

VEECO INSTRUMENTS INC
Form 10-Q
October 28, 2010
Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2010

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 0-16244

VEECO INSTRUMENTS INC.

(Exact Name of Registrant as Specified in Its Charter)

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Delaware
(State or Other Jurisdiction of

11-2989601
(I.R.S. Employer

Incorporation or Organization)

Identification Number)

Terminal Drive
Plainview, New York
(Address of Principal Executive Offices)

11803
(Zip Code)

Registrant's telephone number, including area code: **(516) 677-0200**

Website: **www.veeco.com**

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 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. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a 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

39,904,001 shares of common stock, \$0.01 par value per share, were outstanding as of the close of business on October 27, 2010.

Table of Contents

SAFE HARBOR STATEMENT

This Quarterly Report on Form 10-Q (the Report) contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Discussions containing such forward-looking statements may be found in Part I. Items 2 and 3 hereof, as well as within this Report generally. In addition, when used in this Report, the words believes, anticipates, expects, estimates, plans, intends and similar expressions are intended to identify forward-looking statements. All forward-looking statements are subject to a number of risks and uncertainties that could cause actual results to differ materially from projected results. These risks and uncertainties include, without limitation, the following:

- The reduction or elimination of government subsidies and economic incentives may adversely affect the future order rate for our MOCVD equipment;
- Our failure to successfully implement outsourcing activities or failure of our outsourcing partners to perform as anticipated could adversely affect our results of operations and our ability to realize the benefits of the recent increase in MOCVD order volume;
- Manufacturing interruptions or delays could affect our ability to meet customer demand, while the failure to estimate customer demand accurately could result in excess or obsolete inventory and/or liabilities to our suppliers for products no longer needed;
- We rely on a limited number of suppliers, some of which are sole-source suppliers;
- Our backlog is subject to customer cancellation or modification and such cancellation could result in decreased sales and increased provisions for excess and obsolete inventory and/or liabilities to our suppliers for products no longer needed;
- Our sales to HB LED and data storage manufacturers are highly dependent on these manufacturers sales for consumer electronics applications, which can experience significant volatility due to seasonal and other factors. This could materially adversely impact our future results of operations;
- Negative worldwide economic conditions could result in a decrease in our net sales and an increase in our operating costs, which could adversely affect our business and operating results;
- We are exposed to the risks of operating a global business, including the need to obtain export licenses for certain of our shipments;

- We are exposed to risks associated with our entrance into the emerging solar industry;
- The timing of our orders, shipments, and revenue recognition may cause our quarterly operating results to fluctuate significantly;
- We operate in industries characterized by rapid technological change;
- We face significant competition;
- We depend on a limited number of customers that operate in highly concentrated industries;
- The cyclical nature of the industries we serve directly affects our business;
- Our sales cycle is long and unpredictable;
- Our inability to attract, retain, and motivate key employees could have a material adverse effect on our business;
- The price of our common shares may be volatile and could decline significantly;

Table of Contents

- We are subject to foreign currency exchange risks;

- The enforcement and protection of our intellectual property rights may be expensive and could divert our valuable resources;

- We may be subject to claims of intellectual property infringement by others;

- Our acquisition strategy subjects us to risks associated with evaluating and pursuing these opportunities and integrating these businesses;

- We may be required to take additional impairment charges for goodwill and indefinite-lived intangible assets or definite-lived intangible and long-lived assets;

- Changes in accounting pronouncements or taxation rules or practices may adversely affect our financial results;

- We are subject to the internal control evaluations and attestation requirements of Section 404 of the Sarbanes-Oxley Act;

- We are subject to risks of non-compliance with environmental, health and safety regulations;

- We have adopted certain measures that may have anti-takeover effects which may make an acquisition of our Company by another company more difficult; and

- The matters set forth in this Report generally, including the risk factors set forth in Part 2. Item 1A. Risk Factors.

Consequently, such forward-looking statements should be regarded solely as the Company's current plans, estimates, and beliefs. The Company does not undertake any obligation to update any forward-looking statements to reflect future events or circumstances after the date of such statements.

Available Information

We file annual, quarterly and current reports, information statements and other information with the Securities and Exchange Commission (the SEC). The public may obtain information by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is <http://www.sec.gov>.

Internet Address

We maintain a website where additional information concerning our business and various upcoming events can be found. The address of our website is www.veeco.com. We provide a link on our website, under Investors Financial Information SEC Filings, through which investors can access our filings with the SEC, including our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and all amendments to such reports. These filings are posted to our Internet site, as soon as reasonably practicable after we electronically file such material with the SEC.

Table of Contents

VEECO INSTRUMENTS INC.

INDEX

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1.</u>	<u>Financial Statements:</u>
	<u>Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for the Three and Nine Months Ended September 30, 2010 and 2009 (Unaudited)</u>
	5
	<u>Condensed Consolidated Balance Sheets as of September 30, 2010 (Unaudited) and December 31, 2009</u>
	6
	<u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2010 and 2009 (Unaudited)</u>
	7
	<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>
	8
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>
	19
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>
	31
<u>Item 4.</u>	<u>Controls and Procedures</u>
	31
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1.</u>	<u>Legal Proceedings</u>
	33
<u>Item 1A.</u>	<u>Risk Factors</u>
	33
<u>Item 2.</u>	<u>Unregistered Sale of Equity Securities and Use of Proceeds</u>
	33
<u>Item 6.</u>	<u>Exhibits</u>
	34
<u>SIGNATURES</u>	35

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(In thousands, except per share data)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Net sales	\$ 277,094	\$ 74,688	\$ 633,233	\$ 163,270
Cost of sales	141,612	44,141	342,210	105,566
Gross profit	135,482	30,547	291,023	57,704
Operating expenses (income):				
Selling, general and administrative	24,565	15,631	62,852	41,926
Research and development	18,306	10,662	47,861	29,327
Amortization	1,237	1,270	3,711	3,775
Restructuring		781	(179)	4,770
Asset impairment				304
Other, net	(275)	(307)	75	368
Total operating expenses	43,833	28,037	114,320	80,470
Operating income (loss)	91,649	2,510	176,703	(22,766)
Interest expense, net	1,637	1,656	5,181	5,063
Income (loss) from continuing operations before income taxes	90,012	854	171,522	(27,829)
Income tax (benefit) provision	(1,092)	823	7,663	2,379
Income (loss) from continuing operations	91,104	31	163,859	(30,208)
Discontinued operations:				
(Loss) income from discontinued operations	(4,311)	978	3,546	(5,206)
Income tax provision (benefit)	630	(261)	2,805	(1,037)
(Loss) income from discontinued operations	(4,941)	1,239	741	(4,169)
Net income (loss)	86,163	1,270	164,600	(34,377)
Net loss attributable to noncontrolling interest				(65)
Net income (loss) attributable to Veeco	\$ 86,163	\$ 1,270	\$ 164,600	\$ (34,312)
Income (loss) per common share attributable to Veeco:				
Basic:				
Continuing operations	\$ 2.28	\$	\$ 4.15	\$ (0.96)
Discontinued operations	(0.12)	0.04	0.02	(0.13)
Income (loss)	\$ 2.16	\$ 0.04	\$ 4.17	\$ (1.09)
Diluted :				
Continuing operations	\$ 2.16	\$	\$ 3.89	\$ (0.96)
Discontinued operations	(0.12)	0.04	0.02	(0.13)
Income (loss)	\$ 2.04	\$ 0.04	\$ 3.91	\$ (1.09)

Weighted average shares outstanding:				
Basic	39,946	31,608	39,508	31,540
Diluted	42,258	32,375	42,175	31,540

Veeco Instruments Inc. and Subsidiaries

Condensed Consolidated Statements of Comprehensive Income (Loss)

(In thousands)

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Net income (loss)	\$ 86,163	\$ 1,270	\$ 164,600	\$ (34,377)
Other comprehensive income (loss), net of tax				
Foreign currency translation	985	966	160	20
Unrealized gain on available-for-sale securities	252		252	
Comprehensive income (loss)	87,400	2,236	165,012	(34,357)
Comprehensive loss attributable to noncontrolling interest				(65)
Comprehensive income (loss) attributable to Veeco	\$ 87,400	\$ 2,236	\$ 165,012	\$ (34,292)

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

Table of Contents

Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(In thousands)

	September 30, 2010 (Unaudited)	December 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	\$ 278,144	\$ 148,500
Short-term investments	157,111	135,000
Restricted cash	31,581	
Accounts receivable, net	129,574	67,546
Inventories	80,544	55,807
Prepaid expenses and other current assets	31,146	6,419
Assets of discontinued segment held for sale	80,252	40,058
Deferred income taxes	38,892	3,105
Total current assets	827,244	456,435
Property, plant and equipment at cost, net	45,490	44,707
Goodwill	52,003	52,003
Intangible assets, net	18,058	21,770
Other assets	901	429
Assets of discontinued segment held for sale		30,028
Total assets	\$ 943,696	\$ 605,372
Liabilities and equity		
Current liabilities:		
Accounts payable	\$ 44,793	\$ 24,910
Accrued expenses and other current liabilities	192,122	99,823
Deferred profit	5,853	2,520
Income taxes payable	44,034	829
Liabilities of discontinued segment held for sale	12,000	10,824
Current portion of long-term debt	225	212
Total current liabilities	299,027	139,118
Deferred income taxes	3,019	5,039
Long-term debt	103,063	100,964
Other liabilities	315	1,192
Equity	538,272	359,059
Total liabilities and equity	\$ 943,696	\$ 605,372

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

Table of Contents

Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine months ended September 30,	
	2010	2009
Operating activities		
Net income (loss)	\$ 164,600	\$ (34,377)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	9,952	10,766
Amortization of debt discount	2,269	2,114
Non-cash equity-based compensation	7,003	5,106
Non-cash asset impairment		304
Non-cash inventory write-off		1,526
Non-cash restructuring	(179)	4,770
Deferred income taxes	(37,850)	683
Non-cash cash flows from discontinued operations	7,050	7,995
Other, net	3	34
Changes in operating assets and liabilities:		
Accounts receivable	(61,499)	(5,324)
Inventories	(24,579)	13,406
Accounts payable	19,908	2,378
Accrued expenses, deferred profit and other current liabilities	138,947	12,079
Cash flows from discontinued operations	(11,703)	6,718
Other, net	(26,051)	(6,510)
Net cash provided by operating activities	187,871	21,668
Investing activities		
Capital expenditures	(8,023)	(4,584)
Payments for net assets of businesses acquired		(2,413)
Payments of earn-outs for businesses acquired		(9,839)
Transfers to restricted cash	(31,581)	(482)
Proceeds from the maturity of CDARS	213,641	
Proceeds from sales of short-term investments	11,013	
Payments for purchases of short-term investments	(246,514)	
Purchases of treasury stock	(31,602)	
Proceeds from the sale of property, plant and equipment	13	834
Cash flows from discontinued operations	1,682	(600)
Net cash used in investing activities	(91,371)	(17,084)
Financing activities		
Proceeds from stock option exercises	36,060	2,904
Restricted stock tax withholdings	(2,898)	(495)
Repayments of long-term debt	(157)	(146)
Net cash provided by financing activities	33,005	2,263
Effect of exchange rate changes on cash and cash equivalents	139	(8)
Net increase in cash and cash equivalents	129,644	6,839
Cash and cash equivalents at beginning of period	148,500	102,521
Cash and cash equivalents at end of period	\$ 278,144	\$ 109,360
Non-cash investing and financing activities		
Accrual of payment for net assets of businesses acquired	\$	\$ 1,000
Transfers from property, plant and equipment to inventory	1,114	1,159
Transfers from inventory to property, plant and equipment	850	23
Sale of property, plant and equipment with note receivable	140	

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

Table of Contents

Veeco Instruments Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Veeco Instruments Inc. (together with its consolidated subsidiaries, Veeco, the Company or we) have been prepared in accordance with accounting principles generally accepted in the United States (U.S.) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation (consisting of normal recurring accruals) have been included. Operating results for the three and nine months ended September 30, 2010, are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2009.

