

VEECO INSTRUMENTS INC
Form 10-Q
November 01, 2016
[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, 2016

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)

11-2989601
(I.R.S. Employer Identification No.)

Terminal Drive
Plainview, New York
(Address of principal executive offices)

11803
(Zip Code)

(516) 677-0200

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if 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

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

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| Title of Class | Shares Outstanding |
|----------------------------|------------------------|
| Common Stock | as of October 20, 2016 |
| par value \$0.01 per share | 40,608,880 |

Table of Contents

VEECO INSTRUMENTS INC.

INDEX

| | |
|--|----|
| <u>Safe Harbor Statement</u> | 1 |
| <u>PART I FINANCIAL INFORMATION</u> | 3 |
| <u>Item 1. Financial Statements</u> | 3 |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 21 |
| <u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u> | 29 |
| <u>Item 4. Controls and Procedures</u> | 29 |
| <u>PART II OTHER INFORMATION</u> | 30 |
| <u>Item 1. Legal Proceedings</u> | 30 |
| <u>Item 1A. Risk Factors</u> | 30 |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u> | 30 |
| <u>Item 3. Defaults Upon Senior Securities</u> | 30 |
| <u>Item 4. Mine Safety Disclosures</u> | 30 |
| <u>Item 5. Other Information</u> | 30 |
| <u>Item 6. Exhibits</u> | 31 |
| <u>SIGNATURES</u> | 32 |

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 1, 2, and 3 hereof, as well as within this Report generally. In addition, when used in this Report, the words believes, anticipates, expects, estimates, targets, plans, intends, will, and similar expressions related to the future are intended to represent 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.

In addition, the preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles (U.S. GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Although these estimates and assumptions are based on knowledge of current events and planned actions to be undertaken in the future, they may ultimately differ from actual results. Operating results for the nine months ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. All estimates and assumptions are subject to a number of risks and uncertainties that could cause actual results to differ materially from these estimates and assumptions.

The risks and uncertainties of Veeco Instruments Inc. (together with its consolidated subsidiaries, Veeco, the Company, we, us, and our, unless the context indicates otherwise) include, without limitation, the following:

- Unfavorable market conditions may adversely affect our operating results;
- A reduction or elimination of foreign government subsidies and economic incentives may adversely affect the future order rate for our MOCVD equipment;
- The cyclicity of the industries we serve directly affects our business;
- We operate in industries characterized by rapid technological change;
- We have a concentrated customer base, located primarily in a limited number of regions, which operate in highly concentrated industries;
- We face significant competition;

- The timing of our orders, shipments, and revenue recognition may cause our quarterly operating results to fluctuate significantly;
- Our sales cycle is long and unpredictable;
- Our backlog is subject to customer cancellation or modification which could result in decreased sales, increased inventory obsolescence, and/or liabilities to our suppliers for products no longer needed;
- Our failure to estimate customer demand accurately could result in inventory obsolescence, liabilities to our suppliers for products no longer needed, and/or manufacturing interruptions or delays which could affect our ability to meet customer demand;
- Our failure to successfully manage our outsourcing activities or failure of our outsourcing partners to perform as anticipated could adversely affect our results of operations and our ability to adapt to fluctuating order volumes;
- We rely on a limited number of suppliers, some of whom are our sole source for particular components;
- Our inability to attract, retain, and motivate employees could have a material adverse effect on our business;
- Our acquisition strategy subjects us to risks associated with evaluating and pursuing these opportunities and integrating these businesses;
- Timing of market adoption of LED technology for general lighting is uncertain;
- Our sales to manufacturers are highly dependent on sales of consumer electronics applications, which can experience significant volatility due to seasonal and other factors and materially adversely impact our future results of operations;

Table of Contents

- Our operating results have been, and may continue to be, adversely affected by tightening credit markets;

- We are exposed to the risks of operating a global business, including the need to obtain export licenses for certain of our shipments and political risks in the countries we operate;

- We may be exposed to liabilities under the Foreign Corrupt Practices Act and any determination that we violated these or similar laws could have a material adverse effect on our business;

- We are subject to internal control evaluations and attestation requirements of Section 404 of the Sarbanes-Oxley Act and any delays or difficulty in satisfying these requirements or negative reports concerning our internal controls could adversely affect our future results of operations and our stock price;

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

- Our income taxes can change;

- We may be required to take additional impairment charges on assets;

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

- The enforcement and protection of our intellectual property rights may be expensive and/or divert our limited resources;

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

- We are subject to foreign currency exchange risks;

- If we are subject to cyber-attacks we could incur substantial costs and, if such attacks are successful, we could incur significant liabilities, reputational harm, and disruption to our operations;
- We have adopted certain measures that may have anti-takeover effects which may make an acquisition of our Company by another company more difficult;
- We are subject to risks of non-compliance with environmental, health, and safety regulations;
- Regulations related to conflict minerals will force us to incur additional expenses, may make our supply chain more complex, and may result in damage to our relationships with customers; and
- We have significant operations in locations which could be materially and adversely impacted in the event of a natural disaster, an act of terrorism or other significant disruption.

Consequently, such forward looking statements and estimates should be regarded solely as the current plans and beliefs of Veeco. We do not undertake any obligation to update any forward looking statements to reflect future events or circumstances after the date of such statements.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****Veeco Instruments Inc. and Subsidiaries****Consolidated Balance Sheets**

(in thousands, except share amounts)

| | September 30, 2016 (unaudited) | December 31, 2015 |
|---|--------------------------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 274,018 | \$ 269,232 |
| Short-term investments | 62,835 | 116,050 |
| Accounts receivable, net | 50,463 | 49,524 |
| Inventories | 86,651 | 77,469 |
| Deferred cost of sales | 3,165 | 2,100 |
| Prepaid expenses and other current assets | 19,099 | 22,760 |
| Assets held for sale | 12,129 | 5,000 |
| Total current assets | 508,360 | 542,135 |
| Property, plant and equipment, net | 57,557 | 79,590 |
| Intangible assets, net | 61,812 | 131,674 |
| Goodwill | 114,908 | 114,908 |
| Deferred income taxes | 1,384 | 1,384 |
| Other assets | 21,047 | 21,098 |
| Total assets | \$ 765,068 | \$ 890,789 |
| Liabilities and stockholders equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 27,455 | \$ 30,074 |
| Accrued expenses and other current liabilities | 38,421 | 49,393 |
| Customer deposits and deferred revenue | 79,699 | 76,216 |
| Income taxes payable | 1,825 | 6,208 |
| Current portion of long-term debt | 361 | 340 |
| Total current liabilities | 147,761 | 162,231 |
| Deferred income taxes | 13,146 | 11,211 |
| Long-term debt | 920 | 1,193 |
| Other liabilities | 6,503 | 1,539 |
| Total liabilities | 168,330 | 176,174 |
| Stockholders equity: | | |
| Preferred stock, 500,000 shares authorized; no shares issued and outstanding | | |
| Common stock, \$0.01 par value; 120,000,000 shares authorized; 40,837,811 shares issued and 40,596,820 shares outstanding at September 30, 2016; 40,995,694 shares issued and 40,526,902 shares outstanding at December 31, 2015. | 408 | 410 |
| Additional paid-in capital | 761,975 | 767,137 |
| Accumulated deficit | (163,585) | (45,058) |

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| | | |
|---|-------------------|-------------------|
| Accumulated other comprehensive income | 2,266 | 1,348 |
| Treasury stock, at cost, 240,991 shares at September 30, 2016; 468,792 shares at December 31, 2015. | (4,326) | (9,222) |
| Total stockholders equity | 596,738 | 714,615 |
| Total liabilities and stockholders equity | \$ 765,068 | \$ 890,789 |

See accompanying Notes to the Consolidated Financial Statements.

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Consolidated Statements of Operations**

(in thousands, except per share amounts)

(unaudited)

| | Three months ended September 30, | | Nine months ended September 30, | |
|--------------------------------------|----------------------------------|------------|---------------------------------|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| Net sales | \$ 85,482 | \$ 140,744 | \$ 238,842 | \$ 370,494 |
| Cost of sales | 52,027 | 86,494 | 141,991 | 232,038 |
| Gross profit | 33,455 | 54,250 | 96,851 | 138,456 |
| Operating expenses, net: | | | | |
| Research and development | 19,892 | 19,200 | 63,545 | 57,904 |
| Selling, general, and administrative | 18,396 | 21,905 | 58,230 | 69,153 |
| Amortization of intangible assets | 5,261 | 5,891 | 15,785 | 21,832 |
| Restructuring | 1,798 | 469 | 3,993 | 3,509 |
| Asset impairment | 56,035 | | 69,662 | 126 |
| Other, net | 795 | 207 | 884 | (795) |
| Total operating expenses, net | 102,177 | 47,672 | 212,099 | 151,729 |
| Operating income (loss) | (68,722) | 6,578 | (115,248) | (13,273) |
| Interest income | 283 | 256 | 879 | 787 |
| Interest expense | (23) | (95) | (166) | (345) |
| Income (loss) before income taxes | (68,462) | 6,739 | (114,535) | (12,831) |
| Income tax expense | 1,136 | 1,433 | 2,677 | 9,360 |
| Net income (loss) | \$ (69,598) | \$ 5,306 | \$ (117,212) | \$ (22,191) |
| Income (loss) per common share: | | | | |
| Basic | \$ (1.78) | \$ 0.13 | \$ (2.99) | \$ (0.56) |
| Diluted | \$ (1.78) | \$ 0.13 | \$ (2.99) | \$ (0.56) |
| Weighted average number of shares: | | | | |
| Basic | 39,131 | 40,846 | 39,193 | 39,729 |
| Diluted | 39,131 | 40,979 | 39,193 | 39,729 |

See accompanying Notes to the Consolidated Financial Statements.

