

VEECO INSTRUMENTS INC
Form 10-Q
November 01, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2018

OR

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

Commission file number 0-16244

VEECO INSTRUMENTS INC.

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(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	11-2989601 (I.R.S. Employer Identification No.)
Terminal Drive Plainview, New York (Address of Principal Executive Offices)	11803 (Zip Code)

Registrant's telephone number, including area code:

(516) 677-0200

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 every Interactive Data File required to be submitted 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 such files). Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
	Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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

Title of Class	Shares Outstanding
Common Stock	as of October 24, 2018
par value \$0.01 per share	47,793,001

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Safe Harbor Statement

This quarterly report on Form 10-Q (the “Report”) contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Discussions containing such forward-looking statements may be found in Part I - Items 1, 2, and 3 hereof, as well as within this Report generally. In addition, when used in this Report, the words “believes,” “anticipates,” “expects,” “estimates,” “targets,” “plans,” “intends,” “will,” and similar expressions related to the future are intended to 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.

In addition, the preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles (“U.S. GAAP”) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Although these estimates and assumptions are based on knowledge of current events and planned actions to be undertaken in the future, they may ultimately differ from actual results. Operating results for the nine months ended September 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. All estimates and assumptions are subject to a number of risks and uncertainties that could cause actual results to differ materially from these estimates and assumptions.

The risks and uncertainties of Veeco Instruments Inc. (together with its consolidated subsidiaries, “Veeco,” the “Company,” “we,” “us,” and “our,” unless the context indicates otherwise) including, without limitation, those set forth under the heading “Risk Factors” Part 1, Item 1A in our 2017 Form 10-K and Part 2, Item 1A in this quarterly report, and the following:

- Unfavorable market conditions may adversely affect our operating results;
- We are exposed to the risks of operating a global business;
- We may be unable to effectively enforce and protect our intellectual property rights;
- We may be subject to claims of intellectual property infringement by others;
- We may be unable to successfully integrate the Ultratech business and may not realize the anticipated benefits of the acquisition;
- The price of our common shares is volatile and could further decline;

- We face significant competition;
- We operate in industries characterized by rapid technological change;
- Our sales to manufacturers are highly dependent on sales of consumer electronics applications, which can experience significant volatility due to seasonal and other factors;
- We have a concentrated customer base, located primarily in a limited number of regions, which operate in highly concentrated industries;
- A further reduction or elimination of foreign government subsidies and economic incentives may adversely affect the future order rate for our MOCVD equipment;
- The cyclical nature of the industries we serve directly affects our business;
- The timing of our orders, shipments, and revenue recognition may cause our quarterly operating results to fluctuate significantly;

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- Our sales cycle is long and unpredictable;
- Our backlog is subject to customer cancellation or modification which could result in decreased sales, increased inventory obsolescence, and liabilities to our suppliers for products no longer needed;
- Our failure to estimate customer demand accurately could result in inventory obsolescence, liabilities to our suppliers for products no longer needed, and manufacturing interruptions or delays which could affect our ability to meet customer demand;
- Our failure to successfully manage our outsourcing activities or failure of our outsourcing partners to perform as anticipated could adversely affect our results of operations;
- We rely on a limited number of suppliers, some of whom are our sole source for particular components;
- Our inability to attract, retain, and motivate employees could have a material adverse effect on our business;
- We are exposed to risks associated with business combinations, acquisitions, and strategic investments;
- We may be unable to obtain required export licenses for the sale of our products;
- Our operating results may be adversely affected by tightening credit markets;
- We may be exposed to liabilities under the Foreign Corrupt Practices Act and other similar laws;
- We are subject to internal control evaluations and attestation requirements of Section 404 of the Sarbanes-Oxley Act and any delays or difficulties in satisfying these requirements or negative reports concerning our internal controls could adversely affect our future results of operations and our stock price;
- Changes in accounting pronouncements or taxation rules or practices may adversely affect our financial results;
- Our income taxes may change;
- We may be required to take additional impairment charges on assets;