Consistent with prior years, we report interim quarters, other than fourth quarters which always end on December 31, on a 13-week basis ending on the last Sunday within such period. The interim quarter ends are determined at the beginning of each year based on the 13-week quarters. The 2010 interim quarter ends are March 28, June 27 and September 26. The 2009 interim quarter ends were March 29, June 28 and September 27. For ease of reference, we report these interim quarter ends as March 31, June 30 and September 30 in our interim condensed consolidated financial statements.

Income (Loss) Per Common Share attributable to Veeco

The following table sets forth the reconciliation of basic weighted average shares outstanding and diluted weighted average shares outstanding (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Basic weighted average shares outstanding	39,946	31,608	39,508	31,540
Dilutive effect of stock options and restricted stock	1,301	767	1,540	
Dilutive effect of convertible notes	1,011		1,127	
Diluted weighted average shares outstanding	42,258	32,375	42,175	31,540

Basic income (loss) per common share attributable to Veeco is computed using the weighted average number of common shares outstanding during the period. Diluted income (loss) per common share attributable to Veeco is computed using the weighted average number of common shares and common equivalent shares outstanding during the period. For the nine months ended September 30, 2009, the effect of approximately 0.2 million shares were excluded from the computation of diluted weighted average shares outstanding due to the net loss sustained in the period as their inclusion would have been anti-dilutive. For the three and nine months ended September 30, 2010, no shares were excluded from the computation of diluted weighted average shares outstanding.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Our convertible notes meet the criteria for determining the effect of the assumed conversion using the treasury stock method of accounting, as long as we have the ability and the intent to settle the principal amount of the notes in cash. Under the terms of these notes, we may pay the principal amount of converted notes in cash or in shares of common stock. We have indicated that we intend to pay the principal amount in cash. Using the treasury stock method, it was determined that the impact of the assumed conversion for the three and nine months ended September 30, 2010, had a dilutive affect of 1.0 million and 1.1 million common equivalent shares, respectively, for the three months ended September 30, 2009, the impact was anti-dilutive, due to the conversion price being out of the money for the period and for the nine months ended September 30, 2009, the impact was anti-dilutive, due to the net loss sustained in the period. The effect of the assumed converted shares is dependent on the stock price at the time of the conversion. The maximum number of common equivalent shares issuable upon conversion at September 30, 2010 was approximately 5.4 million.

On or after April 20, 2011, we may redeem the notes, in whole or in part, for cash at 100% of the principal amount of the notes to be redeemed plus accrued and unpaid interest to, but not including, the redemption date. Holders may convert the convertible notes at any time during the period beginning on January 15, 2012 through the

Table of Contents

close of business on the second day prior to April 15, 2012 and earlier upon the occurrence of certain events including if the notes have been called for redemption or if, for a given fiscal quarter our common stock trades at prices equal to 130% of the conversion price for at least 20 trading days during the final 30 trading days of the immediately preceding fiscal quarter. At the end of the third quarter of 2010, our common stock was not trading at prices equal to or above 130% of the conversion price for the specified period and, as a result, the convertible notes will not be convertible during the fourth quarter of 2010. If the convertible notes are converted, we have the ability and intent to pay the principal balance of notes tendered for conversion in cash. We will re-perform this test each quarter up to and including the fourth quarter of 2011. See Note 7 for further details on our debt.

Short-term Investments

We determine the appropriate balance sheet classification of our investments at the time of purchase and evaluate the classification at each balance sheet date. As part of our cash management program, we maintain a portfolio of marketable securities which are classified as available-for-sale. These securities include Federal Deposit Insurance Corporation (FDIC) insured corporate bonds, treasury bills, commercial paper and certificates of deposit placed through an account registry service (CDARS) with maturities of greater than three months when purchased in principal amounts that, when aggregated with interest to accrue over the term, will not exceed FDIC limits. Securities classified as available-for-sale are carried at fair market value, with the unrealized gains and losses, net of tax, included in the determination of comprehensive income (loss) and reported in equity. Net realized gains and losses are included in net income (loss). CDARS, commercial paper and treasury bills classified as cash equivalents are carried at cost, which approximates fair market value.

Derivative Financial Instruments

We use derivative financial instruments to minimize the impact of foreign exchange rate changes on earnings and cash flows. In the normal course of business, our operations are exposed to fluctuations in foreign exchange rates. In order to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known foreign currency exposures, we enter into monthly forward contracts. We do not use derivative financial instruments for trading or speculative purposes. Our forward contracts are not expected to subject us to material risks due to exchange rate movements because gains and losses on these contracts are intended to offset exchange gains and losses on the underlying assets and liabilities. The forward contracts are marked-to-market through earnings. We conduct our derivative transactions with highly rated financial institutions in an effort to mitigate any material credit risk.

The aggregate foreign currency exchange gain (loss) included in determining the condensed consolidated results of operations was approximately \$0.1 million and \$(0.1) million during the three months ended September 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange gain were losses related to forward contracts of \$(0.1) million during the three months ended September 30, 2010. The aggregate foreign currency exchange loss included in determining the condensed consolidated results of operations was approximately \$(0.3) million and \$(0.6) million during the nine months ended September 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange loss were gains related to forward contracts of \$0.1 million during the nine months ended September 30, 2009.

These amounts were recognized and are included in Other, net in the accompanying condensed consolidated statements of operations. As of September 30, 2010, approximately \$0.2 million of losses related to forward contracts were included in accrued expenses and other current liabilities and were subsequently paid in October 2010. As of December 31, 2009, approximately \$0.2 million of gains related to forward contracts were included in prepaid expenses and other current assets and were subsequently received in January 2010. Monthly forward contracts with a notional amount of \$1.7 million, entered into in September 2010 for October 2010, will be settled in October 2010.

The weighted average notional amount of derivative contracts outstanding during the three and nine months ended September 30, 2010 were approximately \$6.8 and \$5.9 million, respectively.

Note 2 Discontinued Operations

On August 15, 2010, we signed a definitive agreement to sell our metrology business to Bruker Corporation for approximately \$229 million, comprising our entire Metrology reporting segment. Accordingly, Metrology's operating results are accounted for as discontinued operations in determining the condensed consolidated results of operations for all periods presented. Additionally, Metrology's assets and liabilities are classified as held for sale on our condensed consolidated balance sheet for all periods presented. The sales transaction closed on October 7, 2010.

Table of Contents

Summary information related to discontinued operations is as follows (*in thousands*):

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Net sales	\$ 31,880	\$ 24,225	\$ 92,011	\$ 70,512
Gross profit	15,623	10,361	44,189	27,970
Total operating expenses	19,934	9,383	40,643	33,176
Operating (loss) income	(4,311)	978	3,546	(5,206)
Net (loss) income from discontinued operations, net of tax	(4,941)	1,239	741	(4,169)

	September 30, 2010	December 31, 2009
Assets		
Cash	\$ 48	\$ 89
Accounts receivable, net	27,669	16,812
Inventories	26,047	21,757
Property, plant and equipment at cost, net	13,412	14,682
Goodwill	7,419	7,419
Other assets	5,657	9,327
Assets of discontinued segment held for sale	\$ 80,252	\$ 70,086
Liabilities		
Accounts payable	\$ 7,287	\$ 4,202
Accrued expenses and other current liabilities	4,713	6,622
Liabilities of discontinued segment held for sale	\$ 12,000	\$ 10,824

Note 3 Equity-based Compensation Plans*Equity-based Compensation*

Equity-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over each employee's requisite service period. The following compensation expense was included in the condensed consolidated statements of operations for the three and nine months ended September 30, 2010 and 2009 (*in thousands*):

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Equity-based compensation expense	\$ 7,514	\$ 2,400	\$ 12,642	\$ 5,953

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

As a result of the sale of our Metrology segment to Bruker Corporation, equity-based compensation expense related to Metrology employees has been classified as discontinued operations in determining the condensed consolidated results of operations for the three and nine months ended September 30, 2010 and 2009. For the three and nine months ended September 30, 2010, \$4.9 million and \$5.6 million of equity-based compensation expense has been classified as discontinued operations. For the three and nine months ended September 30, 2009, \$0.3 million and \$0.9 million of equity-based compensation expense has been classified as discontinued operations. For the three and nine months ended September 30, 2010, total equity-based compensation expense included a charge of \$4.5 million related to the acceleration of equity awards associated with the sale of our Metrology business. We expect to recognize approximately \$2.0 million of additional equity-based compensation expense in the fourth quarter related to the acceleration of these awards.

As of September 30, 2010, the total unrecognized compensation costs related to nonvested stock and stock option awards was \$9.4 million and \$15.7 million, respectively. The related weighted average period over which we

Table of Contents

expect that such unrecognized compensation costs will be recognized is approximately 2.8 years for nonvested stock awards and 2.2 years for option awards.

Stock Option and Restricted Stock Activity

A summary of our restricted stock awards including restricted stock units for the nine months ended September 30, 2010, is presented below:

	Shares (000s)	Weighted Average Grant- Date Fair Value
Nonvested at January 1, 2010	892	\$ 12.97
Granted	179	34.78
Vested	(306)	12.89
Forfeited (including cancelled awards)	(15)	14.25
Nonvested at September 30, 2010	750	18.19

A summary of our stock option awards for the nine months ended September 30, 2010, is presented below:

	Shares (000s)	Weighted- Average Exercise Price	Aggregate Intrinsic Value (000s)	Weighted- Average Remaining Contractual Life (in years)
Outstanding at January 1, 2010	4,506	\$ 16.35		
Granted	631	34.21		
Exercised	(1,951)	18.95		
Forfeited (including cancelled options)	(42)	13.63		
Expirations of vested options	(22)	47.20		
Outstanding at September 30, 2010	3,122	18.15	\$ 57,068	5.7
Options exercisable at September 30, 2010	1,107	15.98	\$ 22,676	3.9

Treasury Stock

On August 24, 2010, our Board of Directors authorized the repurchase of up to \$200 million of our common stock until August 26, 2011. Repurchases are expected to be made from time to time on the open market in accordance with applicable federal securities laws. The timing of repurchases and the exact number of shares of common stock to be purchased will depend upon market conditions, SEC regulations, and other factors. The repurchases will be funded using the Company's available cash balances and cash generated from operations. The program does not obligate the Company to acquire any particular amount of common stock and may be modified or suspended at any time at the Company's discretion. During the three months ended September 30, 2010, we purchased 929,382 shares for \$31.6 million (including transaction costs) under the program at an average cost of \$34.00 per share. This stock repurchase is included as a reduction to Equity in the Condensed Consolidated Balance Sheet.