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Consolidated Statements of Comprehensive Income (Loss)**

(in thousands)

(unaudited)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|-------------|--|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| Net income (loss) | \$ (69,598) | \$ 5,306 | \$ (117,212) | \$ (22,191) |
| Other comprehensive income (loss), net of tax | | | | |
| Unrealized gain (loss) on available-for-sale securities | (7) | (17) | 32 | 9 |
| Reclassifications from AOCI into net income | | | | (1) |
| Minimum pension liability | | | | |
| Reclassifications from AOCI into net income | 866 | | 866 | |
| Foreign currency translation | (7) | (63) | 20 | (93) |
| Total other comprehensive income (loss), net of tax | 852 | (80) | 918 | (85) |
| Comprehensive income (loss) | \$ (68,746) | \$ 5,226 | \$ (116,294) | \$ (22,276) |

See accompanying Notes to the Consolidated Financial Statements.

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Consolidated Statements of Cash Flows**

(in thousands)

(unaudited)

| | Nine months ended September 30, | |
|--|--|-------------|
| | 2016 | 2015 |
| Cash Flows from Operating Activities | | |
| Net income (loss) | \$ (117,212) | \$ (22,191) |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 26,010 | 30,766 |
| Deferred income taxes | 1,529 | 1,794 |
| Share-based compensation expense | 12,133 | 14,038 |
| Asset impairment | 69,662 | 126 |
| Gain on sale of lab tools | | (841) |
| Provision for bad debts | 160 | |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (1,184) | 13,484 |
| Inventories and deferred cost of sales | (10,909) | (13,029) |
| Prepaid expenses and other current assets | 3,661 | 332 |
| Accounts payable and accrued expenses | (13,995) | 368 |
| Customer deposits and deferred revenue | 3,568 | (7,929) |
| Income taxes receivable and payable, net | 80 | 2,323 |
| Other, net | 2,189 | 2,609 |
| Net cash provided by (used in) operating activities | (24,308) | 21,850 |
| Cash Flows from Investing Activities | | |
| Capital expenditures | (10,717) | (11,069) |
| Proceeds from the sale of investments | 131,297 | 68,647 |
| Payments for purchases of investments | (78,376) | (17,000) |
| Proceeds from sale of building | 693 | |
| Proceeds from sale of lab tools | | 2,648 |
| Other | (230) | (662) |
| Net cash provided by investing activities | 42,667 | 42,564 |
| Cash Flows from Financing Activities | | |
| Proceeds from stock option exercises | 473 | 1,344 |
| Restricted stock tax withholdings | (1,184) | (2,129) |
| Purchases of common stock | (13,349) | |
| Proceeds from employee stock purchase plan | 719 | |
| Repayments of long-term debt | (252) | (233) |
| Net cash used in financing activities | (13,593) | (1,018) |
| Effect of exchange rate changes on cash and cash equivalents | 20 | (93) |
| Net increase in cash and cash equivalents | 4,786 | 63,303 |
| Cash and cash equivalents - beginning of period | 269,232 | 270,811 |
| Cash and cash equivalents - end of period | \$ 274,018 | \$ 334,114 |

Supplemental Disclosure of Cash Flow Information

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| | | | | |
|-------------------|----|-------|----|-------|
| Interest paid | \$ | 179 | \$ | 104 |
| Income taxes paid | | 1,456 | | 6,040 |

See accompanying Notes to the Consolidated Financial Statements.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements

(unaudited)

Note 1 - Basis of Presentation

The accompanying unaudited Consolidated Financial Statements of Veeco have been prepared in accordance with U.S. GAAP as defined in Financial Accounting Standards Board (FASB) Accounting Standards Codification 270 for interim financial information and with the instructions to Rule 10-01 of Securities and Exchange Commission Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements as the interim information is an update of the information that was presented in Veeco's most recent annual financial statements. For further information, refer to Veeco's Consolidated Financial Statements and Notes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2015 (2015 Form 10-K). In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal, recurring nature. **Certain amounts previously reported have been reclassified in the financial statements to conform to the current presentation.**

Veeco reports interim quarters on a 13-week basis ending on the last Sunday of each quarter. The fourth quarter always ends on the last day of the calendar year, December 31. The 2016 interim quarters end on April 3, July 3, and October 2, and the 2015 interim quarters ended on March 29, June 28, and September 27. These interim quarters are reported as March 31, June 30, and September 30 in Veeco's interim consolidated financial statements.

Revenue recognition

Veeco recognizes revenue when all of the following criteria have been met: persuasive evidence of an arrangement exists with a customer; delivery of the specified products has occurred or services have been rendered; prices are contractually fixed or determinable; and collectability is reasonably assured. Revenue is recorded including shipping and handling costs and excluding applicable taxes related to sales.

Contracts with customers frequently contain multiple deliverables, such as systems, upgrades, components, spare parts, maintenance, and service plans. Judgment is required to properly identify the accounting units of the multiple-element arrangements and to determine how the revenue should be allocated among the accounting units. Veeco also evaluates whether multiple transactions with the same customer or related parties should be considered part of a single, multiple-element arrangement based on an assessment of whether the contracts or agreements are negotiated or executed within a short time frame of each other or if there are indicators that the contracts are negotiated in contemplation of one another. Moreover, judgment is used in interpreting the commercial terms and determining when all criteria have been met in order to recognize revenue in the appropriate accounting period.

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When there are separate units of accounting, Veeco allocates revenue to each element based on the following selling price hierarchy: vendor-specific objective evidence (VSOE) if available; third party evidence (TPE) if VSOE is not available; or the best estimate of selling price (BESP) if neither VSOE nor TPE is available. Veeco uses BESP for the majority of the elements in its arrangements. **The maximum revenue recognized on a delivered element is limited to the amount that is not contingent upon the delivery of additional items.**

Veeco considers many facts when evaluating each of its sales arrangements to determine the timing of revenue recognition including its contractual obligations, the customer's creditworthiness, and the nature of the customer's post-delivery acceptance provisions. Veeco's system sales arrangements, including certain upgrades, generally include field acceptance provisions that may include functional or mechanical test procedures. For the majority of the arrangements, a customer source inspection of the system is performed in Veeco's facility or test data is sent to the customer documenting that the system is functioning to the agreed upon specifications prior to delivery. Historically, such source inspection or test data replicates the field acceptance provisions that are performed at the customer's site prior to final acceptance of the system. When Veeco objectively demonstrates that the criteria specified in the contractual acceptance provisions are achieved prior to delivery, revenue is recognized upon system delivery since there is no substantive contingency remaining related to the acceptance provisions at that date, subject to the retention amount constraint described below. For new products, new applications of existing products, or for products with substantive customer acceptance provisions

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

where Veeco cannot objectively demonstrate that the criteria specified in the contractual acceptance provisions have been achieved prior to delivery, revenue and the associated costs are deferred and fully recognized upon the receipt of final customer acceptance, assuming all other revenue recognition criteria have been met.

Veeco's system sales arrangements, including certain upgrades, generally do not contain provisions for the right of return, forfeiture, refund, or other purchase price concessions. In the rare instances where such provisions are included, all revenue is deferred until such rights expire. The sales arrangements generally include installation. The installation process is not deemed essential to the functionality of the equipment since it is not complex; it does not require significant changes to the features or capabilities of the equipment or involve constructing elaborate interfaces or connections subsequent to factory acceptance. Veeco has a demonstrated history of consistently completing installations in a timely manner and can reliably estimate the costs of such activities. Most customers engage Veeco to perform the installation services, although there are other third-party providers with sufficient knowledge who could complete these services. Based on these factors, installation is deemed to be inconsequential or perfunctory relative to the system sale as a whole, and as a result, installation service is not considered a separate element of the arrangement. As such, Veeco records the cost of the installation at the earlier of the time of revenue recognition for the system or when installation services are performed.

In many cases Veeco's products are sold with a billing retention, typically 10% of the sales price, which is billed by Veeco and payable by the customer when field acceptance provisions are completed. The amount of revenue recognized upon delivery of a system or upgrade, if any, is limited to the lower of i) the amount billed that is not contingent upon acceptance provisions or ii) the value of the arrangement consideration allocated to the delivered elements, if such sale is part of a multiple-element arrangement.

Veeco's contractual terms with customers in Japan generally specify that title and risk and rewards of ownership transfer upon customer acceptance. A distributor is used for almost all sales to customers in Japan. Title passes to the distributor upon shipment; however, due to customary local business practices, generally the risk and rewards of ownership of the systems transfer to the end-customers upon their acceptance. As a result, for customers in Japan, Veeco recognizes revenue upon receipt of written acceptance from the end-customer.

Veeco recognizes revenue related to maintenance and service contracts ratably over the applicable contract term. Veeco recognizes revenue from the sales of components, spare parts, and specified service engagements at the time of delivery in accordance with the terms of the applicable sales arrangement.

Incremental direct costs incurred related to the acquisition of a customer contract, such as sales commissions, are expensed as incurred, even if the related revenue is deferred in accordance with the above policy.

