

VEECO INSTRUMENTS INC
Form 10-Q
July 29, 2010
Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2010

OR

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

For the transition period from _____ to _____.

Commission file number 0-16244

VEECO INSTRUMENTS INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

11-2989601
(I.R.S. Employer
Identification Number)

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

11803
(Zip Code)

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

Website: **www.veeco.com**

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a Smaller reporting company)

Smaller reporting company

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

40,877,302 shares of common stock, \$0.01 par value per share, were outstanding as of the close of business on July 27, 2010.

Table of Contents

SAFE HARBOR STATEMENT

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

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

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

Table of Contents

- The enforcement and protection of our intellectual property rights may be expensive and could divert our valuable resources;
- We may be subject to claims of intellectual property infringement by others;
- Our acquisition strategy subjects us to risks associated with evaluating and pursuing these opportunities and integrating these businesses;
- We may be required to take additional impairment charges for goodwill and indefinite-lived intangible assets or definite-lived intangible and long-lived assets;
- Changes in accounting pronouncements or taxation rules or practices may adversely affect our financial results;
- We are subject to the internal control evaluations and attestation requirements of Section 404 of the Sarbanes-Oxley Act;
- We are subject to risks of non-compliance with environmental, health and safety regulations;
- We have 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
- The matters set forth in this Report generally, including the risk factors set forth in Part 2. Item 1A. Risk Factors.

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

Available Information

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

Internet Address

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

Table of Contents

VEECO INSTRUMENTS INC.

INDEX

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1.</u>	
<u>Financial Statements:</u>	
<u>Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for the Three and Six Months Ended June 30, 2010 and 2009 (Unaudited)</u>	5
<u>Condensed Consolidated Balance Sheets as of June 30, 2010 (Unaudited) and December 31, 2009</u>	6
<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2010 and 2009 (Unaudited)</u>	7
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	8
<u>Item 2.</u>	
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
<u>Item 3.</u>	
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	29
<u>Item 4.</u>	
<u>Controls and Procedures</u>	29
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1.</u>	
<u>Legal Proceedings</u>	31
<u>Item 1A.</u>	
<u>Risk Factors</u>	31
<u>Item 6.</u>	
<u>Exhibits</u>	31
<u>SIGNATURES</u>	32

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		Six months ended	
	2010	2009	2010	2009
Net sales	\$ 253,040	\$ 72,020	\$ 416,271	\$ 134,869
Cost of sales	139,282	47,636	232,164	90,103
Gross profit	113,758	24,384	184,107	44,766
Operating expenses (income):				
Selling, general and administrative	27,287	19,822	50,707	38,429
Research and development	20,550	13,163	36,990	26,049
Amortization	1,634	1,831	3,319	3,660
Restructuring		1,944	(179)	6,375
Asset impairment charge		304		304
Other, net	512	(77)	359	1,409
Total operating expenses	49,983	36,987	91,196	76,226
Operating income (loss)	63,775	(12,603)	92,911	(31,460)
Interest expense, net	1,762	1,698	3,544	3,407
Income (loss) before income taxes	62,013	(14,301)	89,367	(34,867)
Income tax provision	9,620	402	10,930	780
Net income (loss)	52,393	(14,703)	78,437	(35,647)
Net loss attributable to noncontrolling interest		(23)		(65)
Net income (loss) attributable to Veeco	\$ 52,393	\$ (14,680)	\$ 78,437	\$ (35,582)
Income (loss) per common share attributable to Veeco:				
Basic	\$ 1.32	\$ (0.47)	\$ 2.00	\$ (1.13)
Diluted	\$ 1.20	\$ (0.47)	\$ 1.88	\$ (1.13)
Weighted average shares outstanding:				
Basic	39,761	31,497	39,283	31,506
Diluted	43,506	31,497	41,683	31,506

Veeco Instruments Inc. and Subsidiaries**Condensed Consolidated Statements of Comprehensive Income (Loss)****(In thousands)**

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2010	2009	2010	2009
Net income (loss)	\$ 52,393	\$ (14,703)	\$ 78,437	\$ (35,647)
Other comprehensive (loss) income, net of tax				
Foreign currency translation	(152)	719	(825)	(946)
Comprehensive income (loss)	52,241	(13,984)	77,612	(36,593)
Comprehensive loss attributable to noncontrolling interest		(23)		(65)
Comprehensive income (loss) attributable to Veeco	\$ 52,241	\$ (13,961)	\$ 77,612	\$ (36,528)

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

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

	June 30, 2010 (Unaudited)	December 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	\$ 361,382	\$ 148,589
Short-term investments	53,500	135,000
Accounts receivable, net	140,722	84,358
Inventories	84,210	77,564
Prepaid expenses and other current assets	18,927	7,819
Deferred income taxes	2,963	3,105
Total current assets	661,704	456,435
Property, plant and equipment at cost, net	59,118	59,389
Goodwill	59,422	59,422
Intangible assets, net	25,211	29,697
Other assets	911	429
Total assets	\$ 806,366	\$ 605,372
Liabilities and equity		
Current liabilities:		
Accounts payable	\$ 50,973	\$ 29,112
Accrued expenses and other current liabilities	158,383	106,445
Deferred profit	7,863	2,520
Income taxes payable	14,149	829
Current portion of long-term debt	220	212
Total current liabilities	231,588	139,118
Deferred income taxes		5,039
Long-term debt	102,352	100,964
Other liabilities	411	1,192
Equity	472,015	359,059
Total liabilities and equity	\$ 806,366	\$ 605,372

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

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(In thousands)
(Unaudited)

	Six months ended June 30,	
	2010	2009
Operating activities		
Net income (loss)	\$ 78,437	\$ (35,647)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	9,882	10,866
Amortization of debt discount	1,501	1,400
Non-cash equity-based compensation	5,128	3,553
Non-cash asset impairment charge		304
Non-cash inventory write-off		1,526
Non-cash restructuring	(179)	6,375
Deferred income taxes	(4,756)	360
Other, net	(2)	70
Changes in operating assets and liabilities:		
Accounts receivable	(54,631)	26,883
Inventories	(6,383)	15,063
Accounts payable	21,810	(10,507)
Accrued expenses, deferred profit and other current liabilities	70,050	(12,475)
Other, net	(11,857)	273
Net cash provided by operating activities	109,000	8,044
Investing activities		
Capital expenditures	(6,168)	(3,645)
Payments for net assets of businesses acquired		(500)
Payments of earn-outs for businesses acquired		(9,839)
Proceeds from the redemption of short-term investments	160,141	
Payments for purchases of short-term investments	(78,500)	
Proceeds from the sale of property, plant and equipment	13	275
Net cash provided by (used in) investing activities	75,486	(13,709)
Financing activities		
Proceeds from stock option exercises	33,113	
Restricted stock tax withholdings	(2,898)	(295)
Repayments of long-term debt	(105)	(96)
Net cash provided by (used in) financing activities	30,110	(391)
Effect of exchange rate changes on cash and cash equivalents	(1,803)	(249)
Net increase (decrease) in cash and cash equivalents	212,793	(6,305)
Cash and cash equivalents at beginning of period	148,589	103,799
Cash and cash equivalents at end of period	\$ 361,382	\$ 97,494
Non-cash investing and financing activities		
Accrual of payment for net assets of businesses acquired	\$	\$ 1,000
Transfers from property, plant and equipment to inventory	1,123	241
Transfers from inventory to property, plant and equipment	850	23
Sale of property, plant and equipment with note receivable	140	

