

VEECO INSTRUMENTS INC
Form 10-Q
October 26, 2009
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, 2009

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)

Delaware
(State or Other Jurisdiction of

Incorporation or Organization)

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

11-2989601
(I.R.S. Employer

Identification Number)

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

32,777,024 shares of common stock, \$0.01 par value per share, were outstanding as of the close of business on October 20, 2009.

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 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:

- 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.

- 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;

- 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, which could materially adversely impact our future results of operations;

- We are exposed to risks associated with entering an emerging segment within the solar industry;

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

- Any failure by us to execute our planned cost reductions successfully could result in total costs and expenses that are greater than expected;

- The cyclical nature of the industries we serve directly affects our business;

- We operate in industries characterized by rapid technological change;

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

- We face significant competition;
- We depend on a limited number of customers that operate in highly concentrated industries;
- The timing of our orders, shipments, and revenue recognition may cause our quarterly operating results to fluctuate significantly;
- Changes in our product mix may cause our quarterly operating results to fluctuate significantly;
- 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;
- Our sales cycle is long and unpredictable;
- 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;
- We rely on a limited number of suppliers;
- Our inability to attract, retain, and motivate key employees could have a material adverse effect on our business;
- We are exposed to the risks of operating a global business;

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 are substantially leveraged, which could adversely affect our ability to adjust our business to respond to competitive pressures and to obtain sufficient funds to finance our future needs;

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

- The price of our common shares may be volatile and could decline significantly;

- 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 significant operations in California and other locations which could be materially and adversely impacted, in the event of a natural disaster or other significant disruption;

- 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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

- The other matters discussed under the heading Management's Discussion and Analysis of Financial Condition and Results of Operations contained in this Report and in the Annual Report on Form 10-K for the year ended December 31, 2008 of Veeco Instruments Inc. (Veeco, the Company, or we).

Consequently, such forward-looking statements should be regarded solely as our current plans, estimates and beliefs. We do 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 read and copy any materials we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room 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 for the Three Months and Nine Months Ended September 30, 2009 and 2008 (Unaudited)</u> 5
	<u>Condensed Consolidated Balance Sheets as of September 30, 2009 (Unaudited) and December 31, 2008</u> 6
	<u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2009 and 2008 (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> 20
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u> 36
<u>Item 4.</u>	<u>Controls and Procedures</u> 36
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1.</u>	<u>Legal Proceedings</u> 37
<u>Item 1A.</u>	<u>Risk Factors</u> 37
<u>Item 6.</u>	<u>Exhibits</u> 38
<u>SIGNATURES</u>	39

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		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Net sales	\$ 98,913	\$ 115,709	\$ 233,782	\$ 332,465
Cost of sales	58,005	69,626	148,108	196,026
Gross profit	40,908	46,083	85,674	136,439
Operating expenses:				
Selling, general, and administrative expense	21,042	23,589	59,471	70,528
Research and development expense	13,721	15,302	39,770	45,173
Amortization expense	1,777	3,148	5,437	7,530
Restructuring expense	1,192	4,120	7,567	6,995
Asset impairment charge			304	285
Other (income) expense, net	(312)	(213)	1,097	(591)
Total operating expenses	37,420	45,946	113,646	129,920
Operating income (loss)	3,488	137	(27,972)	6,519
Interest expense, net	1,656	1,792	5,063	5,097
Income (loss) before income taxes	1,832	(1,655)	(33,035)	1,422
Income tax provision	562	812	1,342	2,860
Net income (loss) including noncontrolling interest	1,270	(2,467)	(34,377)	(1,438)
Net loss attributable to the noncontrolling interest		(54)	(65)	(200)
Net income (loss) attributable to Veeco	\$ 1,270	\$ (2,413)	\$ (34,312)	\$ (1,238)
Income (loss) per common share:				
Net income (loss) attributable to Veeco	\$ 0.04	\$ (0.08)	\$ (1.09)	\$ (0.04)
Diluted net income (loss) attributable to Veeco	\$ 0.04	\$ (0.08)	\$ (1.09)	\$ (0.04)
Weighted average shares outstanding	31,608	31,458	31,540	31,293
Diluted weighted average shares outstanding	32,375	31,458	31,540	31,293

See accompanying notes.