- We have indebtedness in the form of convertible senior notes which could adversely affect our financial position, prevent us from implementing our strategy, and dilute the ownership interest of our existing shareholders;
- The accounting method for convertible debt securities that may be settled in cash, such as the Convertible Senior Notes, could have a material effect on our reported financial results;
- We are subject to foreign currency exchange risks;
- Our previously announced share repurchase program could affect the price of our common stock and increase volatility and may be suspended or terminated at any time, which may result in a decrease in the trading price of our common stock;
- If we are subject to cyber-attacks we could incur substantial costs and, if such attacks are successful, we could incur significant liabilities, reputational harm, and disruption to our operations;

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- We have adopted certain measures that may have anti-takeover effects which may make an acquisition of our Company by another company more difficult;
- We are subject to risks of non-compliance with environmental, health, and safety regulations;
- Regulations related to conflict minerals will force us to incur additional expenses, may make our supply chain more complex, and may harm our relationships with customers;
- We have significant operations in locations which could be materially and adversely impacted in the event of a natural disaster, an act of terrorism, or other significant disruption; and
- Our goodwill is sensitive to changes in our stock price and other factors, and we may be required to take additional impairment charges on goodwill.
- We recently discovered an attack on our computer systems that could result in the loss or misuse of confidential information of the Company or that of our customers or others, result in litigation and potential liability, and damage our reputation.

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

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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements

Veeco Instruments Inc. and Subsidiaries

Consolidated Balance Sheets

(in thousands, except share amounts)

(unaudited)

	September 30, 2018	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	\$ 213,506	\$ 279,736
Restricted cash	828	847
Short-term investments	52,063	47,780
Accounts receivable, net	90,816	98,866
Contract assets	7,441	160
Inventories	149,832	120,266
Deferred cost of sales	2,986	15,994
Prepaid expenses and other current assets	23,400	33,437
Total current assets	540,872	597,086
Property, plant, and equipment, net	80,626	85,058
Intangible assets, net	89,398	369,843
Goodwill	307,131	307,131
Deferred income taxes	2,183	3,047
Other assets	30,356	25,310
Total assets	\$ 1,050,566	\$ 1,387,475
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 65,042	\$ 50,318
Accrued expenses and other current liabilities	40,430	58,068
Customer deposits and deferred revenue	64,443	112,032
Income taxes payable	1,819	3,846
Total current liabilities	171,734	224,264
Deferred income taxes	7,170	36,845
Long-term debt	284,369	275,630
Other liabilities	9,206	10,643
Total liabilities	472,479	547,382
Stockholders' equity:		

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Preferred stock, \$0.01 par value; 500,000 shares authorized; no shares issued and outstanding.	—	—
Common stock, \$0.01 par value; 120,000,000 shares authorized; 48,633,204 and 48,229,251 shares issued at September 30, 2018 and December 31, 2017, respectively; 47,793,001 and 48,144,416 shares outstanding at September 30, 2018 and December 31, 2017, respectively.	486	482
Additional paid-in capital	1,060,733	1,051,953
Accumulated deficit	(475,284)	(212,870)
Accumulated other comprehensive income	1,812	1,812
Treasury stock, at cost, 840,203 and 84,835 shares at September 30, 2018 and December 31, 2017, respectively.	(9,660)	(1,284)
Total stockholders' equity	578,087	840,093
Total liabilities and stockholders' equity	\$ 1,050,566	\$ 1,387,475

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See accompanying Notes to the Consolidated Financial Statements.

Veeco Instruments Inc. and Subsidiaries

Consolidated Statements of Operations

(in thousands, except per share amounts)

(unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Net sales	\$ 126,757	\$ 129,308	\$ 443,110	\$ 336,025
Cost of sales	80,372	78,779	284,651	215,150
Gross profit	46,385	50,529	158,459	120,875
Operating expenses, net:				
Research and development	23,544	24,061	72,793	57,669
Selling, general, and administrative	20,186	29,771	70,842	71,574
Amortization of intangible assets	4,183	12,500	28,102	21,722
Restructuring	2,057	5,010	7,669	9,605
Acquisition costs	249	783	2,906	16,277
Asset impairment	—	2	252,343	1,139
Other, net	39	(140)	325	(228)
Total operating expenses, net	50,258	71,987	434,980	177,758
Operating income (loss)	(3,873)	(21,458)	(276,521)	(56,883)
Interest income	823	357	2,266	1,932
Interest expense	(5,602)	(5,105)	(16,113)	(14,301)
Income (loss) before income taxes	(8,652)	(26,206)	(290,368)	(69,252)
Income tax expense (benefit)	301	(2,466)	(27,954)	(26,334)
Net income (loss)	\$ (8,953)	\$ (23,740)	\$ (262,414)	\$ (42,918)
Income (loss) per common share:				
Basic	\$ (0.19)	\$ (0.51)	\$ (5.55)	\$ (1.00)
Diluted	\$ (0.19)	\$ (0.51)	\$ (5.55)	\$ (1.00)
Weighted average number of shares:				
Basic	46,982	46,941	47,283	43,100
Diluted	46,982	46,941	47,283	43,100

See accompanying Notes to the Consolidated Financial Statements.

