

VEECO INSTRUMENTS INC
Form 10-Q
July 30, 2009
Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2009

OR

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

For the transition period from to .

Commission file number 0-16244

VEECO INSTRUMENTS INC.

(Exact Name of Registrant as Specified in Its Charter)

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Delaware
(State or Other Jurisdiction of

11-2989601
(I.R.S. Employer

Incorporation or Organization)

Identification Number)

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

11803
(Zip Code)

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

Website: **www.veeco.com**

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

32,544,275 shares of common stock, \$0.01 par value per share, were outstanding as of the close of business on July 29, 2009.

Table of Contents

SAFE HARBOR STATEMENT

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

- Negative worldwide economic conditions could result in a decrease in our net sales and an increase in our operating costs, which could adversely affect our business and operating results;

- Our sales to data storage and HB-LED manufacturers are highly dependent on these manufacturers' sales for consumer electronics applications, which can experience significant volatility due to seasonal and other factors, which could materially adversely impact our future results of operations;

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

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

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

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

- We operate in industries characterized by rapid technological change;

- We face significant competition;

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

Table of Contents

- We are subject to foreign currency exchange risks;

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

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

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

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

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

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

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

- We are subject to risks of non-compliance with environmental and safety regulation;

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

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

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

Available Information

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

Internet Address

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

Table of Contents

VEECO INSTRUMENTS INC.

INDEX

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1.</u>	<u>Financial Statements:</u>
	<u>Condensed Consolidated Statements of Operations for the Three Months and Six Months Ended June 30, 2009 and 2008 (Unaudited)</u> 5
	<u>Condensed Consolidated Balance Sheets as of June 30, 2009 (Unaudited) and December 31, 2008</u> 6
	<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2009 and 2008 (Unaudited)</u> 7
	<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u> 8
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 19
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u> 34
<u>Item 4.</u>	<u>Controls and Procedures</u> 34
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1.</u>	<u>Legal Proceedings</u> 36
<u>Item 1A.</u>	<u>Risk Factors</u> 36
<u>Item 4.</u>	<u>Submission of Matters to a Vote of Security Holders</u> 37
<u>Item 6.</u>	<u>Exhibits</u> 38
<u>SIGNATURES</u>	39

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****Veeco Instruments Inc. and Subsidiaries****Condensed Consolidated Statements of Operations****(In thousands, except per share data)
(Unaudited)**

	Three months ended		Six months ended	
	June 30,		June 30,	
	2009	2008	2009	2008
Net sales	\$ 72,020	\$ 114,449	\$ 134,869	\$ 216,756
Cost of sales	47,636	66,719	90,103	126,400
Gross profit	24,384	47,730	44,766	90,356
Operating expenses:				
Selling, general, and administrative expense	19,822	24,311	38,429	46,939
Research and development expense	13,163	15,145	26,049	29,871
Amortization expense	1,831	2,426	3,660	4,382
Restructuring expense	1,944		6,375	2,875
Asset impairment charge	304		304	285
Other (income) expense, net	(77)	(382)	1,409	(378)
Total operating expenses	36,987	41,500	76,226	83,974
Operating (loss) income	(12,603)	6,230	(31,460)	6,382
Interest expense, net	1,698	1,700	3,407	3,305
(Loss) income before income taxes	(14,301)	4,530	(34,867)	3,077
Income tax provision	402	1,129	780	2,048
Net (loss) income including noncontrolling interest	(14,703)	3,401	(35,647)	1,029
Net loss attributable to the noncontrolling interest	(23)	(70)	(65)	(146)
Net (loss) income attributable to Veeco	\$ (14,680)	\$ 3,471	\$ (35,582)	\$ 1,175
(Loss) income per common share:				
Net (loss) income attributable to Veeco	\$ (0.47)	\$ 0.11	\$ (1.13)	\$ 0.04
Diluted net (loss) income attributable to Veeco	\$ (0.47)	\$ 0.11	\$ (1.13)	\$ 0.04
Weighted average shares outstanding	31,497	31,255	31,506	31,197
Diluted weighted average shares outstanding	31,497	31,590	31,506	31,435

See accompanying notes.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(In thousands)

	June 30, 2009 (Unaudited)	December 31, 2008
Assets		
Current assets:		
Cash and cash equivalents	\$ 97,494	\$ 103,799
Accounts receivable, net	32,187	59,659
Inventories	78,497	94,930
Prepaid expenses and other current assets	6,051	6,425
Deferred income taxes	2,190	2,185
Total current assets	216,419	266,998
Property, plant, and equipment at cost, net	60,513	64,372
Goodwill	59,160	59,160
Intangible assets, net	34,569	38,818
Other assets	197	193
Total assets	\$ 370,858	\$ 429,541
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	\$ 19,054	\$ 29,610
Accrued expenses	53,431	66,964
Deferred profit	622	1,346
Income taxes payable	153	354
Current portion of long-term debt	204	196
Total current liabilities	73,464	98,470
Deferred income taxes	5,001	4,540
Long-term debt	99,626	98,330
Other non-current liabilities	1,986	2,391
Shareholders' equity:		
Shareholders' equity attributable to Veeco	190,781	225,026
Noncontrolling interest		784
Total shareholders' equity	190,781	225,810
Total liabilities and shareholders' equity	\$ 370,858	\$ 429,541

See accompanying notes.

Table of Contents

Veeco Instruments Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(In thousands)
(Unaudited)

	Six months ended	
	June 30,	
	2009	2008
Operating activities		
Net (loss) income attributable to Veeco	\$ (35,582)	\$ 1,175
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	10,866	11,503
Deferred income taxes	360	962
Amortization of debt discount	1,400	1,444
Non-cash inventory write-off	1,526	
Non-cash share-based compensation	3,553	3,623
Non-cash asset impairment charge	304	285
Other, net	5	(211)
Changes in operating assets and liabilities:		
Accounts receivable	26,883	3,314
Inventories	15,063	(11,135)
Accounts payable	(10,507)	(533)
Accrued expenses, deferred profit, and other current liabilities	(6,100)	(1,069)
Other, net	273	1,097
Net cash provided by operating activities	8,044	10,455
Investing activities		
Capital expenditures	(3,645)	(7,076)
Payments for net assets of businesses acquired, net of cash acquired	(500)	(10,855)
Payment of earn-outs for businesses acquired	(9,839)	
Other, net	275	99
Net cash used in investing activities	(13,709)	(17,832)
Financing activities		
Proceeds from stock issuances		669
Repayments of long-term debt	(96)	(224)
Restricted stock tax withholdings	(295)	(607)
Net cash used in financing activities	(391)	(162)
Effect of exchange rate changes on cash and cash equivalents	(249)	100
Net decrease in cash and cash equivalents	(6,305)	(7,439)
Cash and cash equivalents at beginning of period	103,799	117,083
Cash and cash equivalents at end of period	\$ 97,494	\$ 109,644
Non-cash investing and financing activities		
Accrual of payment for net assets acquired	\$ 1,000	\$
Transfers from property, plant, and equipment to inventory	\$ 241	\$ 385
Transfers from inventory to property, plant, and equipment	\$ 23	\$

See accompanying notes.

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

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

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

Net (Loss) Income Per Common Share

The following table sets forth the reconciliation of weighted average shares outstanding and diluted weighted average shares outstanding:

	Three months ended		Six months ended	
	2009	June 30, 2008	2009	June 30, 2008
Weighted average shares outstanding	31,497	31,255	31,506	31,197
Dilutive effect of stock options and restricted stock awards and units		335		238
Diluted weighted average shares outstanding	31,497	31,590	31,506	31,435

Net (loss) income per common share is computed using the weighted average number of common shares outstanding during the period. Diluted net (loss) income per common share is computed using the weighted average number of common shares and common equivalent shares outstanding during the period. The effect of approximately 95,000 common equivalent shares for the three months ended June 30, 2009 and approximately 78,000 common equivalent shares for the six months ended June 30, 2009 were excluded from the diluted weighted average shares outstanding due to a net loss sustained in each period. During the three-month and six-month periods ended June 30, 2008, options to purchase 3.8 million shares of common stock (at prices ranging from \$18.26 to \$72.00 per share) and options to purchase 5.0 million shares of

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

common stock (at prices ranging from \$16.93 to \$72.00 per share), respectively, were excluded from the computation of diluted earnings per share due to exercise prices that exceeded the average market price of our common stock for the period.

During the second quarter of 2007, we exchanged \$118.8 million of our 4.125% convertible subordinated notes due December 2008 (the Old Notes) for \$117.8 million of a new series of 4.125% convertible subordinated notes due April 15, 2012 (the Notes), leaving \$25.2 million of Old Notes outstanding. For the three and six months ended June 30, 2008, the weighted-average effect of the assumed conversion of the remaining \$25.2 million of Old Notes was approximately 0.7 million shares. The convertible shares were anti-dilutive and, therefore, not included in the weighted shares outstanding for the three or six months ended June 30, 2008. During the fourth quarter of 2008, we repaid the remaining \$25.2 million of Old Notes outstanding.