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

Table of Contents**Veeco Instruments Inc. and Subsidiaries****Notes to Condensed Consolidated Financial Statements (Unaudited)****Note 1 Basis of Presentation**

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

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

Net Income (Loss) Per Common Share

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

	Three months ended June 30,		Six months ended June 30,	
	2010	2009	2010	2009
Basic weighted average shares outstanding	39,761	31,497	39,283	31,506
Dilutive effect of stock options and restricted stock	2,327		1,215	
Dilutive effect of convertible notes	1,418		1,185	
Diluted weighted average shares outstanding	43,506	31,497	41,683	31,506

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. For the three months ended June 30, 2009, the effect of approximately 0.8 million stock options and 0.4 million restricted shares were excluded from the computation of diluted weighted average shares outstanding due to the net loss sustained in the period as their inclusion would have been anti-dilutive. For the six months ended June 30, 2009, the effect of approximately 0.1 million stock options were excluded from the computation of diluted weighted average shares outstanding due to the net loss sustained in the period as their inclusion

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

would have been anti-dilutive. For the three and six months ended June 30, 2010, no shares were excluded from the computation of diluted weighted average shares outstanding.

Our convertible notes meet the criteria for determining the effect of the assumed conversion using the treasury stock method of accounting, as long as we have the ability and the intent to settle the principal amount of the notes in cash. Under the terms of these notes, we may pay the principal amount of converted notes in cash or in shares of common stock. We have indicated that we intend to pay the principal amount in cash. Using the treasury stock method, it was determined that the impact of the assumed conversion for the three and six months ended June 30, 2010, had a dilutive affect of 1,418,000 and 1,185,000 common equivalent shares, respectively and for the three and six months ended June 30, 2009, the impact was anti-dilutive, due to the net loss sustained in the period. The effect of the assumed converted shares is dependent on the stock price at the time of the conversion. The maximum number of common equivalent shares issuable upon conversion at June 30, 2010 was approximately 5.4 million.

Holders may convert the convertible notes at any time during the period beginning on January 15, 2012 through the close of business on the second day prior to April 15, 2012 and earlier upon the occurrence of certain

Table of Contents

events including our common stock trading at prices equal to 130% of the conversion price for a specified period, which is at least 20 trading days during the 30 consecutive trading days of the immediately preceding fiscal quarter and only during such fiscal quarter. At the end of the second quarter of 2010, our common stock was trading at prices equal to or above 130% of the conversion price for the specified period and, as a result, the convertible notes will be convertible during the third quarter of 2010. If the convertible notes are converted, we have the ability and intent to pay the principal balance of notes tendered for conversion in cash. We will re-perform this test each quarter up to and including the fourth quarter of 2011. See Note 6 for further details on our debt.

Short-Term Investments

We determine the appropriate balance sheet classification of our investments at the time of purchase and evaluate the classification at each balance sheet date. As part of our cash management program, we maintain a portfolio of marketable securities which are classified as available-for-sale. These securities include certificates of deposit placed through an account registry service (CDARS) with maturities of greater than three months but less than one year when purchased in principal amounts that, when aggregated with interest to accrue over the term, will not exceed Federal Deposit Insurance Corporation limits. These securities are carried at cost, which approximates market value.

Derivative Financial Instruments

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

The aggregate foreign currency exchange (loss) gain included in determining the condensed consolidated results of operations was approximately \$(0.5) million and \$0.1 million during the three months ended June 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange (loss) gain were gains related to forward contracts of \$0.2 million and \$0.1 million during the three months ended June 30, 2010, and 2009, respectively. The aggregate foreign currency exchange loss included in determining the condensed consolidated results of operations was approximately \$(0.4) million and \$(1.3) million during the six months ended June 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange loss were gains related to forward contracts of \$0.3 million and \$0.2 million during the six months ended June 30, 2010, and 2009, respectively.

These amounts were recognized and are included in other, net in the accompanying condensed consolidated statements of operations. As of June 30, 2010, approximately \$0.1 million of losses related to forward contracts were included in accrued expenses and other current liabilities and were subsequently paid in July 2010. As of December 31, 2009, approximately \$0.2 million of gains related to forward contracts were included in prepaid expenses and other current assets and were subsequently received in January 2010. Monthly forward contracts with a notional amount of \$9.2 million, entered into in June 2010 for July 2010, will be settled in July 2010.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

The weighted average notional amount of derivative contracts outstanding during the three and six months ended June 30, 2010 were approximately \$8.2 and \$5.7 million, respectively.

Note 2 Equity-Based Compensation Plans

Equity-Based Compensation

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

Table of Contents

	Three months ended June 30,		Six months ended June 30,	
	2010	2009	2010	2009
Equity-based compensation expense	\$ 2,958	\$ 2,155	\$ 5,128	\$ 3,553

As of June 30, 2010, the total unrecognized compensation costs related to nonvested stock and stock option awards was \$11.6 million and \$17.7 million, respectively. The related weighted average period over which we expect that such unrecognized compensation costs will be recognized is approximately 2.9 years for nonvested stock awards and 2.4 years for option awards.

Stock Option and Restricted Stock Activity

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

	Shares (000s)	Weighted Average Grant- Date Fair Value
Nonvested at January 1, 2010	892	\$ 12.97
Granted	169	34.42
Vested	(253)	11.28
Forfeited (including cancelled awards)	(13)	14.38
Nonvested at June 30, 2010	795	18.04

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

	Shares (000s)	Weighted- Average Exercise Price	Aggregate Intrinsic Value (000s)	Weighted- Average Remaining Contractual Life (in years)
Outstanding at January 1, 2010	4,506	\$ 16.35		
Granted	610	33.98		
Exercised	(1,709)	19.37		
Forfeited (including cancelled options)	(37)	14.22		
Expirations of vested options	(9)	34.13		
Outstanding at June 30, 2010	3,361	17.99	\$ 70,354	5.8
Options exercisable at June 30, 2010	1,032	16.91	\$ 22,960	3.7

2010 Stock Incentive Plan

On April 1, 2010, the Board of Directors of the Company and on May 14, 2010, our shareholders approved the 2010 Stock Incentive Plan (the 2010 Plan). The 2010 Plan will replace the 2000 Plan as the active stock plan. The Company's employees, directors and consultants are eligible

to receive awards under the 2010 Plan. The 2010 Plan permits the granting of a variety of awards, including both non-qualified and incentive stock options, share appreciation rights, restricted shares, restricted share units and dividend equivalent rights. The Company is authorized to issue up to 3,500,000 shares under the 2010 Plan. Option awards are generally granted with an exercise price equal to the market price of the Company's stock at the prior day close from date of grant; those option awards generally vest over a 3 year period and have 10-year contractual terms. Share awards generally vest over 4-5 years. Certain option and share awards provide for accelerated vesting if there is a change in control, as defined in the 2010 Plan.