Recent accounting pronouncements

In May 2014, the FASB issued Accounting Standards Update (ASU) 2014-09, as amended: *Revenue from Contracts with Customers*, which has been codified as Accounting Standards Codification 606 (ASC606). ASC606 requires Veeco s revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which Veeco expects to be entitled in exchange for those goods or services. ASC606 outlines a five-step model to make the revenue recognition determination and requires new financial statement disclosures. Publicly-traded companies are required to adopt ASC606 for reporting periods beginning after December 15, 2017. ASC606 provides for different transition alternatives. Veeco has not yet determined which method of adoption will be selected. Veeco is evaluating the impact of adopting ASC606 on its consolidated financial statements and related financial statement disclosures. A preliminary assessment of ASC606 indicates that the billing retention will no longer impact the timing of revenue recognition. As a result, a small portion of revenue for system sales arrangements may be recognized earlier under ASC606 than it is under current U.S. GAAP.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

In January 2016, the FASB issued ASU 2016-01: *Financial Instruments - Overall*, which requires certain equity investments to be measured at fair value, with changes in fair value recognized in net income. Publicly-traded companies are required to adopt the update for reporting periods beginning after December 15, 2017; early adoption is permitted. Veeco does not expect this ASU will have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02: *Leases*, which generally requires Veeco's operating lessee rights and obligations to be recognized as assets and liabilities on the Balance Sheet. In addition, interest on lease liabilities is to be recognized separately from the amortization of right-of-use assets in the Statement of Operations. Further, payments of the principal portion of lease liabilities are to be classified as financing activities while payments of interest on lease liabilities and variable lease payments are to be classified as operating activities in the Statement of Cash Flows. When the standard is adopted, Veeco will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, with early application permitted. Veeco is evaluating the impact of adopting the ASU on its consolidated financial statements.

Veeco is also evaluating other pronouncements recently issued but not yet adopted. The adoption of these pronouncements is not expected to have a material impact on Veeco's consolidated financial statements.

Change in Accounting Principle

In March 2016, the FASB issued ASU 2016-09 *Stock Compensation: Improvements to Employee Share-Based Payment Accounting*. Veeco adopted the ASU during the first quarter of 2016. Beginning in 2016, excess tax benefits and deficiencies are recognized as income tax expense or benefit in the income statement in the reporting period incurred. In conjunction with adopting the ASU, Veeco has made an accounting policy election to account for forfeitures when they occur. The ASU transition guidance requires that this election be applied on a modified retrospective basis through a cumulative-effect adjustment to retained earnings as of the beginning of the period in which the ASU is effective. Accordingly, Veeco recorded a \$1.3 million charge to the opening accumulated deficit balance with a corresponding adjustment to additional paid-in capital, resulting in no impact to the opening balance of total stockholders' equity. In addition, Veeco recorded additional deferred tax assets with an equally offsetting valuation allowance of \$2.4 million.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

Note 2 - Income (Loss) Per Common Share

Basic income (loss) per common share is computed using the two-class method by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted income per common share is calculated by dividing net income available to common stockholders by the weighted average number of common shares and common share equivalents outstanding during the period. The dilutive effect of outstanding options to purchase common stock and non-participating restricted share awards and restricted share units is considered in diluted income per common share by application of the treasury stock method. The dilutive effect of performance share units is included in diluted income per common share in the periods the performance targets have been achieved. The computations of basic and diluted income (loss) per common share for the three and nine months ended September 30, 2016 and 2015 are as follows:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|--|----------|---------------------------------|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands, except per share amounts) | | | |
| Net income (loss) | \$ (69,598) | \$ 5,306 | \$ (117,212) | \$ (22,191) |
| Net income (loss) per common share: | | | | |
| Basic | \$ (1.78) | \$ 0.13 | \$ (2.99) | \$ (0.56) |
| Diluted | \$ (1.78) | \$ 0.13 | \$ (2.99) | \$ (0.56) |
| Basic weighted average shares outstanding | 39,131 | 40,846 | 39,193 | 39,729 |
| Effect of potentially dilutive share-based awards | | 133 | | |
| Diluted weighted average shares outstanding | 39,131 | 40,979 | 39,193 | 39,729 |
| Unvested participating shares excluded from basic weighted average shares outstanding since the securityholders are not obligated to fund losses | 469 | | 469 | 1,076 |
| Common share equivalents excluded from the diluted weighted average shares outstanding since Veeco incurred a net loss and their effect would be antidilutive | 140 | | 45 | 165 |
| Potentially dilutive non-participating shares excluded from the diluted calculation as their effect would be antidilutive | 2,030 | 2,264 | 2,042 | 2,066 |

Note 3 - Assets

Investments

Marketable securities are generally classified as available-for-sale and reported at fair value, with unrealized gains and losses, net of tax, presented as a separate component of stockholders' equity under the caption "Accumulated other comprehensive income" in the Consolidated Balance Sheets. These securities may include U.S. treasuries, government agency securities, corporate debt, and commercial paper, all with maturities of greater than three months when purchased. All realized gains and losses and unrealized losses resulting from declines in fair value that are other than temporary are included in "Other, net" in the Consolidated Statements of Operations.

Fair value is the price that would be received for an asset or the amount paid to transfer a liability in an orderly transaction between market participants. Veeco classifies certain assets based on the following fair value hierarchy:

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to the Consolidated Financial Statements - continued****(unaudited)**

Level 1: Quoted prices in active markets that are unadjusted and accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2: Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or financial instruments for which significant inputs are observable, either directly or indirectly; and

Level 3: Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Veeco has evaluated the estimated fair value of financial instruments using available market information and valuations as provided by third-party sources. The use of different market assumptions and/or estimation methodologies could have a significant effect on the estimated fair value amounts.

The following table presents the portion of Veeco's assets that were measured at fair value on a recurring basis at September 30, 2016 and December 31, 2015:

| | Level 1 | Level 2 | Level 3 | Total |
|-------------------------------|------------------|------------------|-----------|------------------|
| | (in thousands) | | | |
| September 30, 2016 | | | | |
| Short-term investments | | | | |
| U.S. treasuries | \$ 40,043 | \$ | \$ | \$ 40,043 |
| Government agency securities | | 5,016 | | 5,016 |
| Corporate debt | | 13,789 | | 13,789 |
| Commercial paper | | 3,987 | | 3,987 |
| Total | \$ 40,043 | \$ 22,792 | \$ | \$ 62,835 |
| December 31, 2015 | | | | |
| Cash equivalents | | | | |
| U.S. treasuries | \$ 9,999 | \$ | \$ | \$ 9,999 |
| Government agency securities | | 4,998 | | 4,998 |
| Commercial paper | | 2,999 | | 2,999 |
| Total | 9,999 | 7,997 | | 17,996 |

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| Short-term investments | | | | | |
|-------------------------------|------------------|------------------|-----------|-----------|----------------|
| U.S. treasuries | 94,918 | | | | 94,918 |
| Government agency securities | | 12,988 | | | 12,988 |
| Corporate debt | | 8,144 | | | 8,144 |
| Total | \$ 94,918 | \$ 21,132 | \$ | \$ | 116,050 |

There were no transfers between fair value measurement levels during the three and nine months ended September 30, 2016.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

At September 30, 2016 and December 31, 2015, the amortized cost and fair value of available-for-sale securities consist of:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|------------------------------|-------------------|------------------------------|-------------------------------|-------------------------|
| (in thousands) | | | | |
| September 30, 2016 | | | | |
| U.S. treasuries | \$ 40,033 | \$ 10 | \$ | \$ 40,043 |
| Government agency securities | 5,016 | | | 5,016 |
| Corporate debt | 13,799 | | (10) | 13,789 |
| Commercial paper | 3,987 | | | 3,987 |
| Total | \$ 62,835 | \$ 10 | \$ (10) | \$ 62,835 |
| December 31, 2015 | | | | |
| U.S. treasuries | \$ 94,935 | \$ 6 | \$ (23) | \$ 94,918 |
| Government agency securities | 12,985 | 3 | | 12,988 |
| Corporate debt | 8,144 | 1 | (1) | 8,144 |
| Total | \$ 116,064 | \$ 10 | \$ (24) | \$ 116,050 |

Available-for-sale securities in a loss position at September 30, 2016 and December 31, 2015 consist of:

| | September 30, 2016 | | December 31, 2015 | |
|------------------------------|-------------------------|-------------------------------|-------------------------|-------------------------------|
| | Estimated Fair Value | Gross Unrealized Losses | Estimated Fair Value | Gross Unrealized Losses |
| (in thousands) | | | | |
| Government agency securities | \$ | \$ | \$ 64,922 | \$ (23) |
| Corporate debt | 13,789 | (10) | 3,353 | (1) |
| Total | \$ 13,789 | \$ (10) | \$ 68,275 | \$ (24) |

At September 30, 2016 and December 31, 2015, there were no short-term investments that had been in a continuous loss position for more than 12 months.

The available-for-sale securities at September 30, 2016 all contractually mature in one year or less. Actual maturities may differ from contractual maturities. Veeco may sell these securities prior to maturity based on the needs of the business. In addition, borrowers may have the right to call or prepay obligations prior to scheduled maturities.

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There were minimal realized gains for the three and nine months ended September 30, 2016 and 2015. The cost of securities liquidated is based on specific identification.

Accounts receivable

Accounts receivable is presented net of an allowance for doubtful accounts of \$0.3 million and \$0.2 million at September 30, 2016 and December 31, 2015, respectively.