Table of Contents

The Notes meet the criteria for determining the effect of the assumed conversion using the treasury stock method of accounting, as long as we have the ability and the intent to settle the principal amount of the Notes in cash. Under the terms of the Notes, we may pay the principal amount of converted Notes in cash or in shares of common stock. We have indicated that we intend to pay such amounts in cash. Using the treasury stock method, the impact of the assumed conversion of the Notes was anti-dilutive for the three and six months ended June 30, 2009 and 2008, as the average stock price for each period was below the conversion price of \$27.23. 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, 2009 was approximately 5.4 million, after giving effect to the \$12.2 million of Notes that we repurchased during the fourth quarter of 2008. See Note 8 for further details on our debt.

Fair Value of Financial Instruments

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

Derivative Financial Instruments

We use derivative financial instruments to minimize the impact of foreign exchange rate changes on earnings and cash flows. In the normal course of business, our operations are exposed to fluctuations in foreign exchange rates. In order to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known foreign currency exposures, we enter into monthly forward contracts. We do not use derivative financial instruments for trading or speculative purposes. Our forward contracts are intended to offset exchange gains and losses on the underlying assets and liabilities; both the forward contracts and the underlying assets and liabilities are adjusted to current exchange rates through earnings. We conduct our derivative transactions with highly rated financial institutions in an effort to mitigate any material credit risk. The weighted average notional amount of derivative contracts outstanding during the three and six months ended June 30, 2009 was approximately \$2.6 million and \$3.6 million, respectively.

The condensed consolidated results of operations for the three and six months ended June 30, 2009 include an aggregate foreign currency gain of approximately \$0.1 million and an aggregate foreign currency loss of approximately \$1.3 million, respectively. The loss of \$1.3 million for the six months ended June 30, 2009 was net of gains of approximately \$0.2 million related to forward contracts. The condensed consolidated results of operations for the three and six months ended June 30, 2008 include aggregate foreign currency losses of less than \$0.1 million and gains of approximately \$0.1 million, respectively, which were net of gains of approximately \$0.1 million and losses of \$0.2 million, respectively, related to forward contracts. These amounts were recognized and included in other (income) expense, net in the accompanying Condensed Consolidated Statements of Operations.

As of June 30, 2009, gains of less than \$0.1 million related to forward contracts were included in prepaid and other current assets, and cash in an amount equivalent to such gains was received in July 2009. As of December 31, 2008, approximately \$0.9 million of losses related to forward contracts were included in accrued expenses and subsequently paid in January 2009. Monthly forward contracts with a total notional amount of \$2.0 million were entered into in June 2009 and settled in July 2009. The fair value of these contracts at inception was zero, which did not significantly change at June 30, 2009.

Convertible Debt

In May 2008, the FASB issued FASB Staff Position No. APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1). We implemented FSP APB 14-1 as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. See Note 8 Debt for a discussion of the impact of implementing FSP APB 14-1.

Subsequent Events

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

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

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

We paid \$0.5 million of the \$1.5 million purchase price of the 80.1% remaining portion of Fluens upon closing, as well as \$0.2 million in respect of the earn-out arrangement. We will pay the remaining \$1.0 million of the \$1.5 million in equal quarterly installments of \$0.5 million in each of the third and fourth quarters of 2009. Prior to our purchase of the remaining 80.1%, approximately 31% of Fluens was owned by a Senior Vice President of Veeco.

Note 3 Share-Based Compensation

Share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over the employee requisite service period in accordance with FASB Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment* (SFAS 123(R)). The following compensation expense was included in the condensed consolidated statements of operations for the three months and six months ended June 30, 2009 and 2008 (in thousands):

	Three months ended		Six months ended	
	June 30,	June 30,	June 30,	June 30,
	2009	2008	2009	2008
Share-based compensation expense	\$ 2,155	\$ 2,014	\$ 3,553	\$ 3,623

As of June 30, 2009, the total unrecognized compensation cost related to nonvested restricted stock awards and stock option awards is \$10.6 million and \$7.9 million, respectively. The related weighted average period over which we expect that such unrecognized compensation costs will be recognized as expense is approximately 2.8 years for the nonvested restricted stock awards and 2.2 years for option awards.

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

	Shares (000s)		Weighted Average Grant-Date Fair Value
Nonvested at beginning of year	679	\$	17.76
Granted	469		8.97
Vested	(110)		18.92
Forfeited (including cancelled awards)	(71)		18.40
Nonvested at June 30, 2009	967		13.31

Table of Contents

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

	Shares (000s)	Weighted- Average Exercise Price	Aggregate Intrinsic Value (000s)	Weighted- Average Remaining Contractual Life (in years)
Outstanding at beginning of year	5,572	\$ 20.29		
Granted	748	8.95		
Exercised	(1)	0.27		
Forfeited (including cancelled options)	(1,658)	23.64		
Outstanding at June 30, 2009	4,661	17.28	\$ 3,448	4.2
Options exercisable at June 30, 2009	2,886	19.40	\$ 685	2.9

Note 4 Balance Sheet Information*Accounts Receivable, net*

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

Inventories

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

	June 30, 2009	December 31, 2008
Raw materials	\$ 51,611	\$ 57,815
Work in process	19,403	28,733
Finished goods	7,483	8,382
	\$ 78,497	\$ 94,930

Accrued Warranty

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

amount as necessary. Changes in our warranty liability during the six months ended June 30, 2009 and 2008 are as follows (in thousands):

	Six months ended	
	June 30,	
	2009	2008
Balance at beginning of period	\$ 6,892	\$ 6,502
Warranties issued during the period	1,304	3,003
Settlements made during the period	(1,922)	(2,329)
Balance at end of period	\$ 6,274	\$ 7,176

Note 5 Segment Information

We manage the business, review operating results and assess performance, as well as allocate resources, based upon three separate reporting segments that reflect the market focus of each business. The Light Emitting Diode (LED) & Solar Process Equipment segment consists of metal organic chemical vapor deposition (MOCVD) systems, molecular beam epitaxy (MBE) systems, thermal deposition sources, and other types of deposition systems used to deposit materials on flexible and glass substrates. These systems are primarily sold to customers in the high-brightness light emitting diode (HB-LED) and solar industries, as well as to scientific research customers. This segment has production facilities in Somerset, New Jersey, St. Paul, Minnesota, and Lowell, Massachusetts. The Data Storage Process Equipment segment consists of the ion beam etch, ion beam deposition, diamond-like carbon, physical vapor deposition, and dicing and slicing products sold primarily to customers in the data storage industry. This segment has production facilities in Plainview, New York, and Ft. Collins, Colorado. In our Metrology segment, we design and manufacture atomic force microscopes, scanning probe microscopes, stylus

Table of Contents

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 production facilities 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 (loss) profit), 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 (loss) profit reports baseline performance and thus provides useful information. Certain items include restructuring expenses, asset impairment charges, inventory write-offs, and equity-based compensation expense. The accounting policies of the reportable segments are the same as those described in the summary of critical accounting policies.

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate Amount	Total
Three months ended 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 expense, net				1,698	1,698
Amortization expense	774	403	578	76	1,831
Equity-based compensation expense	218	337	321	1,279	2,155
Restructuring expense	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)
Three months ended June 30, 2008					
Net sales	\$ 45,090	\$ 36,762	\$ 32,597	\$	\$ 114,449
Segment profit (loss)	\$ 8,834	\$ 5,416	\$ (1,030)	\$ (2,550)	\$ 10,670
Interest expense, net				1,700	1,700
Amortization expense	967	952	394	113	2,426
Equity-based compensation expense	102	238	220	1,454	2,014
Income (loss) before income taxes	\$ 7,765	\$ 4,226	\$ (1,644)	\$ (5,817)	\$ 4,530

Table of Contents

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate Amount	Total
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 expense, net				3,407	3,407
Amortization expense	1,549	808	1,155	148	3,660
Equity-based compensation expense	374	589	557	2,033	3,553
Restructuring expense	929	2,830	2,386	230	6,375
Inventory write-off		1,526			1,526
Asset impairment charge		304			304
Loss before income taxes	\$ (7,036)	\$ (8,698)	\$ (9,815)	\$ (9,318)	\$ (34,867)
Six months ended June 30, 2008					
Net sales	\$ 87,221	\$ 60,841	\$ 68,694	\$	\$ 216,756
Segment profit (loss)	\$ 17,501	\$ 4,096	\$ 918	\$ (4,968)	\$ 17,547
Interest expense, net				3,305	3,305
Amortization expense	1,453	1,904	800	225	4,382
Equity-based compensation expense	177	389	346	2,711	3,623
Restructuring expense		124	190	2,561	2,875
Asset impairment charge				285	285
Income (loss) before income taxes	\$ 15,871	\$ 1,679	\$ (418)	\$ (14,055)	\$ 3,077
As of June 30, 2009					
Goodwill	\$ 51,727	\$	\$ 7,433	\$	\$ 59,160
Total assets	\$ 128,769	\$ 57,102	\$ 73,797	\$ 111,190	\$ 370,858
As of December 31, 2008					
Goodwill	\$ 51,727	\$	\$ 7,433	\$	\$ 59,160
Total assets	\$ 137,037	\$ 84,335	\$ 85,390	\$ 122,779	\$ 429,541

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

Note 6 Income Taxes

We had approximately \$1.0 million of unrecognized tax benefits at June 30, 2009 and December 31, 2008, respectively, which predominantly relate to positions taken on our foreign tax returns and all of which represent the amount of unrecognized tax benefits that, if recognized, would favorably impact the effective income tax rate in future periods.

