

VEECO INSTRUMENTS INC  
Form 10-Q  
October 26, 2009  
Table of Contents

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

---

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended September 30, 2009

OR

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

For the transition period from            to            .

Commission file number 0-16244

## VEECO INSTRUMENTS INC.

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**  
(State or Other Jurisdiction of

Incorporation or Organization)

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

**11-2989601**  
(I.R.S. Employer

Identification Number)

**11803**  
(Zip Code)

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

Website: **www.veeco.com**

---

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)



Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

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

Table of Contents

**SAFE HARBOR STATEMENT**

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

- Our failure to successfully implement outsourcing activities or failure of our outsourcing partners to perform as anticipated could adversely affect our results of operations and our ability to realize the benefits of the recent increase in MOCVD order volume.
- Negative worldwide economic conditions could result in a decrease in our net sales and an increase in our operating costs, which could adversely affect our business and operating results;
- Our sales to HB-LED and data storage manufacturers are highly dependent on these manufacturers' sales for consumer electronics applications, which can experience significant volatility due to seasonal and other factors, which could materially adversely impact our future results of operations;
- We are exposed to risks associated with entering an emerging segment within the solar industry;
- We may be required to take additional impairment charges for goodwill and indefinite-lived intangible assets or definite-lived intangible and long-lived assets;
- Any failure by us to execute our planned cost reductions successfully could result in total costs and expenses that are greater than expected;
- The cyclical nature of the industries we serve directly affects our business;
- We operate in industries characterized by rapid technological change;

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

- We face significant competition;
- We depend on a limited number of customers that operate in highly concentrated industries;
- The timing of our orders, shipments, and revenue recognition may cause our quarterly operating results to fluctuate significantly;
- Changes in our product mix may cause our quarterly operating results to fluctuate significantly;
- Our backlog is subject to customer cancellation or modification and such cancellation could result in decreased sales and increased provisions for excess and obsolete inventory;
- Our sales cycle is long and unpredictable;
- Manufacturing interruptions or delays could affect our ability to meet customer demand, while the failure to estimate customer demand accurately could result in excess or obsolete inventory;
- We rely on a limited number of suppliers;
- Our inability to attract, retain, and motivate key employees could have a material adverse effect on our business;
- We are exposed to the risks of operating a global business;

Table of Contents

- We are subject to foreign currency exchange risks;
- The enforcement and protection of our intellectual property rights may be expensive and could divert our valuable resources;
- We may be subject to claims of intellectual property infringement by others;
- Our acquisition strategy subjects us to risks associated with evaluating and pursuing these opportunities and integrating these businesses;
- We are substantially leveraged, which could adversely affect our ability to adjust our business to respond to competitive pressures and to obtain sufficient funds to finance our future needs;
- Changes in accounting pronouncements or taxation rules or practices may adversely affect our financial results;
- The price of our common shares may be volatile and could decline significantly;
- We are subject to the internal control evaluations and attestation requirements of Section 404 of the Sarbanes-Oxley Act;
- We are subject to risks of non-compliance with environmental, health and safety regulations;
- We have significant operations in California and other locations which could be materially and adversely impacted, in the event of a natural disaster or other significant disruption;
- We have adopted certain measures that may have anti-takeover effects which may make an acquisition of our Company by another company more difficult; and



## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

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

### **Available Information**

We file annual, quarterly and current reports, information statements and other information with the Securities and Exchange Commission (the "SEC" ). The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is <http://www.sec.gov>.

### **Internet Address**

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

Table of Contents

VEECO INSTRUMENTS INC.

INDEX

	<b>Page</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
<b><u>Item 1.</u></b>	<b><u>Financial Statements:</u></b>
	<u>Condensed Consolidated Statements of Operations for the Three Months and Nine Months Ended September 30, 2009 and 2008 (Unaudited)</u> 5
	<u>Condensed Consolidated Balance Sheets as of September 30, 2009 (Unaudited) and December 31, 2008</u> 6
	<u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2009 and 2008 (Unaudited)</u> 7
	<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u> 8
<b><u>Item 2.</u></b>	<b><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b> 20
<b><u>Item 3.</u></b>	<b><u>Quantitative and Qualitative Disclosures About Market Risk</u></b> 36
<b><u>Item 4.</u></b>	<b><u>Controls and Procedures</u></b> 36
<b><u>PART II. OTHER INFORMATION</u></b>	
<b><u>Item 1.</u></b>	<b><u>Legal Proceedings</u></b> 37
<b><u>Item 1A.</u></b>	<b><u>Risk Factors</u></b> 37
<b><u>Item 6.</u></b>	<b><u>Exhibits</u></b> 38
<b><u>SIGNATURES</u></b>	39

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

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

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

*See accompanying notes.*

Table of Contents

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

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

*See accompanying notes.*

Table of Contents

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

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

*See accompanying notes.*



Table of Contents**VEECO INSTRUMENTS INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements (Unaudited)****Note 1 Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation (consisting of normal recurring accruals) have been included. Operating results for the three months and nine months ended September 30, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009. For further information, refer to the financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2008.

Consistent with prior years, we report interim quarters, other than fourth quarters which always end on December 31, on a 13-week basis ending on the last Sunday within such period. The interim quarter ends are determined at the beginning of each year based on the 13-week quarters. The 2009 interim quarter ends are March 29, June 28, and September 27. The 2008 interim quarter ends were March 30, June 29, and September 28. For ease of reference, we report these interim quarter ends as March 31, June 30, and September 30 in our interim condensed consolidated financial statements.

*Net Income (Loss) Per Common Share*

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

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

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

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

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

The Notes meet the criteria for determining the effect of the assumed conversion using the treasury stock method of accounting, as long as we have the ability and the intent to settle the principal amount of the Notes in cash. Under the terms of the Notes, we may pay the principal amount of converted Notes in cash or in shares of common stock. We have indicated that we intend to pay such amounts in cash. Using the treasury stock method, the impact of the assumed conversion of the Notes was anti-dilutive for the three and nine months ended September 30, 2009 and



Table of Contents

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

*Fair Value of Financial Instruments*

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

*Derivative Financial Instruments*

We use derivative financial instruments to minimize the impact of foreign exchange rate changes on earnings and cash flows. In the normal course of business, our operations are exposed to fluctuations in foreign exchange rates. In order to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known foreign currency exposures, we enter into monthly forward contracts. We do not use derivative financial instruments for trading or speculative purposes. Our forward contracts are intended to offset exchange gains and losses on the underlying assets and liabilities; both the forward contracts and the underlying assets and liabilities are adjusted to current exchange rates through earnings. We conduct our derivative transactions with highly rated financial institutions in an effort to mitigate any material credit risk. The weighted average notional amount of derivative contracts outstanding during the three and nine months ended September 30, 2009 was approximately \$1.3 million and \$3.1 million, respectively.

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

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

*Convertible Debt*

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

### *Subsequent Events*

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

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

In 2006 we purchased 19.9% of the common stock of Fluens Corporation ( Fluens ). Veeco and Fluens have jointly developed a next-generation process for high-rate deposition of aluminum oxide for data storage applications. For accounting purposes we had consolidated Fluens into our financial results and financial position, and recorded the remaining 80.1% portion of its net loss and net assets as a noncontrolling interest. On May 14, 2009, we acquired the remaining 80.1% of Fluens for \$1.5 million plus an earn-out arrangement based on future performance. Since we already were consolidating Fluens, the purchase of the remaining 80.1% was treated in accordance with the applicable accounting guidance as a transaction among shareholders and not as a new business acquisition. Thus no gain or loss was recognized upon the purchase of the 80.1% portion, and the difference between the purchase price including the earn-out consideration and the amount by which noncontrolling interest was reduced on the balance sheet was attributed to equity of Veeco. Such difference amounted to approximately \$1.0 million, and was recorded as additional paid-in capital.

We paid \$0.5 million of the \$1.5 million purchase price of the 80.1% remaining portion of Fluens upon closing, as well as \$0.2 million in respect of the earn-out arrangement. We paid a second installment of \$0.5 million of the purchase price on September 30, 2009. We will pay the remaining \$0.5 million of the \$1.5 million in the fourth quarter of 2009, which is included in accrued expenses in the accompanying condensed Balance Sheet at September 30, 2009. Prior to our purchase of the remaining 80.1%, approximately 31% of Fluens was owned by an individual then serving as Senior Vice President of Veeco.