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Veeco Instruments Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income (Loss)

(in thousands)

(unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Net income (loss)	\$ (8,953)	\$ (23,740)	\$ (262,414)	\$ (42,918)
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on available-for-sale securities	4	70	4	10
Foreign currency translation	(4)	1	(4)	25
Total other comprehensive income (loss), net of tax	—	71	—	35
Total comprehensive income (loss)	\$ (8,953)	\$ (23,669)	\$ (262,414)	\$ (42,883)

See accompanying Notes to the Consolidated Financial Statements.

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Veeco Instruments Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Nine months ended September 30,	
	2018	2017
Cash Flows from Operating Activities		
Net income (loss)	\$ (262,414)	\$ (42,918)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	41,110	32,295
Non-cash interest expense	8,739	7,641
Deferred income taxes	(28,872)	(22,600)
Share-based compensation expense	12,720	19,976
Asset impairment	252,343	1,139
Provision for bad debts	—	99
Changes in operating assets and liabilities:		
Accounts receivable and contract assets	769	(6,360)
Inventories and deferred cost of sales	(17,748)	9,328
Prepaid expenses and other current assets	10,037	(331)
Accounts payable and accrued expenses	(4,006)	3,129
Customer deposits and deferred revenue	(47,589)	19,030
Income taxes receivable and payable, net	(3,552)	(16)
Long-term income tax liability	—	(4,877)
Other, net	(915)	(259)
Net cash provided by (used in) operating activities	(39,378)	15,276
Cash Flows from Investing Activities		
Acquisitions of businesses, net of cash acquired	(2,662)	(399,478)
Capital expenditures	(5,788)	(17,403)
Proceeds from the sale of investments	65,365	307,757
Payments for purchases of investments	(72,303)	(279,945)
Proceeds from held for sale assets	—	2,284
Net cash provided by (used in) investing activities	(15,388)	(386,785)
Cash Flows from Financing Activities		
Proceeds (net of tax withholdings) from option exercises and employee stock purchase plan	3,007	2,546
Restricted stock tax withholdings	(3,029)	(7,797)
Proceeds from long-term debt borrowings	—	335,752
Purchases of common stock	(11,457)	—

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Principal payments on long-term debt	—	(1,193)
Net cash provided by (used in) financing activities	(11,479)	329,308
Effect of exchange rate changes on cash and cash equivalents	(4)	25
Net increase (decrease) in cash, cash equivalents, and restricted cash	(66,249)	(42,176)
Cash, cash equivalents, and restricted cash - beginning of period	280,583	277,444
Cash, cash equivalents, and restricted cash - end of period	\$ 214,334	\$ 235,268
Supplemental Disclosure of Cash Flow Information		
Interest paid	\$ 9,655	\$ 4,667
Income taxes paid	4,269	1,767
Non-cash operating and financing activities		
Net transfer of inventory to property, plant and equipment	1,170	33

See accompanying Notes to the Consolidated Financial Statements.

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Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements

(unaudited)

Note 1 — Basis of Presentation

The accompanying unaudited Consolidated Financial Statements of Veeco have been prepared in accordance with U.S. GAAP as defined in Financial Accounting Standards Board (“FASB”) Accounting Standards Codification 270 for interim financial information and with the instructions to Rule 10-01 of Securities and Exchange Commission Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements as the interim information is an update of the information that was presented in Veeco’s most recent annual financial statements. For further information, refer to Veeco’s Consolidated Financial Statements and Notes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2017 (“2017 Form 10-K”). In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal, recurring nature.