We or one of our subsidiaries file income tax returns in the U.S. federal jurisdiction and various state, local, and foreign jurisdictions. All material federal, state, local, and foreign income tax matters have been concluded for years through 2002 subject to subsequent utilization of net

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

operating losses generated in such years. During the third quarter of 2008, the Internal Revenue Service initiated an examination of our Federal income tax return for the calendar year 2006. The majority of our foreign jurisdictions have been reviewed through 2007 with only a few jurisdictions having open tax years between 2004 and 2007. None of our tax returns are currently under examination in foreign jurisdictions.

Table of Contents

We recognize interest and penalties related to income tax matters in income tax expense. The total accrual for interest and penalties related to uncertain tax positions was approximately \$0.3 million as of June 30, 2009 and December 31, 2008.

Note 7 Comprehensive Income

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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

	Three months ended		Six months ended	
	June 30,		June 30,	
	2009	2008	2009	2008
Net (loss) income including noncontrolling interest	\$ (14,703)	\$ 3,401	\$ (35,647)	\$ 1,029
Other comprehensive (loss) income, net of tax:				
Foreign currency translation	719	(1,270)	(946)	1,763
Comprehensive (loss) income:	(13,984)	2,131	(36,593)	2,792
Comprehensive loss attributable to the noncontrolling interest	(23)	(70)	(65)	(146)
Comprehensive (loss) income attributable to Veeco	\$ (13,961)	\$ 2,201	\$ (36,528)	\$ 2,938

Note 8 Debt

Convertible Debt

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

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

We implemented FSP APB 14-1 as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. FSP APB 14-1 requires issuers of convertible debt that can be settled in cash to separately account for (*i.e.*, bifurcate) a portion of the debt associated with the conversion feature and reclassify this portion to stockholders' equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as non-cash interest expense. The Notes are subject to FSP APB 14-1 since they may be settled in cash upon conversion. Thus, as a result of the adoption of FSP APB 14-1, we reclassified approximately \$16.3 million from long-term debt to additional paid-in capital effective as of the date of issuance of the Notes. This reclassification created a \$16.3 million discount on the debt that will be amortized over the remaining life of the Notes, which will be through April 15, 2012. The reclassification generated a \$6.7 million deferred tax liability, which we offset with a corresponding decrease of the valuation allowance by the same amount. FSP APB 14-1 requires that we present prior periods as if the guidance was in effect as of the date of issuance. Thus, we have presented all financial data for prior periods as if we had reclassified this \$16.3 million discount and began amortizing it in April 2007.

Table of Contents

During the fourth quarter of 2008, we repurchased an aggregate principal amount of \$12.2 million of the Notes for \$7.2 million in cash, of which \$7.1 million related to principal and \$0.1 million related to accrued interest, reducing the amount outstanding from \$117.8 million to \$105.6 million. A gross gain of approximately \$5.1 million was recorded on these repurchases offset by the write-off of approximately \$0.1 million of unamortized deferred financing costs associated with the Notes, for a net gain of approximately \$5.0 million. Such net gain was reduced to \$3.8 million upon the adoption of FSP APB 14-1, which required that the gain be calculated based on the fair value of the portion repurchased as of the repurchase date. The fair value approximated the carrying value net of the unamortized discount on the portion repurchased. The difference of approximately \$1.2 million was recorded as a reduction in the gain originally reported, and thus increased the accumulated deficit as of December 31, 2008 by such amount.

For the six months ended June 30, 2009 and 2008, respectively, we recorded approximately \$1.4 million of additional interest expense in each period resulting from the amortization of the debt discount. This additional interest expense did not require the use of cash. The retrospective application of FSP APB 14-1 to the results for the three and six months ended June 30, 2008 decreased the net income attributable to Veeco in those periods from \$4,202 to \$3,471 and from \$2,619 to \$1,175, respectively, and decreased the basic earnings per share attributable to Veeco for those periods from \$0.13 to \$0.11 and from \$0.08 to \$0.04, respectively.

The components of interest expense recorded on the Notes for the three and six months ended June 30, 2009 and 2008 were as follows (in thousands):

	Three months ended		Six months ended	
	2009	June 30, 2008	2009	June 30, 2008
Contractual interest	\$ 1,089	\$ 1,214	\$ 2,177	\$ 2,428
Amortization of the discount on the Notes	707	731	1,400	1,444
Total interest expense on the Notes	\$ 1,796	\$ 1,945	\$ 3,577	\$ 3,872
Effective interest rate	6.8%	6.6%	6.8%	6.6%

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

	June 30, 2009	December 31, 2008
Carrying amount of the equity component	\$ 16,318	\$ 16,318
Principal balance of the liability component	\$ 105,574	\$ 105,574
Less: unamortized discount	8,939	10,339
Net carrying value of the liability component	\$ 96,635	\$ 95,235

At June 30, 2009, \$105.6 million of the New Notes were outstanding with a fair value of approximately \$97.7 million.

Mortgage Payable

We also have a mortgage note payable, with approximately \$3.2 million outstanding at June 30, 2009. The note accrues interest at an annual rate of 7.91%, and the final payment is due on January 1, 2020. The fair value of this note at June 30, 2009 was approximately \$3.5 million.

Credit Agreement

In February 2009, we entered into an amendment to our existing credit agreement with HSBC Bank USA, National Association (HSBC), as administrative agent, and the lenders named therein (as amended, the Credit Agreement). As part of the amendment, we reduced the amount of the revolving credit facility, modified certain

Table of Contents

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

Note 9 Fair Value Measurements

We implemented the guidance in Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157), for our non-financial assets and non-financial liabilities as of January 1, 2009. SFAS 157 defines fair value, establishes a framework for measuring fair value, and enhances fair value measurement disclosure. The accounts subject to the guidance are our long-lived assets, goodwill, and intangible assets. The implementation expanded our fair value disclosures but did not impact our consolidated financial position or results of operations. However, applying the provisions of SFAS 157 may impact our periodic fair value measurements for long-lived assets, goodwill and intangible assets in the future, as fair values calculated under SFAS 157 may be different from the fair values that would have been calculated under previous guidance.

SFAS 157 requires that we disclose the type of inputs we use to value such assets, based on three categories of inputs as defined in SFAS 157. Level 1 inputs are quoted, unadjusted prices in active markets for identical assets or liabilities that the company has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as quoted prices for similar assets or liabilities. Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. We use Level 3 inputs to value all of our property, plant and equipment, goodwill, and intangible assets balances. We value such assets on a non-recurring basis and did not perform a valuation during the first or second quarter of 2009, though the methodology we would use to value such assets has not changed since December 31, 2008. We did not record any gain or loss in adjusting the carrying amounts to fair value in the three months or six months ended June 30, 2009, since we made no such adjustment during that period. The carrying amounts of property, plant and equipment, goodwill, and intangible assets as of June 30, 2009 were \$60,513, \$59,160, and \$34,569, respectively.

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

During 2008 and through the six months ended June 30, 2009, we have continued our multi-quarter plan to improve profitability and reduce and contain spending. We have continued to make progress against the initiatives that management has set, continued our restructuring plan and executed activities with a focus on creating a more variable cost effective organization. These activities included downsizing and consolidating some locations, reducing our workforce, consultants and discretionary expenses and realigning our sales organization and engineering groups. In addition, due to a weakened and deteriorated business environment we intensified and accelerated our restructuring activities.

Table of Contents

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

	Three months ended			Six months ended		
	June 30,			June 30,		
	2009	2008		2009	2008	
Personnel severance costs	\$ 767	\$	\$	5,153	\$	321
Lease-related costs	893			893		2,554
Moving costs and consolidation activities	284			329		
Total restructuring expense	\$ 1,944	\$	\$	6,375	\$	2,875

2009 Restructuring and Other Charges

In conjunction with these activities, during the six months ended June 30, 2009, we recognized restructuring charges of approximately \$6.4 million, principally consisting of personnel severance costs resulting from a headcount reduction of 193 employees and the notification of other employees that will be transitioned out of the Company during 2009. This reduction in workforce included executives, management, administration, sales and service personnel and manufacturing employees companywide.