2010 Stock Incentive Plan

On April 1, 2010, the Board of Directors of the Company and on May 14, 2010, our shareholders approved the 2010 Stock Incentive Plan (the "2010 Plan"). The 2010 Plan replaced the 2000 Stock Incentive Plan as the Company's active stock plan. The Company's employees, directors and consultants are eligible to receive awards under the 2010 Plan. The 2010 Plan permits the granting of a variety of awards, including both non-qualified and incentive stock options, share appreciation rights, restricted shares, restricted share units and dividend equivalent rights. The Company is authorized to issue up to 3,500,000 shares under the 2010 Plan. Option awards are generally granted with an exercise price equal to the closing price of the Company's stock on the trading day prior to the date of grant; those option awards generally vest over a 3 year period and have a 10-year term. Restricted share awards generally vest over 4-5 years. Certain option and share awards provide for accelerated vesting if there is a change in control, as defined in the 2010 Plan.

Table of Contents**Note 4 Balance Sheet Information***Short-term Investments*

Available-for-sale securities consist of the following (*in thousands*):

	September 30, 2010			
	Amortized Cost	Gains in Accumulated Other Comprehensive Income	Losses in Accumulated Other Comprehensive Income	Estimated Fair Value
Commercial paper	\$ 35,915	\$ 32	\$	\$ 35,947
FDIC insured corporate bonds	85,802	160		85,962
Treasury bills	35,142	60		35,202
Total available-for-sale securities	\$ 156,859	\$ 252	\$	\$ 157,111

During the three and nine months ended September 30, 2010, available-for-sale securities were sold for total proceeds of \$11.0 million. The gross realized gains on these sales were minimal for the three and nine months ended September 30, 2010. For purpose of determining gross realized gains, the cost of securities sold is based on specific identification. Net unrealized holding gains on available-for-sale securities amounting to \$0.2 million for the three and nine months ended September 30, 2010, respectively, have been included in accumulated other comprehensive income. We held no available-for-sale securities during the nine months ended September 30, 2009.

Contractual maturities of available-for-sale debt securities at September 30, 2010, are as follows (*in thousands*):

	Estimated Fair Value
Due in one year or less	\$ 60,583
Due in 1 - 2 years	96,528
Total investments in debt securities	\$ 157,111

Actual maturities may differ from contractual maturities because some borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

Restricted Cash

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

At September 30, 2010, the Company has \$31.6 million of restricted cash which serves as collateral for bank guarantees which provide financial assurance that the Company will fulfill certain customer obligations. The cash is held in custody by the issuing bank, and is restricted as to withdrawal or use while the related bank guarantees are outstanding.

Accounts Receivable, net

Accounts receivable are shown net of the allowance for doubtful accounts of \$0.4 million as of September 30, 2010 and December 31, 2009.

Inventories

Inventories are stated at the lower of cost (principally first-in, first-out) or market. Inventories consist of (*in thousands*):

	September 30, 2010	December 31, 2009
Raw materials	\$ 44,461	\$ 34,214
Work in process	33,527	17,908
Finished goods	2,556	3,685
	\$ 80,544	\$ 55,807

Table of Contents*Accrued Warranty*

We estimate the costs that may be incurred under the warranty we provide and record a liability in the amount of such costs at the time the related revenue is recognized. Factors that affect our warranty liability include product failure rates, material usage and labor costs incurred in correcting product failures during the warranty period. We periodically assess the adequacy of our recognized warranty liability and adjust the amount as necessary. Changes in our warranty liability during the period are as follows (*in thousands*):

		Nine months ended September 30,		
		2010		2009
Balance as of beginning of period	\$	6,675	\$	5,533
Warranties issued during the period		7,242		2,414
Settlements made during the period		(4,906)		(2,394)
Balance at end of period	\$	9,011	\$	5,553

Note 5 Segment Information

We manage the business, review operating results and assess performance, as well as allocate resources, based upon two separate reporting segments that reflect the market focus of each business. The Light Emitting Diode (LED) & Solar segment consists of metal organic chemical vapor deposition (MOCVD) systems, molecular beam epitaxy (MBE) systems, Copper, Indium, Gallium, Selenide (CIGS) deposition systems and thermal deposition sources. These systems are primarily sold to customers in the high-brightness LED (HB LED) and solar industries, as well as to scientific research customers. This segment has manufacturing, product development and marketing sites in Somerset, New Jersey, St. Paul, Minnesota and Lowell, Massachusetts and has a product development site in Clifton Park, New York. The Data Storage segment consists of the ion beam etch, ion beam deposition, diamond-like carbon, physical vapor deposition and dicing and slicing products sold primarily to customers in the data storage industry. This segment has manufacturing, product development and marketing sites in Plainview, New York, Camarillo, California and Ft. Collins, Colorado.

We evaluate the performance of our reportable segments based on income (loss) from continuing operations before interest, income taxes, amortization and certain items (Segment profit (loss)), which is the primary indicator used to plan and forecast future periods. The presentation of this financial measure facilitates meaningful comparison with prior periods, as management believes Segment profit (loss) reports baseline performance and thus provides useful information. The other excluded items include restructuring (credits) expenses, asset impairment charges, inventory write-offs and equity-based compensation expense. The accounting policies of the reportable segments are the same as those described in the summary of critical accounting policies.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Table of Contents

The following tables present certain data pertaining to our reportable product segments and a reconciliation of Segment profit (loss) to Income (loss) from continuing operations before income taxes for the three and nine months ended September 30, 2010 and 2009, respectively, and goodwill and total assets as of September 30, 2010 and December 31, 2009 (*in thousands*):

	LED & Solar	Data Storage	Unallocated Corporate Amount	Total
Three months ended September 30, 2010				
Net sales	\$ 242,613	\$ 34,481	\$	\$ 277,094
Segment profit (loss)	\$ 91,785	\$ 9,377	\$ (5,662)	\$ 95,500
Interest, net			1,637	1,637
Amortization	796	383	58	1,237
Equity-based compensation	582	258	1,774	2,614
Income (loss) from continuing operations before income taxes	\$ 90,407	\$ 8,736	\$ (9,131)	\$ 90,012
Three months ended September 30, 2009				
Net sales	\$ 52,965	\$ 21,723	\$	\$ 74,688
Segment profit (loss)	\$ 8,456	\$ 857	\$ (2,642)	\$ 6,671
Interest, net			1,656	1,656
Amortization	792	405	73	1,270
Equity-based compensation	245	303	1,562	2,110
Restructuring	200	224	357	781
Income (loss) from continuing operations before income taxes	\$ 7,219	\$ (75)	\$ (6,290)	\$ 854
Nine months ended September 30, 2010				
Net sales	\$ 539,765	\$ 93,468	\$	\$ 633,233
Segment profit (loss)	\$ 177,538	\$ 21,859	\$ (12,159)	\$ 187,238
Interest, net			5,181	5,181
Amortization	2,388	1,149	174	3,711
Equity-based compensation	1,720	781	4,502	7,003
Restructuring		(179)		(179)
Income (loss) from continuing operations before income taxes	\$ 173,430	\$ 20,108	\$ (22,016)	\$ 171,522
Nine months ended September 30, 2009				
Net sales	\$ 107,050	\$ 56,220	\$	\$ 163,270
Segment loss	\$ 1,948	\$ (3,092)	\$ (6,141)	\$ (7,285)
Interest, net			5,063	5,063
Amortization	2,341	1,213	221	3,775
Equity-based compensation	619	892	3,595	5,106
Restructuring	1,129	3,054	587	4,770
Inventory write-offs		1,526		1,526
Asset impairment charge		304		304
Loss from continuing operations before income taxes	\$ (2,141)	\$ (10,081)	\$ (15,607)	\$ (27,829)
As of September 30, 2010				
Goodwill	\$ 52,003	\$	\$	\$ 52,003

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Total assets	\$	291,902	\$	50,217	\$	601,577	\$	943,696
As of December 31, 2009								
Goodwill	\$	52,003	\$		\$		\$	52,003
Total assets	\$	178,406	\$	54,106	\$	372,860	\$	605,372

Corporate total assets are comprised principally of cash and cash equivalents, short-term investments and assets of discontinued segment held for sale at September 30, 2010 and December 31, 2009, respectively.

Note 6 Income Taxes

In assessing the realizability of deferred tax assets, the Company considers whether it is more-likely-than-not that some portion or all of the deferred tax assets will be realized. Significant judgment is required in making this assessment. The ultimate realization of the net deferred tax assets, consisting of net operating losses, tax credit carryforwards and temporary differences is dependent upon the generation of future taxable income prior to the expiration of any net operating loss carryforwards.

Table of Contents

The Company evaluates the need for a valuation allowance against its deferred tax assets each quarter. For the year ending December 31, 2010, the Company has determined that a significant portion of its deferred tax assets are realizable on a more-likely-than-not basis based on the forecasted results of operations. This tax benefit has been included in calculating the estimated effective tax rate for the year ending December 31, 2010.

Note 7 Debt*Convertible Notes*

Our convertible notes are initially convertible into 36.7277 shares of common stock per \$1,000 principal amount of notes (equivalent to a conversion price of \$27.23 per share or a premium of 38% over the closing market price for Veeco's common stock on April 16, 2007). On or after April 20, 2011, we may redeem the notes, in whole or in part, for cash at 100% of the principal amount of the notes to be redeemed plus accrued and unpaid interest to, but not including, the redemption date. Holders may convert the convertible notes at any time during the period beginning on January 15, 2012 through the close of business on the second day prior to April 15, 2012 and earlier upon the occurrence of certain events including if the notes are called for redemption or if, for a given fiscal quarter, our common stock trades at prices equal to 130% of the conversion price for at least 20 trading days during the final 30 trading days of the immediately preceding fiscal quarter. At the end of the third quarter of 2010, our common stock was not trading at prices equal to or above 130% of the conversion price for the specified period and, as a result, the convertible notes will not be convertible during the fourth quarter of 2010. If the convertible notes are converted, we have the ability and intent to pay the principal balance of notes tendered for conversion in cash. We will re-perform this test each quarter up to and including the fourth quarter of 2011. The notes are unsecured and are effectively subordinated to all of our senior and secured indebtedness and to all indebtedness and other liabilities of our subsidiaries.