Veeco reports interim quarters on a 13-week basis ending on the last Sunday of each quarter. The fourth quarter always ends on the last day of the calendar year, December 31. The 2018 interim quarters end on April 1, July 1, and September 30, and the 2017 interim quarters ended on April 2, July 2, and October 1. These interim quarters are reported as March 31, June 30, and September 30 in Veeco’s interim consolidated financial statements.

Change in Accounting Policy

The Company adopted ASC Topic 606, Revenue from Contracts with Customers (“ASC 606”), as of January 1, 2018, using the full retrospective method. All amounts and disclosures set forth in this Form 10-Q reflect these changes. The most significant financial statement impacts of adopting ASC 606 are the elimination of the constraint on revenue associated with the billing retention related to the receipt of customer final acceptance and the identification of installation services as a performance obligation. The elimination of the constraint on revenue related to customer final acceptance, which is usually about 10 percent of a system sale, is now generally recognized at the time the Company transfers control of the system to the customer, which is earlier than under the Company’s previous revenue recognition model for certain contracts that were subject to the billing constraint. The new performance obligation related to installation services is now recognized as the installation services are performed, which is later than the Company’s previous revenue recognition model.

The Company applied ASC 606 retrospectively and elected to use the disclosure exemption in the transition guidance under which the Company does not disclose prior period information regarding the amount of the transaction price allocated to remaining performance obligations. The cumulative effect of the adoption was recognized as a decrease to Accumulated deficit of \$6.9 million on January 1, 2016. The following tables summarize the impact of adoption on the Company's previously reported financial position and results:

	December 31, 2017		
	As reported (in thousands)	Adjustments	As adjusted
Balance Sheet			
Contract assets	\$ —	\$ 160	\$ 160
Deferred cost of sales	16,060	(66)	15,994
Deferred income taxes	2,953	94	3,047
Accrued expenses and other current liabilities	60,339	(2,271)	58,068
Customer deposits and deferred revenue	108,953	3,079	112,032
Additional paid-in capital	1,053,079	(1,126)	1,051,953
Accumulated deficit	(213,376)	506	(212,870)

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Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

	Three months ended September 30, 2017			Nine months ended September 30, 2017		
	As reported	Adjustments	As adjusted	As reported	Adjustments	As adjusted
	(in thousands, except per share amounts)					
Statement of						
Operations						
Net sales	\$ 131,872	\$ (2,564)	\$ 129,308	\$ 341,324	\$ (5,299)	\$ 336,025
Cost of sales	78,811	(32)	78,779	215,344	(194)	215,150
Income tax expense (benefit)	(1,790)	(676)	(2,466)	(24,969)	(1,365)	(26,334)
Net income (loss)	(21,884)	(1,856)	(23,740)	(39,177)	(3,741)	(42,918)
Diluted earnings (loss) per share	(0.47)	(0.04)	(0.51)	(0.91)	(0.09)	(1.00)

The Company's adoption of the standard had no impact to cash provided by or used in operating, investing, or financing activities on the Consolidated Statements of Cash Flows.

Revenue Recognition

Revenue is recognized upon the transfer of control of the promised product or service to the customer in an amount that reflects the consideration the Company expects to receive in exchange for such product or service. The Company's contracts with customers generally do not contain variable consideration. In the rare instances where variable consideration is included, the Company estimates the amount of variable consideration and determines what portion of that, if any, has a high probability of significant subsequent revenue reversal, and if so, that amount is excluded from the transaction price. The Company's contracts with customers frequently contain multiple deliverables, such as systems, upgrades, components, spare parts, installation, maintenance, and service plans. Judgment is required to properly identify the performance obligations within a contract and to determine how the revenue should be allocated among the performance obligations. The Company also evaluates whether multiple transactions with the same customer or related parties should be considered part of a single contract based on an assessment of whether the contracts or agreements are negotiated or executed within a short time frame of each other or if there are indicators that the contracts are negotiated in contemplation of one another.

When there are separate units of accounting, the Company allocates revenue to each performance obligation on a relative stand-alone selling price basis. The stand-alone selling prices are determined based on the prices at which the Company separately sells the systems, upgrades, components, spare parts, installation, maintenance, and service plans. For items that are not sold separately, the Company estimates stand-alone selling prices generally using an expected cost plus margin approach.