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

**Note 3 Share-Based Compensation**

Share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over the employee requisite service period. The following compensation expense was included in the condensed consolidated statements of operations for the three months and nine months ended September 30, 2009 and 2008 (in thousands):

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

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

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

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

Table of Contents

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

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

**Note 4 Balance Sheet Information***Accounts Receivable, net*

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

*Inventories*

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

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

*Accrued Warranty*

We estimate the costs that may be incurred under the warranty we provide and recognize a liability in the amount of such costs at the time the related revenue is recognized. Factors that affect our warranty liability include product failure rates, material usage and labor costs incurred in correcting product failures during the warranty period. We periodically assess the adequacy of our recognized warranty liability and adjust the amount as necessary. Changes in our warranty liability during the nine months ended September 30, 2009 and 2008 are as follows (in thousands):

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

Table of Contents

**Note 5 Segment Information**

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

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

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





Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

Table of Contents

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

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

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

**Note 6 Income Taxes**

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

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

Table of Contents

**Note 7 Comprehensive Income (Loss)**

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



Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

**Note 8 Debt**

*Convertible Debt*

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

The Notes are initially convertible into 36.7277 shares of common stock per \$1,000 principal amount of Notes (equivalent to a conversion price of \$27.23 per share or a premium of 38% over the closing market price for Veeco's common stock on April 16, 2007). Holders may convert the Notes at any time during the period beginning on January 15, 2012 through the close of business on the second day prior to April 15, 2012 and earlier upon the occurrence of certain events including our common stock trading at prices equal to 130% over the conversion price for a specified period. These Notes bear interest at 4.125% per annum and mature on April 15, 2012. We pay interest on these Notes on April 15 and October 15 of each year. The Notes are unsecured and are effectively subordinated to all of our senior and secured indebtedness, and to all indebtedness and other liabilities of our subsidiaries.

In May 2008, new accounting guidance was issued that requires a portion of convertible debt to be allocated to equity. We implemented the new guidance as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. The new guidance requires issuers of convertible debt that can be settled in cash to separately account for (*i.e.*, bifurcate) a portion of the debt associated with the conversion feature and reclassify this portion to stockholders' equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as non-cash interest expense. The Notes are subject to the new guidance since they may be settled in cash upon conversion. Thus, as a result of the adoption of the new guidance, we reclassified approximately \$16.3 million from long-term debt to additional paid-in capital effective as of the date of issuance of the Notes. This reclassification created a \$16.3 million discount on the debt that will be amortized over the remaining life of the Notes, which will be through April 15, 2012. The reclassification generated a \$6.7 million deferred tax liability, which we offset with a corresponding decrease of the valuation allowance by the same amount. The new guidance requires that we present prior periods as if the guidance was in effect as of the date of issuance. Thus, we have presented all financial data for prior periods as if we had reclassified this \$16.3 million discount and began amortizing it in April 2007. The retrospective application of the new guidance described above to the results for the three and nine months ended September 30, 2008 increased the net loss attributable to Veeco in the three-month period from (\$1,673) to (\$2,413) and decreased the net income attributable to Veeco in the nine-month period from \$946 to a net loss of (\$1,238), and increased the loss per share attributable to Veeco in the three-month period

Table of Contents

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

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

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

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

The carrying amounts of the liability and equity components of the Notes as of September 30, 2009 and December 31, 2008, respectively, were as follows (in thousands):

	September 30, 2009	December 31, 2008
Carrying amount of the equity component	\$ 16,318	\$ 16,318
Principal balance of the liability component	\$ 105,574	\$ 105,574
Less: unamortized discount	8,225	10,339
Net carrying value of the liability component	\$ 97,349	\$ 95,235

At September 30, 2009, \$105.6 million of the Notes were outstanding with a fair value of approximately \$109.8 million.

*Mortgage Payable*



We also have a mortgage note payable, with approximately \$3.1 million outstanding at September 30, 2009. The note accrues interest at an annual rate of 7.91%, and the final payment is due on January 1, 2020. The fair value of this note at September 30, 2009 was approximately \$3.4 million.

*Credit Agreement*

In February 2009, we entered into an amendment to our existing credit agreement with HSBC Bank USA, National Association ( *HSBC* ), as administrative agent, and the lenders named therein (as amended, the *Credit Agreement* ). As part of the amendment, we reduced the amount of the revolving credit facility, modified certain existing covenants and added certain new covenants. As amended, the *Credit Agreement* provides for revolving credit borrowings of up to \$30.0 million. The *Credit Agreement* was further amended effective March 27, 2009 to

Table of Contents

modify certain financial covenants, to provide for the cash collateralization of borrowings under the Credit Agreement, and to permit the acquisition of the 80.1% of Fluens outstanding stock which we did not yet own. The annual interest rate under the Credit Agreement is a floating rate equal to the prime rate of the agent bank plus 2.0%. A LIBOR-based interest rate option is also provided. Borrowings may be used for general corporate purposes, including working capital requirements, as well as permitted acquisitions. The Credit Agreement contains certain restrictive covenants which include the maintenance of minimum cash balances and limitations with respect to incurrence of indebtedness, the payment of dividends, long-term leases, investments, mergers, acquisitions, consolidations and sales of assets. In addition, under the Credit Agreement, we are required to satisfy certain financial tests, including minimum profitability levels. As of September 30, 2009, we were in compliance with all covenants of the Credit Agreement as amended. Substantially all of our assets and those of our material domestic subsidiaries, other than real estate, have been pledged to secure our obligations under the Credit Agreement. The revolving credit facility under the Credit Agreement expires on March 31, 2012. In the first quarter of 2009, we recognized an expense of \$0.2 million representing the amount of deferred financing fees equal to the portion of the revolving credit facility which was terminated in connection with the amendment, which is included in other expense, net. We capitalized \$0.1 million in deferred financing fees that we incurred in connection with the amendment that was effective February 2009. As of September 30, 2009 and December 31, 2008, there were no borrowings outstanding under the Credit Agreement and letters of credit outstanding were approximately \$0.5 million and \$0.4 million, respectively. Interest expense associated with the Credit Agreement recorded during the nine months ended September 30, 2009 and 2008, was approximately \$0.2 million for each period.

**Note 9 Fair Value Measurements**

We implemented new accounting guidance for our non-financial assets and non-financial liabilities as of January 1, 2009. This new guidance defines fair value, establishes a framework for measuring fair value, and enhances fair value measurement disclosure. The accounts subject to the guidance are our long-lived assets, goodwill, and intangible assets. The implementation expanded our fair value disclosures but did not impact our condensed consolidated financial position or results of operations. However, applying the provisions of this new guidance may impact our periodic fair value measurements for long-lived assets, goodwill and intangible assets in the future, as fair values calculated under the new guidance may be different from the fair values that would have been calculated under previous guidance.

This new guidance requires that we disclose the type of inputs we use to value such assets, based on three categories of inputs as defined in such. Level 1 inputs are quoted, unadjusted prices in active markets for identical assets or liabilities that the company has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as quoted prices for similar assets or liabilities. Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. We use Level 3 inputs to value all of our property, plant and equipment, goodwill, and intangible assets balances. We value such assets on a non-recurring basis and did not perform a valuation during the first, second or third quarters of 2009, though the methodology we would use to value such assets has not changed since December 31, 2008. We did not record any gain or loss in adjusting the carrying amounts to fair value in the three months or nine months ended September 30, 2009, since we made no such adjustment during that period. The carrying amounts of property, plant and equipment, goodwill, and intangible assets as of September 30, 2009 were \$59,294, \$59,422, and \$32,116, respectively. The Company primarily applies the market approach for recurring fair value measurements.

**Note 10 Commitments, Contingencies and Other Matters**

*Restructuring Expenses*

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

During 2008 and through the nine months ended September 30, 2009, we have continued our multi-quarter plan to improve profitability and reduce and contain spending. We have continued to make progress against the initiatives that management has set, continued our restructuring plan and executed activities with a focus on creating a more cost effective organization, with a greater percentage of variable costs. These activities have included downsizing and consolidating some locations, reducing our workforce, consultants and discretionary expenses and realigning our sales organization and engineering groups.

