

OR

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

For the transition period from to

Commission File Number: 001-33261

AEROVIRONMENT, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-2705790** (I.R.S. Employer Identification No.)
181 W. Huntington Drive, Suite 202 **Monrovia, California** (Address of principal executive offices)	**91016** (Zip Code)

(626) 357-9983
(Registrant’s telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐	Accelerated filer ☒
Non-accelerated filer ☐ (Do not check if smaller reporting company)	Smaller reporting company ☐

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

As of February 20, 2015, the number of shares outstanding of the registrant’s common stock, $0.0001 par value, was 23,330,876.

AeroVironment, Inc.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

AeroVironment, Inc.
Consolidated Balance Sheets
(In thousands except share and per share data)

	January 31, 2015 (Unaudited)	April 30, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 125,977	$ 126,969
Short-term investments	77,581	70,639
Accounts receivable, net of allowance for doubtful accounts of $622 at January 31, 2015 and $791 at April 30, 2014	37,834	31,739
Unbilled receivables and retentions	8,345	10,929
Inventories, net	48,799	50,699
Income tax receivable	1,940	6,584
Deferred income taxes	5,217	5,038
Prepaid expenses and other current assets	4,203	4,260
Total current assets	309,896	306,857
Long-term investments	54,575	50,505
Property and equipment, net	16,143	19,997
Deferred income taxes	4,638	6,721
Other assets	1,219	874
Total assets	$ 386,471	$ 384,954
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 16,215	$ 13,906
Wages and related accruals	12,968	14,083
Customer advances	4,213	2,984
Other current liabilities	10,264	6,762
Total current liabilities	43,660	37,735
Deferred rent	1,336	1,239
Liability for uncertain tax positions	645	3,513
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.0001 par value:		
Authorized shares — 10,000,000; none issued or outstanding	—	—
Common stock, $0.0001 par value:		
Authorized shares — 100,000,000		
Issued and outstanding shares — 23,330,876 at January 31, 2015 and 23,176,576 at April 30, 2014	2	2
Additional paid-in capital	147,374	143,648
Accumulated other comprehensive loss	(1,441)	(263)
Retained earnings	194,895	199,080
Total stockholders' equity	340,830	342,467
Total liabilities and stockholders' equity	$ 386,471	$ 384,954

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Consolidated Statements of Operations (Unaudited)
(In thousands except share and per share data)

	Three Months Ended		Nine Months Ended	
	January 31, 2015	January 25, 2014	January 31, 2015	January 25, 2014
Revenue:				
Product sales	$ 56,308	$ 57,041	$ 141,993	$ 135,752
Contract services	12,089	12,180	30,934	42,453
	68,397	69,221	172,927	178,205
Cost of sales:				
Product sales	32,901	33,193	91,477	85,891
Contract services	8,503	8,976	22,532	28,839
	41,404	42,169	114,009	114,730
Gross margin:				
Product sales	23,407	23,848	50,516	49,861
Contract services	3,586	3,204	8,402	13,614
	26,993	27,052	58,918	63,475
Selling, general and administrative	13,268	13,168	40,141	38,711
Research and development	8,577	5,241	24,232	19,292
Income (loss) from operations	5,148	8,643	(5,455)	5,472
Other income (expense):				
Interest income	224	197	629	597
Other (expense) income	(284)	4,675	(276)	(1,026)
Income (loss) before income taxes	5,088	13,515	(5,102)	5,043
Provision (benefit) for income taxes	2,763	2,299	(917)	(618)
Net income (loss)	$ 2,325	$ 11,216	$ (4,185)	$ 5,661
Earnings (loss) per share data:				
Basic	$ 0.10	$ 0.50	$ (0.18)	$ 0.25
Diluted	$ 0.10	$ 0.49	$ (0.18)	$ 0.25
Weighted average shares outstanding:				
Basic	22,890,502	22,321,368	22,856,962	22,278,225
Diluted	23,109,354	22,883,583	22,856,962	22,722,795

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Consolidated Statements of Comprehensive Income (Loss) (Unaudited)
(In thousands)

	Three Months Ended		Nine Months Ended	
	January 31, 2015	January 25, 2014	January 31, 2015	January 25, 2014
Net income (loss)	$ 2,325	$ 11,216	$ (4,185)	$ 5,661
Other comprehensive (loss) income:				
Unrealized (loss) gain on investments, net of tax	(582)	58	(1,178)	87
Total comprehensive income (loss)	$ 1,743	$ 11,274	$ (5,363)	$ 5,748

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Consolidated Statements of Cash Flows (Unaudited)
(In thousands)

	Nine Months Ended January 31, 2015	Nine Months Ended January 25, 2014
Operating activities		
Net (loss) income	$ (4,185)	$ 5,661
Adjustments to reconcile net (loss) income to cash provided by operating activities:		
Depreciation and amortization	6,368	6,799
Provision for doubtful accounts	(101)	269
Deferred income taxes	(202)	(333)
Gain on sale of equity securities	(182)	—
Stock-based compensation	2,714	2,687
Foreign currency losses	361	—
(Increase) decrease in fair value of conversion feature of convertible bonds	(73)	1,032
Tax benefit from exercise of stock options	13	304
Excess tax benefit from stock-based compensation	(343)	—
Changes in operating assets and liabilities:		
Accounts receivable	(5,994)	(23,116)
Unbilled receivables and retentions	2,584	2,668
Inventories	1,900	7,120
Income tax receivable	4,644	5,925
Other assets	(76)	662
Accounts payable	2,309	(1,009)
Other liabilities	3,806	(5,197)
Net cash provided by operating activities	13,543	3,472
Investing activities		
Acquisitions of property and equipment	(2,326)	(6,751)
Acquisitions of intangible assets	(150)	(750)
Purchases of held-to-maturity investments	(88,737)	(48,247)
Redemptions of held-to-maturity investments	66,158	68,635
Sales of available-for-sale investments	9,498	175
Net cash (used in) provided by investing activities	(15,557)	13,062
Financing activities		
Excess tax benefit from exercise of stock options	343	—
Tax withholding payment related to net settlement of equity awards	(36)	—
Exercise of stock options	715	883
Net cash provided by financing activities	1,022	883
Net (decrease) increase in cash and cash equivalents	(992)	17,417
Cash and cash equivalents at beginning of period	126,969	75,332
Cash and cash equivalents at end of period	$ 125,977	$ 92,749
Supplemental disclosure:		
Unrealized loss (gain) on available-for-sale investments recorded in other comprehensive (loss) income, net of deferred taxes of $785 and $(57), respectively	$ 1,178	$ (87)
Accrued acquisition of intangible assets	$ 250	$ —
Forfeiture of vested stock-based compensation	$ 23	$ —

See accompanying notes to consolidated financial statements (unaudited).