In May 2008, accounting guidance was issued that requires a portion of convertible debt to be allocated to equity. We implemented this guidance as of January 1, 2009. This guidance requires issuers of convertible debt that can be settled in cash to separately account for (*i.e.*, bifurcate) a portion of the debt associated with the conversion feature and reclassify this portion to equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value over the life of the debt using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as interest expense. Our convertible notes are subject to this accounting guidance since they may be settled in cash upon conversion. Thus, as a result of the adoption of this accounting guidance, we reclassified approximately \$16.3 million from long-term debt to additional paid-in capital effective as of the date of issuance of the notes. This reclassification created a \$16.3 million discount on the debt that is amortized over the remaining life of the notes, which will be through April 15, 2012. This additional interest expense does not require the use of cash.

The components of interest expense recorded on the notes were as follows (*in thousands*):

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Contractual interest	\$ 1,089	\$ 1,089	\$ 3,267	\$ 3,267
Amortization of the discount on the notes	769	714	2,270	2,114
Total interest expense on the notes	\$ 1,858	\$ 1,803	\$ 5,537	\$ 5,381
Effective interest rate	7.0%	6.8%	7.0%	6.8%

The carrying amounts of the liability and equity components of the notes were as follows (*in thousands*):

	September 30, 2010	December 31, 2009
Carrying amount of the equity component	\$ 16,318	\$ 16,318
Principal balance of the liability component	\$ 105,574	\$ 105,574
Less: unamortized discount	5,224	7,493
Net carrying value of the liability component	\$ 100,350	\$ 98,081

Table of Contents

At September 30, 2010, \$105.6 million of the convertible notes outstanding had a fair value of approximately \$145.1 million.

Mortgage Payable

We also have a mortgage payable, with approximately \$3.0 million outstanding at September 30, 2010. The mortgage accrues interest at an annual rate of 7.91%, and the final payment is due on January 1, 2020. The fair value of the mortgage at September 30, 2010 was approximately \$3.2 million.

Note 8 Fair Value Measurements

We have categorized our assets and liabilities recorded at fair value based upon the fair value hierarchy. The levels of fair value hierarchy are as follows:

- Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access.
- Level 2 inputs utilize other-than-quoted prices that are observable, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs such as interest rates and yield curves that are observable at commonly quoted intervals.
- Level 3 inputs are unobservable and are typically based on our own assumptions, including situations where there is little, if any, market activity.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, we categorize such assets or liabilities based on the lowest level input that is significant to the fair value measurement in its entirety. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset.

Both observable and unobservable inputs may be used to determine the fair value of positions that are classified within the Level 3 category. As a result, the unrealized gains and losses for assets within the Level 3 category presented below may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable (e.g., changes in historical company data) inputs.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

The major categories of assets and liabilities measured on a recurring basis, at fair value, as of September 30, 2010 and December 31, 2009, are as follows (*in millions*):

	September 30, 2010			
	Level 1	Level 2	Level 3	Total
Treasury bills	\$ 35.2	\$ 90.0	\$	\$ 125.2
FDIC insured corporate bonds	86.0			86.0
Commercial paper	35.9	107.0		142.9
Derivative instrument		0.2		0.2
Total	\$ 157.1	\$ 197.2	\$	\$ 354.3

	December 31, 2009			
	Level 1	Level 2	Level 3	Total
CDAR s	\$	\$ 180.0	\$	\$ 180.0
Derivative instrument		0.2		0.2
Total	\$	\$ 180.2	\$	\$ 180.2

CDARS, commercial paper and treasury bills that are classified as cash equivalents are carried at cost, which approximates market value. Accordingly, no gains or losses (realized/unrealized) have been incurred for cash equivalents. All investments classified as available-for-sale contain quoted prices in active markets.

Derivative instruments include foreign currency forward contracts to hedge certain foreign currency transactions. Derivative instruments are valued using standard calculations/models that are primarily based on observable inputs, including foreign currency exchange rates, volatilities and interest rates.

Table of Contents

The major categories of assets and liabilities measured on a nonrecurring basis, at fair value, as of September 30, 2010 and December 31, 2009, are as follows (*in millions*):

	September 30, 2010			Total
	Level 1	Level 2	Level 3	
Property, plant and equipment, net	\$	\$	\$ 45.5	\$ 45.5
Goodwill			52.0	52.0
Intangible assets, net			18.1	18.1
Asset retirement obligation			(0.2)	(0.2)
Restructuring liability			(1.0)	(1.0)
Total	\$	\$	\$ 114.4	\$ 114.4

	December 31, 2009			Total
	Level 1	Level 2	Level 3	
Property, plant and equipment, net	\$	\$	\$ 44.7	\$ 44.7
Goodwill			52.0	52.0
Intangible assets, net			21.8	21.8
Asset retirement obligation			(0.2)	(0.2)
Restructuring liability			(2.4)	(2.4)
Total	\$	\$	\$ 115.9	\$ 115.9

Note 9 Commitments, Contingencies and Other Matters*Restructuring and Other Charges (Credits)*

During 2009, we continued our multi-quarter plan to improve profitability and reduce and contain spending, which began in 2007. We made progress against the initiatives that management set in 2007, continued our restructuring plan and executed activities with a focus on creating a more cost effective organization, with a greater percentage of variable costs. These activities included downsizing and consolidating some locations, reducing our workforce, consultants and discretionary expenses and realigning our sales organization and engineering groups.

In conjunction with these activities, we recorded a restructuring credit of approximately \$0.2 million during nine months ended September 30, 2010. We recorded restructuring charges of approximately \$0.8 million and \$4.8 million during the three and nine months ended September 30, 2009, respectively, an asset impairment charge of \$0.3 million and inventory write-offs of \$1.5 million, included in cost of sales in the accompanying Condensed Consolidated Statement of Operations, associated with the discontinuance of certain products in connection with the transition to outsourced manufacturing during the nine months ended September 30, 2009. Restructuring for the three and nine months ended September 30, 2010 and 2009 is as follows (*in thousands*):

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Personnel severance and related costs	\$	\$ 781	\$	\$ 3,455
Lease-related costs (credits)			(179)	893

Moving costs and consolidation activities						422
	\$	\$	781	\$	(179)	\$ 4,770

Personnel Severance and Related Costs

During the three and nine months ended September 30, 2009, we recorded \$0.8 million and \$3.5 million, respectively, in personnel severance and related costs resulting from a headcount reduction of approximately 27 employees during the three month period and 160 employees during the nine month period. This reduction in workforce included executives, management, administration, sales and service personnel and manufacturing employees companywide.

Table of Contents*Lease-related Costs (credits)*

During the first quarter of 2010, we had a change in estimate relating to one of our leased Data Storage facilities. As a result, we incurred a restructuring credit of \$0.2 million, consisting primarily of the remaining lease payment obligations and estimated property taxes for a portion of the facility we will occupy, offset by a reduction in expected sublease income. We made certain assumptions in determining the credit, which included a reduction in estimated sublease income and terms of the sublease as well as the estimated discount rate to be used in determining the fair value of the remaining liability. We developed these assumptions based on our understanding of the current real estate market as well as current market interest rates. The assumptions are based on management's best estimates, and will be adjusted periodically if new information is obtained.

During the second quarter of 2009, we vacated one of our Data Storage facilities. As a result, we incurred a restructuring charge, representing the remaining lease payment obligations and estimated property taxes for the facility we vacated, offset by the estimated expected sublease income to be received. We made certain assumptions in determining the charge, which included estimated sublease income and terms of the sublease as well as the estimated discount rate to be used in determining the fair value of the liability. We developed these assumptions based on our understanding of the current real estate market as well as current market interest rates. The assumptions are based on management's best estimates, and will be adjusted periodically if better information is obtained. We also incurred charges associated with moving and consolidation activities for both of these locations.

Restructuring Liability

The following is a reconciliation of the liability associated with the 2009 and 2008 restructuring charges from inception through September 30, 2010 (in thousands):

	LED & Solar	Data Storage	Unallocated Corporate	Total
<u>Short-term liability</u>				
Balance as of January 1, 2010	\$ 353	\$ 486	\$ 1,597	\$ 2,436
Reversal of lease-related costs		(108)		(108)
Short-term/long-term reclassification		97	536	633
Cash payments	(353)	(299)	(1,312)	(1,964)
Balance as of September 30, 2010	\$	\$ 176	\$ 821	\$ 997
<u>Long-term liability</u>				
Balance as of January 1, 2010	\$	\$ 229	\$ 536	\$ 765
Reversal of lease-related costs		(71)		(71)
Short-term/long-term reclassification		(97)	(536)	(633)
Balance as of September 30, 2010	\$	\$ 61	\$	\$ 61

The balance of the short-term and long-term liability will be paid over the remaining life of the leases for the former corporate headquarters and a former Data Storage facility, which expire in June 2011 and May 2012, respectively. We have not incurred and currently do not anticipate or expect to incur additional restructuring charges during 2010.

Table of Contents

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

Executive Summary

We make equipment to develop and manufacture light-emitting diodes (LEDs), solar panels, hard-disk drives and other devices. We have leading technology positions in our two segments: LED & Solar and Data Storage.

In our LED & Solar segment, we design and manufacture metal organic chemical vapor deposition (MOCVD) systems, molecular beam epitaxy (MBE) systems, Copper, Indium, Gallium, Selenide (CIGS) deposition systems and thermal deposition sources which we sell to manufacturers of high brightness LEDs (HB LEDs) and solar panels, as well as to scientific research customers.

In our Data Storage segment, we design and manufacture ion beam etch, ion beam deposition, diamond-like carbon, physical vapor deposition, chemical vapor deposition, and dicing and slicing systems primarily used to create thin film magnetic heads (TFMHs) that read and write data on hard disk drives.

We support our customers through product development, manufacturing, sales and service sites in the U.S., Korea, Taiwan, China, Singapore, Japan, Europe and other locations.

Highlights of the Third Quarter of 2010

- Revenue was \$277.1 million, a 271% increase from the third quarter of 2009.
- Orders were \$278.2 million, a 42% increase from the third quarter of 2009.
- Net income from continuing operations was \$91.1 million, or \$2.16 per share, compared to no net income, or \$0.00 per share, in the third quarter of 2009.
- Gross margins were 48.9%, compared to 40.9% in the third quarter of 2009.

Fourth Quarter 2010 Outlook

We have recently experienced rescheduling of MOCVD tool shipments from the fourth quarter into the first quarter by several customers in Korea and Taiwan. Due to the recent strong order rate from China, our current plan for fourth quarter revenue includes a significant amount of

large multi-tool MOCVD shipments to key Chinese customers, many of whom are currently building or expanding their facilities. While we currently expect that these tools will ship over the next few months, timing of revenue could shift into the first quarter due to customer facility readiness. Veeco's fourth quarter 2010 revenue is currently forecasted to be between \$285 and \$320 million.