Table of Contents

Restructuring expenses for the three months and nine months ended September 30, 2009 and 2008 are as follows (in thousands):

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Personnel severance costs	\$ 1,086	\$ 820	\$ 6,239	\$ 1,141
Lease-related costs		282	893	2,836
Modification of equity awards		3,018		3,018
Moving and consolidation activity costs	106		435	
Total restructuring expense	\$ 1,192	\$ 4,120	\$ 7,567	\$ 6,995

*2009 Restructuring and Other Charges*

In conjunction with these activities, during the nine months ended September 30, 2009, we recognized restructuring charges of approximately \$7.6 million, principally consisting of personnel severance costs resulting from a headcount reduction of 235 employees as well as the notification of other employees that will be transitioned out of the Company during 2009. This reduction in workforce included executives, management, administration, sales and service personnel and manufacturing employees companywide.

During the second quarter of 2009, we vacated our Data Storage Process Equipment facilities in Camarillo, CA. As a result, we incurred an additional restructuring charge, representing the remaining lease payment obligations and estimated property taxes for the facility we vacated, offset by the estimated expected sublease income to be received. We made certain assumptions in determining the charge, which included estimated sublease income and terms of the sublease as well as the estimated discount rate to be used in determining the fair value of the liability. We developed these assumptions based on our understanding of the current real estate market as well as current market interest rates. The assumptions are based on management's best estimates, and will be adjusted periodically if better information is obtained. We also incurred charges associated with moving and consolidation activities for both of these locations. We relocated 27 employees from the Data Storage Process Equipment segment to Metrology's Santa Barbara, CA facility.

We also recorded an inventory write-off of \$1.5 million in our Data Storage Process Equipment segment associated with the discontinuance of certain products in connection with transitioning to outsourced manufacturing during the first quarter of 2009, which is included in cost of sales.

Table of Contents

The following is a reconciliation of the liability for the 2009 restructuring charge from inception through September 30, 2009 (in thousands):

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate	Total
<u>Short-term Liability</u>					
Personnel severance charges	\$ 998	\$ 1,876	\$ 2,789	\$ 599	\$ 6,262
Moving costs and consolidation activities	135	287	13		435
Total charged to accrual	1,133	2,163	2,802	599	6,697
Lease-related and other costs		516			516
Short-term/long-term Reclassification		74			74
Cash payments	(827)	(1,991)	(2,423)	(281)	(5,522)
Balance as of September 30, 2009	\$ 306	\$ 762	\$ 379	\$ 318	\$ 1,765
<u>Long-term Liability</u>					
Lease-related and other costs	\$	\$ 377	\$	\$	\$ 377
Short-term/long-term Reclassification		(74)			(74)
Balance as of September 30, 2009	\$	\$ 303	\$	\$	\$ 303

**The balance of the short-term 2009 restructuring accrual (other than lease-related and other costs) is expected to be paid over the next six to nine months, and the long-term portion will be paid over the remaining life of the lease until May 1, 2012. We expect to continue our restructuring program and to incur restructuring charges of \$0.3 million throughout the remainder of 2009, which are principally related to severance and associated costs.**

*2008 Restructuring and Other Charges*

During the three months ended March 31, 2008, we recorded a \$2.6 million restructuring charge for lease-related costs as part of the consolidation of our Corporate headquarters into our Plainview, New York manufacturing facility. This charge primarily consisted of the liability for the remaining lease payments and property taxes relating to the facility we vacated, offset by expected sublease income. We made certain assumptions in determining the charge, which included estimated sublease income and terms of the sublease as well as the estimated discount rate to be used in determining the fair value of the net cash flows. We developed these assumptions, based on our understanding of the current real estate market as well as current market interest rates, which are adjusted periodically based upon new information, events and changes in the real estate market. During the fourth quarter of 2008, we adjusted these assumptions which resulted in an additional restructuring charge of \$1.1 million.

Table of Contents

The following is a reconciliation of the liability for the 2008 restructuring charge from December 31, 2008 through September 30, 2009 (in thousands):

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate	Total
<u>Short-term Liability</u>					
Balance as of December 31, 2008	\$ 660	\$ 270	\$ 534	\$ 1,859	\$ 3,323
Short-term/long-term Reclassification				814	814
Cash payments	(370)	(268)	(457)	(1,265)	(2,360)
Reversal of accrual	(4)	(2)	(5)	(12)	(23)
Balance as of September 30, 2009	\$ 286	\$	\$ 72	\$ 1,396	\$ 1,754
<u>Long-term Liability</u>					
Balance as of December 31, 2008	\$	\$	\$	\$ 1,620	\$ 1,620
Short-term/long-term Reclassification				(814)	(814)
Balance as of September 30, 2009	\$	\$	\$	\$ 806	\$ 806

The balance of the 2008 restructuring accrual related to the lease for the former Corporate headquarters is expected to be paid over the remaining life of that lease through June 2011, and the remaining balance of the 2008 restructuring accrual is expected to be paid over the next nine months.

*2007 Restructuring and Other Charges*

As of December 31, 2008, we had a balance of \$0.2 million in the liability related to restructuring charges incurred in 2007. We made cash payments of \$0.1 million against this liability in the first quarter of 2009, and paid the remaining balance of \$0.1 million during the second quarter of 2009.

**Table of Contents**

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

**Executive Summary**

We design, manufacture, market, and service enabling solutions for customers in the high-brightness light emitting diode ( HB-LED ), solar, data storage, scientific research, semiconductor, and industrial markets. We have leading technology positions in our three segments: Light Emitting Diode ( LED ) & Solar Process Equipment, Data Storage Process Equipment, and Metrology.

In our LED & Solar segment, we design and manufacture metal organic chemical vapor deposition ( MOCVD ) systems, molecular beam epitaxy ( MBE ) systems and sources, and other types of deposition systems such as web and glass coaters, which we sell primarily to manufacturers of HB-LEDs and solar panels, as well as to scientific research customers.

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

In our Metrology segment, we design and manufacture atomic force microscopes ( AFMs ), scanning probe microscopes ( SPMs ), stylus profilers, and optical interferometers used to provide critical surface measurements in research and production environments. This broad line of products is used in universities, research facilities and scientific centers worldwide. In production environments such as semiconductor, data storage and other industries, our metrology instruments enable customers to monitor their products throughout the manufacturing process to improve yields, reduce costs, and improve product quality.

We currently maintain facilities in Arizona, California, Colorado, Massachusetts, Minnesota, New Jersey and New York, with sales and service locations in North America, Europe, Japan, and the Asia Pacific region.

**Highlights of the Third Quarter of 2009**

- Revenue was \$98.9 million, a 15% decrease from the third quarter of 2008, and up 37% from the second quarter of 2009.
- Orders were \$225.6 million, up 150% from the third quarter of 2008, and up 129% from the second quarter of 2009.
- Net income was \$1.3 million, or \$0.04 per share, compared to net loss of \$2.4 million, or (\$0.08) per share, in the third quarter of 2008, and a net loss of \$14.7 million or (\$0.47) per share, in the second quarter of 2009.
- Gross margins were 41.4%, compared to 39.8% in the third quarter of 2008, and 33.9% in the second quarter of 2009.

- Restructuring charges totaled \$1.2 million and principally consisted of personnel severance costs.

The third quarter showed marked improvement for Veeco from an order, revenue and earnings perspective. Our earnings improved from the previous quarter due to 37% higher revenues, better product mix, outsourcing initiatives and materials cost management. The significant recovery in revenues is primarily due to the strong demand for Veeco's MOCVD systems sold principally to HB-LED manufacturers.

Third quarter orders of \$225.6 million were the highest in Veeco's history. We received orders of \$179.2 million in our LED & Solar segment, \$17.2 million in our Data Storage segment and \$29.2 million in our Metrology segment. Veeco has experienced a significant increase in industry demand for our MOCVD systems, with a number of HB-LED manufacturers placing multi-unit orders as they ramp production for laptop and TV backlighting. Veeco MOCVD systems were also ordered by leading U.S. HB-LED manufacturers to ramp production for general illumination. Momentum continued in our copper, indium, gallium, selenium ( CIGS ) solar business in the third quarter, with a second key customer win for our FastFlex thermal disposition systems and a repeat multi-million dollar order for thermal deposition components from a leading CIGS manufacturer. Although Data Storage orders remained weak, we experienced a 27% sequential improvement in Metrology orders, driven by new product success and a modest pick-up in activity from both research and industrial customers.