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

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

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

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate	Total
<u>Short-Term Liability</u>					
Personnel severance charges	\$ 850	\$ 1,706	\$ 2,378	\$ 219	\$ 5,153
Moving costs and consolidation activities	83	233	13		329
Total charged to accrual	933	1,939	2,391	219	5,482

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Lease-related and other costs			516				516
Cash payments	(607)		(1,382)	(1,824)	(174)		(3,987)
Balance as of June 30, 2009	\$ 326	\$ 1,073	\$ 567	\$ 45	\$ 2,011		
<u>Long-Term Liability</u>							
Lease-related and other costs	\$	\$ 377	\$	\$	\$ 377		
Balance as of June 30, 2009	\$	\$ 377	\$	\$	\$ 377		

Table of Contents

The balance of the short-term 2009 restructuring accrual is expected to be paid over the next nine to twelve months, and the long-term portion will continue over the remaining life of the lease until May 1, 2012. We expect to continue our restructuring program in light of the overall business decline, and expect to incur restructuring charges of \$0.5 million to \$1.0 million throughout the remainder of 2009 associated with consolidating business units, decreasing the number of manufacturing sites, implementing specific manufacturing initiatives, and centralizing certain functions.

2008 Restructuring and Other Charges

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

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

	LED & Solar Process Equipment	Data Storage Process Equipment	Metrology	Unallocated Corporate	Total
<u>Short-Term Liability</u>					
Balance as of December 31, 2008	\$ 660	\$ 270	\$ 534	\$ 1,859	\$ 3,323
Short-term/long-term Reclassification				540	540
Cash payments	(253)	(268)	(384)	(878)	(1,783)
Reversal of accrual	(4)	(2)	(5)		(11)
Balance as of June 30, 2009	\$ 403	\$	\$ 145	\$ 1,521	\$ 2,069
<u>Long-Term Liability</u>					
Balance as of December 31, 2008	\$	\$	\$	\$ 1,620	\$ 1,620
Short-term/long-term Reclassification				(540)	(540)
Balance as of June 30, 2009	\$	\$	\$	\$ 1,080	\$ 1,080

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

2007 Restructuring and Other Charges

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

Table of Contents

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

Executive Summary

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

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

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

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

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

Highlights of the Second Quarter of 2009

- Revenue was \$72.0 million, a 37% decrease from the second quarter of 2008, but up 15% from the first quarter of 2009.
- Orders were \$98.7 million, down 28% from the second quarter of 2008, but up 86% from the first quarter of 2009.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

- Net loss was \$14.7 million, or (\$0.47) per share, compared to net income of \$3.5 million, or \$0.11 per share, in the second quarter of 2008.
- Gross margins were 33.9%, compared to 41.7% in the second quarter of 2008.
- Restructuring charges totaled \$1.9 million, principally consisting of personnel severance costs as well as lease-related and moving and consolidation costs associated with our Camarillo, CA facilities, which we vacated during the quarter.

The second quarter remained challenging for Veeco from a revenue and loss perspective due to the global economic slowdown that began in the fall of 2008. We have made significant progress on our cost and workforce reduction plans, various outsourcing initiatives and materials cost management.

Veeco's second quarter order improvement compared to the first quarter was primarily driven by significant sequential growth in LED & Solar bookings to \$57 million, as LED manufacturers ramp production for TV and laptop backlighting applications. Data storage orders also improved 147% from the first quarter of 2009 to \$19 million, with hard disk drive customers resuming both technology and capacity purchases. Metrology orders were \$23 million, up 38% from the first quarter of 2009, due to new product traction and some improvement in scientific research spending.

Outlook

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

While Veeco remains cautious about overall economic conditions, we are encouraged by the improvement in bookings over the first quarter of 2009 for all three businesses. Veeco's backlog at June 30, 2009 was \$160 million. The positive trends we experienced in the second quarter in our MOCVD business have accelerated into the beginning of this quarter driven by key customers' investments in LED capacity for backlighting applications. We have already received orders for a total of over \$110 million in MOCVD systems during the month of July from

Table of Contents

multiple customers in APAC. As a result of this pace of orders, we currently believe that third quarter LED & Solar bookings will be between \$125 to 175 million. While we remain cautious to the possibility of cancellations and/or rescheduling of orders, based on these order trends it is our current expectation that Veeco's overall third quarter orders will be significantly higher than the second quarter.

Veeco's outlook for the remainder of the year looks significantly different than it did just one quarter ago, primarily due to the strong LED industry demand. We are currently expecting that Veeco will return to EBITA profitability in the third quarter. Since the global economic situation remains uncertain, it is our intention to continue to carefully manage our expenses, while at the same time making selected investments that are required to support the MOCVD production ramp as well as our new CIGS solar equipment business. Veeco currently anticipates that its 2009 revenues will be in the range of \$310 to \$325 million.

Table of Contents

Results of Operations:

Three Months Ended June 30, 2009 and 2008

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

	Three Months Ended June 30,				Dollar and Percentage Change	
	2009		2008			
Net sales	\$ 72,020	100.0%	\$ 114,449	100.0%	\$ (42,429)	(37.1)%
Cost of sales	47,636	66.1	66,719	58.3	(19,083)	(28.6)
Gross profit	24,384	33.9	47,730	41.7	(23,346)	(48.9)
Operating expenses:						
Selling, general, and administrative expense	19,822	27.5	24,311	21.3	(4,489)	(18.5)
Research and development expense	13,163	18.3	15,145	13.2	(1,982)	(13.1)
Amortization expense	1,831	2.5	2,426	2.1	(595)	(24.5)
Restructuring expense	1,944	2.8			1,944	(100.0)
Asset impairment charge	304	0.4			304	(100.0)
Other income, net	(77)	(0.1)	(382)	(0.3)	305	(79.8)
Total operating expenses	36,987	51.4	41,500	36.3	(4,513)	(10.9)
Operating (loss) income	(12,603)	(17.5)	6,230	5.4	(18,833)	(302.3)
Interest expense, net	1,698	2.4	1,700	1.4	(2)	(0.1)
(Loss) income before income	(14,301)	(19.9)	4,530	4.0	(18,831)	(415.7)
Income tax provision	402	0.6	1,129	1.0	(727)	(64.4)
(Loss) income including noncontrolling interest	(14,703)	(20.4)	3,401	3.0	(18,104)	(532.3)
Noncontrolling interest	(23)	(0.0)	(70)		47	(67.1)
Net (loss) income	\$ (14,680)	(20.4)%	\$ 3,471	3.0%	\$ (18,151)	(522.9)%

Net Sales and Orders

Net sales of \$72.0 million for the three months ended June 30, 2009 were down 37.1% compared to the comparable 2008 quarter. The following is an analysis of sales and orders by segment and by region (dollars in thousands):

Segment	Sales				Orders				Book-to-Bill Ratio	
	Three Months Ended June 30,		Dollar and Percentage Change Year to Year		Three Months Ended June 30,		Dollar and Percentage Change Year to Year			
	2009	2008			2009	2008			2009	2008
Segment Analysis										
LED & Solar Process										
Equipment	\$ 31,882	\$ 45,090	\$ (13,208)	(29.3)%	\$ 56,342	\$ 52,061	\$ 4,281	8.2%	1.77	1.15
Data Storage Process										
Equipment	17,593	36,762	(19,169)	(52.1)	19,318	51,716	(32,398)	(62.6)	1.10	1.41
Metrology	22,545	32,597	(10,052)	(30.8)	23,010	32,735	(9,725)	(29.7)	1.02	1.00
Total	\$ 72,020	\$ 114,449	\$ (42,429)	(37.1)%	\$ 98,670	\$ 136,512	\$ (37,842)	(27.7)%	1.37	1.19
Regional Analysis										
Americas	\$ 23,864	\$ 44,688	\$ (20,824)	(46.6)%	\$ 20,660	\$ 52,769	\$ (32,109)	(60.8)%	0.87	1.18
Europe, Middle East and Africa (EMEA)	14,889	23,142	(8,253)	(35.7)	16,193	19,131	(2,938)	(15.4)	1.09	0.83
Japan	4,511	5,989	(1,478)	(24.7)	7,434	7,809	(375)	(4.8)	1.65	1.30
Asia Pacific	28,756	40,630	(11,874)	(29.2)	54,383	56,803	(2,420)	(4.3)	1.89	1.40

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Total	\$	72,020	\$	114,449	\$	(42,429)	(37.1)%	\$	98,670	\$	136,512	\$	(37,842)	(27.7)%	1.37	1.19
-------	----	--------	----	---------	----	----------	---------	----	--------	----	---------	----	----------	---------	------	------

Sales declined in each segment in the second quarter of 2009 compared with the second quarter in 2008 due to our customers' reluctance to invest in capital equipment during the current difficult economic conditions. LED & Solar Process Equipment sales were down 29.3% from the second quarter of 2008 primarily due to a pause in capacity spending as LED customers absorb the equipment purchased from Veeco during the last two years. However, the book-to-bill ratio in that segment increased to 1.77 from 1.15 in the comparable quarter of 2008, indicating an improvement in business outlook for the LED business. Data Storage Process Equipment segment sales

Table of Contents

declined by 52.1% from the second quarter of 2008 due to the slowdown in capital spending by our data storage customers. Additionally, Metrology sales decreased by 30.8% from the second quarter of 2008, primarily due to a slowdown in the research, industrial and data storage markets. By region, net sales decreased by 46.6%, 35.7%, 24.7%, and 29.2% in the Americas, EMEA, Japan, and Asia Pacific, respectively. We believe that there will continue to be quarter-to-quarter variations in the geographic distribution of sales.