Note 3 Balance Sheet Information

Accounts Receivable, net

Accounts receivable are shown net of the allowance for doubtful accounts of \$0.8 million and \$0.9 million as of June 30, 2010 and December 31, 2009, respectively.

Table of Contents*Inventories*

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

	June 30, 2010		December 31, 2009	
Raw materials	\$	51,480	\$	49,013
Work in process		26,147		21,560
Finished goods		6,583		6,991
	\$	84,210	\$	77,564

Accrued Warranty

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

	Six months ended June 30,			
	2010		2009	
Balance as of beginning of period	\$	7,556	\$	6,892
Warranties issued during the period		5,390		1,304
Settlements made during the period		(3,577)		(1,923)
Balance at end of period	\$	9,369	\$	6,273

Note 4 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. These systems are primarily sold to customers in the high-brightness LED (HB LED) and solar industries, as well as to scientific research customers. This segment has product development and marketing sites in Somerset, New Jersey, St. Paul, Minnesota, Clifton Park, New York 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 and Ft. Collins, Colorado. 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. The other excluded items include restructuring (credits) expenses, asset impairment charges, inventory write-offs and equity-based compensation expense. The accounting policies of the reportable segments are the same as those described in the summary of critical accounting policies.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Table of Contents

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

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate Amount	Total
Three months ended June 30, 2010					
Net sales	\$ 185,646	\$ 35,742	\$ 31,652	\$	\$ 253,040
Segment profit (loss)	\$ 58,856	\$ 9,925	\$ 3,354	\$ (3,768)	\$ 68,367
Interest, net				1,762	1,762
Amortization	796	383	397	58	1,634
Equity-based compensation	671	308	435	1,544	2,958
Income (loss) before income taxes	\$ 57,389	\$ 9,234	\$ 2,522	\$ (7,132)	\$ 62,013
Three months ended June 30, 2009					
Net sales	\$ 31,882	\$ 17,593	\$ 22,545	\$	\$ 72,020
Segment loss	\$ (472)	\$ (1,009)	\$ (3,012)	\$ (1,876)	\$ (6,369)
Interest, net				1,698	1,698
Amortization	774	403	578	76	1,831
Equity-based compensation	218	337	321	1,279	2,155
Restructuring	195	1,444	262	43	1,944
Asset impairment charge		304			304
Loss before income taxes	\$ (1,659)	\$ (3,497)	\$ (4,173)	\$ (4,972)	\$ (14,301)
Six months ended June 30, 2010					
Net sales	\$ 297,150	\$ 58,987	\$ 60,134	\$	\$ 416,271
Segment profit (loss)	\$ 88,673	\$ 13,122	\$ 6,286	\$ (6,902)	\$ 101,179
Interest, net				3,544	3,544
Amortization	1,592	766	844	117	3,319
Equity-based compensation	1,138	523	739	2,728	5,128
Restructuring		(179)			(179)
Income (loss) before income taxes	\$ 85,943	\$ 12,012	\$ 4,703	\$ (13,291)	\$ 89,367
Six months ended June 30, 2009					
Net sales	\$ 54,084	\$ 34,498	\$ 46,287	\$	\$ 134,869
Segment loss	\$ (4,184)	\$ (2,641)	\$ (5,717)	\$ (3,500)	\$ (16,042)
Interest, net				3,407	3,407
Amortization	1,549	808	1,155	148	3,660
Equity-based compensation	374	589	557	2,033	3,553
Restructuring	929	2,830	2,386	230	6,375
Inventory write-offs		1,526			1,526
Asset impairment charge		304			304
Loss before income taxes	\$ (7,036)	\$ (8,698)	\$ (9,815)	\$ (9,318)	\$ (34,867)

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate Amount	Total
As of June 30, 2010					
Goodwill	\$ 51,989	\$	\$ 7,433	\$	\$ 59,422
Total assets	\$ 239,266	\$ 58,669	\$ 81,047	\$ 427,384	\$ 806,366
As of December 31, 2009					
Goodwill	\$ 51,989	\$	\$ 7,433	\$	\$ 59,422
Total assets	\$ 178,406	\$ 54,106	\$ 72,912	\$ 299,948	\$ 605,372

Corporate total assets are comprised principally of cash and cash equivalents and short-term investments at June 30, 2010 and December 31, 2009, respectively.

Note 5 Income Taxes

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

The Company evaluates the need for a valuation allowance against its deferred tax assets each quarter. For the year ending December 31, 2010, the Company has determined that a significant portion of its deferred tax assets

Table of Contents

are realizable on a more-likely-than-not basis based on the forecasted results of operations. This tax benefit has been included in calculating the estimated effective tax rate for the year ending December 31, 2010.

Note 6 Debt*Convertible Notes*

The convertible notes are initially convertible into 36.7277 shares of common stock per \$1,000 principal amount of notes (equivalent to a conversion price of \$27.23 per share or a premium of 38% over the closing market price for Veeco's common stock on April 16, 2007). Holders may convert the convertible notes at any time during the period beginning on January 15, 2012 through the close of business on the second day prior to April 15, 2012 and earlier upon the occurrence of certain events including our common stock trading at prices equal to 130% of the conversion price for a specified period, which is at least 20 trading days during the 30 consecutive trading days of the immediately preceding fiscal quarter and only during such fiscal quarter. At the end of the second quarter of 2010, our common stock was trading at prices equal to or above 130% of the conversion price for the specified period and, as a result, the convertible notes will be convertible during the third quarter of 2010. If the convertible notes are converted, we have the ability and intent to pay the principal balance of notes tendered for conversion in cash. We will re-perform this test each quarter up to and including the fourth quarter of 2011. The notes are unsecured and are effectively subordinated to all of our senior and secured indebtedness and to all indebtedness and other liabilities of our subsidiaries.

In May 2008, accounting guidance was issued that requires a portion of convertible debt to be allocated to equity. We implemented this guidance as of January 1, 2009. This guidance requires issuers of convertible debt that can be settled in cash to separately account for (*i.e.*, bifurcate) a portion of the debt associated with the conversion feature and reclassify this portion to equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value over the life of the debt using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as interest expense. The convertible 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 is amortized over the remaining life of the notes, which will be through April 15, 2012. This additional interest expense does not require the use of cash.