Table of Contents

**Outlook**

Veeco's fourth quarter 2009 revenues are currently forecasted to be between \$120-\$130 million and we currently anticipate that our book-bill ratio will remain positive. Veeco's 2009 revenue guidance is now \$353-\$363 million, up from previous guidance of \$310-\$325 million.

Veeco's backlog at September 30, 2009 was \$286.5 million, \$238.5 million of which is in our LED & Solar segment. In addition, we continue to experience positive business trends in our MOCVD business, with a high level of customer interest in our K465 MOCVD system. We are currently ramping up our manufacturing capacity to satisfy our backlog of orders and anticipated customer requirements.

As we look toward the future, we believe that the HB-LED industry is at the beginning of a multi-year MOCVD tool investment cycle as HB-LEDs increase their penetration in laptop and TV backlighting, and gain momentum for general illumination. We are also seeing strong interest in our thermal deposition solutions for the manufacturing of CIGS solar cells, and believe that Veeco is well positioned to increase our business in this market. In addition, overall business conditions in our Data Storage and Metrology segments appear to be improving from the trough levels we experienced earlier this year.

Our outlook discussion above constitutes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Our expectations regarding future results are subject to risks and uncertainties. Our actual results may differ materially from those anticipated. Risks associated with our ability to achieve these results are set forth in Items 1, 1A, 3, 7 and 7A in our annual report on Form 10-K for the year ended December 31, 2008 and in our most recent quarterly reports on Form 10-Q for the quarters ended March 31, 2009 and June 30, 2009, as well as any modifications or revisions to risk factors contained in our subsequent filings with the SEC.

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

Table of Contents

**Results of Operations:**

*Three Months Ended September 30, 2009 and 2008*



## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

The following table shows our Condensed Consolidated Statements of Operations, percentages of sales, and comparisons between the three months ended September 30, 2009 and 2008 (dollars in thousands):

	Three months ended				Dollar and Percentage Change (1)	
	2009		September 30, 2008			
Net sales	\$ 98,913	100.0%	\$ 115,709	100.0%	\$ (16,796)	(14.5)%
Cost of sales	58,005	58.6	69,626	60.2	(11,621)	(16.7)
Gross profit	40,908	41.4	46,083	39.8	(5,175)	(11.2)
Operating expenses:						
Selling, general, and administrative expense	21,042	21.3	23,589	20.4	(2,547)	(10.8)
Research and development expense	13,721	13.9	15,302	13.2	(1,581)	(10.3)
Amortization expense	1,777	1.8	3,148	2.7	(1,371)	(43.6)
Restructuring expense	1,192	1.2	4,120	3.6	(2,928)	(71.1)
Other income, net	(312)	(0.3)	(213)	(0.2)	(99)	46.5
Total operating expenses	37,420	37.8	45,946	39.7	(8,526)	(18.6)
Operating income	3,488	3.5	137	0.1	3,351	2446.0
Interest expense, net	1,656	1.7	1,792	1.5	(136)	(7.6)
Income (loss) before income taxes	1,832	1.9	(1,655)	(1.4)	3,487	N/M
Income tax provision	562	0.6	812	0.7	(250)	(30.8)
Income (loss) including noncontrolling interest	1,270	1.3	(2,467)	(2.1)	3,737	N/M
Noncontrolling interest		0.0	(54)	0.0	54	(100.0)
Net income (loss) attributable to Veeco	\$ 1,270	1.3%	\$ (2,413)	(2.1)%	\$ 3,683	N/M

(1) N/M denotes not meaningful as change moves from negative to positive, or vice versa.

### Net Sales and Orders

Net sales of \$98.9 million for the three months ended September 30, 2009 were down 14.5% compared to the comparable 2008 quarter. The following is an analysis of sales and orders by segment and by region (dollars in thousands):

	Sales				Orders				Book-to-Bill Ratio	
	Three months ended September 30, 2009		September 30, 2008		Three months ended September 30, 2009		September 30, 2008			
			Dollar and Percentage Change Year to Year				Dollar and Percentage Change Year to Year			
<b>Segment Analysis</b>										
LED & Solar Process										
Equipment	\$ 52,966	\$ 40,983	\$ 11,983	29.2%	\$ 179,229	\$ 25,775	\$ 153,454	595.4%	3.38	0.63
Data Storage Process										
Equipment	21,721	43,256	(21,535)	(49.8)	17,243	32,359	(15,116)	(46.7)	0.79	0.75
Metrology	24,226	31,470	(7,244)	(23.0)	29,165	32,031	(2,866)	(8.9)	1.20	1.02
Total	\$ 98,913	\$ 115,709	\$ (16,796)	(14.5)%	\$ 225,637	\$ 90,165	\$ 135,472	150.2%	2.28	0.78
<b>Regional Analysis</b>										
Americas	\$ 18,268	\$ 38,865	\$ (20,597)	(53.0)%	\$ 38,436	\$ 31,256	\$ 7,180	23.0%	2.10	0.80
Europe, Middle East and Africa ( EMEA )	19,178	28,578	(9,400)	(32.9)	19,392	22,650	(3,258)	(14.4)	1.01	0.79
Japan	5,013	6,604	(1,591)	(24.1)	5,965	7,769	(1,804)	(23.2)	1.19	1.18

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Asia Pacific	56,454	41,662	14,792	35.5	161,844	28,490	133,354	468.1	2.87	0.68
Total	\$ 98,913	\$ 115,709	\$ (16,796)	(14.5)%	\$ 225,637	\$ 90,165	\$ 135,472	150.2%	2.28	0.78

LED & Solar Process Equipment sales were up 29.2% as compared to the third quarter of 2008 primarily due to an increase in demand for HB-LED backlighting applications. The book-to-bill ratio, which is calculated by dividing orders received in a given period by revenue recognized in the same time period, in that segment increased to 3.38 from 0.63 in the comparable quarter of 2008, indicating a strong improvement in business for the LED & Solar segment. Data Storage Process Equipment segment sales declined by 49.8% as compared to the third quarter of 2008 resulting from the continued slowdown in capital spending by our data storage customers. Additionally, Metrology sales decreased by 23.0% as compared to the third quarter of 2008, primarily due to a slowdown in the

Table of Contents

semiconductor and data storage markets. By region, net sales decreased by 53.0%, 32.9% and 24.1% in the Americas, EMEA and Japan, respectively, and were up 35.5% in Asia Pacific primarily as a result of the increase in demand for HB-LED products. We believe that there will continue to be quarter-to-quarter variations in the geographic distribution of sales.

Orders for the third quarter of 2009 increased by 150.2% from the comparable 2008 period, mainly due to the \$179.2 million in LED & Solar Process Equipment orders, which were principally driven by HB-LED manufacturers ramping up production for television and laptop backlighting applications. The 46.7% decrease in Data Storage Process Equipment orders resulted from customers continuing to be cautious about their capital spending. The 8.9% decrease in Metrology orders is principally due to low demand from customers in the semiconductor and data storage markets.

Our overall book-to-bill ratio for the third quarter of 2009 was 2.28 to 1, an improvement over the ratio of 0.78 to 1 in the comparable quarter of 2008. Our backlog as of September 30, 2009 was \$286.5 million, compared to \$147.2 million as of December 31, 2008. During the quarter ended September 30, 2009, we experienced backlog adjustments of approximately \$0.4 million. Due to changing business conditions and weak capital equipment spending by certain customers in our businesses, we may continue to experience cancellations and/or rescheduling of orders.

*Gross Profit*

Gross margin for the quarter ended September 30, 2009, was 41.4%, compared to 39.8% in the third quarter of 2008, primarily due to material cost savings, the impact of manufacturing and overhead cost reductions associated with the reduction in workforce, and favorable product mix. LED & Solar Process Equipment gross margins increased to 41.7% from 36.0% in the prior-year period, primarily due to an increase in sales volume and a decrease in product costs associated with increased purchasing to support multiple tool orders received from our HB-LED customers compared to the prior-year period. In addition, the prior-year period included a reduction in LED & Solar gross profit of \$0.9 million related to the acquisition of Mill Lane. This reduction was the result of purchase accounting, which required adjustments to capitalize inventory at fair value. Data Storage Process Equipment gross margins remained flat despite a 50% decrease in sales volume as a result of cost reductions and improved product mix. Metrology gross margins decreased to 42.0% from 44.9%, principally due to lower sales volume.