Orders for the second quarter of 2009 decreased by 27.7% from the comparable 2008 period. However, orders for LED & Solar Process Equipment increased by 8.2% over the second quarter 2008. This increase was principally driven by LED manufacturers ramping up production for television and laptop backlighting applications. The 62.6% decrease in Data Storage Process Equipment orders resulted from customers continuing to be cautious about their capital spending. The 29.7% decrease in Metrology orders is due to low demand from customers in the semiconductor, research and industrial markets.

Our overall book-to-bill ratio for the second quarter of 2009, which is calculated by dividing orders received in a given period by revenue recognized in the same time period, was 1.37 to 1, an improvement over the ratio of 1.19 to 1 in the comparable quarter of 2008. Our backlog as of June 30, 2009 was \$160 million, compared to \$147.2 million as of December 31, 2008. During the quarter ended June 30, 2009, we experienced backlog adjustments of approximately \$1.8 million, consisting of \$1.1 million for order cancellations and \$0.7 million of adjustments related to foreign currency translation. Due to changing business conditions and weak capital equipment spending by certain customers in our businesses, we may continue to experience cancellations and/or rescheduling of orders. Despite some indications of improvement over the first quarter of 2009, particularly in our LED & Solar Process Equipment segment, we still expect 2009 to be a challenging year for the Company overall.

Gross Profit

Gross profit for the quarter ended June 30, 2009, was 33.9%, compared to 41.7% in the second quarter of 2008, primarily due to the significant decline in sales. LED & Solar Process Equipment gross margins decreased to 32.7% from 41.4% in the prior-year period, primarily due to the significant decrease in sales volume and unfavorable product mix as compared to the prior-year period. Data Storage Process Equipment gross margins decreased to 34.3% from 40.2% in the prior-year period, due to reduced sales volume. Metrology gross margins decreased to 35.2% from 43.8%, principally due to lower sales volume and a less favorable product mix and pricing in Metrology instruments.

Operating Expenses

Selling, general and administrative expenses decreased by \$4.5 million, or 18.5%, from the prior-year period, primarily due to lower salary and related expenses resulting from the personnel reductions taken as part of management's restructuring plan, a reduction in incentive bonus and profit-sharing expense, and lower commissions as well as cost savings initiatives resulting in less travel and entertainment, marketing, and other operating and occupancy expenses.

Research and development expense decreased \$2.0 million from the second quarter of 2008, primarily due to a more focused approach to Metrology and Data Storage product development that resulted from our restructuring activities. As a percentage of sales, research and development increased to 18.3% in the second quarter of 2009 from 13.2% in the second quarter of 2008, as a result of lower sales volume. The Company continues to invest in higher-growth end market opportunities, particularly in its LED & Solar segment.

Amortization expense was \$1.8 million in the second quarter of 2009, compared to \$2.4 million in the second quarter of 2008, due to reduced intangible assets resulting from asset impairment charges taken during the fourth quarter of 2008.

Restructuring expense of \$1.9 million for the second quarter of 2009 consists 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 \$0.3 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. No such costs were incurred in the second quarter of 2008.

Table of Contents

Interest Expense, Net

Net interest expense was \$1.7 million in the second quarter in each of 2009 and 2008, comprised in both years of \$1.0 million in cash net interest expense and \$0.7 million in non-cash interest expense related to the implementation of FASB Staff Position No. APB 14-1 (FSP APB 14-1), *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)*. See *Recent Accounting Pronouncements* for a further discussion of the implementation of FSP APB 14-1.

Income Taxes

The income tax provision for the quarter ended June 30, 2009 was \$0.4 million compared to \$1.1 million in the second quarter of 2008. The 2009 provision for income taxes included \$0.3 million relating to our foreign operations, which continue to be profitable, and \$0.1 million relating to our domestic operations. The 2008 provision for income taxes included \$0.8 million relating to our foreign operations, and \$0.3 million relating to our domestic operations. Due to significant domestic net operating loss carryforwards, which are fully reserved by a valuation allowance, our domestic operations are not expected to incur significant income taxes for the foreseeable future.

Six Months Ended June 30, 2009 and 2008

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

	Six Months Ended June 30,				Dollar and Percentage Change		
	2009		2008				
Net sales	\$	134,869	100.0%	\$	216,756	100.0%	\$ (81,887) (37.8)%
Cost of sales		90,103	66.8		126,400	58.3	(36,297) (28.7)
Gross profit		44,766	33.2		90,356	41.7	(45,590) (50.5)
Operating expenses:							
Selling, general, and administrative expense		38,429	28.5		46,939	21.7	(8,510) (18.1)
Research and development expense		26,049	19.3		29,871	13.8	(3,822) (12.8)
Amortization expense		3,660	2.7		4,382	2.0	(722) (16.5)
Restructuring expense		6,375	4.7		2,875	1.3	3,500 121.7
Asset impairment charge		304	0.3		285	0.1	19 6.7
Other income, net		1,409	1.0		(378)	(0.2)	1,787 (472.8)
Total operating expenses		76,226	56.5		83,974	38.7	(7,748) (9.2)
Operating income		(31,460)	(23.3)		6,382	3.0	(37,842) (592.9)
Interest expense, net		3,407	2.6		3,305	1.5	102 3.1
(Loss) income before income taxes		(34,867)	(25.9)		3,077	1.5	(37,944) (1233.1)
Income tax provision		780	0.5		2,048	0.9	(1,268) (61.9)
(Loss) income before noncontrolling interest		(35,647)	(26.4)		1,029	0.6	(36,676) (3564.2)
Noncontrolling interest		(65)	(0.0)		(146)	(0.1)	81 (55.5)
Net (loss) income	\$	(35,582)	(26.4)%	\$	1,175	0.5%	\$ (36,757) (3128.3)%

Net Sales and Orders

Net sales of \$134.9 million for the six months ended June 30, 2009 were down 37.8% compared to the comparable 2008 period. The following is an analysis of sales and orders by segment and by region (dollars in thousands):

	Sales				Orders				Book-to-Bill Ratio	
	Six Months Ended June 30,		Dollar and Percentage Change		Six Months Ended June 30,		Dollar and Percentage Change			
	2009	2008	Year to Year		2009	2008	Year to Year		2009	2008
Segment Analysis										
LED & Solar Process										
Equipment	\$ 54,084	\$ 87,222	\$ (33,138)	(38.0)%	\$ 84,863	\$ 90,738	\$ (5,875)	(6.5)%	1.57	1.04
Data Storage Process										
Equipment	34,498	60,840	(26,342)	(43.3)	27,136	92,326	(65,190)	(70.6)	0.79	1.52
Metrology	46,287	68,694	(22,407)	(32.6)	39,721	62,707	(22,986)	(36.7)	0.86	0.91
Total	\$ 134,869	\$ 216,756	\$ (81,887)	(37.8)%	\$ 151,720	\$ 245,771	\$ (94,051)	(38.3)%	1.12	1.13
Regional Analysis										
Americas	\$ 43,833	\$ 77,766	\$ (33,933)	(43.6)%	\$ 32,232	\$ 93,410	\$ (61,178)	(65.5)%	0.74	1.20
EMEA	33,150	41,029	(7,879)	(19.2)	27,497	35,014	(7,517)	(21.5)	0.85	0.85
Japan	9,987	22,743	(12,756)	(56.1)	14,360	16,779	(2,419)	(14.4)	1.44	0.74
Asia Pacific	47,899	75,218	(27,319)	(36.3)	77,631	100,568	(22,937)	(22.8)	1.62	1.34
Total	\$ 134,869	\$ 216,756	\$ (81,887)	(37.8)%	\$ 151,720	\$ 245,771	\$ (94,051)	(38.3)%	1.12	1.13

Table of Contents

Sales declined in each segment in the six months ended June 30, 2009 compared with the same period in 2008 due to our customers' reluctance to invest in capital equipment during the current difficult economic conditions. LED & Solar Process Equipment sales were down 38.0% from the same period of 2008 primarily due to a pause in capacity spending as LED customers absorb the equipment purchased from Veeco during the last two years. Data Storage Process Equipment segment sales declined by 43.3% from the same period of 2008 due to a slowdown in capital spending by our data storage customers. Additionally, Metrology sales decreased by 32.6% from the same period of 2008, primarily due to a slowdown in the research, industrial and data storage markets. By region, net sales decreased by 43.6%, 19.2%, 56.1%, and 36.3% in the Americas, EMEA, Japan, and Asia Pacific, respectively. We believe that there will continue to be quarter-to-quarter variations in the geographic distribution of sales.