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

1. Organization and Significant Accounting Policies

Organization

AeroVironment, Inc., a Delaware corporation (the "Company"), is engaged in the design, development, production, support and operation of unmanned aircraft systems and efficient energy systems for various industries and governmental agencies.

Basis of Presentation

The accompanying unaudited 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 of Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments necessary for a fair presentation with respect to the interim financial statements have been included. The results of operations for the three and nine months ended January 31, 2015, are not necessarily indicative of the results for the full year ending April 30, 2015. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended April 30, 2014, included in the Company's Annual Report on Form 10-K.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions, including estimates of anticipated contract costs and revenue utilized in the revenue recognition process, that affect the reported amounts in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

The Company's consolidated financial statements include the assets, liabilities and operating results of wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Segments

The Company's products are sold and divided among two reportable segments to reflect the Company's strategic goals. Operating segments are defined as components of an enterprise from which separate financial information is available that is evaluated regularly by the Chief Operating Decision Maker ("CODM") in deciding how to allocate resources and in assessing performance. The Company's CODM is the Chief Executive Officer, who reviews the revenue and gross margin results for each of these segments in order to make resource allocation decisions, including the focus of research and development ("R&D") activities and performance assessment. The Company's reportable segments are business units that offer different products and services and are managed separately.

Investments

The Company's investments are accounted for as held-to-maturity and available-for-sale and reported at amortized cost and fair value, respectively.

Fair Values of Financial Instruments

Fair values of cash and cash equivalents, accounts receivable, unbilled receivables, retentions and accounts payable approximate cost due to the short period of time to maturity.

Government Contracts

Payments to the Company on government cost reimbursable contracts are based on provisional, or estimated indirect rates, which are subject to an annual audit by the Defense Contract Audit Agency ("DCAA"). The cost audits result in the negotiation and determination of the final indirect cost rates that the Company may use for the period(s) audited. The final rates, if different from the provisional billing rates, may create an additional receivable or liability for the Company. For example, during the course of its audits, the DCAA may question the Company's incurred project costs, and if the DCAA believes the Company has accounted for such costs in a manner inconsistent with the requirements under Federal Acquisition Regulations, the DCAA auditor may recommend to the Company's administrative contracting officer to disallow such costs. The Company can provide no assurance that the DCAA or other government audits will not result in material disallowances for incurred costs in the future.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

As of January 31, 2015 and April 30, 2014, the Company had $4.7 million and $2.1 million, respectively, in contract-related reserves for its estimate of potential refunds to customers for potential cost adjustments on U.S. government cost reimbursable contracts. For the three and nine months ended January 31, 2015, the Company recorded $0 and $2.6 million, respectively, of expense in cost of sales for these contract-related reserves.

Earnings (Loss) Per Share

Basic earnings (loss) per share is computed using the weighted-average number of common shares outstanding, excluding shares of unvested restricted stock. The dilutive effect of potential common shares outstanding is included in diluted earnings per share and excludes any anti-dilutive effects of options, shares of unvested restricted stock and restricted stock units.

The reconciliation of basic to diluted shares is as follows:

	Three Months Ended		Nine Months Ended	
	January 31, 2015	January 25, 2014	January 31, 2015	January 25, 2014
Denominator for basic earnings (loss) per share:				
Weighted average common shares outstanding, excluding unvested restricted stock	22,890,502	22,321,368	22,856,962	22,278,225
Dilutive effect of employee stock options, unvested restricted stock and restricted stock units	218,852	562,215	—	444,570
Denominator for diluted earnings (loss) per share	23,109,354	22,883,583	22,856,962	22,722,795

During the three months ended January 31, 2015 and January 25, 2014 and nine months ended January 25, 2014, certain shares reserved for issuance upon exercise of stock options, shares of unvested restricted stock and restricted stock units were not included in the computation of diluted earnings per share because their inclusion would have been anti-dilutive. The number of shares reserved for issuance upon exercise of stock options, shares of unvested restricted stock and restricted stock units that met this anti-dilutive criterion for the three months ended January 31, 2015 and January 25, 2014 and nine months ended January 25, 2014 was approximately 11,000, 24,000 and 56,000 respectively. Due to the net loss for the nine months ended January 31, 2015 no shares reserved for issuance upon exercise of stock options, restricted stock units or shares of unvested restricted stock were included in the computation of diluted loss per share as their inclusion would have been anti-dilutive.

Recently Issued Accounting Standards

In April 2014, the Financial Accounting Standards Board ("FASB"), issued Accounting Standards Update ("ASU"), No. 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. This ASU changes the threshold for a disposal to qualify as a discontinued operation. To be considered a discontinued operation a disposal now must represent a strategic shift that has or will have a major effect on an entity's operations and financial results. This ASU also requires new disclosures for individually material disposal transactions that do not meet the definition of a discontinued operation. This update will be applied prospectively and is effective for annual periods, and interim periods within those years, beginning after December 15, 2014. Early adoption is permitted provided the disposal was not previously disclosed. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This ASU is effective for annual periods beginning after December 15, 2016 and shall be applied either retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. The Company is evaluating the potential impact of this adoption on its consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-12, *Compensation—Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period (a consensus of the FASB Emerging Issues Task Force)*. This ASU clarifies that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in Topic 718 as it relates to awards with performance conditions that affect vesting to account for such awards. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. This ASU is effective for annual periods, and interim periods within those years, beginning after December 15, 2015. Early adoption is permitted. This ASU may be applied either (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

2. Investments

Investments consist of the following (in thousands):