*Operating Expenses*

Selling, general and administrative expenses decreased by \$2.5 million, or 10.8%, from the prior-year period, primarily due to lower salary and related expenses resulting from the personnel reductions taken as part of management's restructuring plan as well as cost savings initiatives resulting in less occupancy, travel and entertainment, marketing, and other operating expenses. This decrease was partially offset by an increase in bonus and profit sharing and higher variable expenses associated with the sales ramp in our LED & Solar segment.

Research and development expense decreased \$1.6 million from the third quarter of 2008, primarily due to a more focused approach to metrology and data storage product development, which were partially offset by the continuation of investments in higher-growth end market opportunities, particularly in our LED & Solar segment. As a percentage of sales, research and development increased to 13.9% in the third quarter of 2009 from 13.2% in the third quarter of 2008.

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Amortization expense was \$1.8 million in the third quarter of 2009, compared to \$3.1 million in the third quarter of 2008, primarily due to a reduction in our intangible assets resulting from asset impairment charges taken during the fourth quarter of 2008.

Restructuring expense of \$1.2 million for the third quarter of 2009 consisted primarily of personnel severance and related costs resulting from the reduction in workforce. Restructuring expense of \$4.1 million during the third quarter of 2008 consisted of \$3.7 million associated with the mutually agreed upon termination of the employment agreement of the Company's former CEO, as well as \$0.4 million for severance and lease-related charges in our Metrology segment.

Table of Contents

*Interest Expense, Net*

Net interest expense was \$1.7 million in the third quarter of 2009, compared to \$1.8 million in the third quarter of 2008. Included in both periods was \$0.7 million in non-cash interest expense related to the implementation of new accounting guidance that requires a portion of convertible debt to be allocated to equity. The resultant debt discount is then amortized into interest expense. See *Recent Accounting Pronouncements* for a further discussion of the implementation of this new guidance.

*Income Taxes*

The income tax provision for the quarter ended September 30, 2009 was \$0.6 million compared to \$0.8 million in the third quarter of 2008. The 2009 provision for income taxes included \$0.4 million relating to our foreign operations, which continue to be profitable, and \$0.2 million relating to our domestic operations. The 2008 provision for income taxes included \$0.5 million relating to our foreign operations, and \$0.3 million relating to our domestic operations. Due to significant domestic net operating loss carry forwards, which are fully reserved by a valuation allowance, our domestic operations are not expected to incur significant income taxes for the foreseeable future.

*Nine Months Ended September 30, 2009 and 2008*





## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

The following table shows our Condensed Consolidated Statements of Operations, percentages of sales, and comparisons between the nine months ended September 30, 2009 and 2008 (dollars in thousands):

	2009		Nine months ended September 30, 2008		Dollar and Percentage Change (1)		
Net sales	\$	233,782	100.0%	\$	332,465	100.0%	\$ (98,683) (29.7)%
Cost of sales		148,108	63.4		196,026	59.0	(47,918) (24.4)
Gross profit		85,674	36.6		136,439	41.0	(50,765) (37.2)
Operating expenses:							
Selling, general, and administrative expense		59,471	25.4		70,528	21.2	(11,057) (15.7)
Research and development expense		39,770	17.0		45,173	13.6	(5,403) (12.0)
Amortization expense		5,437	2.3		7,530	2.3	(2,093) (27.8)
Restructuring expense		7,567	3.2		6,995	2.1	572 8.2
Asset impairment charge		304	0.1		285	0.1	19 6.7
Other expense (income), net		1,097	0.5		(591)	(0.2)	1,688 N/M
Total operating expenses		113,646	48.6		129,920	39.1	(16,274) (12.5)
Operating (loss) income		(27,972)	(12.0)		6,519	2.0	(34,491) N/M
Interest expense, net		5,063	2.2		5,097	1.5	(34) (0.7)
(Loss) income before income taxes		(33,035)	(14.1)		1,422	0.4	(34,457) N/M
Income tax provision		1,342	0.6		2,860	0.9	(1,518) (53.1)
Loss including noncontrolling interest		(34,377)	(14.7)		(1,438)	(0.4)	(32,939) (2,290.6)
Noncontrolling interest		(65)	(0.0)		(200)	(0.1)	135 (67.5)
Net income (loss) attributable to Veeco	\$	(34,312)	(14.7)%	\$	(1,238)	(0.4)%	\$ (33,074) (2,671.6)%

(1) N/M denotes not meaningful as change moves from negative to positive, or vice versa.

Table of Contents*Net Sales and Orders*

Net sales of \$233.8 million for the nine months ended September 30, 2009 were down 29.7% compared to the comparable 2008 period. The following is an analysis of sales and orders by segment and by region (dollars in thousands):

	Sales				Orders				Book-to-Bill Ratio	
	Nine months ended		Dollar and		Nine months ended		Dollar and		2009	2008
	September 30, 2009	September 30, 2008	Percentage Change	Year to Year	September 30, 2009	September 30, 2008	Percentage Change	Year to Year		
<b>Segment Analysis</b>										
LED & Solar Process Equipment	\$ 107,050	\$ 128,205	\$ (21,155)	(16.5)%	\$ 264,092	\$ 116,513	\$ 147,579	126.7%	2.47	0.91
Data Storage Process Equipment	56,219	104,096	(47,877)	(46.0)	44,379	124,685	(80,306)	(64.4)	0.79	1.20
Metrology	70,513	100,164	(29,651)	(29.6)	68,886	94,738	(25,852)	(27.3)	0.98	0.95
<b>Total</b>	<b>\$ 233,782</b>	<b>\$ 332,465</b>	<b>\$ (98,683)</b>	<b>(29.7)%</b>	<b>\$ 377,357</b>	<b>\$ 335,936</b>	<b>\$ 41,421</b>	<b>12.3%</b>	<b>1.61</b>	<b>1.01</b>
<b>Regional Analysis</b>										
Americas	\$ 62,101	\$ 116,631	\$ (54,530)	(46.8)%	\$ 70,668	\$ 124,666	\$ (53,998)	(43.3)%	1.14	1.07
EMEA	52,328	69,607	(17,279)	(24.8)	46,889	57,664	(10,775)	(18.7)	0.90	0.83
Japan	15,000	29,347	(14,347)	(48.9)	20,325	24,548	(4,223)	(17.2)	1.36	0.84
Asia Pacific	104,353	116,880	(12,527)	(10.7)	239,475	129,058	110,417	85.6	2.29	1.10
<b>Total</b>	<b>\$ 233,782</b>	<b>\$ 332,465</b>	<b>\$ (98,683)</b>	<b>(29.7)%</b>	<b>\$ 377,357</b>	<b>\$ 335,936</b>	<b>\$ 41,421</b>	<b>12.3%</b>	<b>1.61</b>	<b>1.01</b>

Sales declined in each segment for the nine months ended September 30, 2009 compared with the same period in 2008 due to our customers reluctance to order capital equipment during the first half of 2009. LED & Solar Process Equipment sales were down 16.5% from the same period of 2008 primarily due to a pause in capacity spending as HB-LED customers were cautious in ordering new equipment during the economic slowdown. Data Storage Process Equipment segment sales declined by 46.0% compared to the same period of 2008 due to a slowdown in capital spending by our data storage customers. Metrology sales decreased by 29.6% from the same period of 2008, primarily due to a slowdown in the semiconductor, data storage and research and industrial markets. By region, net sales decreased by 46.8%, 24.8%, 48.9%, and 10.7% in the Americas, EMEA, Japan, and Asia Pacific, respectively. We believe that there will continue to be quarter-to-quarter variations in the geographic distribution of sales.

Orders for the nine months ended September 30, 2009 increased by 12.3% from the comparable 2008 period. On a segment basis, orders for LED & Solar Process Equipment increased by 126.7% from the comparable period in 2008, principally driven by HB-LED manufacturers increasing production for television and laptop backlighting applications and demand for CIGS deposition systems and components. The 64.4% decrease in Data Storage Process Equipment orders resulted from the continued slow down in our customers capital spending. The 27.3% decrease in Metrology orders is due to a decrease in demand from customers in the semiconductor, data storage and research and industrial markets.