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to the Consolidated Financial Statements - continued****(unaudited)***Inventories*

Inventories are stated at the lower of cost or net realizable value on a first-in, first-out basis. Inventories at September 30, 2016 and December 31, 2015 consist of the following:

| | September 30, 2016 | | December 31, 2015 |
|-----------------|-------------------------------|-----------|------------------------------|
| | (in thousands) | | |
| Materials | \$ 50,370 | \$ | 42,373 |
| Work-in-process | 30,960 | | 30,327 |
| Finished goods | 5,321 | | 4,769 |
| Total | \$ 86,651 | \$ | 77,469 |

Prepaid expenses and other current assets

Prepaid expenses and other current assets primarily consist of supplier deposits, prepaid value-added tax, lease deposits, prepaid insurance, and prepaid licenses. Veeco had deposits with its suppliers of \$13.1 million and \$14.6 million at September 30, 2016 and December 31, 2015, respectively.

Assets held for sale

During the second quarter of 2016, the Company undertook initiatives to streamline operations, enhance efficiency, and reduce costs. As part of that initiative, the Company listed its facility in Yongin-city, South Korea for sale. At that time, Veeco determined that the carrying value of the building exceeded its fair market value, less cost to sell, and recorded an impairment charge. During the third quarter of 2016, Veeco engaged potential buyers and re-evaluated market conditions for the building. As a result, Veeco updated its assessment of fair market value and increased the carrying value of the building by \$1.6 million, which is still lower than the original pre-impairment carrying value. The increase in the carrying value was recorded as a contra-impairment charge in the Consolidated Statements of Operations.

During the third quarter of 2016, Veeco sold its building in Hyeongok-ri, South Korea, which had been designated as held for sale in the second quarter of 2016, at a price which approximated carrying value. The Company also continues to market one of its properties in St. Paul, Minnesota. The carrying value of assets held for sale reflects Veeco's estimate of fair value less costs to sell using the sales comparison market approach.

Property, plant, and equipment

Property, plant, and equipment at September 30, 2016 and December 31, 2015 consist of the following:

| | September 30, 2016 | December 31, 2015 |
|---|-----------------------|----------------------|
| | (in thousands) | |
| Land | \$ 5,061 | \$ 9,592 |
| Building and improvements | 47,242 | 54,622 |
| Machinery and equipment(1) | 98,220 | 110,075 |
| Leasehold improvements | 3,771 | 5,554 |
| Gross property, plant and equipment | 154,294 | 179,843 |
| Less: accumulated depreciation and amortization | 96,737 | 100,253 |
| Net property, plant, and equipment | \$ 57,557 | \$ 79,590 |

(1) Machinery and equipment also includes software, furniture and fixtures

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to the Consolidated Financial Statements - continued****(unaudited)**

For the three and nine months ended September 30, 2016, depreciation expense was \$3.5 million and \$10.2 million, respectively, and \$3.2 million and \$8.9 million for the comparable 2015 periods. During the second quarter of 2016, and as part of the Company's efforts to streamline operations, enhance efficiency, and reduce costs, the Company removed certain lab equipment that was no longer required and recorded a non-cash impairment charge of \$6.1 million. In addition, during the second quarter of 2016, land and buildings with a net carrying value of \$13.7 million were classified as assets held for sale on the Consolidated Balance Sheets. During the third quarter of 2016, the Company decided to significantly reduce future investments in its Atomic Layer Deposition (ALD) technology development and, as a result, recorded a charge for impairment of its ALD assets, including a \$3.3 million impairment of property, plant, and equipment.

Goodwill

Goodwill represents the future economic benefits arising from assets acquired in a business combination that are not individually identified and separately recognized. There were no changes to goodwill during the nine months ended September 30, 2016.

Intangible assets

Intangible assets consist of purchased technology, customer-related intangible assets, patents, trademarks (both long-lived and indefinite-lived), covenants not-to-compete, and software licenses and are initially recorded at fair value. Long-lived intangibles are amortized over their estimated useful lives in a method reflecting the pattern in which the economic benefits are consumed or amortized on a straight-line basis if such pattern cannot be reliably determined.

During the third quarter of 2016, the Company decided to significantly reduce future investments in its ALD technology development and, as a result, recorded a charge for impairment of its ALD assets, including \$54.3 million for the full impairment of the intangible purchased ALD technology. The impairment charges were based on projected cash flows that required the use of unobservable inputs.

The components of purchased intangible assets at September 30, 2016 and December 31, 2015 consist of the following:

| | September 30, 2016 | | | December 31, 2015 | | |
|--|-----------------------|---|------------|-----------------------|---|------------|
| | Gross Carrying Amount | Accumulated Amortization and Impairment | Net Amount | Gross Carrying Amount | Accumulated Amortization and Impairment | Net Amount |

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(in thousands)

| | | | | | | | | | | | | |
|----------------------------|----|---------|----|---------|----|--------|----|---------|----|---------|----|---------|
| Technology | \$ | 222,358 | \$ | 185,341 | \$ | 37,017 | \$ | 222,358 | \$ | 120,496 | \$ | 101,862 |
| Customer relationships | | 47,885 | | 27,111 | | 20,774 | | 47,885 | | 22,470 | | 25,415 |
| Trademarks and tradenames | | 2,590 | | 1,910 | | 680 | | 2,730 | | 1,937 | | 793 |
| Indefinite-lived trademark | | 2,900 | | | | 2,900 | | 2,900 | | | | 2,900 |
| Other | | 2,026 | | 1,585 | | 441 | | 6,241 | | 5,537 | | 704 |
| Total | \$ | 277,759 | \$ | 215,947 | \$ | 61,812 | \$ | 282,114 | \$ | 150,440 | \$ | 131,674 |

Other intangible assets primarily consist of patents, licenses, and non-compete agreements.

Other assets

Veeco has an ownership interest of less than 20% in a non-marketable investment, Kateeva, Inc. (Kateeva). Veeco does not exert significant influence over Kateeva and therefore the investment is carried at cost. There was no change to the \$21.0 million carrying value of the investment during the nine months ended September 30, 2016. The investment is

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to the Consolidated Financial Statements - continued****(unaudited)**

included in Other assets on the Consolidated Balance Sheet. The investment is subject to a periodic impairment review; as there are no open-market valuations, the impairment analysis requires judgment. The analysis includes assessments of Kateeva's financial condition, the business outlook for its products and technology, its projected results and cash flow, business valuation indications from recent rounds of financing, the likelihood of obtaining subsequent rounds of financing, and the impact of equity preferences held by Veeco relative to other investors. Fair value of the investment is not estimated unless there are identified events or changes in circumstances that could have a significant adverse effect on the fair value of the investment. No such events or circumstances are present.

Note 4 - Liabilities*Accrued expenses and other current liabilities*

The components of accrued expenses and other current liabilities at September 30, 2016 and December 31, 2015 consist of:

| | September 30, 2016 | December 31, 2015 |
|------------------------------|-----------------------|----------------------|
| | (in thousands) | |
| Payroll and related benefits | \$ 22,830 | \$ 30,917 |
| Warranty | 4,849 | 8,159 |
| Professional fees | 1,795 | 2,224 |
| Installation | 1,826 | 1,110 |
| Sales, use, and other taxes | 953 | 1,132 |
| Restructuring liability | 2,053 | 824 |
| Other | 4,115 | 5,027 |
| Total | \$ 38,421 | \$ 49,393 |

Other liabilities include accruals for costs related to customer training, royalties, and travel.

Warranty

Warranties are typically valid for one year from the date of system final acceptance, and Veeco estimates the costs that may be incurred under the warranty. Estimated warranty costs are determined by analyzing specific product and historical configuration statistics and regional warranty support costs and are 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. Changes in product warranty reserves for the nine months ended September 30, 2016 include:

| | (in thousands) | |
|-------------------------------------|----------------|---------|
| Balance - December 31, 2015 | \$ | 8,159 |
| Warranties issued | | 3,223 |
| Consumption of reserves | | (5,739) |
| Changes in estimate | | (794) |
| Balance - September 30, 2016 | \$ | 4,849 |

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to the Consolidated Financial Statements - continued****(unaudited)***Restructuring accruals*

During the nine months ended September 30, 2016, additional accruals were recognized and payments made related to previous years restructuring initiatives. During the second and third quarters of 2016, the Company undertook additional restructuring activities as part of its initiative to streamline operations, enhance efficiency, and reduce costs. As a result of these actions, the Company notified approximately 50 employees of their termination from the Company and recorded restructuring charges related to these actions of \$2.9 million, consisting of \$2.8 million of personnel severance and related costs and \$0.1 million of facility closing costs. In addition, during the third quarter of 2016, the Company decided to significantly reduce future investments in its ALD technology development, which impacts approximately 25 additional employees. As a result, the Company recorded personnel severance and related restructuring charges of \$0.9 million in the third quarter of 2016. Over the next few quarters, the Company expects to incur additional restructuring costs of \$4 to \$7 million as it finalizes all of these activities.

| | Personnel Severance and Related Costs | Facility Closing Costs (in thousands) | Total |
|-------------------------------------|--|--|-----------------|
| Balance - December 31, 2015 | \$ 824 | \$ | \$ 824 |
| Provision | 3,721 | 274 | 3,995 |
| Changes in estimate | (2) | | (2) |
| Payments | (2,490) | (274) | (2,764) |
| Balance - September 30, 2016 | \$ 2,053 | \$ | \$ 2,053 |

Customer deposits

Customer deposits totaled \$25.8 million and \$28.2 million at September 30, 2016 and December 31, 2015, respectively.

Long-term debt

Debt consists of a mortgage note payable with a carrying value of \$1.3 million and \$1.5 million at September 30, 2016 and December 31, 2015, respectively. The mortgage note payable is secured by certain land and buildings. One of the buildings is currently held for sale. The annual interest rate on the mortgage is 7.91%, and the final payment is due on January 1, 2020. Veeco estimated the mortgage fair value as \$1.3 million and \$1.6 million at September 30, 2016 and December 31, 2015, respectively, using a discounted cash flow model.