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

	Three months ended		Six months ended	
	2010	June 30, 2009	2010	June 30, 2009
Contractual interest	\$ 1,089	\$ 1,089	\$ 2,178	\$ 2,178
Amortization of the discount on the Notes	760	707	1,501	1,400
Total interest expense on the Notes	\$ 1,849	\$ 1,796	\$ 3,679	\$ 3,578
Effective interest rate	7.0%	6.8%	7.0%	6.8%

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

	June 30, 2010	December 31, 2009
Carrying amount of the equity component	\$ 16,318	\$ 16,318
Principal balance of the liability component	\$ 105,574	\$ 105,574
Less: unamortized discount	5,993	7,493
Net carrying value of the liability component	\$ 99,581	\$ 98,081

At June 30, 2010, \$105.6 million of the notes outstanding had a fair value of approximately \$156.7 million.

Table of Contents

Mortgage Payable

We also have a mortgage payable, with approximately \$3.0 million outstanding at June 30, 2010. The mortgage accrues interest at an annual rate of 7.91%, and the final payment is due on January 1, 2020. The fair value of the mortgage at June 30, 2010 was approximately \$3.3 million.

Note 7 Fair Value Measurements

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

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

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

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

As of June 30, 2010, major categories of assets measured at fair value on a recurring basis under Level 2 consisted of CDARS totaling \$159.5 million and treasury bills totaling \$147.0 million. As of December 31, 2009, major categories of assets measured at fair value on a recurring basis under Level 2 consisted of CDARS totaling \$180.0 million and derivative instruments totaling \$0.2 million. As of June 30, 2010, the major category of liabilities measured at fair value on a recurring basis under Level 2 consisted of derivative instruments totaling \$0.1 million. The Company had no Level 1 and Level 3 assets and liabilities measured on a recurring basis at June 30, 2010 and December 31, 2009.

CDARS and treasury bills are carried at cost, which approximates market value. Accordingly, no gains or losses (realized/ unrealized) have been incurred.

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

As of June 30, 2010, major categories of assets and liabilities measured at fair value under Level 3 on a nonrecurring basis consisted of property, plant and equipment totaling \$59.1 million, goodwill totaling \$59.4 million, intangible assets totaling \$25.2 million, an asset retirement obligation totaling (\$0.2) million and a restructuring liability totaling (\$1.3) million. As of December 31, 2009, major categories of assets and liabilities measured at fair value under Level 3 on a nonrecurring basis consisted of property, plant and equipment totaling \$59.4 million, goodwill totaling \$59.4 million, intangible assets totaling \$29.7 million, an asset retirement obligation totaling (\$0.2) million and a restructuring liability totaling (\$2.5) million. The Company had no Level 1 or Level 2 assets and liabilities measured on a nonrecurring basis at June 30, 2010 and December 31, 2009.

Table of Contents**Note 8 Commitments, Contingencies and Other Matters***Restructuring and Other Charges (Credits)*

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

In conjunction with these activities, we recorded a restructuring credit of approximately \$0.2 million during six months ended June 30, 2010. We recorded restructuring charges of approximately \$1.9 million and \$6.4 million during the three and six months ended June 30, 2009, respectively, and inventory write-offs of \$1.5 million, included in cost of sales in the accompanying Condensed Consolidated Statement of Operations, associated with the discontinuance of certain products in connection with the transitioning to outsourced manufacturing during the three and six months ended June 30, 2009. Restructuring for the three and six months ended June 30, 2010 and 2009 is as follows (in thousands):

	Three months ended			Six months ended		
	June 30,			June 30,		
	2010	2009		2010	2009	
Personnel severance and related costs	\$	\$	767	\$	\$	5,153
Lease-related costs (credits)			893		(179)	893
Moving costs and consolidation activities			284			329
	\$	\$	1,944	\$	(179)	\$ 6,375

Personnel severance and related costs

During the three and six months ended June 30, 2009, we recorded \$0.8 million and \$5.2 million, respectively, in personnel severance and related costs resulting from a headcount reduction of approximately 53 employees during the three month period and 193 employees during the six month period. This reduction in workforce included executives, management, administration, sales and service personnel and manufacturing employees companywide.

Lease-related costs (credits)

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

During the second quarter of 2009, we vacated 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.

Table of Contents*Restructuring liability*

The following is a reconciliation of the liability for the 2009 and 2008 restructuring charge from inception through June 30, 2010 (in thousands):

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate	Total
<u>Short-term liability</u>					
Balance as of January 1, 2010	\$ 353	\$ 486	\$ 15	\$ 1,597	\$ 2,451
Reversal of lease-related costs		(108)			(108)
Short-term/long-term reclassification		70		536	606
Cash payments	(353)	(253)	(15)	(1,030)	(1,651)
Balance as of June 30, 2010	\$	\$ 195	\$	\$ 1,103	\$ 1,298
<u>Long-term liability</u>					
Balance as of January 1, 2010	\$	\$ 229	\$	\$ 536	\$ 765
Reversal of lease-related costs		(71)			(71)
Short-term/long-term reclassification		(70)		(536)	(606)
Balance as of June 30, 2010	\$	\$ 88	\$	\$	\$ 88

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

Table of Contents

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

Executive Summary

We design, manufacture, market and service enabling solutions for customers in the high brightness (HB) light emitting diode (LED) (HB LED), solar, data storage, scientific research, semiconductor, and industrial markets. We have leading technology positions in our three segments: 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 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, chemical vapor deposition, and dicing and slicing systems primarily used to create thin film magnetic heads (TFMHs) that read and write data on hard disk drives.

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 Minnesota, Pennsylvania, France, England, Germany, Netherlands, Japan, Singapore, China, Taiwan, Korea, Malaysia, Philippines and Thailand.

Highlights of the Second Quarter of 2010

- Revenue was \$253.0 million, a 251.3% increase from the second quarter of 2009.
- Orders were \$346.9 million, a 251.6% increase from the second quarter of 2009.
- Net income was \$52.4 million, or \$1.20 per share, compared to a net loss of \$(14.7) million, or \$(0.47) per share, in the second quarter of 2009.

- Gross margins were 45.0%, compared to 33.9% in the second quarter of 2009.

Outlook

With backlog of \$597 million at the end of June 2010, Veeco continues to have very strong business momentum. We continue to experience high levels of activity in our LED business, similar to the last three quarters, with multi-tool MOCVD system orders being quoted across a large number of customers. Our K465i is performing well in the market and we are increasing manufacturing capacity to satisfy customer demand. In the second quarter of 2010, we shipped 81 systems. We currently plan to ship approximately 100 MOCVD tools in the third quarter 2010 and plan to reach a production capacity of 120 tools or more by the fourth quarter. As a result of our variable-cost, outsourced manufacturing strategy, we have dramatically increased our production capacity with the ability to flex our actual MOCVD shipments up or down each quarter depending upon specific customer demand and delivery requirements.