Most of the Company's revenue is recognized at a point in time when the performance obligation is satisfied. The Company considers many facts when evaluating each of its sales arrangements to determine the timing of revenue recognition, including its contractual obligations and the nature of the customer's post-delivery acceptance provisions. The Company's system sales arrangements, including certain upgrades, generally include field acceptance provisions that may include functional or mechanical test procedures. For many of these arrangements, a customer source inspection of the system is performed in the Company's facility or test data is sent to the customer documenting that the system is functioning to the agreed upon specifications prior to delivery. Historically, such source inspection or test data replicates the field acceptance provisions that are performed at the customer's site prior to final acceptance of the system. When the Company objectively demonstrates that the criteria specified in the contractual acceptance provisions are achieved prior to delivery, transfer of control of the product to the customer is considered to have occurred and revenue is recognized upon system delivery since there is no substantive contingency remaining related to the acceptance provisions at that date. For new products, new applications of existing products, or for products with substantive customer acceptance provisions where the Company cannot objectively demonstrate that the criteria specified in the contractual acceptance provisions have been achieved prior to delivery, revenue and the associated costs are deferred. The Company recognizes such revenue and costs upon obtaining objective evidence that the acceptance provisions can be achieved, assuming all other revenue recognition criteria have been met.

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Notes to the Consolidated Financial Statements - continued

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In certain cases the Company's contracts with customers contain a billing retention, typically 10% of the sales price, which is billed by the Company and payable by the customer when field acceptance provisions are completed. Revenue recognized in advance of the amount that has been billed is recorded as a contract asset on the Consolidated Balance Sheets.

The Company recognizes revenue related to maintenance and service contracts over time based upon the respective contract term. Installation revenue is recognized over time as the installation services are performed. The Company recognizes revenue from the sales of components, spare parts, and specified service engagements at a point in time, which is typically consistent with the time of delivery in accordance with the terms of the applicable sales arrangement.

The Company may receive customer deposits on system transactions. The timing of the transfer of goods or services related to the deposits is either at the discretion of the customer or expected to be within one year from the deposit receipt. As such, the Company does not adjust transaction prices for the time value of money. Incremental direct costs incurred related to the acquisition of a customer contract, such as sales commissions, are expensed as incurred since the expected amortization period is one year or less.

The Company has elected to treat shipping and handling costs as a fulfillment activity, and such costs are included in cost of services when the Company recognizes revenue for the related goods. Taxes assessed by governmental authorities that are collected by the Company from a customer are excluded from revenue.

Income Taxes

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act ("2017 Tax Act"), which makes broad and complex changes to the U.S. tax code. Certain income tax effects of the 2017 Tax Act are reflected in the Company's financial results in accordance with Staff Accounting Bulletin No. 118 ("SAB 118"), which provides SEC staff guidance regarding the application of ASC Topic 740, Income Taxes ("ASC 740"). Refer to Note 10, "Income Taxes," for further information on the financial statement impact of the 2017 Tax Act.

Because of the complexity of the new global intangible low-taxed income (“GILTI”) rule, the Company is continuing to evaluate this provision of the 2017 Tax Act and the application of ASC 740. Under U.S. GAAP, the Company is allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (“period cost method”) or (2) factoring such amounts into a company’s measurement of its deferred taxes (“deferred method”). The Company’s selection of an accounting policy with respect to the new GILTI tax rules will depend, in part, on analyzing its global income to determine whether it expects to have future U.S. inclusions in taxable income related to GILTI, and if so, what the impact will be. This assessment depends not only on the Company’s current structure and estimated future results of global operations, but also on its intent and ability to modify its structure and/or business. The Company is not yet able to reasonably estimate the effect of this provision of the 2017 Tax Act; therefore, the Company has not made any deferred tax adjustments related to potential GILTI tax in its consolidated financial statements and has not made a policy election decision regarding whether to record deferred taxes on GILTI.

Recent Accounting Pronouncements

In February 2016, the FASB issued ASU 2016-02: Leases, which generally requires operating lessee rights and obligations to be recognized as assets and liabilities on the balance sheet. In addition, in July 2018, the FASB issued ASU 2018-11: Leases, Targeted Improvements, which adds a transition option whereby companies can recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption rather than in the earliest period presented. The Company plans to adopt using this transition option. These ASUs are effective for fiscal

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Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

years beginning after December 15, 2018. The Company is evaluating the impact of adopting these ASUs on the consolidated financial statements.