	January 31, 2015	April 30, 2014
Short-term investments:		
Held-to-maturity securities:		
Municipal securities	$ 58,664	$ 69,898
U.S. government securities	10,537	—
Corporate bonds	1,322	—
Certificates of deposit	4,626	741
Total held-to-maturity investments	75,149	70,639
Available-for-sale securities:		
Equity securities	2,432	—
Total short-term investments	$ 77,581	$ 70,639
Long-term investments:		
Held-to-maturity securities:		
Municipal securities	$ 41,096	$ 29,759
U.S. government securities	6,033	—
Corporate bonds	4,585	—
Certificates of deposit	—	3,889
Total held-to-maturity investments	51,714	33,648
Available-for-sale securities:		
Auction rate securities	2,861	5,683
Convertible bond	—	5,865
Equity securities	—	5,309
Total available-for-sale investments	2,861	16,857
Total long-term investments	$ 54,575	$ 50,505

Held-To-Maturity Securities

As of January 31, 2015 and April 30, 2014, the balance of held-to-maturity securities consisted of state and local government municipal securities, U.S. treasury securities and certificates of deposit. Interest earned from these investments is recorded in interest income.

The amortized cost, gross unrealized gains, gross unrealized losses, and estimated fair value of the held-to-maturity investments as of January 31, 2015, were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Municipal securities	$ 99,760	$ 41	$ (10)	$ 99,791
U.S. government securities	16,570	17	—	16,587
Corporate bonds	5,907	2	(4)	5,905
Certificates of deposit	4,626	—	—	4,626
Total held-to-maturity investments	$ 126,863	$ 60	$ (14)	$ 126,909

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The amortized cost, gross unrealized gains, gross unrealized losses, and estimated fair value of the held-to-maturity investments as of April 30, 2014, were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Municipal securities	$ 99,657	$ 65	$ (9)	$ 99,713
Certificates of deposit	4,630	—	—	4,630
Total held-to-maturity investments	$ 104,287	$ 65	$ (9)	$ 104,343

The amortized cost and fair value of the held-to-maturity securities by contractual maturity at January 31, 2015, were as follows (in thousands):

	Cost	Fair Value
Due within one year	$ 75,150	$ 75,177
Due after one year through three years	51,713	51,732
Total	$ 126,863	$ 126,909

Available-For-Sale Securities

Auction Rate Securities

As of January 31, 2015 and April 30, 2014, the entire balance of available-for-sale, auction rate securities, consisted of two and three investment grade auction rate municipal bonds, respectively, with maturities ranging from approximately 4 to 19 years. These investments have characteristics similar to short-term investments, because at pre-determined intervals, generally ranging from 30 to 35 days, there is a new auction process at which the interest rates for these securities are reset to current interest rates. At the end of such period, the Company chooses to roll-over its holdings or redeem the investments for cash. A market maker facilitates the redemption of the securities and the underlying issuers are not required to redeem the investment within 365 days. Interest earned from these investments is recorded in interest income.

During the fourth quarter of the fiscal year ended April 30, 2008, the Company began experiencing failed auctions on some of its auction rate securities. A failed auction occurs when a buyer for the securities cannot be obtained and the market maker does not buy the security for its own account. The Company continues to earn interest on the investments that failed to settle at auction, at the maximum contractual rate until the next auction occurs. In the event the Company needs to access funds invested in these auction rate securities, the Company may not be able to liquidate these securities at the fair value recorded on January 31, 2015, until a future auction of these securities is successful or a buyer is found outside of the auction process.

As a result of the failed auctions, the fair values of these securities are estimated utilizing a discounted cash flow analysis as of January 31, 2015. The analysis considers, among other items, the collateralization underlying the security investments, the creditworthiness of the counterparty, the timing of expected future cash flows, and the estimated date upon which the security is expected to have a successful auction. Based on the Company’s ability to access its cash and cash equivalents, expected operating cash flows, and other sources of cash, the Company does not anticipate the current lack of liquidity of these investments will affect its ability to operate the business in the ordinary course. The Company believes the current lack of liquidity of these investments is temporary and expects that the securities will be redeemed or refinanced at some point in the future. The Company will continue to monitor the value of its auction rate securities at each reporting period for a possible impairment if a further decline in fair value occurs. The auction rate securities have been in an unrealized loss position for more than 12 months. The Company has the ability and the intent to hold these investments until a recovery of fair value, which may be at maturity and as of January 31, 2015, the Company did not consider these investments to be other-than-temporarily impaired.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The amortized cost, gross unrealized gains, gross unrealized losses, and estimated fair value of the auction rate securities as of January 31, 2015, were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Auction rate securities	$ 3,200	$ —	$ (339)	$ 2,861
Total available-for-sale investments	$ 3,200	$ —	$ (339)	$ 2,861

The amortized cost, gross unrealized gains, gross unrealized losses, and estimated fair value of the available-for-sale investments as of April 30, 2014, were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Auction rate securities	$ 6,575	$ —	$ (892)	$ 5,683
Total available-for-sale investments	$ 6,575	$ —	$ (892)	$ 5,683

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The amortized cost and fair value of the auction rate securities by contractual maturity at January 31, 2015, were as follows (in thousands):

	Cost	Fair Value
Due after two through five years	$ 1,200	$ 1,152
Due after 10 years	2,000	1,709
Total	$ 3,200	$ 2,861

Equity Securities

As of January 31, 2015 and April 30, 2014, the entire balance of available-for-sale equity securities consisted of CybAero common shares. The shares are classified as available-for-sale. During the three and nine months ended January 31, 2015, the Company realized gains of $0.3 million and $4.5 million, respectively, on the sale of CybAero shares.

The amortized cost, gross unrealized gains, gross unrealized losses, and estimated fair value of the equity securities as of January 31, 2015, were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Equity securities	$ 4,556	$ —	$ (2,124)	$ 2,432
Total available-for-sale investments	$ 4,556	$ —	$ (2,124)	$ 2,432

The equity securities have been in an unrealized loss position for less than six months. The Company evaluated the near-term prospects of the issuer in relation to the severity and duration of the impairment. Based on that evaluation and the Company's ability and intent to hold these investments for a reasonable period of time sufficient for a recovery of fair value, the Company does not consider these investments to be other-than-temporarily impaired at January 31, 2015.

3. Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The fair value hierarchy contains three levels as follows:

- Level 1 — Inputs to the valuation based upon quoted prices (unadjusted) for identical assets or liabilities in active markets that are accessible as of the measurement date.
- Level 2 — Inputs to the valuation include quoted prices in either markets that are not active, or in active markets for similar assets or liabilities, inputs other than quoted prices that are observable, and inputs that are derived principally from or corroborated by observable market data.
- Level 3 — Inputs to the valuation that are unobservable inputs for the asset or liability.

The Company's financial assets measured at fair value on a recurring basis at January 31, 2015, were as follows (in thousands):

	Fair Value Measurement Using			
Description	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Auction rate securities	$ —	$ —	$ 2,861	$ 2,861
Equity securities	2,432	—	—	2,432
Total	$ 2,432	$ —	$ 2,861	$ 5,293

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The following table provides a reconciliation between the beginning and ending balances of items measured at fair value on a recurring basis in the table above that used significant unobservable inputs (Level 3) (in thousands):

Description	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)
Balance at May 1, 2014	$ 7,297
Transfers to Level 3	—
Total gains (realized or unrealized)	
Included in earnings	—
Included in other comprehensive loss	(1,061)
Purchases, issuances and settlements, net	(3,375)
Balance at January 31, 2015	$ 2,861
The amount of total gains or (losses) for the period included in earnings (or change in net assets) attributable to the change in unrealized gains or losses relating to assets still held at January 31, 2015	$ —

The auction rate securities are valued using a discounted cash flow model. The analysis considers, among other items, the collateralization underlying the security investments, the creditworthiness of the counterparty, the timing of expected future cash flows, and the estimated date upon which the security is expected to have a successful auction. As of January 31, 2015, the inputs used in the Company's discounted cash flow analysis included current coupon rates of 0.10% to 0.14%, estimated redemption periods of approximately 4 to 19 years and discount rates of 4.20% to 14.69%. The discount rates were based on market rates for municipal bond securities, as adjusted for a risk premium to reflect the lack of liquidity of these investments.

4. Inventories, net

Inventories consist of the following (in thousands):

	January 31, 2015	April 30, 2014
Raw materials	$ 15,817	$ 15,102
Work in process	5,796	7,542
Finished goods	30,865	31,289
Inventories, gross	52,478	53,933
Reserve for inventory obsolescence	(3,679)	(3,234)
Inventories, net	$ 48,799	$ 50,699

5. Warranty Reserves

The Company accrues an estimate of its exposure to warranty claims based upon both current and historical product sales data and warranty costs incurred. The warranty reserve is included in other current liabilities. The related expense is included in cost of sales. Warranty reserve activity is summarized as follows for the three and nine months ended January 31, 2015 and January 25, 2014 (in thousands):

	Three Months Ended		Nine Months Ended	
	January 31, 2015	January 25, 2014	January 31, 2015	January 25, 2014
Beginning balance	$ 1,959	$ 1,640	$ 1,280	$ 1,514
Warranty expense	579	534	1,988	1,352
Warranty claims settled	(402)	(317)	(1,132)	(1,009)
Ending balance	$ 2,136	$ 1,857	$ 2,136	$ 1,857

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

6. Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss are as follows (in thousands):

	Available-for-Sale Securities	Accumulated Other Comprehensive Loss
Balance as of April 30, 2014	$ (263)	$ (263)
Unrealized loss	(1,963)	(1,963)
Income taxes	785	785
Balance as of January 31, 2015	$ (1,441)	$ (1,441)

7. Customer-Funded Research & Development

Customer-funded R&D costs are incurred pursuant to contracts (revenue arrangements) to perform R&D activities according to customer specifications. These costs are direct contract costs and are expensed to cost of sales when the corresponding revenue is recognized, which is generally as the R&D services are performed. Revenue from customer-funded R&D was approximately $8.0 million and $17.9 million for the three and nine months ended January 31, 2015, respectively. Revenue from customer-funded R&D was approximately $5.0 million and $21.9 million for the three and nine months ended January 25, 2014, respectively.

8. Restructuring Charges

During the three and nine months ended January 25, 2014, the Company recorded restructuring charges consisting primarily of severance charges of $0 and $1.8 million, respectively. During the nine months ended January 25, 2014, $1.7 million in restructuring charges were recorded in cost of sales, of which $1.4 million was related to UAS and $0.3 million was related to the Efficient Energy Systems ("EES") business segment. During the nine months ended January 25, 2014, $0.1 million in restructuring charges were recorded in selling, general and administrative costs. The Company does not report SG&A costs by segment as the CODM only reviews the revenue and gross margin results for each of these segments when making resource allocation decisions.

The purpose of the organizational realignment and workforce reduction on May 29, 2013, within the Company's UAS and EES business segments, was to enhance the Company's focus on new product introductions and the adoption of new solutions designed to support the Company's long-term growth plans. The workforce reduction was necessitated by continuing delays in U.S. government procurements from the Company's UAS business segment and delays in the growth of plug-in electric vehicle adoption and associated recharging solution sales in the Company's EES business segment.

The purpose of the organizational realignment and workforce reduction on September 26, 2013, within the Company's UAS business segment, was to address shifts in the UAS segment's business mix and align the skills within the UAS business segment more closely with market requirements to support ongoing programs and emerging growth opportunities.

9. Income Taxes

For the three and nine months ended January 31, 2015, the Company recorded a provision (benefit) for income taxes of $2.8 million and $(0.9) million, respectively, yielding an effective tax rate of 54.3% and 18.0%, respectively. For the three and nine months ended January 25, 2014, the Company recorded a provision (benefit) for income taxes of $2.3 million and $(0.6) million, respectively, yielding an effective tax rate of 17.0% and (12.3)%, respectively. The variance from statutory tax rates for the three and nine months ended January 31, 2015, was primarily due to federal legislation reinstating the federal research and development tax credit. The variance from statutory tax rates for the three and nine months ended January 25, 2014, was primarily due to the federal research and development tax credit.

10. Segment Data

The Company's product segments are as follows:

- Unmanned Aircraft Systems — The UAS segment focuses primarily on the design, development, production, support and operation of innovative UAS and tactical missile systems that provide situational awareness, multi-band communications, force protection and other mission effects to increase the security and effectiveness of the operations of the Company's customers.