We currently believe that the third quarter will be another strong order quarter for our MOCVD business. In particular, China's initiative to subsidize the HB LED industry via seven national industrial parks is spurring strong order quoting patterns for Veeco, both from Chinese entities as well as from Korean and Taiwanese customers that are partnering with Chinese entities. We believe the HB LED industry is at the beginning of a multi-year MOCVD investment cycle as HB LEDs increase their penetration in laptop and TV backlighting and gain momentum for general illumination.

We are continuing to invest in our copper, indium, gallium, selenide (CIGS) Solar business, with a goal to build a best of breed deposition product line and ultimately help to drive CIGS technology as a low-cost, high

Table of Contents

efficiency solar technology. We shipped our first tool from our FastFlex family of deposition systems to an Asia customer during the second quarter of 2010.

Business conditions in our other segments, Data Storage and Metrology, also remain positive. In 2010, our Data Storage business is currently anticipated to perform well as customers invest in capacity additions and next-generation recording head technology. Order rates have improved significantly from the low levels of business experienced in late 2008 and early 2009, with customers again investing in technology and capacity purchases. In Metrology we are winning in the market due to our new AFM and Optical products and have higher demand in the semiconductor, research and industrial markets as the global economy improved from 2009

Based upon Veeco's strong backlog, the Company is currently forecasting that 2010 revenues will be over \$1 billion, with strong year-over year growth from 2009 in revenue and profitability in all three business segments.

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

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

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

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

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

	2010		Three months ended June 30, 2009		Dollar and Percentage Change Period to Period				
Net sales	\$	253,040	100.0%	\$	72,020	100.0%	\$	181,020	251.3%
Cost of sales		139,282	55.0		47,636	66.1		91,646	192.4
Gross profit		113,758	45.0		24,384	33.9		89,374	366.5
Operating expenses (income):									
Selling, general and administrative		27,287	10.8		19,822	27.5		7,465	37.7
Research and development		20,550	8.1		13,163	18.3		7,387	56.1
Amortization		1,634	0.6		1,831	2.5		(197)	(10.8)
Restructuring					1,944	2.7		(1,944)	(100.0)
Asset impairment charge					304	0.4		(304)	(100.0)
Other, net		512	0.2		(77)	(0.1)		589	*
Total operating expenses		49,983	19.8		36,987	51.4		12,996	35.1
Operating income (loss)		63,775	25.2		(12,603)	(17.5)		76,378	*
Interest expense, net		1,762	0.7		1,698	2.4		64	3.8
Income (loss) before income taxes		62,013	24.5		(14,301)	(19.9)		76,314	*
Income tax provision		9,620	3.8		402	0.6		9,218	2,293.0
Net income (loss)		52,393	20.7		(14,703)	(20.4)		67,096	*
Net loss attributable to noncontrolling interest					(23)	0.1		23	(100.0)
Net income (loss) attributable to Veeco	\$	52,393	20.7%	\$	(14,680)	(20.4)%	\$	67,073	*

* Not Meaningful

Net Sales and Orders

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Net sales of \$253.0 million for the three months ended June 30, 2010 were up 251.3% compared to the comparable 2009 quarter. The following is an analysis of net sales and orders by segment and by region (dollars in thousands):

	Sales				Orders				Book to Bill Ratio	
	Three months ended June 30,		Dollar and Percentage Change		Three months ended June 30,		Dollar and Percentage Change			
	2010	2009	Period to Period		2010	2009	Period to Period		2010	2009
Segment Analysis										
LED & Solar										
Process Equipment	\$ 185,646	\$ 31,882	\$ 153,764	482.3%	\$ 260,439	\$ 56,342	\$ 204,097	362.2%	1.40	1.77
Data Storage										
Process Equipment	35,742	17,593	18,149	103.2	50,025	19,318	30,707	159.0	1.40	1.10
Metrology	31,652	22,545	9,107	40.4	36,499	23,010	13,489	58.6	1.15	1.02
Total	\$ 253,040	\$ 72,020	\$ 181,020	251.3%	\$ 346,963	\$ 98,670	\$ 248,293	251.6%	1.37	1.37
Regional Analysis										
Americas	\$ 30,200	\$ 23,864	\$ 6,336	26.6%	\$ 33,101	\$ 20,660	\$ 12,441	60.2%	1.10	0.87
Europe, Middle East and Africa (EMEA)	26,637	14,889	11,748	78.9	26,830	16,193	10,637	65.7	1.01	1.09
Japan	12,414	4,511	7,903	175.2	10,151	7,434	2,717	36.5	0.82	1.65
Asia Pacific	183,789	28,756	155,033	539.1	276,881	54,383	222,498	409.1	1.51	1.89
Total	\$ 253,040	\$ 72,020	\$ 181,020	251.3%	\$ 346,963	\$ 98,670	\$ 248,293	251.6%	1.37	1.37

Sales and orders increased in each segment in the second quarter of 2010 compared with the comparable 2009 quarter due to our customers requirements in response to increasingly favorable economic conditions compared to 2009. LED & Solar Process Equipment sales were up 482.3% from the comparable 2009 quarter primarily due to an increase in end user demand for HB LED backlighting applications and continued strong customer acceptance of Veeco's newest generation systems. Data Storage Process Equipment segment sales were up 103.2% from the

Table of Contents

comparable 2009 quarter due to an increase in demand by our data storage customers as the global economy improved from 2009. Additionally, Metrology sales were up 40.4% from the comparable 2009 quarter, due to higher demand in the semiconductor, research and industrial markets as the global economy improved from 2009. By region, net sales increased by 539.1% in the Asia Pacific region, primarily due to MOCVD sales to HB LED customers, while sales in the Americas, EMEA and Japan also increased 26.6%, 78.9% and 175.2%, respectively. We believe that there will continue to be period-to-period variations in the geographic distribution of sales.

Orders for the second quarter of 2010 increased 251.6% from the comparable 2009 quarter. By segment, the 362.2% increase in orders for LED & Solar Process Equipment was principally driven by HB LED based manufacturers increasing production for television and laptop backlighting applications. The 159.0% increase in Data Storage Process Equipment orders resulted from an increase in demand by our data storage customers due to both capacity expansion and technology buys. The 58.6% increase in Metrology orders is due to higher demand in the semiconductor, research and industrial markets.

Our book-to-bill ratio for the second quarter of 2010, which is calculated by dividing orders received in a given time period by revenue recognized in the same time period, was 1.37 to 1, reflecting the increasingly favorable economic conditions experienced in the last four quarters, specifically related to our LED & Solar Process Equipment segment. Our backlog as of June 30, 2010 was \$597.5 million, compared to \$402.0 million as of December 31, 2009. During the three months ended June 30, 2010, we experienced backlog adjustments of approximately \$1.4 million, principally due to adjustments related to foreign currency translation. For certain sales arrangements we require a deposit for a portion of the sales price before shipment. As of June 30, 2010 we had customer deposits and advanced billings of \$113.6 million.