Other Liabilities

Other liabilities primarily consist of income taxes payable and other liabilities not expected to be paid within one year. Non-current income taxes payable were \$4.9 million and less than \$0.1 million at September 30, 2016 and December 31, 2015, respectively.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

Note 5 - Commitments and Contingencies

Minimum lease commitments

At September 30, 2016, Veeco's total future minimum lease payments under non-cancelable operating leases have not changed significantly from the disclosure in the 2015 Form 10-K.

Purchase commitments

Veeco has purchase commitments of \$60.1 million at September 30, 2016, substantially all of which become due within one year.

Bank guarantees

Veeco has bank guarantees and letters of credit issued by a financial institution on its behalf as needed. At September 30, 2016, outstanding bank guarantees and letters of credit totaled \$5.3 million, and unused bank guarantees and letters of credit of \$59.8 million were available to be drawn upon.

Legal proceedings

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

Note 6 - Equity

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Accumulated Other Comprehensive Income (AOCI)

The following table presents the changes in the balances of each component of AOCI, net of tax:

| | Foreign Currency Translation | Minimum Pension Liability | Unrealized Gains (Losses) on Available for Sale Securities | Total |
|--|---------------------------------|------------------------------|---|----------|
| | (in thousands) | | | |
| Balance - December 31, 2015 | \$ 2,246 | \$ (866) | \$ (32) | \$ 1,348 |
| Other comprehensive income, before taxes | 20 | 1,290 | 14 | 1,324 |
| Provision for income taxes | | (424) | 18 | (406) |
| Other comprehensive income, net of tax | 20 | 866 | 32 | 918 |
| Balance - September 30, 2016 | \$ 2,266 | \$ | \$ | \$ 2,266 |

Late in 2015, the Company began the process to terminate a defined benefit plan it had acquired in the year 2000. The plan had been frozen as of September 30, 1991, and no further benefits have been accrued by participants since that date. In connection with the termination, responsibility for the payment of benefits under the plan was transferred to an insurance company during the third quarter of 2016. As a result, the Company reclassified the minimum pension liability of \$1.3 million and the \$0.4 million income tax benefit from AOCI to Other, net and Income tax expense, respectively, on the Consolidated Statements of Operations.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

Note 7 - Share-based compensation

Restricted share awards are issued to employees that are subject to specified restrictions and a risk of forfeiture. The restrictions typically lapse over one to five years and may entitle holders to dividends and voting rights. Other types of share-based compensation include performance share awards, performance share units, and restricted share units (collectively with restricted share awards, restricted shares), as well as options to purchase common stock.

Share-based compensation expense was recognized in the following line items in the Consolidated Statements of Operations for the three and nine months ended September 30, 2016 and 2015

| | Three months ended September 30, | | Nine months ended September 30, | |
|--------------------------------------|----------------------------------|-----------------|---------------------------------|------------------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | | |
| Cost of sales | \$ 607 | \$ 787 | \$ 1,639 | \$ 2,102 |
| Research and development | 993 | 1,044 | 3,032 | 2,739 |
| Selling, general, and administrative | 2,143 | 3,288 | 7,462 | 9,197 |
| Total | \$ 3,743 | \$ 5,119 | \$ 12,133 | \$ 14,038 |

For the nine months ended September 30, 2016, equity activity related to stock options was as follows:

| | Number of Shares (in thousands) | Weighted Average Exercise Price |
|-------------------------------------|---------------------------------------|---------------------------------------|
| Balance - December 31, 2015 | 2,064 | \$ 32.91 |
| Granted | | |
| Exercised | (193) | 12.12 |
| Expired or forfeited | (170) | 34.28 |
| Balance - September 30, 2016 | 1,701 | \$ 35.13 |

For the nine months ended September 30, 2016, equity activity related to restricted shares and performance shares was as follows:

Weighted Average

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| | Number of Shares (in thousands) | | Grant Date Fair Value |
|-------------------------------------|---------------------------------------|----|--------------------------|
| Balance - December 31, 2015 | 1,398 | \$ | 31.97 |
| Granted | 1,138 | | 17.13 |
| Released | (208) | | 33.10 |
| Forfeited | (173) | | 28.33 |
| Balance - September 30, 2016 | 2,155 | \$ | 24.31 |

Note 8 - Income Taxes

Income taxes are estimated for each of the jurisdictions in which the Company operates. Deferred income taxes reflect the net tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, as well as the tax effect of carryforwards. A valuation allowance is recorded to reduce deferred tax assets to the amount that is more likely than not to be realized. Realization of net

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to the Consolidated Financial Statements - continued****(unaudited)**

deferred tax assets is dependent on future taxable income.

At the end of each interim reporting period, the effective tax rate is aligned to expectations for the full year. This estimate is used to determine the income tax provision on a year-to-date basis and may change in subsequent interim periods. Income (loss) before income taxes and income tax expense for the three and nine months ended September 30, 2016 and 2015 were as follows:

| | Three months ended September 30, | | Nine months ended September 30, | |
|--------------------------|---|-------------|--|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | | |
| Loss before income taxes | \$ (68,462) | \$ 6,739 | \$ (114,535) | \$ (12,831) |
| Income tax expense | \$ 1,136 | \$ 1,433 | \$ 2,677 | \$ 9,360 |

For the three months ended September 30, 2016, the \$1.1 million net expense for income taxes included \$0.3 million relating to Veeco's U.S. operations and \$0.8 million relating to Veeco's non-U.S. operations. For the nine months ended September 30, 2016, the \$2.7 million net expense for income taxes included \$1.2 million relating to Veeco's U.S. operations and \$1.5 million relating to Veeco's non-U.S. operations. For the three and nine months ended September 30, 2016, Veeco did not provide a current tax benefit on U.S. pre-tax losses as the amounts are not realizable on a more-likely-than-not basis. The U.S. tax expense is primarily related to U.S. tax amortization expense of indefinite-lived intangible assets that is not available to offset existing deferred tax assets.

For three and nine months ended September 30, 2015, Veeco did not provide a current tax benefit on U.S. pre-tax losses as the amounts are not realizable on a more-likely-than-not basis. The U.S. tax expense is primarily related to withholding taxes and is also related to U.S. tax amortization expense of indefinite-lived intangible assets that is not available to offset existing deferred tax assets.

Note 9 - Segment Reporting and Geographic Information

Veeco operates and measures its results in one operating segment and therefore has one reportable segment: the design, development, manufacture, and support of thin film process equipment primarily sold to make electronic devices.

Veeco categorizes its sales into the following four end-markets:

Lighting, Display & Power Electronics

Lighting refers to Light Emitting Diode (LED); semiconductor illumination sources used in various applications including backlights, general lighting, automotive running lights, and head lamps. Display refers to LED displays including outdoor display/signage applications. Power Electronics refers to GaN-on-Silicon semiconductor devices such as rectifiers, inverters, and converters for the control and conversion of electric power.

Advanced Packaging, MEMS & RF

Advanced Packaging includes a portfolio of wafer-level assembly technologies that enable the miniaturization and performance improvement of electronic products, such as smartphones, smartwatches, tablets, and laptops. Micro-Electro Mechanical Systems (MEMS) includes tiny mechanical devices such as sensors, switches, mirrors, and actuators embedded in semiconductor chips used in vehicles, smartphones, tablets, and games. Radio Frequency (RF) includes semiconductor devices that make use of radio waves (RF fields) for wireless broadcasting and/or communications.

Scientific & Industrial

Scientific refers to advanced materials research at university research institutions, industry research institutions, industry

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

consortiums, and government research agencies. Industrial refers to large-scale product manufacturing applications including optical coatings: thin layers of material deposited on a lens or mirror that alters how light reflects and transmits; extreme ultraviolet (EUV) photomask: an opaque plate that allows light to shine through in a defined pattern for use in photolithography; front end semiconductor: early steps in the process of integrated circuit fabrication where the microchips are created but still remain on the silicon wafer; and high power lasers such as fiber lasers used for industrial materials processing.

Data Storage

The Data Storage end-market refers to the archiving of data in electromagnetic or other forms for use by a computer or device, including hard disk drives used in large capacity storage applications.

Sales by end-market and geographic region for the three and nine months ended September 30, 2016 and 2015 were as follows:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---------------------------------------|----------------------------------|-------------------|---------------------------------|-------------------|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | | |
| Sales by end-market | | | | |
| Lighting, Display & Power Electronics | \$ 49,427 | \$ 94,302 | \$ 97,132 | \$ 240,751 |
| Advanced Packaging, MEMS & RF | 12,092 | 13,541 | 52,400 | 40,545 |
| Scientific & Industrial | 13,938 | 14,897 | 48,675 | 46,493 |
| Data Storage | 10,025 | 18,004 | 40,635 | 42,705 |
| Total | \$ 85,482 | \$ 140,744 | \$ 238,842 | \$ 370,494 |
| Sales by geographic region | | | | |
| United States | \$ 19,104 | \$ 19,405 | \$ 66,550 | \$ 67,006 |
| China | 21,238 | 81,156 | 54,621 | 191,874 |
| EMEA(1) | 19,703 | 21,304 | 61,999 | 51,618 |
| Rest of World | 25,437 | 18,879 | 55,672 | 59,996 |
| Total | \$ 85,482 | \$ 140,744 | \$ 238,842 | \$ 370,494 |

(1) EMEA consists of Europe, the Middle East, and Africa

For geographic reporting, sales are attributed to the location in which the customer facility is located.