Our overall book-to-bill ratio was 1.61 for the nine months ended September 30, 2009, compared to 1.01 for the comparable period in 2008. The book-to-bill ratio for the LED & Solar Process Equipment segment improved to 2.47 to 1 from 0.91 to 1 in the same period in 2008. Our backlog as of September 30, 2009 was \$286.5 million, compared to \$147.2 million as of December 31, 2008. During the nine months ended September 30, 2009, we experienced backlog adjustments of approximately \$4.3 million, consisting of \$3.3 million for order cancellations and \$1.0 million of adjustments related to foreign currency translation. Due to changing business conditions and weak capital equipment spending by certain customers in our businesses, we may continue to experience cancellations and/or rescheduling of orders.



Table of Contents

*Gross Profit*

Gross margin for the nine months ended September 30, 2009, was 36.6%, compared to 41.0% in the comparable 2008 period, primarily due to the significant decline in sales. LED & Solar Process Equipment gross margins decreased from 39.6% in the prior-year period to 36.4%, primarily due to a 16.5% decrease in sales volume as compared to the prior-year period. Data Storage Process Equipment gross margins decreased from 38.9% in the prior-year period to 34.4%, due to reduced sales volume as well as a charge of \$1.5 million to write-off inventory in the first quarter of 2009 associated with certain discontinued data storage product lines. Metrology gross margins decreased from 45.2% in the prior year period to 38.8%, principally due to lower sales volume.

*Operating Expenses*

Selling, general and administrative expenses decreased by \$11.1 million, or 15.7%, from the prior-year period, primarily due to lower salary and related expenses resulting from the personnel reductions taken as part of management's restructuring plan, a reduction in incentive bonuses and profit sharing as well as cost savings initiatives resulting in less travel and entertainment, occupancy, and consulting, legal, and professional expenses.

Research and development expense decreased \$5.4 million from the comparable period of 2008, primarily due to a more focused approach to metrology and data storage product development, which was partially offset by the continuation of investments in areas that we believe are higher-growth end market opportunities, particularly in our LED & Solar segment. As a percentage of sales, research and development increased to 17.0% in the nine months ended September 30, 2009 from 13.6% in the same period in 2008.

Amortization expense was \$5.4 million in the nine months ended September 30, 2009, compared to \$7.5 million in comparable period of 2008, due to a reduction in our intangible assets resulting from asset impairment charges taken during the fourth quarter of 2008.

Restructuring expense of \$7.6 million for the nine months ended September 30, 2009 consisted of \$6.3 million of personnel severance costs resulting from a reduction in workforce. In addition, there were \$0.9 million of lease-related costs and \$0.4 million of moving and consolidation costs incurred in our Data Storage Process Equipment segment associated with vacating our Camarillo, CA facilities. Restructuring expense of \$7.0 million incurred during the nine months ended September 30, 2008 consisted of \$3.7 million associated with the mutually agreed upon termination of the employment agreement of the Company's former CEO, \$2.6 million of costs associated with the consolidation and relocation of our Corporate headquarters, \$0.4 million of personnel severance and related costs and \$0.3 million for lease-related charges in Metrology.

Other expense (income), net for the nine months ended September 30, 2009 includes foreign currency exchange losses of \$1.4 million.

*Interest Expense, Net*

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Net, interest expense for the nine months ended September 30, 2009 was \$5.1 million, comprised of \$3.0 million in cash net interest expense and \$2.1 million in non-cash interest expense related to the implementation of new accounting guidance that requires a portion of convertible debt to be allocated to equity. See *Recent Accounting Pronouncements* for further discussion of the implementation of this new guidance. Net interest expense for the nine months ended September 30, 2008 was \$5.1 million, comprised of \$2.9 million in cash net interest expense and \$2.2 million in non-cash interest expense that is presented pursuant to the retroactive presentation requirements of the new accounting guidance.

### *Income Taxes*

Income tax provision for the nine months ended September 30, 2009 was \$1.3 million compared to \$2.9 million in the comparable prior year period. The 2009 provision for income taxes included \$0.9 million relating to our foreign operations, and \$0.4 million relating to our domestic operations. The 2008 provision for income taxes included \$1.9 million relating to our foreign operations, and \$1.0 million relating to our domestic operations. Due to significant domestic net operating loss carry forwards, which are fully reserved by a valuation allowance, our domestic operations are not expected to incur significant income taxes for the foreseeable future.

Table of Contents**Liquidity and Capital Resources**

Historically, our principal cash requirements have included the funding of acquisitions, capital expenditures and the repayment of debt. We traditionally have generated cash from operations and financing activities with the issuance of debt and common stock. Our ability to generate sufficient cash flows from operations is dependent on the continued demand for our products and services. A summary of the cash flow activity for the nine months ended September 30, 2009 and 2008 is as follows (in thousands):

	Nine months ended September 30,	
	2009	2008
Net cash provided by operating activities	\$ 20,471	\$ 22,420
Net cash used in investing activities	(17,084)	(21,296)
Net cash provided by (used in) financing activities	2,263	(558)
Effect of exchange rates on cash and cash equivalents	(8)	35
Net change in cash and cash equivalents	5,642	601
Cash and cash equivalents at beginning of period	103,799	117,083
Cash and cash equivalents at end of period	\$ 109,441	\$ 117,684

We had a net increase in cash of \$5.6 million during the nine months ended September 30, 2009. Cash provided by operations was \$20.5 million for this period, as compared to cash provided by operations of \$22.4 million for the comparable 2008 period. Net loss adjusted for non-cash items used operating cash flows of \$7.6 million for the nine months ended September 30, 2009. Net cash provided by operations for the nine months ended September 30, 2009 was favorably impacted by a net decrease in net operating assets and liabilities of \$28.1 million. This was driven by a decrease in inventories of approximately \$19.5 million due to reduction efforts and the impact of outsourcing and a \$14.9 million increase in accrued expenses, principally resulting from customer deposits associated primarily with the significant increase in orders in our LED & Solar segment. These amounts were partially offset by an increase in accounts receivable of \$4.1 million.

We had a net increase in cash of \$0.6 million during the nine months ended September 30, 2008. Cash provided by operations was \$22.4 million for this period. Net income adjusted for non-cash items provided operating cash flows of \$29.1 million for the nine months ended September 30, 2008. Net cash provided by operations for the nine months ended September 30, 2008 was unfavorably impacted by a net increase in net operating assets and liabilities of \$6.6 million. This was driven by a decrease in accounts payable and accrued expenses of approximately \$9.6 million over the prior period and an increase of \$2.0 million in capitalized patent costs, which were partially offset by a decrease in accounts receivable of \$6.6 million.

Cash used in investing activities of \$17.1 million for the nine months ended September 30, 2009 resulted primarily from \$9.8 million of earn-out payments made to the former owners of Mill Lane and Fluens, capital expenditures of \$5.2 million, \$1.9 million in payments made to acquire assets from Daystar Technologies, Inc. and \$0.5 million of payments made to purchase the remaining 80.1% interest in Fluens. During the remainder of 2009, we expect to invest an estimated additional \$5.0 million in capital projects primarily related to engineering equipment and lab tools used in producing, testing and process development of our products and enhanced manufacturing facilities. Cash used in investing activities of \$21.3 million for the nine months ended September 30, 2008 resulted primarily from the acquisition of Mill Lane for \$11.0 million, net of cash acquired, as well as capital expenditures of \$10.4 million.





Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Cash provided by financing activities for the nine months ended September 30, 2009 totaled \$2.3 million, resulting primarily from \$2.9 million of proceeds received from stock issuances resulting from stock option exercises

Table of Contents

during the third quarter of 2009. Cash used in financing activities for the nine months ended September 30, 2008 totaled \$0.6 million, resulting from \$1.0 million in restricted stock tax withholdings and \$0.3 million in mortgage payments, offset by proceeds of \$0.7 million from stock issuances resulting from stock option exercises.

As of September 30, 2009, we have outstanding \$105.6 million aggregate principal amount of 4.125% convertible subordinated notes due April 15, 2012 (the Notes). We pay interest on the Notes on April 15 and October 15 of each year. We have previously engaged in repurchase transactions of our Notes and may enter into similar transactions in the future depending on market conditions, our cash position and other factors.