Gross Profit

Gross profit, as a percentage of net sales, for the second quarter of 2010, was 45.0%, compared to 33.9% in the comparable 2009 quarter. LED & Solar Process Equipment gross margins increased to 44.0% from 32.7%, Data Storage Process Equipment gross margins increased to 48.6% from 34.3% and Metrology gross margins increased to 46.6% from 35.2%. The increases in gross margin were driven primarily by increased sales volume in each of our segments.

Operating Expenses

Selling, general and administrative expenses increased by \$7.5 million, or 37.7%, from the comparable 2009 quarter, however, decreased from 27.5% of net sales to 10.8% of sales. The dollar increase was primarily due to an increase in bonus and profit sharing expense, equity-based compensation, travel and entertainment expenses, salary and related expenses and professional fees associated primarily with the significant increase in business activity in our LED & Solar Process Equipment segment.

Research and development expenses increased \$7.4 million from the comparable 2009 quarter, however, decreased from 18.3% of net sales to 8.1%. The dollar increase was primarily due to increased spending in our LED & Solar Process Equipment segment to support future growth.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Restructuring expense of \$1.9 million for the second quarter of 2009 consisted of \$0.8 million of personnel severance costs resulting from a reduction in workforce. In addition, there were \$0.9 million of lease-related costs and \$0.2 million of moving and consolidation costs incurred in our Data Storage Process Equipment segment associated with vacating our Camarillo, CA facilities. In addition to the \$1.9 million in restructuring expense, we incurred \$0.3 million of asset impairment costs.

Other, net for the second quarter of 2010 includes a foreign currency exchange loss of \$0.5 million compared to a foreign currency exchange gain of \$0.1 million in the comparable 2009 quarter.

Income Taxes

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

For the three months ended June 30, 2010, the Company had an effective tax rate of 15.5% and recorded a provision for income taxes of \$9.6 million which includes \$2.0 million relating to our foreign operations and \$7.6 million relating to U.S. federal, state and local taxes. The effective tax rate is lower than the statutory rate primarily

Table of Contents

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

For the three months ended June 30, 2009, the Company had an effective tax rate of (2.8)% and recorded a provision for income taxes of \$0.4 million which included \$0.2 million relating to our foreign operations and \$0.2 million relating to state and local taxes.

Results of Operations:**Six Months Ended June 30, 2010 and 2009**

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

	2010		Six months ended June 30, 2009		Dollar and Percentage Change Period to Period				
Net sales	\$	416,271	100.0%	\$	134,869	100.0%	\$	281,402	208.6%
Cost of sales		232,164	55.8		90,103	66.8		142,061	157.7
Gross profit		184,107	44.2		44,766	33.2		139,341	311.3
Operating expenses (income):									
Selling, general and administrative		50,707	12.2		38,429	28.5		12,278	31.9
Research and development		36,990	8.9		26,049	19.3		10,941	42.0
Amortization		3,319	0.8		3,660	2.7		(341)	(9.3)
Restructuring		(179)	(0.0)		6,375	4.7		(6,554)	*
Asset impairment charge					304	0.2		(304)	(100.0)
Other, net		359	0.1		1,409	1.0		(1,050)	(74.5)
Total operating expenses		91,196	21.9		76,226	56.5		14,970	19.6
Operating income (loss)		92,911	22.3		(31,460)	(23.3)		124,371	*
Interest expense, net		3,544	0.9		3,407	2.5		137	4.0
Income (loss) before income taxes		89,367	21.5		(34,867)	(25.9)		124,234	*
Income tax provision		10,930	2.6		780	0.6		10,150	1,301.3
Net income (loss)		78,437	18.8		(35,647)	(26.4)		114,084	*
Net loss attributable to noncontrolling interest					(65)	0.1		65	(100.0)
Net income (loss) attributable to Veeco	\$	78,437	18.8%	\$	(35,582)	(26.4)%	\$	114,019	*

* Not Meaningful

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Net Sales and Orders

Net sales of \$416.3 million for the six months ended June 30, 2010 were up 208.6% compared to the comparable 2009 period. The following is an analysis of net sales and orders by segment and by region (dollars in thousands):

	Sales				Orders				Book to Bill Ratio	
	Six months ended June 30,		Dollar and Percentage Change		Six months ended June 30,		Dollar and Percentage Change		2010	2009
	2010	2009	Period to Period		2010	2009	Period to Period			
Segment Analysis										
LED & Solar Process										
Equipment	\$ 297,150	\$ 54,084	\$ 243,066	449.4%	\$ 472,102	\$ 84,863	\$ 387,239	456.3%	1.59	1.57
Data Storage Process										
Equipment	58,987	34,498	24,489	71.0	76,398	27,136	49,262	181.5	1.30	0.79
Metrology	60,134	46,287	13,847	29.9	66,307	39,721	26,586	66.9	1.10	0.86
Total	\$ 416,271	\$ 134,869	\$ 281,402	208.6%	\$ 614,807	\$ 151,720	\$ 463,087	305.2%	1.48	1.12
Regional Analysis										
Americas	\$ 57,410	\$ 43,833	\$ 13,577	31.0%	\$ 65,344	\$ 32,232	\$ 33,112	102.7%	1.14	0.74
EMEA	50,394	33,150	17,244	52.0	65,955	27,497	38,458	139.9	1.31	0.83
Japan	22,839	9,987	12,852	128.7	16,937	14,360	2,577	17.9	0.74	1.44
Asia Pacific	285,628	47,899	237,729	496.3	466,571	77,631	388,940	501.0	1.63	1.62
Total	\$ 416,271	\$ 134,869	\$ 281,402	208.6%	\$ 614,807	\$ 151,720	\$ 463,087	305.2%	1.48	1.12

Sales and orders increased in each segment in the first half of 2010 compared with the comparable 2009 period due to our customers requirements in response to increasingly favorable economic conditions compared to 2009. LED & Solar Process Equipment sales were up 449.4% from the comparable 2009 period primarily due to an increase in end user demand for HB LED backlighting applications and strong customer acceptance of Veeco s

Table of Contents

newest generation systems. Data Storage Process Equipment sales were up 71.0% from the comparable 2009 period due to an increase in demand by our data storage customers as the global economy improved from 2009. Additionally, Metrology sales were up 29.9% from the comparable 2009 period, due to higher demand in the semiconductor, research and industrial markets as the global economy improved from 2009. By region, net sales increased by 496.3% in the Asia Pacific region, primarily due to MOCVD sales to HB LED customers, while sales in the Americas, EMEA and Japan also increased 31.0%, 52.0% and 128.7%, respectively. We believe that there will continue to be period-to-period variations in the geographic distribution of sales.