Table of Contents

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

Cautionary Statement Regarding Forward Looking Statements

Our discussion below 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. When used in this Report, the words believes, anticipates, expects, estimates, targets, plans, intends, will, and similar expressions related to the future 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. You should not place undue reliance on any forward-looking statements, which speak only as of the dates they are made.

Executive Summary

We create process equipment that enables technologies for a cleaner, more productive and connected world. We design, develop, manufacture, market, and service thin film process equipment to meet the demands of key global trends such as improving energy efficiency, enhancing mobility, and increasing connectivity. Our equipment is used to make electronic devices which enable these trends, including light emitting diodes (LEDs), micro-electromechanical systems (MEMS), wireless devices, power electronics, hard disk drives (HDDs), and semiconductors.

We develop highly differentiated, best-in-class equipment for critical performance steps in thin film processing. Our products provide leading technology solutions with competitive cost-of-ownership. Core competencies in advanced thin film technologies and decades of specialized process know-how help us stay at the forefront of these rapidly advancing industries.

Our solutions sell into four key end-markets: Lighting, Display & Power Electronics; Advanced Packaging, MEMS & RF; Scientific & Industrial; and Data Storage.

Sales in the Lighting, Display & Power Electronics markets increased in the third quarter, reflecting an improvement in LED industry conditions. Following a prolonged period of weakness, demand for TV display backlighting has started to stabilize and consume excess LED capacity. As a result, LED chip manufacturers have begun to make capital investments to support ongoing growth in LED demand for general lighting, signage, and automotive applications. While we have limited long-term visibility, we believe these trends are positive for metal organic chemical vapor deposition (MOCVD) demand in the near term. Our broad portfolio of MOCVD technologies has been developed to support the most significant industry trends, including developing mid-power LEDs, utilizing larger wafer sizes, and optimizing cost-of-ownership. Our TurboDisc® EPIK 700 Gallium-Nitride (GaN) MOCVD system continues to win new business for blue LEDs. Our recently introduced TurboDisc K475i Arsenic-Phosphide (AsP) MOCVD system targets red-orange-yellow LEDs, laser diodes, and high-efficiency triple junction photovoltaic solar cells and has quickly gained market momentum.

Following record sales in the first half of the year, sales in the Advanced Packaging, MEMS & RF markets declined in the third quarter. RF applications represented the largest portion of sales in these markets as customers made incremental investments to support next generation

mobile devices. We continue to focus on expanding into the advanced packaging markets with our Precision Surface Processing (PSP) product family. Our versatile PSP product architecture is well suited for a multitude of advanced packaging process schemes, including WLFO (wafer level fan out) and 3D TSV (thru silicon via) applications.

Sales in the Scientific & Industrial market were comprised of a broad range of customers, spanning multiple product lines. Our SPECTOR ion beam deposition products represented the largest component of these sales. SPECTOR is used by optical coating suppliers to manufacture a variety of products including laser mirrors, optical fibers, and anti-reflective coatings. We continue to win a majority of research opportunities, supported by our molecular beam epitaxy (MBE) GENXplor R&D product. Our MBE systems enable universities and research consortia to conduct advanced materials research. Our MBE systems are also used for production applications, such as fiber lasers, where high volume throughput

Table of Contents

and low cost of ownership are required. The diverse customer base represented by the Industrial & Scientific markets support ongoing demand for our products; however, sales can be highly variable quarter to quarter.

Sales in the Data Storage market were lower in the third quarter, although disk drive manufacturers continued to make incremental investments to upgrade their installed base of equipment. This mature market is facing softening demand for personal computers in the near term and a shift from HDDs to solid state drives in the longer term. Accordingly, our customers in the HDD industry are not expected to make significant investments in new capacity. This is consistent with recent experience that investments are being made on an as-needed basis. Orders are expected to continue to fluctuate from quarter to quarter.

Results of Operations**For the three months ended September 30, 2016 and 2015**

The following table presents operating results as a percentage of net sales, as well as period-over-period dollar and percentage changes for those line items. Our results of operations are reported as one business segment.

| | Three months ended September 30, | | | | Change | | | | |
|--------------------------------------|----------------------------------|----------|-------|----|------------------|------|----|----------|-------|
| | 2016 | | 2015 | | Period to Period | | | | |
| | (dollars in thousands) | | | | | | | | |
| Net sales | \$ | 85,482 | 100% | \$ | 140,744 | 100% | \$ | (55,262) | (39)% |
| Cost of sales | | 52,027 | 61% | | 86,494 | 61% | | (34,467) | (40)% |
| Gross profit | | 33,455 | 39% | | 54,250 | 39% | | (20,795) | (38)% |
| Operating expenses, net: | | | | | | | | | |
| Research and development | | 19,892 | 23% | | 19,200 | 14% | | 692 | 4% |
| Selling, general, and administrative | | 18,396 | 22% | | 21,905 | 16% | | (3,509) | (16)% |
| Amortization | | 5,261 | 6% | | 5,891 | 4% | | (630) | (11)% |
| Restructuring | | 1,798 | 2% | | 469 | 0% | | 1,329 | * |
| Asset impairment | | 56,035 | 66% | | | 0% | | 56,035 | * |
| Other, net | | 795 | 1% | | 207 | 0% | | 588 | * |
| Total operating expenses, net | | 102,177 | 120% | | 47,672 | 34% | | 54,505 | 114% |
| Operating income (loss) | | (68,722) | (80)% | | 6,578 | 5% | | (75,300) | * |
| Interest income, net | | 260 | 0% | | 161 | 0% | | 99 | 61% |
| Income (loss) before income taxes | | (68,462) | (80)% | | 6,739 | 5% | | (75,201) | * |
| Income tax expense | | 1,136 | 1% | | 1,433 | 1% | | (297) | (21)% |
| Net income (loss) | \$ | (69,598) | (81)% | \$ | 5,306 | 4% | \$ | (74,904) | * |

* Not meaningful

Table of Contents*Net Sales*

The following is an analysis of sales by market and by region:

| | Three months ended September 30, | | | | Change | |
|---------------------------------------|----------------------------------|------|------------|------|------------------|-------|
| | 2016 | | 2015 | | Period to Period | |
| | (dollars in thousands) | | | | | |
| Sales by market | | | | | | |
| Lighting, Display & Power Electronics | \$ 49,427 | 58% | \$ 94,302 | 67% | \$ (44,875) | (48)% |
| Advanced Packaging, MEMS & RF | 12,092 | 14% | 13,541 | 10% | (1,449) | (11)% |
| Scientific & Industrial | 13,938 | 16% | 14,897 | 10% | (959) | (6)% |
| Data Storage | 10,025 | 12% | 18,004 | 13% | (7,979) | (44)% |
| Total | \$ 85,482 | 100% | \$ 140,744 | 100% | \$ (55,262) | (39)% |
| Sales by geographic region | | | | | | |
| United States | \$ 19,104 | 22% | \$ 19,405 | 14% | \$ (301) | (2)% |
| China | 21,238 | 25% | 81,156 | 58% | (59,918) | (74)% |
| EMEA | 19,703 | 23% | 21,304 | 15% | (1,601) | (8)% |
| Rest of World | 25,437 | 30% | 18,879 | 13% | 6,558 | 35% |
| Total | \$ 85,482 | 100% | \$ 140,744 | 100% | \$ (55,262) | (39)% |

The overall sales decline was primarily due to reduced sales in Lighting, Display & Power Electronics, which was driven by an oversupply of LED units in this market, and a decline in Data Storage, which was a result of demand variability associated with this mature market. By geography, the largest sales decline was in China, which was attributable to the decline in Lighting, Display & Power Electronics, partially offset by increases in Rest of World. We expect there will continue to be variations in our future sales distribution across markets and geographies.

Bookings increased to \$118.0 million for the three months ended September 30, 2016 from \$51.7 million for the comparable prior year period. The increase in bookings was primarily attributable to improvements in the Lighting, Display & Power Electronics market as we are seeing some improvement in LED industry conditions. We expect continued variations in quarter-to-quarter results, and we expect Data Storage demand to generally be weak as customers make limited technology purchases.

One of the performance measures we use as a leading indicator of the business is the book-to-bill ratio. The ratio is defined as orders recorded in a given period divided by revenue recognized in the same period. For the three months ended September 30, 2016, the book-to-bill ratio was about 1.4. Our backlog increased from \$144.2 million at June 30, 2016 to \$176.5 million at September 30, 2016.

Gross Profit

In the third quarter of 2016, gross profit decreased compared to 2015 due to a sharp decline in sales volume. Gross margins remained steady despite the decline in overall sales volume principally due to a favorable mix of products sold in the period and from the benefits associated with

ongoing cost reduction activities.

Research and development expenses

Research and development expenses increased slightly due to small changes in personnel-related expenses. However, we expect research and development expenses to decline in the fourth quarter as certain development programs are completed. We expect to fund research and development programs that position the Company for future growth.

Table of Contents

Selling, general, and administrative expenses

Selling, general, and administrative expenses decreased primarily due to reductions in personnel and personnel-related expenses, equity compensation, and professional fees as a result of our initiative to streamline operations, enhance efficiency, and reduce costs in response to market conditions.

Amortization expense

The decrease in amortization expense is a result of certain intangible assets becoming fully amortized, including the backlog and trademark/tradename assets associated with the December 2014 Precision Surface Processing (PSP) acquisition. In addition, during the third quarter of 2016, we decided to significantly reduce future investments in our Atomic Layer Deposition (ALD) technology development and, as a result, recorded a charge for impairment of the ALD assets, including a non-cash \$54.3 million impairment of intangible purchased technology. As a result, going forward we expect there will be a significant decline in amortization expense.