Orders for the six months ended June 30, 2009 decreased by 38.3% from the comparable 2008 period. On a segment basis, orders for LED & Solar Process Equipment decreased by 6.5% from the comparable period in 2008, principally driven by economic conditions in recent quarters, which had caused some potential customers to delay investing in these emerging markets. The 70.6% decrease in Data Storage Process Equipment orders resulted from customers continuing to significantly slow down their capital spending. The 36.7% decrease in Metrology orders is due to low demand from customers in the semiconductor and research and industrial markets.

Our overall book-to-bill ratio, which is calculated by dividing orders received in a given time period by revenue recognized in the same time period, was 1.12 for the six months ended June 30, 2009, vs. 1.13 for the comparable period in 2008. However the book-to-bill ratio for the LED & Solar Process Equipment segment improved to 1.57 to 1 from 1.04 to 1 in the same period in 2008. Our backlog as of June 30, 2009 was \$160 million, compared to \$147.2 million as of December 31, 2008. During the six months ended June 30, 2009, we experienced backlog adjustments of approximately \$3.9 million, consisting of \$2.9 million for order cancellations and \$1.0 million of adjustments related to foreign currency translation. Due to changing business conditions and weak capital equipment spending by certain customers in our businesses, we may continue to experience cancellations and/or rescheduling of orders. Despite some indications of improvement over the first quarter of 2009, particularly in the LED & Solar Process Equipment segment, we still expect 2009 to be a challenging year for the Company as we continue to experience weak new order conditions and customers foregoing capacity and technology investments in our Data Storage and Metrology segments.

Gross Profit

Gross profit for the six months ended June 30, 2009, was 33.2%, compared to 41.7% in the comparable 2008 period, primarily due to the significant decline in sales. LED & Solar Process Equipment gross margins decreased from 41.2% in the prior-year period to 31.3%, primarily due to the significant decrease in sales volume as compared to the prior-year period. Additionally, Data Storage Process Equipment gross margins decreased from 38.3% in the prior-year period to 30.9%, due to reduced sales volume as well as a charge of \$1.5 million to write-off inventory in the first quarter of 2009 associated with certain discontinued data storage product lines. Metrology gross margins decreased from 45.3% in the prior year period to 37.2%, principally due to lower sales volume and a less favorable product mix in Metrology instrumentation product sales.

Operating Expenses

Selling, general and administrative expenses decreased by \$8.5 million, or 18.1%, from the prior-year period, primarily due to lower salary and related expenses resulting from the personnel reductions taken as part of management's restructuring plan, a reduction in incentive bonuses and profit sharing, and decreased commissions expense, as well as cost savings initiatives resulting in less consulting, legal, and professional fees and travel and entertainment expenses.

Table of Contents

Research and development expense decreased \$3.8 million from the comparable period of 2008, primarily due to a more focused approach to metrology and data storage product development resulting from our restructuring activities. As a percentage of sales, research and development increased to 19.3% in the six months ended June 30, 2009 from 13.8% in the same period in 2008 as a result of lower sales.

Amortization expense was \$3.7 million in the six months ended June 30, 2009, compared to \$4.4 million in comparable period of 2008, due to reduced intangible assets resulting from asset impairment charges taken during the fourth quarter of 2008.

Restructuring expense of \$6.4 million for the six months ended June 30, 2009 consists of \$5.2 million of personnel severance costs resulting from a reduction in workforce. In addition, there were \$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 to the \$6.4 million restructuring expense, there was also a \$0.3 million asset impairment charge. Restructuring expense of \$2.9 million incurred in the six months ended June 30, 2008 consists of \$2.6 million in lease-related costs associated with the consolidation and relocation of our Corporate headquarters into our Plainview, New York facility, and \$0.3 million of personnel severance costs.

Other expense, net for the six months ended June 30, 2009 includes a foreign currency exchange loss of \$1.3 million.

Interest Expense, Net

Net interest expense in the second quarter of 2009 was \$3.4 million, comprised of \$2.0 million in cash net interest expense and \$1.4 million in non-cash interest expense related to the implementation of FSP APB 14-1. Net interest expense in the second quarter of 2008 was \$3.3 million, comprised of \$1.9 million in cash net interest expense and \$1.4 million in non-cash interest expense that is presented pursuant to the retroactive presentation requirements of FSP APB 14-1. See *Recent Accounting Pronouncements* for a further discussion of the implementation of FSP APB 14-1. The slight increase in net interest expense is due to lower interest income resulting from lower interest rates and lower average cash balances invested during the current period compared to the comparable 2008 period, partially offset by decreases in interest expense resulting from the extinguishment of \$25.2 million of the convertible subordinated notes in December 2008, and the repurchase of \$12.2 million of our 4.125% convertible subordinated notes due April 2012 during the fourth quarter of 2008.

Income Taxes

Income tax provision for the six months ended June 30, 2009 was \$0.8 million compared to \$2.0 million in the comparable prior year period. The 2009 provision for income taxes included \$0.5 million relating to our foreign operations, and \$0.3 million relating to our domestic operations. The 2008 provision for income taxes included \$1.4 million relating to our foreign operations, and \$0.6 million relating to our domestic operations. Due to significant domestic net operating loss carryforwards, which are fully reserved by a valuation allowance, our domestic operations are not expected to incur significant income taxes for the foreseeable future.

Liquidity and Capital Resources

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Historically, our principal capital requirements have included the funding of acquisitions and capital expenditures. 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, 2009 and 2008 is as follows (in thousands):

	Six Months Ended	
	2009	June 30, 2008
Net cash provided by operating activities	\$ 8,044	\$ 10,455
Net cash used in investing activities	(13,709)	(17,832)
Net cash used in financing activities	(391)	(162)
Effect of exchange rates on cash and cash equivalents	(249)	100
Net change in cash and cash equivalents	(6,305)	(7,439)
Cash and cash equivalents at beginning of period	103,799	117,083
Cash and cash equivalents at end of period	\$ 97,494	\$ 109,644

Table of Contents

We had a net decrease in cash of \$6.3 million during the six months ended June 30, 2009 as a result of having paid out \$9.6 million in earn-out consideration to the former owners of Mill Lane Engineering Co. (Mill Lane), which we acquired in May 2008, and \$9.7 million in bonus and profit-sharing in the first quarter of 2009. Cash provided by operations was \$8.0 million for this period, as compared to cash provided by operations of \$10.5 million for the comparable 2008 period. Net loss adjusted for non-cash items used operating cash flows of \$17.6 million for the six months ended June 30, 2009, as compared to \$18.8 million provided in the comparable 2008 period. Net cash provided by operations for the six months ended June 30, 2009 was favorably impacted by a net change in net operating assets and liabilities of \$25.6 million. This was driven by a decrease in accounts receivable of \$26.9 million due to reduced sales volume and shorter collection periods, and a decrease in inventories of approximately \$15.1 million due to reduction efforts and the impact of outsourcing. These amounts were partially offset by a decrease in accounts payable of \$10.5 million and a decrease in accrued expenses of \$6.1 million, primarily due to the payment of incentive bonus and profit sharing during the first quarter of 2009.

We had a net decrease in cash of \$7.4 million during the six months ended June 30, 2008. Cash provided by operations was \$10.5 million for this period. Net income adjusted for non-cash items provided operating cash flows of \$18.8 million for the six months ended June 30, 2008. Net cash provided by operations for the six months ended June 30, 2008 was unfavorably impacted by a net change in net operating assets and liabilities of \$8.3 million. This was driven by an increase in inventories of approximately \$11.1 million over the prior period due to an increase in finished goods for process equipment systems which shipped in subsequent quarters.

Cash used in investing activities of \$13.7 million for the six months ended June 30, 2009 resulted primarily from the \$9.6 million earn-out payment to the former owners of Mill Lane, as well as capital expenditures of \$3.6 million. During the remainder of 2009, we expect to invest an estimated additional \$8.8 million in capital projects primarily related to engineering equipment and lab tools used in producing, testing and process development of our products and enhanced manufacturing facilities. Cash used in investing activities of \$17.8 million for the six months ended June 30, 2008 resulted primarily from the acquisition of Mill Lane for \$10.9 million.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

Cash used in financing activities for the six months ended June 30, 2009 totaled \$0.4 million, resulting from \$0.3 million in restricted stock tax withholdings and \$0.1 million in mortgage payments. Cash used in financing activities for the six months ended June 30, 2008 totaled \$0.2 million, resulting from \$0.6 million in restricted stock tax withholdings and \$0.2 million in mortgage payments, offset by proceeds of \$0.7 million from stock issuances resulting from stock option exercises.