- Efficient Energy Systems — The EES segment focuses primarily on the design, development, production, marketing, support and operation of innovative efficient electric energy systems that address the growing demand for electric transportation solutions.

AeroVironment, Inc.
Notes to Consolidated Financial Statements (Unaudited)

The accounting policies of the segments are the same as those described in Note 1, "Organization and Significant Accounting Policies." The operating segments do not make sales to each other. Depreciation and amortization related to the manufacturing of goods is included in gross margin for the segments. The Company does not discretely allocate assets to its operating segments, nor does the CODM evaluate operating segments using discrete asset information. Consequently, the Company operates its financial systems as a single segment for accounting and control purposes, maintains a single indirect rate structure across all segments, has no inter-segment sales or corporate elimination transactions, and maintains limited financial statement information by segment. The segment results are as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	January 31, 2015	January 25, 2014	January 31, 2015	January 25, 2014
Revenue:				
UAS	$ 58,026	$ 57,491	$ 142,257	$ 148,781
EES	10,371	11,730	30,670	29,424
Total	68,397	69,221	172,927	178,205
Cost of sales:				
UAS	33,259	33,565	91,849	93,444
EES	8,145	8,604	22,160	21,286
Total	41,404	42,169	114,009	114,730
Gross margin:				
UAS	24,767	23,926	50,408	55,337
EES	2,226	3,126	8,510	8,138
Total	26,993	27,052	58,918	63,475
Selling, general and administrative	13,268	13,168	40,141	38,711
Research and development	8,577	5,241	24,232	19,292
Income (loss) from operations	5,148	8,643	(5,455)	5,472
Other income (expense):				
Interest income	224	197	629	597
Other (expense) income	(284)	4,675	(276)	(1,026)
Income (loss) before income taxes	$ 5,088	$ 13,515	$ (5,102)	$ 5,043

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

This section and other parts of this Quarterly Report on Form 10-Q contain forward-looking statements that involve risks and uncertainties. In some cases, forward-looking statements can be identified by words such as "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "will," "would" or similar expressions. Such forward-looking statements are based on current expectations, estimates and projections about our industry, our management's beliefs and assumptions made by our management. Forward-looking statements are not guarantees of future performance and our actual results may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in Part II, Item 1A, "Risk Factors."

Unless required by law, we expressly disclaim any obligation to update publicly any forward-looking statements, whether as result of new information, future events or otherwise.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. When we prepare these consolidated financial statements, we are required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Some of our accounting policies require that we make subjective judgments, including estimates that involve matters that are inherently uncertain. Our most critical estimates include those related to revenue recognition, inventories and reserves for excess and obsolescence, self-insured liabilities, accounting for stock-based awards, and income taxes. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for our judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Our actual results may differ from these estimates under different assumptions or conditions.

There have been no material changes made to the critical accounting estimates during the periods presented in the consolidated financial statements from those disclosed in the Form 10-K for the fiscal year ended April 30, 2014.

We review cost performance and estimates to complete at least quarterly and in many cases more frequently. Adjustments to original estimates for a contract's revenue, estimated costs at completion and estimated profit or loss are often required as work progresses under a contract, as experience is gained and as more information is obtained, even though the scope of work required under the contract may not change, or if contract modifications occur. The impact of revisions in profit estimates for all types of contracts are recognized on a cumulative catch-up basis in the period in which the revisions are made. During the three and nine months ended January 31, 2015 and January 25, 2014, changes in accounting estimates on fixed-price contracts recognized using the percentage of completion method of accounting are presented below.

For the three months ended January 31, 2015 and January 25, 2014, favorable and unfavorable cumulative catch-up adjustments included in cost of sales were as follows (in thousands):

	Three Months Ended	
	January 31, 2015	January 25, 2014
Gross favorable adjustments	$ 976	$ 121
Gross unfavorable adjustments	(257)	(1,409)
Net favorable (unfavorable) adjustments	$ 719	$ (1,288)

For the three months ended January 31, 2015, favorable cumulative catch-up adjustments of $1.0 million were primarily due to final cost adjustments on 29 contracts, which individually were not material. For the same period, unfavorable cumulative catch-up adjustments of $0.3 million were primarily related to higher than expected costs on 235 contracts, which individually were not material.

For the three months ended January 25, 2014, favorable cumulative catch-up adjustments of $0.1 million were primarily due to final cost adjustments on 16 contracts, which individually were not material. For the same period, unfavorable cumulative catch-up adjustments of $1.4 million were primarily related to higher than expected costs on 201 contracts, which individually were not material.

For the nine months ended January 31, 2015 and January 25, 2014, favorable and unfavorable cumulative catch-up adjustments included in cost of sales were as follows (in thousands):

	Nine Months Ended	
	January 31, 2015	January 25, 2014
Gross favorable adjustments	$ 992	$ 253
Gross unfavorable adjustments	(933)	(1,778)
Net favorable (unfavorable) adjustments	$ 59	$ (1,526)

For the nine months ended January 31, 2015, favorable cumulative catch-up adjustments of $1.0 million were primarily due to final cost adjustments on 27 contracts, which individually were not material. For the same period, unfavorable cumulative catch-up adjustments of $0.9 million were primarily related to higher than expected costs on 171 contracts, which individually were not material.

For the nine months ended January 25, 2014, favorable cumulative catch-up adjustments of $0.3 million were primarily due to final cost adjustments on 31 contracts, which individually were not material. For the same period, unfavorable cumulative catch-up adjustments of $1.8 million were primarily related to higher than expected costs on 157 contracts, which individually were not material.

Fiscal Periods

Due to our fixed year end date of April 30, our first and fourth quarters each consist of approximately 13 weeks. The second and third quarters each consist of exactly 13 weeks. Our first three quarters end on a Saturday. Our 2015 fiscal year ends on April 30, 2015 and our fiscal quarters end on August 2, 2014, November 1, 2014 and January 31, 2015.

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Results of Operations

Our operating segments are Unmanned Aircraft Systems, or UAS, and Efficient Energy Systems, or EES. The accounting policies for each of these segments are the same. In addition, a significant portion of our research and development, or R&D, selling, general and administrative, or SG&A, and general overhead resources are shared across our segments.