Table of Contents

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

	September 30, 2009 (Unaudited)	December 31, 2008
Assets		
Current assets:		
Cash and cash equivalents	\$ 109,441	\$ 103,799
Accounts receivable, net	64,260	59,659
Inventories	74,999	94,930
Prepaid expenses and other current assets	8,059	6,425
Deferred income taxes	2,226	2,185
Total current assets	258,985	266,998
Property, plant, and equipment at cost, net	59,294	64,372
Goodwill	59,422	59,160
Intangible assets, net	32,116	38,818
Other assets	8	193
Total assets	\$ 409,825	\$ 429,541
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	\$ 28,521	\$ 29,610
Accrued expenses	73,445	66,964
Deferred profit	2,337	1,346
Current portion of long-term debt	208	196
Income taxes payable	23	354
Total current liabilities	104,534	98,470
Deferred income taxes	5,233	4,540
Long-term debt	100,286	98,330
Other non-current liabilities	1,652	2,391
Shareholders' equity:		
Shareholders' equity attributable to Veeco	198,120	225,026
Noncontrolling interest		784
Total shareholders' equity	198,120	225,810
Total liabilities and shareholders' equity	\$ 409,825	\$ 429,541

See accompanying notes.

Table of Contents

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

	Nine months ended September 30,	
	2009	2008
Operating activities		
Net loss attributable to Veeco	\$ (34,312)	\$ (1,238)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	16,070	18,138
Deferred income taxes	683	1,260
Amortization of debt discount	2,114	2,184
Non-cash inventory write-off	1,526	
Non-cash share-based compensation	5,953	5,671
Non-cash restructuring charge		3,018
Non-cash asset impairment charge	304	285
Other, net	13	(263)
Changes in operating assets and liabilities:		
Accounts receivable	(4,059)	6,663
Inventories	19,540	(1,703)
Accounts payable	(1,183)	(4,168)
Accrued expenses, deferred profit, and other current liabilities	14,930	(5,449)
Other, net	(1,108)	(1,978)
Net cash provided by operating activities	20,471	22,420
Investing activities		
Capital expenditures	(5,184)	(10,430)
Payments for net assets of businesses acquired, net of cash acquired	(2,413)	(10,970)
Payments for earn-outs of businesses acquired	(9,839)	
Other, net	352	104
Net cash used in investing activities	(17,084)	(21,296)
Financing activities		
Proceeds from stock issuances	2,904	681
Repayments of long-term debt	(146)	(270)
Restricted stock tax withholdings	(495)	(969)
Net cash provided by (used in) financing activities	2,263	(558)
Effect of exchange rate changes on cash and cash equivalents	(8)	35
Net increase in cash and cash equivalents	5,642	601
Cash and cash equivalents at beginning of period	103,799	117,083
Cash and cash equivalents at end of period	\$ 109,441	\$ 117,684
Non-cash investing and financing activities		
Accrual of payments for net assets of businesses acquired	\$ 1,000	\$ 3,527
Transfers from property, plant, and equipment to inventory	\$ 1,159	\$ 404
Transfers from inventory to property, plant, and equipment	\$ 23	\$ 385

See accompanying notes.

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 have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-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 months and nine months ended September 30, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009. For further information, refer to the financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2008.

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 2009 interim quarter ends are March 29, June 28, and September 27. The 2008 interim quarter ends were March 30, June 29, and September 28. 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.

Net Income (Loss) Per Common Share

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

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Weighted average shares outstanding	31,608	31,458	31,540	31,293
Dilutive effect of stock options and restricted stock awards and units	767			
Diluted weighted average shares outstanding	32,375	31,458	31,540	31,293

Net income (loss) per common share is computed using the weighted average number of common shares outstanding during the period. Diluted net income (loss) per common share is computed using the weighted average number of common shares and common equivalent shares outstanding during the period. The effect of approximately 308,000, 140,000 and 205,000 common equivalent shares for the nine month period ended September 30, 2009 and the three-month and nine-month periods ended September 30, 2008, respectively, were excluded from the diluted weighted average shares outstanding due to the net loss sustained in the period. During the three-month period ended September 30, 2009, options to purchase 1.6 million shares of common stock (at prices ranging from \$18.31 to \$72.00 per share) were excluded from the computation

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

of diluted earnings per share due to exercise prices that exceeded the average market price of our common stock for the period.