Orders for the second half of 2010 increased 305.2% from the comparable 2009 period. By segment, the 456.3% increase in orders for LED & Solar Process Equipment was principally driven by HB LED based manufacturers increasing production for television and laptop backlighting applications. The 181.5% increase in Data Storage Process Equipment orders resulted from an increase in demand by our data storage customers due to both capacity expansion and technology buys. The 66.9% increase in Metrology orders was due to higher demand in the semiconductor, research and industrial markets.

Gross Profit

Gross profit, as a percentage of net sales, for the first half of 2010, was 44.2%, compared to 33.2% in the comparable 2009 period. LED & Solar Process Equipment gross margins increased to 43.5% from 31.2%, Data Storage Process Equipment gross margins increased to 45.0% from 38.3% and Metrology gross margins increased to 46.9% from 37.2%. The increases in gross margin were driven primarily by increased sales volume in each of our segments. In the first half of 2009, Data Storage Process Equipment gross margins were also negatively impacted by a charge of \$1.5 million for the write-off of inventory associated with the discontinuance of certain product lines.

Operating Expenses

Selling, general and administrative expenses increased by \$12.3 million, or 31.9%, from the comparable 2009 period, however, decreased from 28.5% of net sales to 12.2% of sales. The increase was primarily due to an increase in bonus and profit sharing expense, equity-based compensation, travel and entertainment expenses, salary and related expenses and professional fees associated primarily with the significant increase in business activity in our LED & Solar Process Equipment segment.

Research and development expenses increased \$10.9 million from the comparable 2009 period, however, decreased from 19.3% of net sales to 8.9% of sales. The dollar increase was primarily due to increased spending in our LED & Solar Process Equipment segment to support future growth.

Restructuring included a credit of approximately \$0.2 million during the first half of 2010 due to a change in estimate for one of our leased facilities. Restructuring expense of \$6.4 million in the first half of 2009 consisted of \$5.2 million of personnel severance costs resulting from a reduction in workforce, \$0.9 million of lease-related costs and \$0.3 million of moving and consolidation costs incurred in our Data Storage Process Equipment segment associated with vacating our Camarillo, CA facilities. In addition, there was also a \$0.3 million asset impairment charge.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Other, net for the first half of 2010 included a foreign currency exchange loss of \$0.4 million compared to a foreign exchange loss of \$1.3 million in the comparable 2009 period.

Income Taxes

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

For the six months ended June 30, 2010, the Company had an effective tax rate of 12.2% and recorded a provision for income taxes of \$10.9 million which includes \$3.0 million relating to our foreign operations and \$7.9 million relating to U.S. federal, state and local taxes. The effective tax rate is lower than the statutory rate primarily due to the Company's ability to realize a significant portion of its deferred tax assets, primarily related to net operating loss carryforwards and federal tax credits, on a more-likely-than-not basis based on the forecasted results of operations for the year ending December 31, 2010.

For the six months ended June 30, 2009, the Company had an effective tax rate of (2.2)% and recorded a provision for income taxes of \$0.8 million which included \$0.5 million relating to our foreign operations and \$0.3

Table of Contents

million relating to state and local taxes.

Liquidity and Capital Resources

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

	Six months ended June 30,	
	2010	2009
Net income (loss)	\$ 78,437	\$ (35,647)
Net cash provided by operating activities	\$ 109,000	\$ 8,044
Net cash provided by (used in) investing activities	75,486	(13,709)
Net cash provided by (used in) financing activities	30,110	(391)
Effect of exchange rates on cash and cash equivalents	(1,803)	(249)
Net increase (decrease) in cash and cash equivalents	212,793	(6,305)
Cash and cash equivalents at beginning of period	148,589	103,799
Cash and cash equivalents at end of period	\$ 361,382	\$ 97,494

We had a net increase in cash of \$212.8 million during the six months ended June 30, 2010. Cash provided by operations was \$109.0 million for this period, as compared to cash provided by operations of \$8.0 million for the comparable 2009 period. Net income adjusted for non-cash items provided operating cash flows of \$90.0 million for the six months ended June 30, 2010, whereas \$17.6 million was used in the comparable 2009 period. Net cash provided by operations for the six months ended June 30, 2010 included a net change in operating assets and liabilities of \$19.0 million. Inventories increased by approximately \$6.4 million, principally due to an increase in purchases to support the significant MOCVD orders from the comparable 2009 period. Accounts receivable increased \$54.6 million during the six months ended June 30, 2010, due to higher sales volume when compared to the fourth quarter of 2009. Accrued expenses and other current liabilities increased \$51.9 million during the six months ended June 30, 2010, due primarily to an increase in customer deposits, partially offset by the payment of management bonuses and profit sharing in the first quarter of 2010. Accounts payable also increased by \$21.8 million during the first half of 2010 due to the higher level of business activity.

Cash provided by investing activities of \$75.5 million for the six months ended June 30, 2010 primarily related to the redemption of short-term investments of \$160.1 million, partially offset by purchases of additional short-term investments of \$78.5 million and \$6.2 million in capital expenditures principally in our LED & Solar Process Equipment segment. Cash used in investing activities of \$13.7 million for the six months ended June 30, 2009 primarily related to the \$9.8 million earn-out payments and \$3.6 million in capital expenditures, of which \$2.4 million is principally attributable to our LED & Solar Process Equipment segment. During the remainder of 2010, we estimate we will invest an additional \$22.5 million in capital expenditures primarily related to lab tools for high-growth opportunities, as well as for plant expansion and building improvements.

Cash provided by financing activities of \$30.1 million for the six months ended June 30, 2010 primarily related to stock option exercises. Cash used in financing activities of \$0.4 million for the six months ended June 30, 2009 primarily related to restricted stock tax withholdings.

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

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

The Notes are initially convertible into 36.7277 shares of common stock per \$1,000 principal amount of Notes (equivalent to a conversion price of \$27.23 per share or a premium of 38% over the closing market price for Veeco s common stock on April 16, 2007). 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

Table of Contents

occurrence of certain events including our common stock trading at prices equal to 130% of the conversion price for a specified period, which is at least 20 trading days during the 30 consecutive trading days of the immediately preceding fiscal quarter and only during such fiscal quarter. At the end of the second quarter of 2010, our common stock was trading at prices equal to or above 130% of the conversion price for the specified period and, as a result, the Notes will be convertible during the third quarter of 2010. If the Notes are converted, we have the ability and intent to pay the principal balance of notes tendered for conversion in cash. We will re-perform this test each quarter up to and including the fourth quarter of 2011.

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

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

Contractual Obligations

There have been no significant changes to our Contractual Obligations table, except for purchase commitments, in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations of our 2009 Annual Report on Form 10-K. The purchase commitments outstanding at June 30, 2010 were \$283.4 million.