In February 2009, we entered into an amendment to our existing credit agreement with HSBC Bank USA, National Association (HSBC), as administrative agent, and the lenders named therein (as amended, the Credit Agreement). As part of the amendment, we reduced the amount of the revolving credit facility, modified certain existing covenants and added certain new covenants. As amended, the Credit Agreement provides for revolving credit borrowings of up to \$30.0 million. The Credit Agreement was amended effective March 27, 2009 to modify certain financial covenants, to provide for the cash collateralization of borrowings and letters of credit outstanding under the Credit Agreement, and to permit the acquisition of the 80.1% of the outstanding stock of Fluens Corporation (Fluens) which we did not yet own. The annual interest rate under the Credit Agreement is a floating rate equal to the prime rate of the agent bank plus 2.0%. A LIBOR-based interest rate option is also provided. Borrowings may be used for general corporate purposes, including working capital requirements, as well as permitted acquisitions. The Credit Agreement contains certain restrictive covenants which include the maintenance of minimum cash balances and limitations with respect to incurrence of indebtedness, the payment of dividends, long-term leases, investments, mergers, acquisitions, consolidations and sales of assets. In addition, under the Credit Agreement, we are required to satisfy certain financial tests, including minimum profitability levels. As of September 30, 2009, we were in compliance with all covenants of the Credit Agreement as amended. Substantially all of our assets and those of our material domestic subsidiaries, other than real estate, have been pledged to secure our obligations under the Credit Agreement. The revolving credit facility under the Credit Agreement expires on March 31, 2012. During the first nine months of 2009, we recognized an expense of \$0.2 million representing the amount of deferred financing fees equal to the portion of the revolving credit facility which was terminated in connection with the amendment, which is included in other expense, net. We also capitalized \$0.1 million in deferred financing fees that we incurred in connection with the February 2009 amendment. There were no borrowings outstanding as of September 30, 2009 under the Credit Agreement, and no borrowings outstanding as of December 31, 2008 under the prior credit agreement. Letters of credit outstanding at September 30, 2009 and December 31, 2008 totaled approximately \$0.5 million and \$0.4 million, respectively. In the second quarter of 2009 we transferred \$0.5 million of cash into a restricted cash account pursuant to the terms of the March 2009 amendment, which requires cash collateralization of borrowings and letters of credit. This amount is included in prepaid and other current assets. We recorded interest expense associated with the Credit Agreement during the nine months ended September 30, 2009 and 2008, respectively, of approximately \$0.2 million in each period.

We believe that existing cash balances together with cash generated from operations and amounts available under the Credit Agreement will be sufficient to meet our projected working capital and other cash flow requirements for the next twelve months, as well as our contractual obligations. We believe we will be able to meet our obligation to repay the \$105.6 million outstanding Notes that mature on April 15, 2012 through a combination of conversion of the notes outstanding, refinancing, cash generated from operations, and other means.

In 2006, we invested \$0.5 million to purchase 19.9% of the common stock of Fluens. Veeco and Fluens have jointly developed a next-generation process for high-rate deposition of aluminum oxide for data storage applications. In May 2009, we purchased the remaining 80.1% of the outstanding stock of Fluens for \$1.5 million plus an earn-out arrangement based on future performance. We paid \$0.5 million of the \$1.5 million upon closing, as well as \$0.2 million in respect of the earn-out arrangement. We paid a second installment of \$0.5 million of the purchase price on September 30, 2009. We will pay the remaining \$0.5 million of the \$1.5 million in the fourth quarter of 2009, which is included in accrued expenses in the accompanying condensed Balance Sheet at September 30, 2009. Prior to our purchase of the remaining 80.1%, approximately 31% of Fluens was owned by an individual then serving as Senior Vice President of Veeco.

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

Table of Contents

**Contractual Obligations**

Significant changes to our Contractual Obligations table in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations of our 2008 Annual Report on Form 10-K include the following:

- a \$9.6 million earn-out payment related to the Mill Lane acquisition, which we made in the first quarter of 2009;
- Payment of \$0.5 million of the purchase price for Fluens was made on September 30, 2009. We will pay the remaining \$0.5 million of the \$1.5 million in the fourth quarter of 2009, which is included in accrued expenses in the accompanying condensed Balance Sheet at September 30, 2009;
- potential earn-out payments related to the purchase of Fluens, \$0.2 million of which we paid in the second quarter of 2009; and
- the increase in our purchase commitments from \$27.7 million at December 31, 2008 to \$76.7 million at September 30, 2009. The majority of the increase in purchase commitments at September 30, 2009 relates to increases in purchase orders for materials to fulfill customer sales orders for MOCVD tools.

Table of Contents

**Application of Critical Accounting Policies**

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

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

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

**Instruments** For standard products produced according to our published specifications, principally metrology instruments sold typically to universities, research facilities and scientific centers and in general industrial applications where installation is inconsequential or perfunctory and no substantive customer acceptance provisions exist, revenue is recognized when title and risk of loss pass to the customer, either at time of shipment or delivery. Acceptance of the product by the customer is based upon meeting standard published specifications. Customer acceptance provisions include initial setup at the customer site, performance of functional test procedures and calibration testing of the basic features and functionality of the product. These provisions are a replication of the testing performed in our facilities prior to shipment. The skills and equipment required to complete installation of such instruments are not specialized and are readily available in the market and are often performed by distributors or representative organizations.

Systems - Process equipment systems and certain metrology systems, which are sold to manufacturers in the HB-LED, solar, data storage and semiconductor industries and are used in manufacturing facilities and commercial production environments typically include process acceptance criteria based upon Veeco and/or customer specifications. We are generally required to install these products and demonstrate compliance with acceptance tests at the customer's facility. Generally, based upon the terms of the sales arrangement, these products are sold with a retention (typically 10% to 20% of the sales contract value) which is payable by the customer when installation and field acceptance is completed. Such installations are not considered complex and are not deemed essential to the functionality of the equipment because they do not involve significant changes to the features or capabilities of the equipment or involve building complex interfaces or connections. Installation normally represents only 2% - 4% of the fair value of the sales contract. Sales arrangements for these systems are bifurcated into separate units of accounting or elements based on objective evidence of fair value. The two elements are the system and installation of the system. The amount of revenue allocated to each element is based upon its relative fair value. The price charged when the system or installation service is sold separately generally determines fair value. The value of the installation service is based upon the fair value of the service performed, including labor, which is based upon the estimated time to complete the installation at hourly rates, and material components. We recognize revenue for the system or delivered element since the delivered item has value to the customer on a standalone basis, there is objective and

Table of Contents

reliable evidence of the fair value of the undelivered item (*i.e.*, the installation service) and delivery or performance of the undelivered item is considered probable and substantially in our control, based on our historical experience. The value of the undelivered element is the greater of the fair value of the installation or the portion of the sales price that will not be received until the installation is completed (*i.e.*, the retention amount). System revenue is generally recognized upon shipment or delivery provided title and risk of loss has passed to the customer. Revenue from installation services is recognized at the time acceptance is received from the customer. If the arrangement does not meet all the above criteria, the entire amount of the sales arrangement is deferred until the criteria have been met or all elements have been delivered to the customer or been completed.

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

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

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

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

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

Pursuant to relevant accounting pronouncements we are required to determine if it is appropriate to use the operating segment as defined under such pronouncements as the reporting unit, or one level below the operating segment, depending on whether certain criteria are met. We have identified four reporting units that are required to be reviewed for impairment. The reporting units are Data Storage Process Equipment, LED &

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Solar Process Equipment, AFM and Optical Metrology. AFM and Optical Metrology comprise the Metrology operating segment. In identifying the reporting units management considered the economic characteristics of operating segments including the products and services provided, production processes, types or classes of customer and product distribution.

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



Table of Contents

premium.

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

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

*Fair Value Measurements:* On January 1, 2009, we implemented new accounting guidance for our non-financial assets and non-financial liabilities. This new guidance requires that we disclose the type of inputs we use to value our assets and liabilities, based on three categories of inputs as defined in such. Level 1 inputs are quoted, unadjusted prices in active markets for identical assets or liabilities that the company has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as quoted prices for similar assets or liabilities. Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. These requirements apply to our long-lived assets, goodwill, and intangible assets. We use Level 3 inputs to value all of such assets, and the methodology we use to value such assets has not changed since December 31, 2008. The Company primarily applies the market approach for recurring fair value measurements.

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

*Income Taxes:* As part of the process of preparing our Consolidated Financial Statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating the actual current

tax expense, together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our Consolidated Balance Sheets. The carrying value of our deferred tax assets is adjusted by a valuation allowance to recognize the extent to which the future tax benefits will be recognized on a more likely than not basis. Our net deferred tax assets consist primarily of net operating loss and tax credit carry forwards, and timing differences between the book and tax treatment of inventory, acquired intangible assets and other asset valuations. Realization of these net deferred tax assets is dependent upon our ability to generate future taxable income.