During the second quarter of 2007, we exchanged \$118.8 million of our 4.125% convertible subordinated notes due December 2008 (the Old Notes) for \$117.8 million of a new series of 4.125% convertible subordinated notes due April 15, 2012 (the Notes), leaving \$25.2 million of Old Notes outstanding. During the fourth quarter of 2008, we repaid the remaining \$25.2 million of Old Notes outstanding.

The 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 the 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 such amounts in cash. Using the treasury stock method, the impact of the assumed conversion of the Notes was anti-dilutive for the three and nine months ended September 30, 2009 and

Table of Contents

2008, as the average stock price for each period was below the conversion price of \$27.23. The maximum number of common equivalent shares issuable upon conversion at September 30, 2009 was approximately 5.4 million, after giving effect to the \$12.2 million of Notes that we repurchased during the fourth quarter of 2008. See Note 8 for further details on our debt.

Fair Value of Financial Instruments

We believe the carrying amounts of our financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, and accrued expenses, reflected in the accompanying condensed consolidated financial statements approximate fair value due to their short-term maturities. The fair value of our debt, including current maturities, is estimated using a discounted cash flow analysis based on the estimated current incremental borrowing rates for similar types of securities, or based on market value for our publicly-traded debt (see Note 8).

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 intended to offset exchange gains and losses on the underlying assets and liabilities; both the forward contracts and the underlying assets and liabilities are adjusted to current exchange rates through earnings. We conduct our derivative transactions with highly rated financial institutions in an effort to mitigate any material credit risk. The weighted average notional amount of derivative contracts outstanding during the three and nine months ended September 30, 2009 was approximately \$1.3 million and \$3.1 million, respectively.

The condensed consolidated results of operations for the three and nine months ended September 30, 2009 include aggregate foreign currency losses of approximately \$0.1 million and \$1.4 million, respectively. The loss of \$1.4 million for the nine months ended September 30, 2009 was net of gains of approximately \$0.2 million related to forward contracts. The condensed consolidated results of operations for the three and nine months ended September 30, 2008 include aggregate foreign currency gains of less than \$0.1 million and approximately \$0.1 million, respectively, which were net of losses of approximately \$0.1 million and \$0.3 million, respectively, related to forward contracts. These amounts were recognized and included in other (income) expense, net in the accompanying Condensed Consolidated Statements of Operations.

As of September 30, 2009, losses of \$0.1 million related to forward contracts were included in accrued expenses and subsequently paid in October 2009. As of December 31, 2008, approximately \$0.9 million of losses related to forward contracts were included in accrued expenses and subsequently paid in January 2009. Monthly forward contracts with a total notional amount of \$3.1 million were entered into in September 2009 and will be settled in October 2009. The fair value of these contracts at inception was zero, which did not significantly change at September 30, 2009.

Convertible Debt

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

In May 2008, new accounting guidance was issued that requires a portion of our convertible debt to be allocated to equity. We implemented the new guidance as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. See Note 8 Debt for a discussion of the impact of implementing the new guidance.

Subsequent Events

We have evaluated the condensed consolidated financial statements for subsequent events through the filing date of this Form 10-Q.

Table of Contents**Note 2 Acquisitions***Fluens Corporation*

In 2006 we purchased 19.9% of the common stock of Fluens Corporation (Fluens). Veeco and Fluens have jointly developed a next-generation process for high-rate deposition of aluminum oxide for data storage applications. For accounting purposes we had consolidated Fluens into our financial results and financial position, and recorded the remaining 80.1% portion of its net loss and net assets as a noncontrolling interest. On May 14, 2009, we acquired the remaining 80.1% of Fluens for \$1.5 million plus an earn-out arrangement based on future performance. Since we already were consolidating Fluens, the purchase of the remaining 80.1% was treated in accordance with the applicable accounting guidance as a transaction among shareholders and not as a new business acquisition. Thus no gain or loss was recognized upon the purchase of the 80.1% portion, and 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. We paid a second installment of \$0.5 million of the purchase price on September 30, 2009. We will pay the remaining \$0.5 million of the \$1.5 million in the fourth quarter of 2009, which is included in accrued expenses in the accompanying condensed Balance Sheet at September 30, 2009. Prior to our purchase of the remaining 80.1%, approximately 31% of Fluens was owned by an individual then serving as Senior Vice President of Veeco.