Restructuring expense

During the third quarter of 2016, we undertook additional restructuring activities as part of our initiative to streamline operations, enhance efficiency, and reduce costs that was announced during the second quarter of 2016. As a result of these actions, we notified approximately 10 additional employees of their termination. We also incurred restructuring costs associated with our decision to reduce future investments in our ALD technology development, which impacts approximately 25 employees. We incurred \$1.7 million of personnel severance and related costs and \$0.1 million of facility closing costs. Over the next few quarters, we expect to incur additional restructuring costs of \$4 to \$7 million as we finalize these activities.

Asset impairment expense

As a result of our decision to significantly reduce future investments in our ALD technology development, during the third quarter of 2016 we recorded non-cash asset impairment charges of \$57.6 million, the vast majority of which relates to the impairment of the intangible ALD technology asset. In addition, we engaged potential buyers and re-evaluated market conditions for the sale of a building that was previously impaired when it was designated as held for sale during the second quarter of 2016. Our updated assessment of fair market value for the building required us to increase the carrying value of the building, which is still lower than the original pre-impairment carrying value, and record a contra-impairment charge of \$1.6 million.

Income tax expense

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At the end of each interim reporting period, we estimate the effective income tax rate expected to be applicable for the full year. This estimate is used to determine the income tax provision or benefit on a year-to-date basis and may change in subsequent interim periods.

Our tax expense for the three months ended September 30, 2016 and 2015 was \$1.1 million and \$1.4 million, respectively. The 2016 tax expense included \$0.3 million relating to our U.S. operations and \$0.8 million relating to our non-U.S. operations, compared to 2015 when our expense included \$0.4 million benefit related to U.S. operations and \$1.8 million expense related to non-U.S. operations. The decrease in our expense in 2016 was primarily related to reduced pretax income from our non-U.S. operations, offset by an increase in our U.S. tax expense.

Table of Contents**For the nine months ended September 30, 2016 and 2015**

The following table presents operating results as a percentage of net sales, as well as period-over-period dollar and percentage changes for those line items. Our results of operations are reported as one business segment.

| | Nine months ended September 30, | | | | Change | |
|--|---------------------------------|-------|-------------|------|------------------|-------|
| | 2016 | | 2015 | | Period to Period | |
| | (dollars in thousands) | | | | | |
| Net sales | \$ 238,842 | 100% | \$ 370,494 | 100% | \$ (131,652) | (36)% |
| Cost of sales | 141,991 | 59% | 232,038 | 63% | (90,047) | (39)% |
| Gross profit | 96,851 | 41% | 138,456 | 37% | (41,605) | (30)% |
| Operating expenses, net: | | | | | | |
| Research and development | 63,545 | 27% | 57,904 | 16% | 5,641 | 10% |
| Selling, general, and administrative | 58,230 | 24% | 69,153 | 19% | (10,923) | (16)% |
| Amortization | 15,785 | 7% | 21,832 | 6% | (6,047) | (28)% |
| Restructuring | 3,993 | 2% | 3,509 | 1% | 484 | 14% |
| Asset impairment | 69,662 | 29% | 126 | 0% | 69,536 | * |
| Other, net | 884 | 0% | (795) | 0% | 1,679 | * |
| Total operating expenses, net | 212,099 | 89% | 151,729 | 41% | 60,370 | 40% |
| Operating income (loss) | (115,248) | (48)% | (13,273) | (4)% | (101,975) | * |
| Interest income (expense), net | 713 | 0% | 442 | 0% | 271 | 61% |
| Income (loss) before income taxes | (114,535) | (48)% | (12,831) | (3)% | (101,704) | * |
| Income tax provision (benefit) | 2,677 | 1% | 9,360 | 3% | (6,683) | 71% |
| Income (loss) from continuing operations | \$ (117,212) | (49)% | \$ (22,191) | (6)% | \$ (95,021) | * |

* Not Meaningful

Net Sales

The following is an analysis of sales by market and by region:

| | Nine months ended September 30, | | | | Change | |
|---------------------------------------|---------------------------------|------|------------|------|------------------|-------|
| | 2016 | | 2015 | | Period to Period | |
| | (dollars in thousands) | | | | | |
| Market Analysis | | | | | | |
| Lighting, Display & Power Electronics | \$ 97,132 | 41% | \$ 240,751 | 65% | \$ (143,619) | (60)% |
| Advanced Packaging, MEMS & RF | 52,400 | 22% | 40,545 | 11% | 11,855 | 29% |
| Scientific & Industrial | 48,675 | 20% | 46,493 | 13% | 2,182 | 5% |
| Data Storage | 40,635 | 17% | 42,705 | 11% | (2,070) | (5)% |
| Total Sales | \$ 238,842 | 100% | \$ 370,494 | 100% | \$ (131,652) | (36)% |
| Regional Analysis | | | | | | |
| United States | \$ 66,550 | 28% | \$ 67,006 | 18% | \$ (456) | (1)% |

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| | | | | | | |
|---------------|------------|------|------------|------|--------------|-------|
| China | 54,621 | 23% | 191,874 | 52% | (137,253) | (72)% |
| EMEA | 61,999 | 26% | 51,618 | 14% | 10,381 | 20% |
| Rest of World | 55,672 | 23% | 59,996 | 16% | (4,324) | (7)% |
| Total Sales | \$ 238,842 | 100% | \$ 370,494 | 100% | \$ (131,652) | (36)% |

The overall sales decline was primarily due to reduced sales in Lighting, Display & Power Electronics driven by an oversupply of LED units in the market. The decrease was partially offset by increased sales into the Advanced Packaging, MEMS & RF and Scientific & Industrial markets. By geography, sales decreased in all regions, except EMEA. The largest sales decline was in China, which was attributable to the decline in Lighting, Display & Power Electronics. We expect there will continue to be variations in our future sales distribution across markets and geographies.

Table of Contents

Bookings decreased to \$247.3 million for the nine months ended September 30, 2016 from \$277.3 million for the comparable prior year period. The decrease in bookings was primarily attributable to weak activity in the Lighting, Display & Power Electronics market in the first half of 2016 driven by an oversupply of LED units in the market. Beginning in the third quarter of 2016, we are seeing some improvement in LED industry conditions. While there may continue to be quarter-to-quarter variations, we also expect Data Storage demand to generally be weak as customers make limited technology purchases.

For the nine months ended September 30, 2016, the book-to-bill ratio was 1.04. Our backlog decreased slightly from \$186.0 million at December 31, 2015 to \$176.5 million at September 30, 2016, which includes a backlog adjustment of approximately \$17.6 million relating to a partial cancellation of a prior period sales order.

Gross Profit

For the nine months ended September 30, 2016, gross profit decreased compared to 2015 due to a sharp decline in sales volume partially offset by improved gross margins. Gross margins increased despite the decline in overall sales volume principally due to a favorable mix of products sold in the period and from the benefits associated with ongoing cost reduction activities.

Research and development expenses

Research and development expenses increased due to the additional use of third party contractors to accelerate the development of products for the Lighting, Display & Power Electronics market, personnel-related expenses, and depreciation of research and development-related property, plant, and equipment, partially offset by decreased incentive compensation. We expect research and development expenses to decline in the fourth quarter as certain development programs are completed. We expect to fund research and development programs that position the Company for future growth.

Selling, general, and administrative expenses

Selling, general, and administrative expenses decreased primarily due to reductions in sales commissions, incentive compensation, as a result of the decline in our financial performance as well as a decrease in personnel-related expenses as a result of our initiative to streamline operations, enhance efficiency, and reduce costs in response to market conditions.

Amortization expense

The decrease in amortization expense is a result of certain intangible assets become fully amortized, including the backlog and trademark/tradename assets associated with the December 2014 Precision Surface Processing (PSP) acquisition. In addition, during the third

quarter of 2016, we decided to significantly reduce future investments in our ALD technology development and, as a result, recorded a charge for impairment of the ALD assets, including a non-cash \$54.3 million impairment of intangible purchased technology. As a result, going forward, we expect there will be a significant decline in amortization expense.

Restructuring expense

During the nine months ended September 30, 2016, we undertook restructuring activities as part of our initiative to streamline operations, enhance efficiency, and reduce costs. As a result of these actions, we notified approximately 50 employees of their termination. During the first nine months of 2016, we recorded restructuring charges of \$3.1 million, consisting of \$2.8 million of personnel severance and related costs and \$0.3 million of facility closing costs. In addition, during the third quarter of 2016, we decided to significantly reduce our future investments in ALD technology development and, as a result, recorded personnel severance and related restructuring charges of \$0.9 million. Over the next few quarters, we expect to incur additional restructuring costs of \$4 to \$7 million as we finalize these activities.

Table of Contents*Asset Impairment expense*

As a result of our decision to significantly reduce future investments in our ALD technology development, during third quarter we recorded non-cash asset impairment charges of \$57.6 million, the vast majority of which relates to the impairment of the intangible ALD technology asset. We evaluated the market conditions for all of our assets held for sale and made adjustments to the carrying value of the assets to match their fair market value, less cost to sell. As a result, we recorded net non-cash impairment charges of approximately \$5.9 million. Additionally, we removed certain lab equipment that was no longer required from our facilities and recorded a non-cash impairment of \$6.1 million.

Income tax expense

At the end of each interim reporting period, we estimate the effective income tax rate expected to be applicable for the full year. This estimate is used to determine the income tax provision or benefit on a year-to-date basis and may change in subsequent interim periods.