At the beginning of the fourth quarter, Veeco continues to experience high levels of quoting activity, and we currently expect that fourth quarter bookings will be equal to or better than the third quarter. Strong quoting activity continues for MOCVD tools particularly in China and Taiwan, and overall market conditions in Data Storage also remain healthy.

2011 Outlook

Veeco's backlog of \$569 million at the end of September, plus further strength in MOCVD bookings currently forecasted for the fourth quarter, should position Veeco for solid revenue performance in the first half of 2011. The Company has built its MOCVD manufacturing capacity to 120 or more tools per quarter, and will head into 2011 with the ability to flex quarterly shipments up or down as required by customer demand.

While it is difficult to predict future business trends in LED, we believe there may be an opportunity to sell thousands of MOCVD systems as LEDs fully penetrate display applications and see accelerated adoption in solid state lighting over the next few years. In order to capitalize upon this potential opportunity, Veeco is expanding training, service and support functions in China, Taiwan and Korea, and accelerating our new product roadmap.

In our other businesses, quoting activity is picking up for our CIGS solar depositions systems as we make progress advancing these tools' process capabilities for high-efficiency/low cost solar cells. Our Data Storage business continues to perform exceptionally well this year, with new products that are meeting customer technology challenges and a flexible outsourced manufacturing model.

Table of Contents

Our outlook discussion above constitutes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Our expectations regarding future results are subject to risks and uncertainties. Our actual results may differ materially from those anticipated. Risks associated with our ability to achieve these results are set forth in Items 1, 1A, 3, 7 and 7A in our annual report on Form 10-K for the year ended December 31, 2009, as well as any modifications or revisions to risk factors contained in our subsequent filings with the SEC.

You should not place undue reliance on any forward-looking statements, which speak only as of the dates they are made.

Table of Contents**Results of Operations:****Three Months Ended September 30, 2010 and 2009**

Consistent with prior years, we report interim quarters, other than fourth quarters which always end on December 31, on a 13-week basis ending on the last Sunday within such period. The interim quarter ends are determined at the beginning of each year based on the 13-week quarters. The 2010 interim quarter ends are March 28, June 27 and September 26. The 2009 interim quarter ends were March 29, June 28 and September 27. For ease of reference, we report these interim quarter ends as March 31, June 30 and September 30 in our interim condensed consolidated financial statements.

The following table shows our Condensed Consolidated Statements of Operations, percentages of sales, and comparisons between the three months ended September 30, 2010 and 2009 (*dollars in thousands*):

	2010		Three months ended September 30, 2009		Dollar and Percentage Change Year to Year				
Net sales	\$	277,094	100.0%	\$	74,688	100.0%	\$	202,406	271.0%
Cost of sales		141,612	51.1		44,141	59.1		97,471	220.8
Gross profit		135,482	48.9		30,547	40.9		104,935	343.5
Operating expenses (income):									
Selling, general and administrative		24,565	8.9		15,631	20.9		8,934	57.2
Research and development		18,306	6.6		10,662	14.3		7,644	71.7
Amortization		1,237	0.4		1,270	1.7		(33)	(2.6)
Restructuring					781	1.0		(781)	(100.0)
Other, net		(275)	(0.1)		(307)	(0.4)		32	(10.4)
Total operating expenses		43,833	15.8		28,037	37.5		15,796	56.3
Operating income		91,649	33.1		2,510	3.4		89,139	*
Interest expense, net		1,637	0.6		1,656	2.2		(19)	(1.1)
Income from continuing operations before income taxes		90,012	32.5		854	1.1		89,158	*
Income tax (benefit) provision		(1,092)	(0.4)		823	1.1		(1,915)	*
Income from continuing operations		91,104	32.9		31	0.0		91,073	32.9
Discontinued operations:									
(Loss) income from discontinued operations		(4,311)	(1.6)		978	0.4		(5,289)	(1.9)
Income tax provision (benefit)		630	0.2		(261)	(0.1)		891	0.3
(Loss) income from discontinued operations		(4,941)	(1.8)		1,239	1.7		89,158	32.2
Net income	\$	86,163	31.1%	\$	1,270	1.7%	\$	85,784	42.4%

* Not Meaningful

Net Sales and Orders

Net sales of \$277.1 million for the three months ended September 30, 2010 were up 271.0% compared to the comparable 2009 quarter. The following is an analysis of net sales and orders by segment and by region (*dollars in thousands*):

	Sales				Orders				Book to Bill	
	Three months ended		Dollar and Percentage		Three months ended		Dollar and Percentage			
	September 30, 2010	September 30, 2009	Change Year to Year		September 30, 2010	September 30, 2009	Change Year to Year		Ratio 2010	Ratio 2009
Segment Analysis										
LED & Solar	\$ 242,613	\$ 52,965	\$ 189,648	358.1%	\$ 243,218	\$ 179,229	\$ 63,989	35.7%	1.00	3.38
Data Storage	34,481	21,723	12,758	58.7	34,972	17,242	17,730	102.8	1.01	0.79
Total	\$ 277,094	\$ 74,688	\$ 202,406	271.0%	\$ 278,190	\$ 196,471	\$ 81,719	41.6%	1.00	2.63
Regional Analysis										
Americas	\$ 20,915	\$ 11,448	\$ 9,467	82.7%	\$ 23,440	\$ 30,136	\$ (6,696)	-22.2%	1.12	2.63
Europe, Middle East and Africa (EMEA)	33,236	11,293	21,943	194.3	9,672	11,373	(1,701)	(15.0)	0.29	1.01
Asia Pacific	222,943	51,947	170,996	329.2	245,078	154,962	90,116	58.2	1.10	2.98
Total	\$ 277,094	\$ 74,688	\$ 202,406	271.0%	\$ 278,190	\$ 196,471	\$ 81,719	41.6%	1.00	2.63

Sales and orders increased in each segment in the third quarter of 2010 compared with the comparable 2009 quarter due to our customers requirements in response to increasingly favorable economic conditions compared to 2009. LED & Solar sales were up 358.1% from the comparable 2009 quarter primarily due to an increase in end user demand for HB LED backlighting applications and continued strong customer acceptance of Veeco's newest generation systems. Data Storage segment sales were up 58.7% from the comparable 2009 quarter due to an increase

Table of Contents

in demand by our data storage customers as the global economy improved from 2009. By region, net sales increased by 329.2% in the Asia Pacific region, primarily due to MOCVD sales to HB LED customers, while sales in the Americas and EMEA also increased 82.7% and 194.3%, respectively. We believe that there will continue to be period-to-period variations in the geographic distribution of sales.

Orders for the third quarter of 2010 increased 41.6% from the comparable 2009 quarter. By segment, the 35.7% increase in orders for LED & Solar was principally driven by HB LED based manufacturers increasing production of LEDs. The 102.8% increase in Data Storage orders resulted from an increase in demand by our data storage customers due to both capacity expansion and technology buys.

Our book-to-bill ratio for the third quarter of 2010, which is calculated by dividing orders received in a given time period by revenue recognized in the same time period, was 1 to 1. Our backlog as of September 30, 2010 was \$569.0 million, compared to \$377.0 million as of December 31, 2009. During the three months ended September 30, 2010, we experienced backlog adjustments of approximately \$0.4 million, principally due to adjustments related to foreign currency translation. For certain sales arrangements we require a deposit for a portion of the sales price before shipment. As of September 30, 2010, we had customer deposits and advanced billings of \$131.5 million.

Gross Profit

Gross profit, as a percentage of net sales, for the third quarter of 2010, was 48.9%, compared to 40.9% in the comparable 2009 quarter. LED & Solar gross margins increased to 48.7% from 41.7% primarily resulting from favorable product mix, cost reductions and increased sales volume. Data Storage gross margins increased to 51.0% from 39.9%, driven primarily by favorable product mix, cost reductions and increased sales volume.

Operating Expenses

Selling, general and administrative expenses increased by \$8.9 million, or 57.2%, from the comparable 2009 quarter, however, decreased from 20.9% of net sales to 8.9% of sales. The dollar increase was primarily due to an increase in bonus and profit sharing expense, equity-based compensation, travel and entertainment expenses, salary and related expenses and professional fees associated primarily with the significant increase in business activity in our LED & Solar segment.

Research and development expenses increased \$7.6 million from the comparable 2009 quarter, however, decreased from 14.3% of net sales to 6.6%. The dollar increase was primarily due to increased spending in our LED & Solar segment to support future growth.

Restructuring expense of \$0.8 million for the third quarter of 2009 consisted primarily of personnel severance costs resulting from a reduction in workforce. There were no such charges in 2010.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Other, net for the third quarter of 2010 includes a foreign currency exchange loss of \$0.1 million compared to none in the comparable 2009 quarter.

Income Taxes

Our provision for income taxes consists of U.S. federal, state and local and foreign taxes in amounts necessary to align our quarter-to-date tax provision with the effective tax rate we expect to achieve for the full year.

For the three months ended September 30, 2010, the Company had an effective tax rate of (1.2%) and recorded a benefit for income taxes of \$1.1 million. The benefit for income taxes includes a tax provision of \$2.4 million relating to U.S federal, state and local and foreign taxes offset by a discrete tax benefit of \$3.5 million primarily related to state research and development tax credits as the Company had a favorable resolution of an income tax audit.

The effective tax rate is lower than the statutory rate primarily due to the Company's ability to realize a significant portion of its deferred tax assets, primarily related to net operating loss carryforwards and federal tax credits, on a more-likely-than-not basis based on the forecasted results of operations for the year ending December 31, 2010.

For the three months ended September 30, 2009, the Company recorded a provision for income taxes of \$0.6 million related to U.S federal, state and local and foreign taxes.