In July 2009, Veeco acquired certain assets from DayStar Technologies, Inc. (DayStar) in order to accelerate Veeco's penetration of the rapidly growing copper, indium, gallium, selenium (CIGS) solar market. Veeco purchased selected equipment, took over leased facilities and hired employees from DayStar's R&D group in Clifton Park, New York. In connection with these transactions, Veeco paid DayStar \$1.9 million in cash.

Note 3 Share-Based Compensation

Share-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. The following compensation expense was included in the condensed consolidated statements of operations for the three months and nine months ended September 30, 2009 and 2008 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
Share-based compensation expense	\$ 2,400	\$ 2,048	\$ 5,953	\$ 5,671

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

As of September 30, 2009, the total unrecognized compensation cost related to nonvested restricted stock awards and stock option awards is \$9.5 million and \$10.2 million, respectively. The related weighted-average period over which we expect that such unrecognized compensation costs will be recognized as expense is approximately 2.63 years for the nonvested restricted stock awards and 2.28 years for option awards.

A summary of our restricted stock awards including restricted stock units as of and for the nine months ended September 30, 2009, is presented below:

	Shares (000s)	Weighted- Average Grant-Date Fair Value
Nonvested at beginning of year	679	\$ 17.76
Granted	501	9.28
Vested	(164)	19.54
Forfeited (including cancelled awards)	(115)	16.42
Nonvested at September 30, 2009	901	12.89

Table of Contents

A summary of our stock option plans as of and for the nine months ended September 30, 2009, is presented below:

	Shares (000s)	Weighted- Average Exercise Price	Aggregate Intrinsic Value (000s)	Weighted- Average Remaining Contractual Life (in years)
Outstanding at beginning of year	5,572	\$ 20.29		
Granted	1,609	10.83		
Exercised	(192)	15.10		
Forfeited (including cancelled options)	(1,858)	22.85		
Outstanding at September 30, 2009	5,131	16.59	\$ 30,127	4.4
Options exercisable at September 30, 2009	2,705	19.69	\$ 8,794	2.8

Note 4 Balance Sheet Information*Accounts Receivable, net*

Accounts receivable are shown net of the allowance for doubtful accounts of \$0.9 million as of September 30, 2009 and December 31, 2008.

Inventories

Inventories have been determined by the lower of cost (principally first-in, first-out) or market. Inventories consist of (in thousands):

	September 30, 2009	December 31, 2008
Raw materials	\$ 47,117	\$ 57,815
Work in process	19,502	28,733
Finished goods	8,380	8,382
	\$ 74,999	\$ 94,930

Accrued Warranty

We estimate the costs that may be incurred under the warranty we provide and recognize 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 nine months ended September 30, 2009 and 2008 are as follows (in thousands):

	Nine months ended			
	September 30,			
	2009		2008	
Balance at beginning of period	\$	6,892	\$	6,502
Warranties issued during the period		2,716		4,962
Settlements made during the period		(3,069)		(4,096)
Balance at end of period	\$	6,539	\$	7,368

Table of Contents

Note 5 Segment Information

We manage the business, review operating results and assess performance, as well as allocate resources, based upon three separate reporting segments that reflect the market focus of each business. The Light Emitting Diode (LED) & Solar Process Equipment segment consists of metal organic chemical vapor deposition (MOCVD) systems, molecular beam epitaxy (MBE) systems, thermal deposition sources, and other types of deposition systems used to deposit materials on flexible and glass substrates. These systems are primarily sold to customers in the high-brightness light emitting diode (HB-LED) and solar industries, as well as to scientific research customers. This segment has product development and marketing sites in Somerset, New Jersey, St. Paul, Minnesota, and Lowell, Massachusetts. The Data Storage Process Equipment 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 product development and marketing sites in Plainview, New York, Ft. Collins, Colorado and Santa Barbara, California. In our Metrology segment, we design and manufacture atomic force microscopes, scanning probe microscopes, stylus profilers, and optical interferometers used to provide critical surface measurements in research and production environments. This broad line of products is used in universities, research facilities and scientific centers worldwide. In production environments such as semiconductor, data storage and other broad industries, our metrology instruments enable customers to monitor their products throughout the manufacturing process to improve yields, reduce costs, and improve product quality. This segment has product development and marketing sites in Camarillo and Santa Barbara, California and Tucson, Arizona.