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

Table of Contents

At September 30, 2009, we had a valuation allowance of approximately \$90.5 million against substantially all of our domestic net deferred tax assets, which consist of net operating loss and tax credit carry forwards, as well as temporary deductible differences. If we are able to realize part or all of the domestic deferred tax assets in future periods, we will reduce our provision for income taxes with a release of the valuation allowance in an amount that corresponds with the income tax liability generated.

Relevant accounting guidance addresses the determination of how tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under such guidance, we must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such uncertain tax positions are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate resolution. We had approximately \$1.1 million and \$1.0 million of unrecognized tax benefits at September 30, 2009 and December 31, 2008, respectively, which predominantly relate to positions taken on our foreign tax returns and all of which represent the amount of unrecognized tax benefits that, if recognized, would favorably impact the effective income tax rate in future periods.

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

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

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

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

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

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

#### **Recent Accounting Pronouncements**

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

Table of Contents

In October 2009, the FASB issued amended guidance that is expected to significantly affect how entities account for revenue arrangements that contain both hardware and software elements. As a result, many tangible products that rely on software will be accounted for under the revised multiple-element arrangements revenue recognition guidance, rather than the software revenue recognition guidance. The revised guidance must be adopted by all entities no later than fiscal years beginning on or after June 15, 2010. An entity must select the same transition method and same period for the adoption of both this guidance and the revisions to the multiple-element arrangements guidance noted above. The Company does not believe that this guidance will have a material impact on its consolidated financial statements.

*Convertible debt:* In May 2008, new accounting guidance was issued that requires a portion of convertible debt to be allocated to equity. We implemented the new guidance as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. This new guidance requires issuers of convertible debt that can be settled in cash to separately account for (*i.e.*, bifurcate) a portion of the debt associated with the conversion feature and reclassify this portion to stockholders' equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value over the life of the debt using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as interest expense. The Notes are subject to such accounting guidance since they may be settled in cash upon conversion. Thus, as a result of the adoption of this accounting guidance, we reclassified approximately \$16.3 million from long-term debt to additional paid-in capital effective as of the date of issuance of the Notes. This reclassification created a \$16.3 million discount on the debt that will be amortized over the remaining life of the Notes, which will be through April 15, 2012. The reclassification generated a \$6.7 million deferred tax liability, which we offset with a corresponding decrease of the valuation allowance by the same amount. Prior periods are presented as if the new guidance was in effect as of the date of issuance. Thus, we have presented all financial data for prior periods in this report as if we had reclassified the \$16.3 million and began amortizing the resultant debt discount in April 2007. The retrospective application of the new guidance described above to the results for the three and nine months ended September 30, 2008 increased the net loss attributable to Veeco in the three-month period from (\$1,673) to (\$2,413) and decreased the net income attributable to Veeco in the nine-month period from \$946 to a net loss of (\$1,238), and increased the loss per share attributable to Veeco in the three-month period from (\$0.05) to (\$0.08) and decreased the earnings per share in the nine-month period from \$0.03 to a loss per share of (\$0.04).

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

For the three months ended September 30, 2009 and 2008, respectively, we recorded approximately \$0.7 million of additional interest expense in each period resulting from the amortization of the debt discount. For the nine months ended September 30, 2009 and 2008, respectively, we recorded approximately \$1.4 million of additional interest expense in each period resulting from the amortization of the debt discount. This additional interest expense did not require the use of cash.

## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

The total effect on equity as of the date of adoption on January 1, 2009 was a net increase of \$10.3 million, comprised of an increase in additional paid-in capital of \$16.3 million and an increase in the accumulated deficit of \$6.0 million. The \$6.0 million is comprised of \$2.9 million and \$1.9 million in amortization of the debt discount for 2008 and 2007, respectively, as well as the \$1.2 million reduction in the gain that was recorded on the November 2008 repurchases.

*Noncontrolling Interest:* In December 2007, new accounting requirements were issued by the FASB with the objective to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements. The most significant provisions of this statement result in changes to the presentation of noncontrolling interests in the consolidated financial statements. We implemented these new rules as of January 1, 2009. The adoption of this statement impacted the manner in which we present

Table of Contents

noncontrolling interests for all periods included in this report, but did not impact our consolidated financial position or results of operations.

*Fair Value:* In April 2009, the FASB issued new guidance to require disclosures about the fair value of financial instruments in interim financial statements in addition to the existing requirement for annual financial statements. We adopted these new rules for the period ended June 30, 2009.

*Subsequent Events:* In May 2009, the FASB issued a new pronouncement relating to subsequent events. The term *subsequent events* refers to events that occur after the last date in the period on which we are reporting through the date the financial statements are issued, and which may require recognition or disclosure in the financial statements. Adoption of this pronouncement should not result in significant changes in the subsequent events that are reported, but rather requires disclosure of the date through which the company evaluates whether subsequent events have occurred. We have evaluated subsequent events from the date of these financial statements through the date on which these financial statements were issued.

Table of Contents

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

Our net sales to foreign customers represented approximately 81.5% and 73.4%, respectively, of our total net sales for the three months and nine months ended September 30, 2009, and 66.4% and 64.9%, respectively, for the comparable 2008 periods. We expect that net sales to foreign customers will continue to represent a large percentage of our total net sales. Our net sales denominated in foreign currencies represented approximately 13.6% and 9.7%, of our total net sales for the three months and nine months ended September 30, 2009, respectively, and 13.2% and 13.9%, respectively, for the comparable 2008 periods.

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

We are exposed to financial market risks, including changes in foreign currency exchange rates. The changes in currency exchange rates that have the largest impact on translating our international operating profit to U.S. dollars are the Euro and the Japanese Yen. We use derivative financial instruments to mitigate these risks. We do not use derivative financial instruments for speculative or trading purposes. We generally enter into monthly forward contracts to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known currency exposures. The weighted average notional amount of derivative contracts outstanding during the three months and nine months ended September 30, 2009 was \$1.3 million and \$3.1 million, respectively.

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

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

Assuming third quarter 2009 variable debt and investment levels, the effect of a one-point change in interest rates would not have a material effect on net interest expense.

**Item 4. Controls and Procedures.**



## Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

We have evaluated the effectiveness of the design and operation of our disclosure controls and procedures under the supervision of and with the participation of management, including the chief executive officer and chief financial officer, as of the end of the period covered by this report. Based on that evaluation, our chief executive officer and our chief financial officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Table of Contents

**Part II. OTHER INFORMATION**

**Item 1. Legal Proceedings.**

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

**Item 1A. Risk Factors.**

Information regarding risk factors appears in the Safe Harbor Statement at the beginning of this Quarterly Report on Form 10-Q and in Part I Item 1A of our 2008 Annual Report and Quarterly Report on form 10-Q for the quarterly period ended June 30, 2009. There have been no material changes from the risk factors previously disclosed in our 2008 Annual Report and Quarterly Report on form 10-Q for the quarterly period ended June 30, 2009.

Table of Contents**Item 6. Exhibits.**

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

Number	Description	Incorporated by Reference to the Following Document:
3.1	Amendment to Certificate of Incorporation of Veeco dated May 16, 2002	*
10.1	Veeco Instruments Inc. 2009 Management Bonus Plan dated February 27, 2009	*
10.2	Veeco Instruments Inc. 2009 Supplemental Management Profit Sharing Plan dated August 20, 2009	*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	*

---

\* Filed herewith

Table of Contents

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: October 26, 2009

Veeco Instruments Inc.

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

By: /s/ JOHN F. REIN, JR.  
John F. Rein, Jr.  
*Executive Vice President and Chief Financial Officer*

Table of Contents**INDEX TO EXHIBITS**

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

<b>Number</b>	<b>Description</b>	<b>Incorporated by Reference to the Following Document:</b>
3.1	Amendment to Certificate of Incorporation of Veeco dated May 16, 2002	*
10.1	Veeco Instruments Inc. 2009 Management Bonus Plan dated February 27, 2009	*
10.2	Veeco Instruments Inc. 2009 Supplemental Management Profit Sharing Plan dated August 20, 2009	*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities and Exchange Act of 1934.	*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*

---

\* Filed herewith