Table of Contents**Results of Operations:****Nine Months Ended September 30, 2010 and 2009**

The following table shows our Condensed Consolidated Statements of Operations, percentages of sales, and comparisons between the nine months ended September 30, 2010 and 2009 (*dollars in thousands*):

	2010		Nine months ended September 30, 2009		Dollar and Percentage Change Year to Year				
Net sales	\$	633,233	100.0%	\$	163,270	100.0%	\$	469,963	287.8%
Cost of sales		342,210	54.0		105,566	64.7		236,644	224.2
Gross profit		291,023	46.0		57,704	35.3		233,319	404.3
Operating expenses (income):									
Selling, general and administrative									
		62,852	9.9		41,926	25.7		20,926	49.9
Research and development		47,861	7.6		29,327	18.0		18,534	63.2
Amortization		3,711	0.6		3,775	2.3		(64)	(1.7)
Restructuring		(179)	(0.0)		4,770	2.9		(4,949)	*
Asset impairment					304	0.2		(304)	(100.0)
Other, net		75	0.0		368	0.2		(293)	(79.6)
Total operating expenses		114,320	18.1		80,470	49.3		33,850	42.1
Operating income (loss)		176,703	27.9		(22,766)	(13.9)		199,469	*
Interest expense, net		5,181	0.8		5,063	3.1		118	2.3
Income (loss) from continuing operations before income taxes									
		171,522	27.1		(27,829)	(17.0)		199,351	*
Income tax provision		7,663	1.2		2,379	1.5		5,284	222.1
Income (loss) from continuing operations		163,859	25.9		(30,208)	(4.8)		194,067	30.6
Discontinued operations:									
Income (loss) from discontinued operations									
		3,546	0.6		(5,206)	(0.8)		8,752	*
Income tax provision (benefit)		2,805	0.4		(1,037)	(0.2)		3,842	*
Income (loss) from discontinued operations		741	0.1		(4,169)	(2.6)		199,351	*
Net income (loss)		164,600	26.0		(34,377)	(21.1)		202,819	43.2
Net loss attributable to noncontrolling interest					(65)	0.1		65	(100.0)
Net income (loss) attributable to Veeco	\$	164,600	26.0%	\$	(34,312)	(21)%	\$	198,912	*

* Not Meaningful

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Net Sales and Orders

Net sales of \$633.2 million for the nine months ended September 30, 2010 were up 287.8% compared to the comparable 2009 period. The following is an analysis of net sales and orders by segment and by region (*dollars in thousands*):

	Sales				Orders				Book to Bill Ratio	
	Nine months ended September 30,		Dollar and Percentage Change		Nine months ended September 30,		Dollar and Percentage Change		2010	2009
	2010	2009	Year to Year		2010	2009	Year to Year			
Segment Analysis										
LED & Solar	\$ 539,765	\$ 107,050	\$ 432,715	404.2%	\$ 715,320	\$ 264,092	\$ 451,228	170.9%	1.33	2.47
Data Storage	93,468	56,220	37,248	66.3	111,370	44,379	66,991	151.0	1.19	0.79
Total	\$ 633,233	\$ 163,270	\$ 469,963	287.8%	\$ 826,690	\$ 308,471	\$ 518,219	168.0%	1.31	1.89
Regional Analysis										
Americas	\$ 63,484	\$ 39,361	\$ 24,123	61.3%	\$ 72,551	\$ 51,645	\$ 20,906	40.5%	1.14	1.31
EMEA	65,673	33,454	32,219	96.3	57,604	27,817	29,787	107.1	0.88	0.83
Asia Pacific	504,076	90,455	413,621	457.3	696,535	229,009	467,526	204.2	1.38	2.53
Total	\$ 633,233	\$ 163,270	\$ 469,963	287.8%	\$ 826,690	\$ 308,471	\$ 518,219	168.0%	1.31	1.89

Sales and orders increased in each segment for the nine months ended September 30, 2010 compared with the comparable 2009 period due to our customers' requirements in response to increasingly favorable economic conditions compared to 2009. LED & Solar sales were up 404.2% from the comparable 2009 period primarily due to an increase in end user demand for HB LED backlighting applications and strong customer acceptance of Veeco's newest generation systems. Data Storage sales were up 66.3% from the comparable 2009 period due to an increase in demand by our data storage customers as the global economy improved from 2009. By region, net sales increased by 457.3% in the Asia Pacific region, primarily due to MOCVD sales to HB LED customers, while sales in the Americas and EMEA also increased 61.3% and 96.3%, respectively. We believe that there will continue to be period-to-period variations in the geographic distribution of sales.

Table of Contents

Orders for the nine months ended September 30, 2010 increased 168.0% from the comparable 2009 period. By segment, the 170.9% increase in orders for LED & Solar was principally driven by HB LED based manufacturers increasing production for television and laptop backlighting applications. The 151.0% increase in Data Storage orders resulted from an increase in demand by our data storage customers due to both capacity expansion and technology buys.

Gross Profit

Gross profit, as a percentage of net sales, for the nine months ended September 30, 2010, was 46.0%, compared to 35.3% in the comparable 2009 period. LED & Solar gross margins increased to 45.9% from 36.4% and Data Storage gross margins increased to 47.2% from 34.4%, driven primarily by cost reduction, favorable product mix and increased sales volume in each segment. For the nine months ended September 30, 2009, Data Storage gross margins were also negatively impacted by a charge of \$1.5 million for the write-off of inventory associated with the discontinuance of certain product lines.

Operating Expenses

Selling, general and administrative expenses increased by \$20.9 million, or 49.9%, from the comparable 2009 period, however, decreased from 25.7% of net sales to 9.9% of sales. The dollar increase was primarily due to an increase in bonus and profit sharing expense, equity-based compensation, travel and entertainment expenses, salary and related expenses and professional fees associated primarily with the significant increase in business activity in our LED & Solar segment.

Research and development expenses increased \$18.5 million from the comparable 2009 period, however, decreased from 18.0% of net sales to 7.6% of sales. The dollar increase was primarily due to increased spending in our LED & Solar segment to support future growth.

Restructuring included a credit of approximately \$0.2 million during the nine months ended September 30, 2010 due to a change in estimate for one of our abandoned leased facilities. Restructuring expense of \$4.8 million in the nine months ended September 30, 2009 consisted of \$3.5 million of personnel severance costs resulting from a reduction in workforce, \$0.9 million of lease-related costs and \$0.4 million of moving and consolidation costs incurred in our Data Storage segment associated with vacating our Camarillo, CA facilities. In addition, there was also a \$0.3 million asset impairment charge.

Other, net for the nine months ended September 30, 2010 included a no foreign currency exchange gain or loss compared to a foreign exchange gain of \$0.1 million in the comparable 2009 period.

Income Taxes

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Our provision for income taxes consists of U.S. federal, state and local and foreign taxes in amounts necessary to align our quarter-to-date tax provision with the effective tax rate we expect to achieve for the full year.

For the nine months ended September 30, 2010, the Company had an effective tax rate of 4.5% and recorded a provision for income taxes of \$7.7 million. The provision for income taxes includes \$11.2 million relating to U.S federal, state and local and foreign taxes offset by a discrete tax benefit of \$3.5 million primarily related to state research and development tax credits as the Company had a favorable resolution of an income tax audit.

The effective tax rate is lower than the statutory rate primarily due to the Company's ability to realize a significant portion of its deferred tax assets, primarily related to net operating loss carryforwards and federal tax credits, on a more-likely-than-not basis based on the forecasted results of operations for the year ending December 31, 2010.

For the nine months ended September 30, 2009, the Company recorded a provision for income taxes of \$1.3 million related to U.S federal, state and local and foreign taxes.

Table of Contents**Liquidity and Capital Resources**

Historically, our principal capital requirements have included the funding of acquisitions, capital expenditures and repayment of debt. We traditionally have generated cash from operations and debt and stock issuances. Our ability to generate sufficient cash flows from operations is dependent on the continued demand for our products and services. A summary of the cash flow activity for the nine months ended September 30, 2010 and 2009, respectively, is as follows (*in thousands*):

	Nine months ended September 30,	
	2010	2009
Net income (loss)	\$ 164,600	\$ (34,377)
Net cash provided by operating activities	\$ 187,871	\$ 21,668
Net cash used in investing activities	(91,371)	(17,084)
Net cash provided by financing activities	33,005	2,263
Effect of exchange rates on cash and cash equivalents	139	(8)
Net increase in cash and cash equivalents	129,644	6,839
Cash and cash equivalents at beginning of period	148,500	102,521
Cash and cash equivalents at end of period	\$ 278,144	\$ 109,360

We had a net increase in cash of \$129.6 million during the nine months ended September 30, 2010. Cash provided by operations was \$187.9 million for this period, as compared to cash provided by operations of \$21.7 million for the comparable 2009 period. Net income adjusted for non-cash items provided operating cash flows of \$152.8 million for the nine months ended September 30, 2010, whereas \$1.1 million was used in operating cash flows in the comparable 2009 period. Net cash provided by operations for the nine months ended September 30, 2010 included a decrease in net operating assets of \$35.0 million. Inventories increased by approximately \$24.6 million, principally to support significant MOCVD order activity. Accounts receivable increased \$61.5 million, due to higher sales volume when compared to the fourth quarter of 2009. Accrued expenses and other current liabilities increased \$138.9 million, due primarily to an increase in customer deposits. Accounts payable also increased by \$19.9 million, due to the higher level of business activity.

Cash used in investing activities of \$91.4 million for the nine months ended September 30, 2010 primarily related to purchases of additional short-term investments of \$246.5 million, \$31.6 million transferred to restricted cash and \$31.6 million in purchases of treasury stock, capital expenditures of \$8.0 million, partially offset by the sale or redemption of short-term investments of \$224.7 million. Cash used in investing activities of \$17.1 million for the nine months ended September 30, 2009 primarily related to the \$9.8 million earn-out payments and \$4.6 million in capital expenditures, of which \$4.1 million is principally attributable to our LED & Solar segment. During the remainder of 2010, we estimate we will invest an additional \$10.7 million in capital expenditures primarily related to lab tools for high-growth opportunities, as well as for plant expansion and building improvements.

Cash provided by financing activities of \$33.0 million and \$2.3 million for the nine months ended September 30, 2010 and 2009 primarily related to stock option exercises.

Based on forecasted results of operations for the year ending December 31, 2010, we expect to exhaust our net federal operating loss carryforwards (NOLs) and federal tax credits (FTCs) this year. As a result, we anticipate paying taxes when the NOLs and FTCs are exhausted.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

At September 30, 2010, we have \$31.6 million of restricted cash which serves as collateral for bank guarantees which provide financial assurance that we will fulfill certain customer obligations. The cash is held in custody by the issuing bank, and is restricted as to withdrawal or use while the related bank guarantees are outstanding.

On August 15, 2010, we signed a definitive agreement to sell our metrology business to Bruker Corporation comprising our entire Metrology reporting segment. At closing, on October 7, 2010, we received \$229.4 million in cash consideration of which 10% of such consideration will be held in escrow. The final purchase price is subject to certain post-closing adjustments related to final working capital. We expect to record a net gain on the sale of approximately \$99 million during the fourth quarter.

As of September 30, 2010, we have outstanding \$105.6 million aggregate principal amount of 4.125% convertible subordinated notes due April 15, 2012 (the Notes). We pay interest on the Notes on April 15 and October 15 of each year. We have previously engaged in repurchase transactions of our Notes and may enter into

Table of Contents

similar transactions in the future depending on market conditions, our cash position and other factors.