We evaluate the performance of our reportable segments based on income (loss) from 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. Certain items excluded from segment profit (loss) include restructuring 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.

The following tables present certain data pertaining to our reportable segments and a reconciliation of segment profit (loss) to income (loss) before income taxes for the three months and nine months ended September 30, 2009 and 2008, and goodwill and total assets as of September 30, 2009 and December 31, 2008, respectively (in thousands):

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate Amount	Total
Three months ended September 30, 2009					
Net sales	\$ 52,966	\$ 21,721	\$ 24,226	\$	\$ 98,913
Segment profit (loss)	\$ 9,594	\$ 1,498	\$ 408	\$ (2,643)	\$ 8,857
Interest expense, net				1,656	1,656
Amortization expense	792	405	507	73	1,777
Equity-based compensation expense	245	303	290	1,562	2,400
Restructuring expense	200	224	411	357	1,192
Income (loss) before income taxes	\$ 8,357	\$ 566	\$ (800)	\$ (6,291)	\$ 1,832
Three months ended September 30, 2008					
Net sales	\$ 40,983	\$ 43,256	\$ 31,470	\$	\$ 115,709
Segment profit (loss)	\$ 5,630	\$ 7,044	\$ 297	\$ (2,591)	\$ 10,380
Interest expense, net				1,792	1,792
Amortization expense	1,587	952	495	114	3,148
Equity-based compensation expense	146	304	251	1,347	2,048
Restructuring expense			437	3,683	4,120
Purchase accounting adjustment (1)	927				927
Income (loss) before income taxes	\$ 2,970	\$ 5,788	\$ (886)	\$ (9,527)	\$ (1,655)

Table of Contents

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate Amount	Total
Nine months ended September 30, 2009					
Net sales	\$ 107,050	\$ 56,219	\$ 70,513	\$	\$ 233,782
Segment profit (loss)	\$ 5,410	\$ (1,143)	\$ (5,309)	\$ (6,143)	\$ (7,185)
Interest expense, net				5,063	5,063
Amortization expense	2,341	1,213	1,662	221	5,437
Equity-based compensation expense	619	892	847	3,595	5,953
Restructuring expense	1,129	3,054	2,797	587	7,567
Inventory write-off		1,526			1,526
Asset impairment charge		304			304
Income (loss) before income taxes	\$ 1,321	\$ (8,132)	\$ (10,615)	\$ (15,609)	\$ (33,035)
Nine months ended September 30, 2008					
Net sales	\$ 128,205	\$ 104,096	\$ 100,164	\$	\$ 332,465
Segment profit (loss)	\$ 23,130	\$ 11,139	\$ 1,215	\$ (7,557)	\$ 27,927
Interest expense, net				5,097	5,097
Amortization expense	3,040	2,856	1,295	339	7,530
Equity-based compensation expense	323	693	597	4,058	5,671
Restructuring expense		124	627	6,244	6,995
Asset impairment charge				285	285
Purchase accounting adjustment (1)	927				927
Income (loss) before income taxes	\$ 18,840	\$ 7,466	\$ (1,304)	\$ (23,580)	\$ 1,422
As of September 30, 2009					
Goodwill	\$ 51,989	\$	\$ 7,433	\$	\$ 59,422
Total assets	\$ 163,471	\$ 48,573	\$ 77,413	\$ 120,368	\$ 409,825
As of December 31, 2008					
Goodwill	\$ 51,727	\$	\$ 7,433	\$	\$ 59,160
Total assets	\$ 137,037	\$ 84,335	\$ 85,390	\$ 122,779	\$ 429,541

(1) This adjustment relates to the required capitalization of profit in inventory associated with the acquisition of Mill Lane, which is included in cost of sales.

Corporate total assets are comprised principally of cash and cash equivalents at September 30, 2009 and December 31, 2008.

Note 6 Income Taxes

We or one of our subsidiaries file income tax returns in the U.S. federal jurisdiction and various state, local, and foreign jurisdictions. During the quarter ended September 30, 2009, the Internal Revenue Service concluded its examination of our 2006 income tax return with a minor adjustment to our credit carry forwards. All material federal income tax matters have been concluded for years through 2006 subject to subsequent utilization of net operating losses generated in such years. All material state and local income tax matters have been concluded for

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

years through 2005. The majority of our foreign jurisdictions have been reviewed through 2007 with only a few jurisdictions having open tax years between 2004 and 2007. None of our tax returns are currently under examination in the federal and foreign tax jurisdictions. We are currently under examination in one state tax jurisdiction.