The following table sets forth our revenue and gross margin generated by each operating segment for the periods indicated (in thousands):

Three Months Ended January 31, 2015 Compared to Three Months Ended January 25, 2014

	Three Months Ended	
	January 31, 2015	January 25, 2014
Revenue:		
UAS	$ 58,026	$ 57,491
EES	10,371	11,730
Total	68,397	69,221
Cost of sales:		
UAS	33,259	33,565
EES	8,145	8,604
Total	41,404	42,169
Gross margin:		
UAS	24,767	23,926
EES	2,226	3,126
Total	26,993	27,052
Selling, general and administrative	13,268	13,168
Research and development	8,577	5,241
Income from operations	5,148	8,643
Other income (expense):		
Interest income	224	197
Other (expense) income	(284)	4,675
Income before income taxes	$ 5,088	$ 13,515

Revenue. Revenue for the three months ended January 31, 2015 was $68.4 million, as compared to $69.2 million for the three months ended January 25, 2014, representing a decrease of $0.8 million, or 1%. The decrease in revenue was due to a decrease in product deliveries of $0.7 million and a decrease in service revenue of $0.1 million. UAS revenue increased $0.5 million, or 1%, to $58.0 million for the three months ended January 31, 2015, primarily due to an increase in customer-funded R&D work of $2.9 million, offset by a decrease in service revenue of $2.0 million and a decrease in product deliveries of $0.4 million. The increase in customer-funded R&D was primarily due to an increase in small UAS-related customer funded R&D work. The decrease in service revenue was primarily due to reduced repair activities related to Switchblade. The decrease in product deliveries was primarily due to a decrease in deliveries of small UAS. EES revenue decreased $1.4 million, or 12%, to $10.4 million for the three months ended January 31, 2015, primarily due to a deacrease in product deliveries of our electric vehicle test systems and industrial fast charge systems, offset by an increase in deliveries of passenger electric vehicle charging systems.

Cost of Sales. Cost of sales for the three months ended January 31, 2015 was $41.4 million, as compared to $42.2 million for the three months ended January 25, 2014, representing a decrease of $0.8 million, or 2%. As a percentage of revenue, cost of sales remained at 61%. The decrease in cost of sales was primarily due to lower product cost of $0.3 million due to a decrease in product deliveries and lower cost of services of $0.5 million primarily due to a decrease in repair activities. UAS cost of sales decreased $0.3 million, or 1%, to $33.3 million for the three months ended January 31, 2015, primarily due to a decrease in sales volume. As a percentage of revenue, cost of sales for UAS decreased from 58% to 57%. EES cost of sales decreased $0.5 million, or 5%, to $8.1 million for the three months ended January 31, 2015. As a percentage of revenue, cost of sales for EES increased from 73% to 79%, primarily due to lower absorption of manufacturing and engineering overhead support costs.

Gross Margin. Gross margin for the three months ended January 31, 2015 was $27.0 million, as compared to $27.1 million for the three months ended January 25, 2014, representing a decrease of $0.1 million. The decrease in gross margin was due to lower product margins of $0.4 million, partially offset by higher services margins of $0.4 million. As a percentage of revenue, gross margin remained at 39%. UAS gross margin increased $0.8 million, or 4%, to $24.8 million for the three months ended January 31, 2015. As a percentage of revenue, gross margin for UAS increased from 42% to 43%, primarily due to higher services margin. EES gross margin decreased $0.9 million, or 29%, to $2.2 million for the three months ended January 31, 2015, primarily due to higher manufacturing and engineering overhead support costs, a decrease in sales and unfavorable product mix. As a percentage of revenue, EES gross margin decreased from 27% to 21%, primarily due to higher manufacturing and engineering overhead support costs, a decrease in sales and unfavorable product mix.

Selling, General and Administrative. SG&A expense for the three months ended January 31, 2015 was $13.3 million, or 19% of revenue, compared to SG&A expense of $13.2 million, or 19% of revenue, for the three months ended January 25, 2014.

Research and Development. R&D expense for the three months ended January 31, 2015 was $8.6 million, or 13% of revenue, compared to R&D expense of $5.2 million, or 8% of revenue, for the three months ended January 25, 2014. R&D expense increased by $3.3 million for the three months ended January 31, 2015, primarily due to increased development activities for certain strategic initiatives.

Interest Income. Interest income for the three months ended January 31, 2015 was $0.2 million, reflecting no change from the three months ended January 25, 2014.

Other Expense. Other expense for the three months ended January 31, 2015 was $0.3 million compared to other income of $4.7 million for the three months ended January 25, 2014. The three months ended January 25, 2014 included a $4.7 million increase in fair value of the embedded conversion feature of our convertible bond investment. During the three months ended January 31, 2015, we did not have any convertible bond investments.

Income Taxes. Our effective income tax expense rate was 54.3% for the three months ended January 31, 2015, as compared to an effective income tax expense rate of 17.0% for the three months ended January 25, 2014. The increase in the tax rate was primarily due to lower taxable income.

Nine Months Ended January 31, 2015 Compared to Nine Months Ended January 25, 2014

	Nine Months Ended	
	January 31, 2015	**January 25, 2014**
Revenue:		
UAS	$ 142,257	$ 148,781
EES	30,670	29,424
Total	172,927	178,205
Cost of sales:		
UAS	91,849	93,444
EES	22,160	21,286
Total	114,009	114,730
Gross margin:		
UAS	50,408	55,337
EES	8,510	8,138
Total	58,918	63,475
Selling, general and administrative	40,141	38,711
Research and development	24,232	19,292
(Loss) income from operations	(5,455)	5,472
Other income (expense):		
Interest income	629	597
Other expense	(276)	(1,026)
(Loss) income before income taxes	$ (5,102)	$ 5,043

Revenue. Revenue for the nine months ended January 31, 2015 was $172.9 million, as compared to $178.2 million for the nine months ended January 25, 2014, representing a decrease of $5.3 million, or 3%. The decrease in revenue was due to a decrease in service revenue of $11.5 million, offset by an increase in product deliveries of $6.2 million. UAS revenue decreased $6.5 million, or 4%, to $142.3 million for the nine months ended January 31, 2015, primarily due to a decrease in service revenue of $5.5 million and a decrease in customer-funded R&D work of $4.0 million, offset by an increase in product deliveries of $3.1 million. The decrease in service revenue was primarily due to reduced repair activities in small UAS. The decrease in customer-funded R&D was primarily due to a decrease in development programs as Switchblade and Wasp moved from development to production. The increase in product deliveries was primarily due to an increase in deliveries of small UAS. EES revenue increased $1.2 million, or 4%, to $30.7 million for the nine months ended January 31, 2015, primarily due to increased product deliveries of our industrial fast charge systems, partially offset by a decrease in product deliveries of our electric vehicle test systems and passenger electric vehicle charging systems.