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

Recently Adopted Accounting Pronouncements

The Company adopted ASU 2016-01, Financial Instruments – Overall, as of January 1, 2018. This ASU requires certain equity investments to be measured at fair value, with changes in fair value recognized in net income. The Company measures equity investments without readily observable market prices at cost, adjusted for changes in observable prices minus impairment. Changes in measurement are included in “Other, net” in the Consolidated Statements of Operations. This ASU has not had a material impact on the consolidated financial statements upon adoption, and the Company will monitor its equity investments each reporting period for changes in observable market prices, if any, which may be material in future periods.

The Company adopted ASU 2016-16, Income Taxes: Intra-Entity Transfers of Assets Other Than Inventory, as of January 1, 2018. This ASU requires the Company to recognize the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. This ASU has not had a material impact on the consolidated financial statements.

The Company adopted ASU 2016-18, Statement of Cash Flows: Restricted Cash, as of January 1, 2018. This ASU requires the Company to include restricted cash with cash and cash equivalents when reconciling the beginning and end of period total amounts shown on the Statement of Cash Flows. This ASU has not had a material impact on the consolidated financial statements.

Note 2 — Income (Loss) Per Common Share

The Company considers unvested share-based awards that have non-forfeitable rights to dividends prior to vesting to be participating shares, which are treated as a separate class of security from the Company's common shares for calculating per share data. Therefore, the Company applies the two-class method when calculating income (loss) per share. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared and participation rights in undistributed earnings. However, since the holders of the participating shares are not obligated to fund losses, participating shares are excluded from the calculation of loss per share.

The dilutive effect of the Convertible Senior Notes on income (loss) per share is calculated using the treasury stock method since the Company has both the current intent and ability to settle the principal amount of the Convertible Senior Notes in cash. See Note 5, "Liabilities," for additional information on the Convertible Senior Notes.

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Notes to the Consolidated Financial Statements - continued

(unaudited)

Basic income (loss) per share is calculated by dividing net income (loss) by the weighted average number of shares outstanding during the period under the two-class method. Diluted income per share is calculated by dividing net income by the weighted average number of shares used to calculate basic income (loss) per share plus the weighted average number of common share equivalents outstanding during the period. The dilutive effect of outstanding options to purchase common stock and non-participating share-based awards is considered in diluted income per share by application of the treasury stock method. The dilutive effect of performance share units is included in diluted income per common share in the periods the performance targets have been achieved. The computations of basic and diluted income (loss) per share for the three and nine months ended September 30, 2018 and 2017 are as follows:

	Three months ended September 30, 2018		Nine months ended September 30, 2018	
	2017		2017	
	(in thousands, except per share amounts)			
Net income (loss)	\$ (8,953)	\$ (23,740)	\$ (262,414)	\$ (42,918)
Net income (loss) per common share:				
Basic	\$ (0.19)	\$ (0.51)	\$ (5.55)	\$ (1.00)
Diluted	\$ (0.19)	\$ (0.51)	\$ (5.55)	\$ (1.00)
Basic weighted average shares outstanding	46,982	46,941	47,283	43,100
Effect of potentially dilutive share-based awards	—	—	—	—
Diluted weighted average shares outstanding	46,982	46,941	47,283	43,100
Unvested participating shares excluded from basic weighted average shares outstanding since the securityholders are not obligated to fund losses	2	166	2	166
Common share equivalents excluded from the diluted weighted average shares outstanding since Veeco incurred a net loss and their effect would be antidilutive	16	220	17	275
Potentially dilutive non-participating shares excluded from the diluted calculation as their effect would be antidilutive	2,617	1,956	2,469	1,628
Maximum potential shares to be issued for settlement of Convertible Senior Notes excluded from the diluted calculation as their effect would be antidilutive	8,618	8,618	8,618	8,618

Note 3 — Business Combinations

Ultratech

On May 26, 2017, the Company completed its acquisition of Ultratech, Inc. (“Ultratech”). Ultratech develops, manufactures, sells, and supports lithography, laser annealing, and inspection equipment for manufacturers of semiconductor devices, including front-end semiconductor manufacturing and advanced packaging. Ultratech also develops, manufactures, sells, and supports ALD equipment for scientific and industrial applications. Ultratech’s customers are primarily located throughout the United States, Europe, China, Japan, Taiwan, Singapore, and Korea. The results of Ultratech’s operations have been included in the consolidated financial statements since the date of acquisition.