Table of Contents

Note 7 Comprehensive Income (Loss)

Total comprehensive income (loss) for the three months and nine months ended September 30, 2009 and 2008 was as follows (in thousands):

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Net income (loss) including noncontrolling interest	\$ 1,270	\$ (2,467)	\$ (34,377)	\$ (1,438)
Other comprehensive income (loss), net of tax:				
Foreign currency translation	966	(555)	20	1,208
Comprehensive income (loss) including noncontrolling interest	2,236	(3,022)	(34,357)	(230)
Comprehensive loss attributable to the noncontrolling interest		(54)	(65)	(200)
Comprehensive income (loss) attributable to Veeco	\$ 2,236	\$ (2,968)	\$ (34,292)	\$ (30)

Note 8 Debt

Convertible Debt

During the second quarter of 2007, we exchanged \$118.8 million of Old Notes for \$117.8 million of Notes pursuant to privately negotiated exchange agreements with certain holders of the Old Notes. During the fourth quarter of 2008, we repaid in full the \$25.2 million of the Old Notes that remained outstanding after the exchange transactions.

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). 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 our common stock trading at prices equal to 130% over the conversion price for a specified period. These Notes bear interest at 4.125% per annum and mature on April 15, 2012. We pay interest on these Notes on April 15 and October 15 of each year. 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, new accounting guidance was issued that requires a portion of convertible debt to be allocated to equity. We implemented the new guidance as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. The new 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 stockholders' equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as non-cash interest expense. The Notes are subject to the new guidance since they may be settled in cash upon conversion. Thus, as a result of the adoption of the new 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 will be amortized over the remaining life of the Notes, which will be through April 15, 2012. The reclassification generated a \$6.7 million deferred tax liability, which we offset with a corresponding decrease of the valuation allowance by the same amount. The new guidance requires that we present prior periods as if the guidance was in effect as of the date of issuance. Thus, we have presented all financial data for prior periods as if we had reclassified this \$16.3 million discount and began amortizing it in April 2007. The retrospective application of the new guidance described above to the results for the three and nine months ended September 30, 2008 increased the net loss attributable to Veeco in the three-month period from (\$1,673) to (\$2,413) and decreased the net income attributable to Veeco in the nine-month period from \$946 to a net loss of (\$1,238), and increased the loss per share attributable to Veeco in the three-month period

Table of Contents

from (\$0.05) to (\$0.08) and decreased the earnings per share in the nine-month period from \$0.03 to a loss per share of (\$0.04).

During the fourth quarter of 2008, we repurchased an aggregate principal amount of \$12.2 million of the Notes for \$7.2 million in cash, of which \$7.1 million related to principal and \$0.1 million related to accrued interest, reducing the amount outstanding from \$117.8 million to \$105.6 million. A gross gain of approximately \$5.1 million was recorded on these repurchases offset by the write-off of approximately \$0.1 million of unamortized deferred financing costs associated with the Notes, for a net gain of approximately \$5.0 million. Such net gain was reduced to \$3.8 million upon the adoption of the new guidance described above, which required that the gain be calculated based on the fair value of the portion repurchased as of the repurchase date. The fair value approximated the carrying value net of the unamortized discount on the portion repurchased. The difference of approximately \$1.2 million was recorded as a reduction in the gain originally reported, and thus increased the accumulated deficit as of December 31, 2008 by such amount.

For the nine months ended September 30, 2009 and 2008, respectively, we recorded approximately \$2.1 million and \$2.2 million, respectively, of additional interest expense in each period resulting from the amortization of the debt discount. This additional interest expense did not require the use of cash. The components of interest expense recorded on the Notes for the three and nine months ended September 30, 2009 and 2008 were as follows (in thousands):

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Contractual interest	\$ 1,089	\$ 1,214	\$ 3,266	\$ 3,643
Amortization of the discount on the Notes	714	740	2,114	2,184
Total interest expense on the Notes	\$ 1,803	\$ 1,954	\$ 5,380	\$ 5,827
Effective interest rate	6.8%	6.6%	6.8	