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

In February 2009, we entered into an amendment to our existing credit agreement with HSBC Bank USA, National Association (HSBC), as administrative agent, and the lenders named therein (as amended, the Credit Agreement). As part of the amendment, we reduced the amount of the revolving credit facility, modified certain existing covenants and added certain new covenants. As amended, the Credit Agreement provides for revolving credit borrowings of up to \$30.0 million. The Credit Agreement was amended effective March 27, 2009 to modify certain financial covenants, to provide for the cash collateralization of borrowings and letters of credit outstanding under the Credit Agreement, and to permit the acquisition of the 80.1% of the outstanding stock of Fluens Corporation (Fluens) which we did not yet own. The annual interest rate under the Credit Agreement is a floating rate equal to the prime rate of the agent bank plus 2.0%. A LIBOR-based interest rate option is also provided. Borrowings may be used for general corporate purposes, including working capital requirements, as well as permitted acquisitions. The Credit Agreement contains certain restrictive covenants which include the maintenance of minimum cash balances and limitations with respect to incurrence of indebtedness, the payment of dividends, long-term leases, investments, mergers, acquisitions, consolidations and sales of assets. In addition, under the Credit Agreement, we are required to satisfy certain financial tests, including minimum profitability levels. As of June 30, 2009, we were in compliance with all covenants of the Credit Agreement as amended. Substantially all of our assets and those of our material domestic subsidiaries, other than real estate, have been pledged to secure our obligations.

Table of Contents

under the Credit Agreement. The revolving credit facility under the Credit Agreement expires on March 31, 2012. In the first six months of 2009, we recognized an expense of \$0.2 million representing the amount of deferred financing fees equal to the portion of the revolving credit facility which was terminated in connection with the amendment, which is included in other expense, net. We also capitalized \$0.1 million in deferred financing fees that we incurred in connection with the February 2009 amendment. There were no borrowings outstanding as of June 30, 2009 under the Credit Agreement, and no borrowings outstanding as of or December 31, 2008 under the prior credit agreement. Letters of credit outstanding at June 30, 2009 and December 31, 2008 totaled approximately \$0.5 million and \$0.4 million, respectively. In the second quarter of 2009 we transferred \$0.5 million of cash into a restricted cash account pursuant to the terms of the March 2009 amendment, which requires cash collateralization of borrowings and letters of credit. This amount is included in prepaid and other current assets. We recorded interest expense associated with the Credit Agreement during the six months ended June 30, 2009 and 2008, respectively, of approximately \$0.1 million in each period.

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

In 2006, we invested \$0.5 million to purchase 19.9% of the common stock of Fluens. Veeco and Fluens have jointly developed a next-generation process for high-rate deposition of aluminum oxide for data storage applications. In May 2009, we purchased the remaining 80.1% of the outstanding stock of Fluens for \$1.5 million plus an earn-out arrangement based on future performance. We paid \$0.5 million of the \$1.5 million upon closing, as well as \$0.2 million in respect of the earn-out arrangement. We will pay the remaining \$1.0 million of the \$1.5 million in equal quarterly installments of \$0.5 million in each of the third and fourth quarters of 2009. Approximately 31% of Fluens was owned by a Senior Vice President of Veeco just prior to our purchase of the remaining 80.1%.

In July 2009, Veeco acquired certain assets from DayStar Technologies, Inc. ("DayStar") in order to accelerate Veeco's penetration of the rapidly growing copper, indium, gallium, selenium (CIGS) solar market. Veeco purchased selected equipment, took over leased facilities and hired DayStar's R&D group in Clifton Park, New York. In connection with these transactions, Veeco paid DayStar \$2 million in cash.

Contractual Obligations

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

- a \$9.6 million earn-out payment related to the Mill Lane acquisition, which we made in the first quarter of 2009;
- a commitment to pay \$1.5 million for the purchase of the remaining 80.1% of Fluens, \$0.5 million of which we made in the second quarter of 2009, with the remaining \$1 million to be paid in the third and fourth quarters of 2009;

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

- potential earn-out payments related to the purchase of Fluens, \$0.2 million of which we paid in the second quarter of 2009; and
- the increase in our purchase commitments from \$27.7 million at December 31, 2008 to \$47.4 million at June 30, 2009. The majority of our purchase commitments at June 30, 2009 relate to increases in spending to fulfill orders for MOCVD tools.

Table of Contents

Application of Critical Accounting Policies

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

Revenue Recognition: We recognize revenue based on guidance provided in Securities and Exchange Commission Staff Accounting Bulletin No. 104, *Revenue Recognition*. 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, in accordance with the provisions of Emerging Issues Task Force (EITF) 00-21, *Revenue Arrangements with Multiple Deliverables*.

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

Instruments - 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

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

represents only 2% - 4% of the fair value of the sales contract. Sales arrangements for these systems are accounted for in accordance with EITF 00-21, as the Company bifurcates transactions 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

Table of Contents

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 Consolidated Balance Sheets.

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

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

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

Goodwill and Indefinite-Lived Intangible Asset Impairment: The Company accounts for goodwill and intangible assets with indefinite useful lives in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets* (SFAS 142), which states that goodwill and intangible assets with indefinite useful lives should not be amortized, but instead tested 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 SFAS 142 we are required to determine if it is appropriate to use the operating segment as defined under SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information* (SFAS 131) as the reporting unit, or one level below the operating segment, depending on whether certain criteria are met. We have identified four reporting units that are required to be reviewed for impairment. The reporting units are Data Storage Process Equipment, LED & Solar Process Equipment, AFM and Optical Metrology. AFM and Optical Metrology comprise the Metrology operating segment. In identifying the reporting units management considered the economic characteristics of

operating segments including the products and services provided, production processes, types or classes of customer and product distribution.

We perform this impairment test by first comparing the fair value of our reporting units to their respective carrying amount. When determining the estimated fair value of a reporting unit, we utilize a discounted future cash flow approach since reported quoted market prices are not available for our reporting units. Developing the estimate of the discounted future cash flow requires significant judgment and projections of future financial performance. The key assumptions used in developing the discounted future cash flows are the projection of future revenues and

Table of Contents

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 are identifiable cash flows that are largely independent of the cash flows generated by other asset groups. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge would be recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset.

Fair Value Measurements: We implemented the guidance in Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157) for our non-financial assets and non-financial liabilities as of January 1, 2009. SFAS 157 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 SFAS 157. 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. The requirements of SFAS 157 apply to our long-lived assets, goodwill, and intangible assets. We use Level 3 inputs to value all of such assets, and the methodology we use to value such assets has not changed since December 31, 2008.

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

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

We record valuation allowances in order to reduce our deferred tax assets to the amount expected to be realized. In assessing the adequacy of recorded valuation allowances, we consider a variety of factors, including the scheduled reversal of deferred tax liabilities, future taxable income, and prudent and feasible tax planning strategies. Under SFAS No. 109, factors such as current and previous operating losses are given significantly greater weight than the outlook for future profitability in determining the deferred tax asset carrying value.

Table of Contents

At June 30, 2009, we had a valuation allowance of approximately \$91.2 million against substantially all of our domestic net deferred tax assets, which consist of net operating loss and tax credit carry forwards, as well as temporary deductible differences. If we are able to realize part or all of the domestic deferred tax assets in future periods, we will reduce our provision for income taxes with a release of the valuation allowance in an amount that corresponds with the income tax liability generated.

Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement 109* (FIN 48) 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 FIN 48, we must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such uncertain tax positions are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate resolution. We had approximately \$1.0 million of unrecognized tax benefits at June 30, 2009 and December 31, 2008, which predominantly relate to positions taken on our foreign tax returns and all of which represent the amount of unrecognized tax benefits that, if recognized, would favorably impact the effective income tax rate in future periods.

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

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

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

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

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

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

Recent Accounting Pronouncements

Convertible debt: In May 2008, the FASB issued FSP APB 14-1. We implemented FSP APB 14-1 as of January 1, 2009 and have applied it retrospectively to all periods presented, as required. FSP APB 14-1 requires issuers of convertible debt that can be settled in cash to separately account for (*i.e.*, bifurcate) a portion of the debt associated with the conversion feature and reclassify this portion to stockholders' equity. The liability portion, which represents the fair value of the debt without the conversion feature, is accreted to its face value over the life of the debt using the effective interest method by amortizing the discount between the face amount and the fair value. The amortization is recorded as interest expense. The Notes are subject to FSP APB 14-1 since they may be settled in

Table of Contents

cash upon conversion. Thus, as a result of the adoption of FSP APB 14-1, we reclassified approximately \$16.3 million from long-term debt to additional paid-in capital effective as of the date of issuance of the Notes. This reclassification created a \$16.3 million discount on the debt that will be amortized over the remaining life of the Notes, which will be through April 15, 2012. The reclassification generated a \$6.7 million deferred tax liability, which we offset with a corresponding decrease of the valuation allowance by the same amount. FSP APB 14-1 requires that we present prior periods as if the guidance was in effect as of the date of issuance. Thus, we have presented all financial data for prior periods in this report as if we had reclassified the \$16.3 million and began amortizing the resultant debt discount in April 2007.

During the fourth quarter of 2008, we repurchased an aggregate principal amount of \$12.2 million of the Notes for \$7.2 million in cash, of which \$7.1 million related to principal and \$0.1 million related to accrued interest, reducing the amount outstanding from \$117.8 million to \$105.6 million. A gross gain of approximately \$5.1 million was recorded on these repurchases offset by the write-off of approximately \$0.1 million of unamortized deferred financing costs associated with the Notes, for a net gain of approximately \$5.0 million. Such net gain was reduced to \$3.8 million upon the adoption of FSP APB 14-1, which required that the gain be calculated based on the fair value of the portion repurchased as of the date bought back. The fair value approximated the carrying value net of the unamortized discount on the portion repurchased. The difference of approximately \$1.2 million between the fair value and the amount paid was recorded as a reduction in the gain originally reported, which increased the accumulated deficit as of December 31, 2008 by that amount.