Application of Critical Accounting Policies

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

Table of Contents

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

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

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

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

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

Table of Contents

market value are management's estimates related to our future manufacturing schedules, customer demand, technological and/or market obsolescence, possible alternative uses, and ultimate realization of excess inventory.

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

Pursuant to relevant accounting pronouncements we are required to determine if it is appropriate to use the operating segment as defined under accounting guidance as the reporting unit or one level below the operating segment, depending on whether certain criteria are met. We have identified four reporting units that are required to be reviewed for impairment. The reporting units are LED & Solar Process Equipment, Data Storage Process Equipment and 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 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 is identifiable cash flows that are largely independent of the cash flows generated by other asset groups. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

Fair Value Measurements: Accounting guidance for our non-financial assets and non-financial liabilities requires that we disclose the type of inputs we use to value our assets and liabilities, based on three categories of inputs as defined in such. Level 1 inputs are quoted, unadjusted prices in active markets for identical assets or liabilities that the company has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as quoted

prices for similar assets or liabilities. Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. These requirements apply to our long-lived assets, goodwill and intangible assets. We use Level 3 inputs to value all of such assets and the methodology we use to value such assets has not changed since December 31, 2009. The Company primarily applies the market approach for recurring fair value measurements.

Warranty Costs: We estimate the costs that may be incurred under the warranty we provide and record a liability in the amount of such costs at the time the related revenue is recognized. Estimated warranty costs are determined by analyzing specific product and historical configuration statistics and regional warranty support costs. Our warranty obligation is affected by product failure rates, material usage, and labor costs incurred in correcting product

Table of Contents

failures during the warranty period. Unforeseen component failures or exceptional component performance can also result in changes to warranty costs. If actual warranty costs differ substantially from our estimates, revisions to the estimated warranty liability would be required.

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

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

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

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

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

Table of Contents

Recent Accounting Pronouncements

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

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

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

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

Table of Contents

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Our net sales to foreign customers represented approximately 88.2% and 86.5% of our total net sales for the three and six months ended June 30, 2010, respectively, and 66.9% and 67.5% for the comparable 2009 periods. We expect that net sales to foreign customers will continue to represent a large percentage of our total net sales. Our net sales denominated in foreign currencies represented approximately 6.9% and 8.3% of our total net sales for the three and six months ended June 30, 2010 respectively, and 16.2% and 15.4% for the comparable 2009 periods.

The aggregate foreign currency exchange (loss) gain included in determining the condensed consolidated results of operations was approximately \$(0.5) million and \$0.1 million during the three months ended June 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange (loss) gain were gains related to forward contracts of \$0.2 million and \$0.1 million during the three months ended June 30, 2010, and 2009, respectively. The aggregate foreign currency exchange loss included in determining the condensed consolidated results of operations was approximately \$0.4 million and \$1.3 million during the six months ended June 30, 2010 and 2009, respectively. Included in the aggregate foreign currency exchange loss were gains related to forward contracts of \$0.3 million and \$0.2 million during the six months ended June 30, 2010, and 2009, respectively. These amounts were recognized and are included in other, net in the accompanying condensed consolidated statements of operations.

We are exposed to financial market risks, including changes in foreign currency exchange rates. The changes in currency exchange rates that have the largest impact on translating our international operating profit are the Japanese Yen and the Euro. We use derivative financial instruments to mitigate these risks. We do not use derivative financial instruments for speculative or trading purposes. We generally enter into monthly forward contracts to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known currency exposures. The weighted average notional amount of derivative contracts outstanding during the three and six months ended June 30, 2010 was approximately \$8.2 and \$5.7 million, respectively.

As of June 30, 2010, approximately \$0.1 million of losses related to forward contracts were included in accrued expenses and other current liabilities and were subsequently paid in July 2010. As of December 31, 2009, approximately \$0.2 million of gains related to forward contracts were included in prepaid expenses and other current assets and were subsequently received in January 2010. Monthly forward contracts with a notional amount of \$9.2 million, entered into in June 2010, will be settled in July 2010. The fair value of the contracts at inception was zero, which did not significantly change at June 30, 2010.

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

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

Item 4. Controls and Procedures.

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

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

Table of Contents

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

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

Table of Contents

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

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

Item 1A. Risk Factors.

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

The reduction or elimination of government subsidies and economic incentives may adversely affect the future order rate for our MOCVD equipment.

The Chinese government has provided various incentives to encourage development of the LED industry, including subsidizing a significant portion of the purchase cost of MOCVD equipment. These subsidies have enabled and encouraged certain customers in this region to purchase more of our MOCVD equipment than these customers might have purchased without these subsidies. These subsidies are expected to decline over time and may end or be reduced at some point in the future. The reduction or elimination of these incentives may result in a reduction in future orders for our MOCVD equipment in this region.

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 No. 1 to the Fourth Amended and Restated Bylaws of Veeco effective May 20, 2010	Current report on Form 8-K filed on May 26, 2010, Exhibit 3.1
10.1	Second Amendment to Employment Agreement of John R. Peeler, effective June 11, 2010.	*
10.2	Veeco Instruments Inc. Performance-Based Restricted Stock 2010	*

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

10.3	Veeco Instruments Inc. 2010 Stock Incentive Plan	Registration Statement on Form S-8 (File No. 333-166852) filed May 14, 2010, Exhibit 10.1
10.4	Form of 2010 Stock Incentive Plan, Stock Option Agreement	Registration Statement on Form S-8 (File No. 333-166852) filed May 14, 2010, Exhibit 10.2
10.5	Form of 2010 Stock Incentive Plan, Restricted Stock Agreement	Registration Statement on Form S-8 (File No. 333-166852) filed May 14, 2010, Exhibit 10.3
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: July 28, 2010

Veeco Instruments Inc.

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

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

Table of Contents**INDEX TO EXHIBITS**

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

Number	Description	Incorporated by Reference to the Following Document:
3.1	Amendment No. 1 to the Fourth Amended and Restated Bylaws of Veeco effective May 20, 2010	Current report on Form 8-K filed on May 26, 2010, Exhibit 3.1
10.1	Second Amendment to Employment Agreement of John R. Peeler, effective June 11, 2010.	*
10.2	Veeco Instruments Inc. Performance-Based Restricted Stock 2010	*
10.3	Veeco Instruments Inc. 2010 Stock Incentive Plan	Registration Statement on Form S-8 (File No. 333-166852) filed May 14, 2010, Exhibit 10.1
10.4	Form of 2010 Stock Incentive Plan, Stock Option Agreement	Registration Statement on Form S-8 (File No. 333-166852) filed May 14, 2010, Exhibit 10.2
10.5	Form of 2010 Stock Incentive Plan, Restricted Stock Agreement	Registration Statement on Form S-8 (File No. 333-166852) filed May 14, 2010, Exhibit 10.3
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