The Notes are initially convertible into 36.7277 shares of common stock per \$1,000 principal amount of Notes (equivalent to a conversion price of \$27.23 per share or a premium of 38% over the closing market price for Veeco's common stock on April 16, 2007). On or after April 20, 2011, we may redeem the notes, in whole or in part, for cash at 100% of the principal amount of the notes to be redeemed plus accrued and unpaid interest to, but not including, the redemption date. Holders may convert the Notes at any time during the period beginning on January 15, 2012 through the close of business on the second day prior to April 15, 2012 and earlier upon the occurrence of certain events including if the notes have been called for redemption or if, for a given fiscal quarter, our common stock trades at prices equal to 130% of the conversion price for at least 20 trading days during the final 30 trading days of the immediately preceding fiscal quarter. At the end of the third quarter of 2010, our common stock was not trading at prices equal to or above 130% of the conversion price for the specified period and, as a result, the Notes will not be convertible during the fourth quarter of 2010. If the Notes are converted, we have the ability and intent to pay the principal balance of notes tendered for conversion in cash. We will re-perform this test each quarter up to and including the fourth quarter of 2011.

We believe that existing cash balances together with cash generated from operations will be sufficient to meet our projected working capital and other cash flow requirements for the next twelve months, as well as our contractual obligations. We believe we will be able to meet our obligation to repay the \$105.6 million of outstanding Notes that mature on April 15, 2012 with cash and short-term investments on hand.

In 2006 we purchased 19.9% of the common stock of Fluens Corporation (Fluens). On May 14, 2009, we acquired the remaining 80.1% of Fluens for \$1.5 million and an earn-out arrangement based on future performance. No gain or loss was recognized upon the purchase of the 80.1% portion. The difference between the purchase price including the earn-out consideration and the amount by which noncontrolling interest was reduced on the balance sheet was attributed to equity of Veeco. Such difference amounted to approximately \$1.0 million, and was recorded as additional paid-in capital. We paid \$0.5 million of the \$1.5 million purchase price of the 80.1% remaining portion of Fluens upon closing, as well as \$0.2 million in respect of the earn-out arrangement for periods prior to 2009. We paid a second installment of \$0.5 million of the purchase price on September 30, 2009. We paid the remaining \$0.5 million of the \$1.5 million in the first quarter of 2010, which was included in accrued expenses in the accompanying condensed consolidated Balance Sheet at December 31, 2009.

Common Stock Repurchase Program

The Company's share repurchase activity for the three and nine months ended September 30, 2010 was as follows (*in thousands, except share data*):

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Cost of repurchases	\$ 31,602	\$	\$ 31,602	\$
Shares repurchased and held in treasury	929,382		929,382	
Average cost per share	\$ 34.00	\$	\$ 34.00	\$

At September 30, 2010, there remained \$168.4 million of authorization for future repurchases.

Contractual Obligations

There have been no significant changes to our Contractual Obligations table, except for purchase commitments, in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations of our 2009 Annual Report on Form 10-K. The purchase commitments outstanding at September 30, 2010 were \$244.0 million.

Table of Contents

Application of Critical Accounting Policies

General: Our discussion and analysis of our financial condition and results of operations are based upon our Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. Management continually monitors and evaluates its estimates and judgments, including those related to bad debts, inventories, intangible and other long-lived assets, income taxes, warranty obligations, restructuring costs, and contingent liabilities, including potential litigation. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We consider certain accounting policies related to revenue recognition, the valuation of inventories, the impairment of goodwill and indefinite-lived intangible assets, the impairment of long-lived assets, fair value measurements, warranty costs, the accounting for income taxes and equity-based compensation to be critical policies due to the estimation processes involved in each.

Revenue Recognition: We recognize revenue based on current accounting guidance provided by the Securities and Exchange Commission and the Financial Accounting Standards Board (FASB). Our revenue transactions include sales of products under multiple-element arrangements. Revenue under these arrangements is allocated to each element based upon its estimated fair market value.

We consider a broad array of facts and circumstances when evaluating each of our sales arrangements in determining when to recognize revenue, including specific terms of the purchase order, contractual obligations to the customer, the complexity of the customer's post delivery acceptance provisions, customer creditworthiness and the installation process. Revenue is recognized when persuasive evidence of an arrangement exists, the sales price is fixed or determinable, collectability is reasonably assured and no uncertainties exist regarding customer acceptance. For transactions on which we recognize systems revenue, either at the time of shipment or delivery, our contractual arrangements with customers do not contain provisions for right of return or forfeiture, refund or other purchase price concessions. Sales arrangements are reviewed on a case-by-case basis; however, we have established a revenue recognition protocol as described below.

Systems, which are sold to manufacturers in the LED, solar, data storage and semiconductor industries and are used in manufacturing facilities and commercial production environments typically include process acceptance criteria based upon Veeco and/or customer specifications. We are generally required to install these products and demonstrate compliance with acceptance tests at the customer's facility. Generally, based upon the terms of the sales arrangement, these products are sold with a retention (typically 10% to 20% of the sales contract value) which is payable by the customer when installation and field acceptance is completed. Such installations are not considered complex and are not deemed essential to the functionality of the equipment because they do not involve significant changes to the features or capabilities of the equipment or involve building complex interfaces or connections. Installation normally represents only 2% - 4% of the fair value of the sales contract. Sales arrangements for these systems are bifurcated into separate units of accounting or elements based on objective evidence of fair value. The two elements are the system and installation of the system. The amount of revenue allocated to each element is based upon its relative fair value. The price charged when the system or installation service is sold separately generally determines fair value. The value of the installation service is based upon the fair value of the service performed, including labor, which is based upon the estimated time to complete the installation at hourly rates, and material components. We recognize revenue for the system or delivered element since the delivered item has value to the customer on a standalone basis, there is objective and reliable evidence of the fair value of the undelivered item (i.e., the installation service) and delivery or performance of the undelivered item is considered probable and substantially in our control, based on our historical experience. The value of the undelivered element is the greater of the fair value of the installation or the portion of the sales price that will not be received until the installation is completed (i.e., the retention amount). System revenue is generally recognized upon shipment or delivery provided title and risk of loss has passed to the customer. Revenue from installation services is recognized at the time acceptance is received from the customer. If the arrangement does not meet all the above criteria, the entire amount of the sales arrangement is deferred until the criteria have been met or all elements have been delivered to the customer or been completed.

For new products, new applications of existing products, or for products with substantive customer acceptance provisions where performance cannot be fully assessed prior to meeting customer specifications at the customer site, revenue is recognized upon completion of installation and receipt of final customer acceptance. Since title to goods generally passes to the customer upon shipment or delivery and 80% to 90% of the contract amount becomes payable at that time, inventory is relieved and accounts receivable is recognized for the amount billed at the time of shipment. The

Table of Contents

profit on the amount billed for these transactions is deferred and recognized as deferred profit in the accompanying Condensed Consolidated Balance Sheets.

In Japan, where our contractual terms with customers generally specify risk of loss and title transfers upon customer acceptance, revenue is recognized and the customer is billed upon receipt of written customer acceptance.

Revenue related to maintenance and service contracts is recognized ratably over the applicable contract term. Component and spare part revenue is recognized at the time of shipment or delivery in accordance with the terms of the applicable sales arrangement.

Inventory Valuation: Inventories are stated at the lower of cost (principally first-in, first-out method) or market. Management evaluates the need to record adjustments for impairment of inventory on a quarterly basis. Our policy is to assess the valuation of all inventories, including raw materials, work-in-process, finished goods, and spare parts and other service inventory. Obsolete inventory or inventory in excess of management's estimated usage for the next 12 months requirements is written-down to its estimated market value, if less than its cost. Inherent in the estimates of market value are management's estimates related to our future manufacturing schedules, customer demand, technological and/or market obsolescence, possible alternative uses, and ultimate realization of excess inventory.

Goodwill and Indefinite-Lived Intangible Asset Impairment: The Company does not amortize goodwill or intangible assets with indefinite useful lives, but instead tests the balances in these asset accounts for impairment at least annually at the reporting unit level. Our policy is to perform this annual impairment test in the fourth quarter of each fiscal year or more frequently if impairment indicators arise. Impairment indicators include, among other conditions, cash flow deficits, a historical or anticipated decline in revenue or operating profit, adverse legal or regulatory developments, and a material decrease in the fair value of some or all of the assets.

Pursuant to relevant accounting pronouncements we are required to determine if it is appropriate to use the operating segment as defined under accounting guidance as the reporting unit or one level below the operating segment, depending on whether certain criteria are met. We have identified two reporting units that are required to be reviewed for impairment. The reporting units are LED & Solar and Data Storage. In identifying the reporting units management considered the economic characteristics of operating segments including the products and services provided, production processes, types or classes of customer and product distribution.

We perform this impairment test by first comparing the fair value of our reporting units to their respective carrying amount. When determining the estimated fair value of a reporting unit, we utilize a discounted future cash flow approach since reported quoted market prices are not available for our reporting units. Developing the estimate of the discounted future cash flow requires significant judgment and projections of future financial performance. The key assumptions used in developing the discounted future cash flows are the projection of future revenues and expenses, working capital requirements, residual growth rates and the weighted average cost of capital. In developing our financial projections, we consider historical data, current internal estimates and market growth trends. Changes to any of these assumptions could materially change the fair value of the reporting unit. We reconcile the aggregate fair value of our reporting units to the Company's adjusted market capitalization as a supporting calculation. The adjusted market capitalization is calculated by multiplying the average share price of our common stock for the last ten trading days prior to the measurement date by the number of outstanding common shares and adding a control premium.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

If the carrying value of the reporting units exceed the fair value we would then compare the implied fair value of our goodwill to the carrying amount in order to determine the amount of the impairment, if any.

Definite-Lived Intangible and Long-Lived Asset Impairment: Long-lived assets, such as property, plant, and equipment, and intangible assets with definite useful lives, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment indicators include, among other conditions, cash flow deficits, a historical or anticipated decline in revenue or operating profit, adverse legal or regulatory developments, and a material decrease in the fair value of some or all of the assets. Assets are grouped at the lowest level for which there is identifiable cash flows that are largely independent of the cash flows generated by other asset groups. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

Fair Value Measurements: Accounting guidance for our non-financial assets and non-financial liabilities requires that we disclose the type of inputs we use to value our assets and liabilities, based on three categories of

Table of Contents

inputs as defined in such. Level 1 inputs are quoted, unadjusted prices in active markets for identical assets or liabilities that the company has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as quoted prices for similar assets or liabilities. Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. These requirements apply to our long-lived assets, goodwill and intangible assets. We use Level 3 inputs to value all of such assets and the methodology we use to value such assets has not changed since December 31, 2009. The Company primarily applies the market approach for recurring fair value measurements.

Warranty Costs: We estimate the costs that may be incurred under the warranty we provide and record a liability in the amount of such costs at the time the related revenue is recognized. Estimated warranty costs are determined by analyzing specific product and historical configuration statistics and regional warranty support costs. Our warranty obligation is affected by product failure rates, material usage, and labor costs incurred in correcting product failures during the warranty period. Unforeseen component failures or exceptional component performance can also result in changes to warranty costs. If actual warranty costs differ substantially from our estimates, revisions to the estimated warranty liability would be required.