For the three months ended June 30, 2009 and 2008, respectively, we recorded approximately \$0.7 million of additional interest expense in each period resulting from the amortization of the debt discount. For the six months ended June 30, 2009 and 2008, respectively, we recorded approximately \$1.4 million of additional interest expense in each period resulting from the amortization of the debt discount. This additional interest expense did not require the use of cash. The retrospective application of FSP APB 14-1 to the results for the three and six months ended June 30, 2008 decreased net income attributable to Veeco in that period from \$4,202 to \$3,471 and decreased earnings per share attributable to Veeco from \$0.13 to \$0.11. The retrospective application of FSP APB 14-1 to the results for the six months ended June 30, 2008 decreased net income attributable to Veeco in that period from \$2,619 to \$1,175 and decreased earnings per share attributable to Veeco from \$0.08 to \$0.04.

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

Noncontrolling Interest: In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, *Noncontrolling Interests in Consolidated Financial Statements – an Amendment of ARB No. 51* (SFAS 160). The purpose of SFAS 160 is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements. The most significant provisions of this statement result in changes to the presentation of noncontrolling interests in the consolidated financial statements. We implemented SFAS 160 as of January 1, 2009. The adoption of this statement impacted the manner in which we present noncontrolling interests for all periods included in this report, but did not impact our consolidated financial position or results of operations.

Fair Value: In April 2009, the FASB issued FASB Staff Position FAS 107-1 (FSP 107-1) and Accounting Principles Board Opinion No. 28-1 (APB 28-1), *Interim Disclosures about Fair Value of Financial Instruments*. FSP 107-1 and APB 28-1 amend SFAS 107, *Disclosures about Fair Value of Financial Instruments*, and Accounting Principles Board Opinion No. 28, *Interim Financial Reporting* to require disclosures about the fair value of financial instruments in interim financial statements in addition to the existing requirement for annual financial statements. We adopted FSP 107-1 and APB 28-1 for the period ending June 30, 2009.

Subsequent Events: In May 2009, the FASB issued SFAS 165, *Subsequent Events*. The term *subsequent events* refers to events that occur after the last date in the period on which we are reporting through the date the financial statements are issued, and which may require recognition or disclosure in the financial statements. SFAS 165 should not result in significant changes in the subsequent events that are reported, but rather requires disclosure of the date through which the company evaluates whether subsequent events have occurred. We have evaluated

Table of Contents

subsequent events from the date of these financial statements through the date on which these financial statements were issued. During this period we did not have any material recognizable subsequent events.

Table of Contents

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Our net sales to foreign customers represented approximately 66.9% and 67.5%, respectively, of our total net sales for the three months and six months ended June 30, 2009, and 61.0% and 64.1%, respectively, for the comparable 2008 periods. We expect that net sales to foreign customers will continue to represent a large percentage of our total net sales. Our net sales denominated in foreign currencies represented approximately 16.2% and 15.4%, of our total net sales for the three months and six months ended June 30, 2009, respectively, and 19.7% and 17.8%, respectively, for the comparable 2008 periods.

The condensed consolidated results of operations for the three and six months ended June 30, 2009 include an aggregate foreign currency gain of approximately \$0.1 million and an aggregate foreign currency loss of approximately \$1.3 million, respectively. The loss of \$1.3 million for the six months ended June 30, 2009 was net of gains of approximately \$0.2 million related to forward contracts. The condensed consolidated results of operations for the three months and six months ended June 30, 2008 include aggregate foreign currency losses of less than \$0.1 million and gains of approximately \$0.1 million, respectively, which were net of gains of approximately \$0.1 million and losses of \$0.2 million, respectively, related to forward contracts. These amounts were recognized and included in other expense, net.

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 months and six months ended June 30, 2009 was \$2.6 million and \$3.6 million, respectively.

As of June 30, 2009, gains of less than \$0.1 million related to forward contracts were included in prepaid and other current assets. Cash in an amount equivalent to such gains was received in July 2009. As of December 31, 2008, approximately \$0.9 million of losses related to forward contracts were included in accrued expenses and subsequently paid in January 2009. Monthly forward contracts with a total notional amount of \$2.0 million were entered into in June 2009 and will be settled in July 2009. The fair value of these contracts at inception was zero, which did not significantly change at June 30, 2009.

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

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

Item 4. Controls and Procedures.

Edgar Filing: VEECO INSTRUMENTS INC - Form 10-Q

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

We have evaluated the effectiveness of the design and operation of our disclosure controls and procedures under the supervision of and with the participation of management, including the chief executive officer and chief financial officer, as of the end of the period covered by this report. Based on that evaluation, our chief executive officer and our chief financial officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded,

Table of Contents

processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Table of Contents

Part II. OTHER INFORMATION

Item 1. Legal Proceedings.

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

Item 1A. Risk Factors.

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

Our failure to successfully implement outsourcing activities or failure of our outsourcing partners to perform as anticipated could adversely affect our results of operations and our ability to realize the benefits of the recent increase in MOCVD order volume.

To better align our costs with market conditions, increase the percentage of variable costs relative to total costs and to increase productivity and operational efficiency, we have outsourced, and plan to increase the outsourcing of, certain functions to third parties, including the manufacture of all or substantially all of our new MOCVD systems, data storage process equipment systems, solar deposition systems and ion sources. We are relying heavily on our outsourcing partners to successfully execute the ramp in MOCVD system production to fill the substantial increase in recent MOCVD orders. Dependence on contract manufacturing and outsourcing may adversely affect our ability to satisfy the recent strong demand for our MOCVD equipment and to bring other new products to market. If our outsourcing partners do not perform successfully, our results of operations may be adversely affected and we could suffer damage to our reputation. Although we attempt to select reputable providers, it is possible that one or more of these providers could fail to perform as we expect. In addition, the expanded role of third party providers has required and will continue to require us to implement changes to our existing operations and adopt new procedures and processes for retaining and managing these providers in order to realize operational efficiencies, assure quality, and protect our intellectual property. If we do not timely and effectively develop and implement our outsourcing strategy or if third party providers do not perform as anticipated, we may not realize the benefits of the recent increase in MOCVD order volume or gross margin or productivity improvements and we may experience operational difficulties, increased costs, manufacturing interruptions or delays, inefficiencies in the structure and/or operation of our supply chain, loss of intellectual property rights, quality issues, increased product time-to-market and/or inefficient allocation of human resources, any or all of which could materially and adversely affect our business, financial condition and results of operations.

Table of Contents**Item 4. Submission of Matters to a Vote of Security Holders.**

The annual meeting of stockholders of the Company was held on May 15, 2009. The matters voted on at the meeting were: (a) the election of two directors: (i) Edward H. Braun and (ii) Richard A. D'Amore; and (b) ratification of the Board's appointment of Ernst & Young LLP as the Company's independent registered public accounting firm for the year ending December 31, 2009. The terms of each of the following directors continued after the meeting: Joel A. Elftmann, John R. Peeler, Peter J. Simone, Heinz K. Fridrich, Roger D. McDaniel and Irwin H. Pfister. As of the record date for the meeting, there were 32,174,530 shares of common stock outstanding, each of which was entitled to one vote with respect to each of the matters voted on at the meeting. Each of the directors up for reelection was reelected and the appointment of Ernst & Young LLP as the Company's independent registered public accounting firm was ratified by the required number of votes on each such matter. The results of the voting were as follows:

Matter	For	Withheld
(a)(i)	27,016,665	668,882
(a)(ii)	26,434,145	1,251,402

Matter	For	Against	Abstained	Broker Non-Votes
(b)	27,519,786	155,844	9,917	

Table of Contents

Item 6. Exhibits.

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

Number	Description	Incorporated by Reference to the Following Document:
10.1	Third Amendment dated as of May 7, 2009 (effective March 27, 2009) to the Credit Agreement dated August 20, 2007 among Veeco Instruments Inc., HSBC Bank USA, National Association, as administrative agent, and the lenders named therein.	Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2009, Exhibit 10.3
10.2	Letter agreement effective as of June 19, 2009 between John P. Kiernan and Veeco Instruments Inc.	*
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 30, 2009

Veeco Instruments Inc.

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

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

Table of Contents**INDEX TO EXHIBITS**

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

Number	Description	Incorporated by Reference to the Following Document:
10.1	Third Amendment dated as of May 7, 2009 (effective March 27, 2009) to the Credit Agreement dated August 20, 2007 among Veeco Instruments Inc., HSBC Bank USA, National Association, as administrative agent, and the lenders named therein.	Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2009, Exhibit 10.3
10.2	Letter agreement effective as of June 19, 2009 between John P. Kiernan and Veeco Instruments Inc.	*
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