Cost of Sales. Cost of sales for the nine months ended January 31, 2015 was $114.0 million, as compared to $114.7 million for the nine months ended January 25, 2014, representing a decrease of $0.7 million, or 1% . As a percentage of revenue, cost of sales increased from 64% to 66%. Services cost of sales was lower by $6.3 million primarily due to a decrease in customer-funded R&D work as Switchblade and Wasp transitioned into low-rate production and a reduction in repair activities, offset by higher product costs of $5.6 million due to an increase in product deliveries. UAS cost of sales decreased $1.6 million, or 2%, to $91.8 million for the nine months ended January 31, 2015. As a percentage of revenue, cost of sales for UAS increased from 63% to 65%. EES cost of sales increased $0.9 million, or 4%, to $22.2 million for the nine months ended January 31, 2015. As a percentage of revenue, cost of sales for EES remained at 72%.

Gross Margin. Gross margin for the nine months ended January 31, 2015 was $58.9 million, as compared to $63.5 million for the nine months ended January 25, 2014, representing a decrease of $4.6 million, or 7%. The decrease in gross margin was due to lower service margins of $5.2 million, offset by higher product margins of $0.7 million. As a percentage of revenue, gross margin decreased from 36% to 34%. UAS gross margin decreased $4.9 million, or 9%, to $50.4 million for the nine months ended January 31, 2015. The decrease was primarily due to a termination settlement for our Global Observer Joint Capability Technology Demonstration contract that occurred during the nine months ended January 25, 2014 that was not in the nine months ended January 31, 2015 and lower margins on service-related contracts. As a percentage of revenue, gross margin for UAS decreased from 37% to 35%. EES gross margin increased $0.4 million, or 5%, to $8.5 million for the nine months ended January 31, 2015, primarily due to an increase in sales volume. As a percentage of revenue, EES gross margin remained at 28%.

Selling, General and Administrative. SG&A expense for the nine months ended January 31, 2015 was $40.1 million, or 23% of revenue, compared to SG&A expense of $38.7 million, or 22% of revenue, for the nine months ended January 25, 2014. SG&A expense increased by $1.4 million for the nine months ended January 31, 2015, primarily due to higher proposal and business development activity.

Research and Development. R&D expense for the nine months ended January 31, 2015 was $24.2 million, or 14% of revenue, compared to R&D expense of $19.3 million, or 11% of revenue, for the nine months ended January 25, 2014. R&D expense increased by $4.9 million for the nine months ended January 31, 2015, primarily due to increased development activities for certain strategic initiatives.

Interest Income. Interest income for the nine months ended January 31, 2015 was $0.6 million, reflecting no change from the nine months ended January 25, 2014.

Other Expense. Other expense for the nine months ended January 31, 2015 was $0.3 million, as compared to other expense of $1.0 million for the nine months ended January 25, 2014. During the nine months ended January 25, 2014, other expense was primarily related to the conversion feature of two convertible bonds that decreased in value. During the nine months ended January 31, 2015, there was only one bond outstanding, which was converted into equity securities on August 11, 2014.

Income Taxes. Our effective income tax rate was 18.0% for the nine months ended January 31, 2015, as compared to an effective income tax rate of (12.3)% for the nine months ended January 25, 2014. The variance in the tax rate was primarily due to lower taxable income for the nine months ended January 31, 2015.

Backlog

We define funded backlog as unfilled firm orders for products and services for which funding currently is appropriated to us under the contract by the customer. As of January 31, 2015 and April 30, 2014, our funded backlog was approximately $89.3 million and $65.9 million, respectively.

In addition to our funded backlog, we also had unfunded backlog of $29.4 million and $22.9 million as of January 31, 2015 and April 30, 2014, respectively. We define unfunded backlog as the total remaining potential order amounts under cost reimbursable and fixed price contracts with multiple one-year options, and indefinite delivery, indefinite quantity, or IDIQ contracts. Unfunded backlog does not obligate the U.S. government to purchase goods or services. There can be no assurance that unfunded backlog will result in any orders in any particular period, if at all. Management believes that unfunded backlog does not provide a reliable measure of future estimated revenue under our contracts. Unfunded backlog does not include the remaining potential value associated with a U.S. Army IDIQ-type contract for small UAS because the contract was awarded to five companies in 2012, including AeroVironment, and we cannot be certain that we will receive task orders issued against the contract.

Because of possible future changes in delivery schedules and/or cancellations of orders, backlog at any particular date is not necessarily representative of actual sales to be expected for any succeeding period, and actual sales for the year may not meet or exceed the backlog represented. Our backlog is typically subject to large variations from quarter to quarter as existing contracts expire, or are renewed, or new contracts are awarded. A majority of our contracts, specifically our IDIQ contracts, do not currently obligate the U.S. government to purchase any goods or services. Additionally, all U.S. government contracts included in backlog, whether or not they are funded, may be terminated at the convenience of the U.S. government.

Liquidity and Capital Resources

We currently have no material cash commitments, except for normal recurring trade payables, accrued expenses and ongoing research and development costs, all of which we anticipate funding through our existing working capital and funds provided by operating activities. The majority of our purchase obligations are pursuant to funded contractual arrangements with our customers. In addition, we do not currently anticipate significant investment in property, plant and equipment, and we believe that our existing cash, cash equivalents, cash provided by operating activities and other financing sources will be sufficient to meet our anticipated working capital, capital expenditure and debt service requirements, if any, during the next twelve months. There can be no assurance, however, that our business will continue to generate cash flow at current levels. If we are unable to generate sufficient cash flow from operations, then we may be required to sell assets, reduce capital expenditures or obtain additional financing. We anticipate that existing sources of liquidity and cash flows from operations will be sufficient to satisfy our cash needs for the foreseeable future.