Income Taxes: As part of the process of preparing our Condensed Consolidated Financial Statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating the actual current tax expense, together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our Condensed Consolidated Balance Sheets. The carrying value of our deferred tax assets is adjusted by a partial valuation allowance to recognize the extent to which the future tax benefits will be recognized on a more likely than not basis. Our net deferred tax assets consist primarily of net operating loss and tax credit carry forwards, and timing differences between the book and tax treatment of inventory, acquired intangible assets and other asset valuations. Realization of these net deferred tax assets is dependent upon our ability to generate future taxable income.

We record valuation allowances in order to reduce our deferred tax assets to the amount expected to be realized. In assessing the adequacy of recorded valuation allowances, we consider a variety of factors, including the scheduled reversal of deferred tax liabilities, future taxable income, and prudent and feasible tax planning strategies. Under the relevant accounting guidance, factors such as current and previous operating losses are given significantly greater weight than the outlook for future profitability in determining the deferred tax asset carrying value.

Relevant accounting guidance addresses the determination of how tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under such guidance, we must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such uncertain tax positions are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate resolution.

Equity-based Compensation: Equity-based compensation cost is measured at the grant date, based on the fair value of the award and is recognized as expense over the employee requisite service period. In order to determine the fair value of stock options on the date of grant, we apply the Black-Scholes option-pricing model. Inherent in the model are assumptions related to risk-free interest rate, dividend yield, expected stock-price volatility and option life.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

The risk-free rate assumed in valuing the options is based on the U.S. Treasury yield curve in effect at the time of grant for the expected term of the option. The dividend yield assumption is based on the Company's historical and future expectation of dividend payouts. While the risk-free interest rate and dividend yield are less subjective assumptions, typically based on factual data derived from public sources, the expected stock-price volatility and option life assumptions require a level of judgment which make them critical accounting estimates.

We use an expected stock-price volatility assumption that is a combination of both historical volatility, calculated based on the daily closing prices of our common stock over a period equal to the expected term of the option and implied volatility, utilizing market data of actively traded options on our common stock, which are obtained from public data sources. We believe that the historical volatility of the price of our common stock over the expected term of the option is a strong indicator of the expected future volatility and that implied volatility takes into consideration market expectations of how future volatility will differ from historical volatility. Accordingly, we believe a combination of both historical and implied volatility provides the best estimate of the future volatility of the market price of our common stock.

Table of Contents

The expected term, representing the period of time that options granted are expected to be outstanding, is estimated using a lattice-based model incorporating historical post vest exercise and employee termination behavior.

We estimate forfeitures using our historical experience, which is adjusted over the requisite service period based on the extent to which actual forfeitures differ or are expected to differ, from such estimates. Because of the significant amount of judgment used in these calculations, it is reasonably likely that circumstances may cause the estimate to change.

With regard to the weighted-average option life assumption, we consider the exercise behavior of past grants and model the pattern of aggregate exercises.

Recent Accounting Pronouncements

Subsequent Events: The FASB has issued amended guidance for subsequent events. The amendment removes the requirement for an SEC filer to disclose a date through which subsequent events have been evaluated in both issued and revised financial statements. Revised financial statements include financial statements revised as a result of either correction of an error or retrospective application of U.S. GAAP. The FASB also clarified that if the financial statements have been revised, then an entity that is not an SEC filer should disclose both the date that the financial statements were issued or available to be issued and the date the revised financial statements were issued or available to be issued. The FASB believes these amendments remove potential conflicts with the SEC's literature. All of the amendments were effective upon issuance (February 24, 2010). The adoption of this guidance did not have a material impact on the Company's condensed consolidated financial statements.

Fair Value Measurements: In January 2010, the FASB issued amended guidance for Fair Value Measurements and Disclosures. This update requires some new disclosures and clarifies existing disclosure requirements about fair value measurement. The FASB's objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Specifically, this update requires that a reporting entity disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers; and in the reconciliation for fair value measurements using significant unobservable inputs, a reporting entity should present separately information about purchases, sales, issuances, and settlements. In addition, this update clarifies the requirements of existing disclosures. For purposes of reporting fair value measurement for each class of assets and liabilities, a reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities; and a reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. This update was adopted on January 1, 2010, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. The adoption of this guidance did not have a material impact on the Company's condensed consolidated financial statements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. Early application is permitted. The Company does not believe that this guidance will have a material impact on its condensed consolidated financial statements.

Revenue Recognition: In October 2009, the FASB issued amended guidance related to multiple-element arrangements which requires an entity to allocate arrangement consideration at the inception of an arrangement to all of its deliverables based on their relative selling prices. This update eliminates the use of the residual method of allocation and requires the relative-selling-price method in all circumstances. All entities must adopt the guidance no later than the beginning of their first fiscal year beginning on or after June 15, 2010. Entities may elect to adopt the guidance through either prospective application for revenue arrangements entered into or materially modified, after the effective date or through retrospective application to all revenue arrangements for all periods presented. The Company does not believe that this guidance will have a material impact on its condensed consolidated financial statements.

In October 2009, the FASB issued amended guidance that is expected to significantly affect how entities account for revenue arrangements that contain both hardware and software elements. As a result, many tangible products that rely on software will be accounted for under the revised multiple-element arrangements revenue recognition guidance, rather than the software revenue recognition guidance. The revised guidance must be adopted by all entities no later than fiscal years beginning on or after June 15, 2010. An entity must select the same transition method and same period for the adoption of both this guidance and the revisions to the multiple-element

Table of Contents

arrangements guidance noted above. The Company does not believe that this guidance will have a material impact on its condensed consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Our net sales to foreign customers represented approximately 92.5% and 90.0% of our total net sales for the three and nine months ended September 30, 2010, respectively, and 84.7% and 76.0% for the comparable 2009 periods. We expect that net sales to foreign customers will continue to represent a large percentage of our total net sales. Our net sales denominated in foreign currencies represented approximately 1.5% and 2.2% of our total net sales for the three and nine months ended September 30, 2010 respectively, and 3.4% and 5.9% for the comparable 2009 periods.

The aggregate foreign currency exchange gain (loss) included in determining the condensed consolidated results of operations was approximately \$0.1 million and \$(0.1) million during the three months ended September 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange gain were losses related to forward contracts of \$(0.1) million during the three months ended September 30, 2010. The aggregate foreign currency exchange loss included in determining the condensed consolidated results of operations was approximately \$(0.3) million and \$(0.6) million during the nine months ended September 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange loss were gains related to forward contracts of \$0.1 million during the nine months ended September 30, 2009. These amounts were recognized and are included in other, net in the accompanying condensed consolidated statements of operations.

We are exposed to financial market risks, including changes in foreign currency exchange rates. The change in currency exchange rates that have the largest impact on translating our international operating profit is the Japanese Yen. We use derivative financial instruments to mitigate these risks. We do not use derivative financial instruments for speculative or trading purposes. We generally enter into monthly forward contracts to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known currency exposures. The weighted average notional amount of derivative contracts outstanding during the three and nine months ended September 30, 2010 was approximately \$6.8 and \$5.9 million, respectively.

As of September 30, 2010, approximately \$0.2 million of losses related to forward contracts were included in accrued expenses and other current liabilities and were subsequently paid in October 2010. As of December 31, 2009, approximately \$0.2 million of gains related to forward contracts were included in prepaid expenses and other current assets and were subsequently received in January 2010. Monthly forward contracts with a notional amount of \$1.7 million, entered into in September 2010, will be settled in October 2010. The fair value of the contracts at inception was zero, which did not significantly change at September 30, 2010.

We believe that based upon our hedging program, a 10% change in foreign exchange rates would have an immaterial impact on the consolidated results of operations. We believe that this quantitative measure has inherent limitations because, as discussed in the first paragraph of this section, it does not take into account any governmental actions or changes in either customer purchasing patterns or our financing and operating strategies.

Assuming third quarter 2010 variable debt and investment levels, the effect of a one-point change in interest rates would not have a material effect on net interest expense.

Item 4. Controls and Procedures.

Our senior management is responsible for establishing and maintaining a system of disclosure controls and procedures (as defined in Rule 13a-15 and 15d-15 under the Securities Exchange Act of 1934 (the Exchange Act)) designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

We have evaluated the effectiveness of the design and operation of our disclosure controls and procedures under the supervision of and with the participation of management, including the chief executive officer and chief financial officer, as of the end of the period covered by this report. Based on that evaluation, our chief executive

Table of Contents

officer and our chief financial officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

There have been no significant changes in our internal controls or other factors during the fiscal quarter ended September 30, 2010 that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

Table of Contents**Part II. OTHER INFORMATION****Item 1. Legal Proceedings**

We are involved in various legal proceedings arising in the normal course of our business. We do not believe that the ultimate resolution of these matters will have a material adverse effect on our consolidated financial position, results of operations or cash flows.

Item 1A. Risk Factors.

Information regarding risk factors appears in the Safe Harbor Statement at the beginning of this Quarterly Report on Form 10-Q, in Part I Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2009 and in Part II Item 1A of our Quarterly Report on Form 10-Q for the quarter ended June 30, 2010. There have been no material changes from the risk factors previously disclosed in our 2009 Annual Report and our Quarterly Report on Form 10-Q for the quarter ended June 30, 2010.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table contains the Company's stock repurchases of equity securities in the second quarter of 2010:

Period	Total Number of Shares Repurchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Program (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program (1)
Fiscal month of September 2010 (August 30, 2010 - September 26, 2010)	929,382	\$ 34.00	929,382	\$ 168,397,600

(1) On August 24, 2010, we announced that our Board of Directors had authorized the repurchase of up to \$200 million of our common stock until August 26, 2011. The program does not obligate the Company to acquire any particular amount of common stock and may be modified or suspended at any time at the Company's discretion.

Table of Contents

Item 6. Exhibits.

Unless otherwise indicated, each of the following exhibits has been previously filed with the SEC by the Company under File No. 0-16244.

Number	Description	Incorporated by Reference to the Following Document:
2.1	Stock Purchase Agreement dated August 15, 2010 among Veeco Instruments Inc., Veeco Metrology Inc. and Bruker Corporation	*
10.1	Letter Agreement dated September 23, 2010 between Veeco Instruments Inc. and Mark R. Munch	*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*

* Filed herewith

Table of Contents

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: October 27, 2010

Veeco Instruments Inc.

By: /s/ JOHN R. PEELER
John R. Peeler
Chief Executive Officer

By: /s/ DAVID D. GLASS
David D. Glass
Executive Vice President and Chief Financial Officer

Table of Contents

INDEX TO EXHIBITS

Unless otherwise indicated, each of the following exhibits has been previously filed with the Securities and Exchange Commission by the Company under File No. 0-16244.

Number	Description	Incorporated by Reference to the Following Document:
2.1	Stock Purchase Agreement dated August 15, 2010 among Veeco Instruments Inc., Veeco Metrology Inc. and Bruker Corporation	*
10.1	Letter Agreement dated September 23, 2010 between Veeco Instruments Inc. and Mark R. Munch	*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*

* Filed herewith