Our tax expense for the nine months ended September 30, 2016 and 2015 was \$2.7 million and \$9.4 million, respectively. The 2016 tax expense included \$1.2 million relating to our U.S. operations and \$1.5 million relating to our non-U.S. operations, compared to 2015 when our expense included \$4.9 million related to U.S. operations and \$4.5 million related to non-U.S. operations. The decrease in our expense in 2016 was primarily related to a significant reduction in our withholding taxes included in our 2015 U.S. tax expense as well as reduced pretax income from our non-U.S. operations in 2016.

Liquidity and Capital Resources

We believe that our projected cash flow from operations, combined with our cash and short term investments, will be sufficient to meet our projected working capital, contractual obligations, and other cash flow needs for the next twelve months. Our cash and cash equivalents as well as short-term investments at September 30, 2016 and December 31, 2015 were:

| | September 30, 2016 | December 31, 2015 |
|---------------------------|-----------------------|----------------------|
| | (in thousands) | |
| Cash and cash equivalents | \$ 274,018 | \$ 269,232 |
| Short-term investments | 62,835 | 116,050 |
| Total | \$ 336,853 | \$ 385,282 |

At September 30, 2016 and December 31, 2015, cash and cash equivalents of \$161.5 million and \$135.3 million, respectively, were held outside the United States. It is our current intention to permanently reinvest the cash and cash equivalent balances held in China, Taiwan, and Malaysia, and our current forecasts do not require repatriation of the funds back to the United States. At September 30, 2016, we had \$108.4 million in cash held outside the United States on which we may have to pay significant U.S. income taxes to repatriate. Additionally, local government regulations may restrict our ability to move cash balances to meet cash needs under certain circumstances. We currently do not expect such regulations and restrictions to impact our ability to pay vendors, conduct operations throughout our global organization, or make acquisitions.

Table of Contents*Cash Flows from Operating Activities*

| | Nine months ended September 30, | |
|--|---------------------------------|------------------|
| | 2016 | 2015 |
| | (in thousands) | |
| Net income (loss) | \$ (117,212) | \$ (22,191) |
| Non-cash items: | | |
| Depreciation and amortization | 26,010 | 30,766 |
| Deferred income taxes | 1,529 | 1,794 |
| Share-based compensation expense | 12,133 | 14,038 |
| Asset impairment | 69,662 | 126 |
| Other | 160 | (841) |
| Changes in operating assets and liabilities | (16,590) | (1,842) |
| Net cash provided by (used in) operating activities | \$ (24,308) | \$ 21,850 |

Cash used in operating activities for the nine months ended September 30, 2016 reflects net income adjusted for the effect of non-cash charges and changes in working capital components. Non-cash charges included depreciation, amortization, share-based compensation expense, asset impairment, and deferred taxes. Cash from operating activities was negatively impacted by changes in inventory, accounts payable and accrued expenses, and accounts receivable, partially offset by changes in customer deposits and deferred revenue and prepaid expenses and other current assets.

Cash Flows from Investing Activities

| | Nine months ended September 30, | |
|--|---------------------------------|------------------|
| | 2016 | 2015 |
| | (in thousands) | |
| Capital expenditures | \$ (10,717) | \$ (11,069) |
| Changes in investments, net | 52,921 | 51,647 |
| Proceeds from sale of lab tools | | 2,648 |
| Other | 463 | (662) |
| Net cash provided by investing activities | \$ 42,667 | \$ 42,564 |

Cash provided by investing activities during the nine months ended September 30, 2016 is primarily attributed to net liquidations of short-term investments, offset by capital expenditures. As part of our efforts to streamline operations, enhance efficiency, and reduce costs, we are making certain investments in our facilities to support the consolidation activities, and we expect to incur additional capital expenditures of \$6 to \$9 million over the next few quarters related to these activities.

Cash Flows from Financing Activities

Nine months ended September 30,

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| | 2016 | (in thousands) | 2015 |
|---|-----------|-----------------|-------------------|
| Settlement of equity awards, net of withholding taxes | \$ | (711) | \$ (785) |
| Proceeds from employee stock purchase plan | | 719 | \$ |
| Purchases of common stock | | (13,349) | |
| Repayments of long-term debt | | (252) | (233) |
| Net cash used in financing activities | \$ | (13,593) | \$ (1,018) |

Cash flows used in financing activities during the nine months ended September 30, 2016 is primarily a result of our purchases of common shares as part of the share buyback program initiated during the fourth quarter of 2015.

Table of Contents

Off-Balance Sheet Arrangements and Contractual Obligations

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on our financial condition, results of operations, liquidity, capital expenditures or capital resources other than operating leases, bank guarantees, and purchase commitments disclosed in the preceding footnotes.

Contractual Obligations and Commitments

We have commitments under certain contractual arrangements to make future payments for goods and services. These contractual arrangements secure the rights to various assets and services to be used in the future in the normal course of business. We expect to fund these contractual arrangements with cash generated from operations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

Our exposure to interest rate changes primarily relates to our investment portfolio. We centrally manage our investment portfolio considering investment opportunities and risks, tax consequences, and overall financing strategies. Our short term investment portfolio includes fixed income securities with a fair value of \$62.8 million at September 30, 2016. These securities are subject to interest rate risk; a 100 basis point increase in interest rates would result in a decrease in the fair value of the September 30, 2016 investment portfolio of \$0.2 million. While an increase in interest rates may reduce the fair value of the investment portfolio, we would not realize the losses in the Consolidated Statements of Operations unless the individual fixed income securities are sold prior to maturity or a loss position is determined to be other-than-temporary.

Currency Exchange Risk

We conduct business on a worldwide basis exposing a portion of our revenues, operating costs, and net investments in foreign affiliates to changes in currency exchange rates. The economic impact of currency exchange rate movements is complex because such changes are often linked to variability in real growth, inflation, interest rates, governmental actions, and other factors. These changes, if material, could cause us to adjust our financing and operating strategies. Consequently, isolating the effect of changes in currency does not incorporate these other important economic factors.

We may manage our risks and exposures to currency exchange rates through the use of derivative financial instruments. We only use derivative financial instruments in the context of hedging and do not use them for speculative purposes. During the nine months ended September 30, 2016 and 2015, we did not own any derivatives.

Our net sales to customers located outside of the United States represented approximately 78% and 72% of our total net sales for the three and nine months ended September 30, 2016, respectively and 86% and 82% for the comparable 2015 periods. We expect that net sales to customers outside the United States will continue to represent a large percentage of our total sales. Our sales denominated in currencies other than the U.S. dollar represented 2% and 4% of total net sales in the three and nine months ended September 30, 2016, respectively, and 2% for the comparable 2015 periods.

A 10% change in foreign exchange rates would have an immaterial impact on the consolidated results of operations.

Item 4. Controls and Procedures

Management's Report on Internal Control Over Financial Reporting

Our principal executive and financial officers have evaluated and concluded that our disclosure controls and procedures are effective at September 30, 2016. The disclosure controls and procedures are designed to ensure that the information required to be disclosed in this report filed under the Securities Exchange Act of 1934 is recorded, processed, summarized, and

Table of Contents

reported within the time periods specified in the Securities and Exchange Commission's rules and forms and is accumulated and communicated to our principal executive and financial officers as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

During the three months ended September 30, 2016, there were no changes in internal control that have materially affected or are reasonably likely to materially affect internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

Information regarding legal proceedings appears in the Commitments and Contingencies Note to the Consolidated Financial Statements in this quarterly report on Form 10-Q and in Part I Item 3 of our 2015 Form 10-K.

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 and in Part I Item 1A of our 2015 Form 10-K. There have been no material changes from the risk factors previously disclosed in our 2015 Form 10-K.

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

On October 28, 2015, our Board of Directors authorized a program to repurchase up to \$100 million of our common stock to be completed through October 28, 2017. At March 31, 2016, \$22.3 million of the \$100 million had been utilized. No repurchases occurred during the second and third quarter of 2016. Repurchases may be made from time to time on the open market or in privately negotiated transactions in accordance with applicable federal securities laws. The timing and amount of future repurchases, if any, will depend upon market conditions, SEC regulations, and other factors. The repurchases would be funded using available cash balances and cash generated from operations. The program does not obligate us to acquire any particular amount of common stock and may be modified or suspended at any time at our discretion.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not Applicable.

Item 5. Other Information

None.

Table of Contents**Item 6. Exhibits**

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

| Number | Description | Incorporated by Reference to the Following Document: |
|---------------|--|---|
| 10.1 | Form of Notice of Performance Share Award and related terms and conditions pursuant to the Veeco 2010 Stock Incentive Plan, effective June 2016. | * |
| 10.2 | Form of Notice of Critical Priorities Performance Share Award and related terms and conditions pursuant to the Veeco 2010 Stock Incentive Plan, effective June 2016. | * |
| 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. | * |
| 101.INS | XBRL Instance | ** |
| 101.SCH | XBRL Schema | ** |
| 101.PRE | XBRL Presentation | ** |
| 101.CAL | XBRL Calculation | ** |
| 101.DEF | XBRL Definition | ** |
| 101.LAB | XBRL Label | ** |

* Filed herewith

** Filed herewith electronically

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, on November 1, 2016.

Veeco Instruments Inc.

By:

/S/ JOHN R. PEELER
John R. Peeler
Chairman and Chief Executive Officer

By:

/s/ SHUBHAM MAHESHWARI
Shubham Maheshwari
Executive Vice President and Chief Financial Officer