Ultratech shareholders received (i) \$21.75 per share in cash and (ii) 0.2675 of a share of Veeco common stock for each Ultratech common share outstanding on the acquisition date. Approximately \$2.7 million of the cash merger consideration is included in “Accrued expenses and other current liabilities” on the Consolidated Balance Sheets as of December 31, 2017, related to shareholder appraisal proceedings that were subsequently settled and paid during the third quarter of 2018.

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Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

The following table presents unaudited pro forma financial information as if the acquisition of Ultratech had occurred on January 1, 2016:

	Three months ended September 30, 2017	Nine months ended September 30, 2017
	(in thousands, except per share amounts)	
Net sales	\$ 129,308	\$ 406,767
Loss before income taxes	(24,847)	(72,091)
Diluted earnings per share	\$ (0.49)	\$ (1.23)

The pro-forma results were calculated by combining the unaudited results of the Company with the stand-alone unaudited results of Ultratech for the pre-acquisition period, and adjusting for the following:

- (i) Additional amortization expense related to identified intangible assets valued as part of the purchase price allocation that would have been incurred starting on January 1, 2016.
- (ii) Additional depreciation expense for the property, plant, and equipment fair value adjustments that would have been incurred starting on January 1, 2016.
- (iii) All acquisition related costs incurred by the Company as well as by Ultratech pre-acquisition have been removed from the year ended December 31, 2017 and included in the year ended December 31, 2016, as such expenses would have been incurred in the first quarter following the acquisition.
- (iv) All amortization of inventory step-up has been removed from the year ended December 31, 2017 and recorded in the year ended December 31, 2016, as such costs would have been incurred as the corresponding inventory was sold.
- (v) Additional interest expense related to the Convertible Senior Notes (see Note 5, "Liabilities") as if the Notes had been issued on January 1, 2016.

(vi) Income tax expense (benefit) was adjusted for the impact of the above adjustments for each period.

(vii) All shares issued in connection with the acquisition were considered outstanding as of January 1, 2016 for purposes of calculating diluted earnings per share.

During the second quarter of 2018, the Company lowered its projected results for the Ultratech asset group and determined that the revised projections were significantly lower than projected results at the time of the acquisition and that these revised projections required the Company to assess the Ultratech asset group for impairment. See Note 4, "Assets" - Intangible Assets, for additional information.

Note 4 — Assets

Investments

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

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Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

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

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

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

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

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

The following table presents the portion of Veeco's assets that were measured at fair value on a recurring basis at September 30, 2018 and December 31, 2017:

	Level 1 (in thousands)	Level 2	Level 3	Total
September 30, 2018				
Short-term investments				
U.S. treasuries	\$ 36,527	\$ —	\$ —	\$ 36,527

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Corporate debt	—	8,561	—	8,561
Commercial paper	—	6,975	—	6,975
Total	\$ 36,527	\$ 15,536	\$ —	\$ 52,063
December 31, 2017				
Cash equivalents				
U.S. treasuries	\$ 12,490	\$ —	\$ —	\$ 12,490
Total	\$ 12,490	\$ —	\$ —	\$ 12,490
Short-term investments				
U.S. treasuries	\$ 33,895	\$ —	\$ —	\$ 33,895
Corporate debt	—	10,886	—	10,886
Commercial paper	—	2,999	—	2,999
Total	\$ 33,895	\$ 13,885	\$ —	\$ 47,780

There were no transfers between fair value measurement levels during the three and nine months ended September 30, 2018.

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Veeco Instruments Inc. and Subsidiaries

Notes to the Consolidated Financial Statements - continued

(unaudited)

At September 30, 2018 and December 31, 2017, the amortized cost and fair value of available-for-sale securities consist of:

	Amortized Cost (in thousands)	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
September 30, 2018				
U.S. treasuries	\$ 36,538	\$ 1	\$ (12)	\$ 36,527
Corporate debt	8,573	—	(12)	8,561
Commercial paper	6,975	—	—	6,975
Total	\$ 52,086	\$ 1	\$ (24)	\$ 52,063
December 31, 2017				
U.S. treasuries				