Our primary liquidity needs are for financing working capital, investing in capital expenditures, supporting product development efforts, introducing new products and enhancing existing products, and marketing acceptance and adoption of our products and services. Our future capital requirements, to a certain extent, are also subject to general conditions in or affecting the defense and electric vehicle industries and are subject to general economic, political, financial, competitive, legislative and regulatory factors that are beyond our control. Moreover, to the extent that existing cash, cash equivalents, cash from operations, and cash from short-term borrowing are insufficient to fund our future activities, we may need to raise additional funds through public or private equity or debt financing. Although we are currently not a party to any agreement or letter of intent with respect to potential investment in, or acquisitions of, businesses, services or technologies, we may enter into these types of arrangements in the future, which could also require us to seek additional equity or debt financing.

Our working capital requirements vary by contract type. On cost-plus-fee programs, we typically bill our incurred costs and fees monthly as work progresses, and therefore working capital investment is minimal. On fixed-price contracts, we typically are paid as we deliver products, and working capital is needed to fund labor and expenses incurred during the lead time from contract award until contract deliveries begin.

Cash Flows

The following table provides our cash flow data for the nine months ended January 31, 2015 and January 25, 2014 (in thousands):

	Nine Months Ended	
	January 31, 2015	January 25, 2014
	(Unaudited)	
Net cash provided by operating activities	$ 13,543	$ 3,472
Net cash (used in) provided by investing activities	$ (15,557)	$ 13,062
Net cash provided by financing activities	$ 1,022	$ 883

Cash Provided by Operating Activities. Net cash provided by operating activities for the nine months ended January 31, 2015, increased by $10.1 million to $13.5 million, compared to net cash provided by operating activities of $3.5 million for the nine months ended January 25, 2014. The increase in net cash provided by operating activities was primarily due to lower working capital needs of $22.1 million, partially offset by lower income of $9.8 million and a non-cash change in fair value of the embedded conversion feature of our convertible bond investment of $1.1 million.

Cash (Used in) Provided by Investing Activities. Net cash used in investing activities increased by $28.6 million to $15.6 million for the nine months ended January 31, 2015, compared to net cash provided by investing activities of $13.1 million for the nine months ended January 25, 2014. The increase in net cash used in investing activities was primarily due to an increase in net purchases of investments of $33.6 million, partially offset by lower acquisitions of property and equipment of $4.4 million.

Cash Provided by Financing Activities. Net cash provided by financing activities was $1.0 million for the nine months ended January 31, 2015, compared to net cash provided by financing activities of $0.9 million for the nine months ended January 25, 2014.

Off-Balance Sheet Arrangements

During the third quarter, there were no material changes in our off-balance sheet arrangements or contractual obligations and commercial commitments from those disclosed in the Form 10-K for the fiscal year ended April 30, 2014.

Inflation

Our operations have not been, and we do not expect them to be, materially affected by inflation. Historically, we have been successful in adjusting prices to our customers to reflect changes in our material and labor costs.

New Accounting Standards

Please refer to Note 1 “Organization and Significant Accounting Policies” to our unaudited consolidated financial statements in Part I, Item 1 of this quarterly report for a discussion of new accounting pronouncements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In the ordinary course of business, we are exposed to various market risk factors, including fluctuations in interest rates, changes in general economic conditions, domestic and foreign competition, and foreign currency exchange rates.

Interest Rate Risk

It is our policy not to enter into interest rate derivative financial instruments. We do not currently have any significant interest rate exposure.

Foreign Currency Exchange Rate Risk

Since a significant part of our sales and expenses are denominated in U.S. dollars, we have not experienced significant foreign exchange gains or losses to date, and do not expect to incur significant foreign exchange gains or losses in the future. We occasionally engage in forward contracts in foreign currencies to limit our exposure on non-U.S. dollar transactions.

ITEM 4. CONTROLS AND PROCEDURES

Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure.

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by Rule 13a-15(b) under the Exchange Act, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures.

Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective and were operating at a reasonable assurance level.

Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting or in other factors identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during the quarter ended January 31, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are, from time to time, party to a variety of legal proceedings arising in the ordinary course of business, including lawsuits, investigations and other governmental proceedings, audits and reviews. While the results of legal proceedings cannot be predicted with certainty, management believes that the final outcome of these proceedings will not have a material adverse effect on our financial condition taken as a whole.

ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors disclosed under Part I, Item 1A, "Risk Factors," in our Annual Report on Form 10-K for the fiscal year ended April 30, 2014. Please refer to that section for disclosures regarding the risks and uncertainties related to our business.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit Number	Description
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Label Linkbase Document.
101.PRE	XBRL Taxonomy Presentation Linkbase Document.

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.

Date: March 3, 2015		AEROVIRONMENT, INC.
	By:	/s/ Timothy E. Conver
		Timothy E. Conver Chairman, Chief Executive Officer and President (Principal Executive Officer)
		/s/ Teresa Covington
		Teresa Covington Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)

Exhibit 31.1

Certification of Principal Executive Officer
Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934

I, Timothy E. Conver, certify that:

1. I have reviewed this quarterly report on Form 10-Q of AeroVironment, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 3, 2015

/s/ Timothy E. Conver
Timothy E. Conver
Chairman, Chief Executive Officer and President

Exhibit 31.2

Certification of Principal Financial Officer
Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934

I, Teresa Covington, certify that:

1. I have reviewed this quarterly report on Form 10-Q of AeroVironment, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 3, 2015

/s/ Teresa Covington
Teresa Covington
Vice President and Chief Financial Officer

Exhibit 32

Certification

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) (the "Act"), each of the undersigned officers of AeroVironment, Inc., a Delaware corporation (the "Company"), does hereby certify, to each such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended January 31, 2015 (the "Periodic Report") of the Company fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)) and information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Timothy E. Conver
Timothy E. Conver
Chairman, Chief Executive Officer and President

/s/ Teresa Covington
Teresa Covington
Vice President and Chief Financial Officer

Dated: March 3, 2015

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.