

VEECO INSTRUMENTS INC

FORM 10-Q (Quarterly Report)

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SIC Code	3559 - Special Industry Machinery, Not Elsewhere Classified
Industry	Semiconductors
Sector	Technology
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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 March 31, 2013

OR

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

For the transition period from _____ to _____

Commission file number 0-16244

VEECO INSTRUMENTS INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

(State or Other Jurisdiction of
Incorporation or Organization)

11-2989601

(I.R.S. Employer
Identification Number)

Terminal Drive

Plainview, New York

(Address of Principal Executive Offices)

11803

(Zip Code)

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

Website: **www.veeco.com**

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a Smaller reporting company)

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

39,246,279 shares of common stock were outstanding as of the close of business on October 24, 2013.

Safe Harbor Statement

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

- Our operating results have been, and may continue to be, adversely affected by unfavorable market conditions;
- Timing of market adoption of light emitting diode (“LED”) technology for general lighting is uncertain;
- Our failure to successfully manage our outsourcing activities or failure of our outsourcing partners to perform as anticipated could adversely affect our results of operations and our ability to adapt to fluctuating order volumes;
- The further reduction or elimination of foreign government subsidies and economic incentives may adversely affect the future order rate for our metal organic chemical vapor deposition (“MOCVD”) equipment;
- Our operating results have been, and may continue to be, adversely affected by tightening credit markets;
- Our backlog is subject to customer cancellation or modification and such cancellation could result in decreased sales and increased provisions for excess and obsolete inventory and/or liabilities to our suppliers for products no longer needed;
- Our failure to estimate customer demand accurately could result in excess or obsolete inventory and/or liabilities to our suppliers for products no longer needed, while manufacturing interruptions or delays could affect our ability to meet customer demand;
- The cyclical nature of the industries we serve directly affects our business;
- We rely on a limited number of suppliers, some of whom are our sole source for particular components;
- Our sales to LED and data storage manufacturers are highly dependent on these manufacturers’ sales for consumer electronics applications, which can experience significant volatility due to seasonal and other factors, which could materially adversely impact our future results of operations;
- We are exposed to the risks of operating a global business, including the need to obtain export licenses for certain of our shipments and political risks in the countries we operate;
- We may be exposed to liabilities under the Foreign Corrupt Practices Act and any determination that we violated these or similar laws could have a material adverse effect on our business;
- The timing of our orders, shipments, and revenue recognition may cause our quarterly operating results to fluctuate significantly;
- We operate in industries characterized by rapid technological change;
- We face significant competition;
- We depend on a limited number of customers, located primarily in a limited number of regions, that operate in highly concentrated industries;
- Our sales cycle is long and unpredictable;
- Our material weaknesses in our internal control which have impeded, and may continue to impede, our ability to file timely and accurate periodic reports may cause us to incur significant additional costs and may continue to affect our stock price;
- The price of our common shares may be volatile and could decline significantly;
- Our inability to attract, retain, and motivate key employees could have a material adverse effect on our business;
- We are subject to foreign currency exchange risks;
- The enforcement and protection of our intellectual property rights may be expensive and could divert our limited resources;
- We may be subject to claims of intellectual property infringement by others;
- If we are subject to cyber-attacks we could incur substantial costs and, if such attacks are successful, could result in significant liabilities, reputational harm and disruption of our operations;
- Our acquisition strategy subjects us to risks associated with evaluating and pursuing these opportunities and integrating these businesses;
- We may be required to take additional impairment charges for goodwill and indefinite-lived intangible assets or definite-lived intangible and long-lived assets;
- Changes in accounting pronouncements or taxation rules or practices may adversely affect our financial results;
- We are subject to internal control evaluations and attestation requirements of Section 404 of the Sarbanes-Oxley Act and any delays or difficulty in satisfying these requirements or negative reports concerning our internal controls could adversely affect our future results of operations and our stock price;
- We are subject to risks of non-compliance with environmental, health and safety regulations;

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- We have significant operations in 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;
- New regulations related to conflict minerals will force us to incur additional expenses, may make our supply chain more complex, and may result in damage to our relationships with customers; and
- The matters set forth in this Report generally, including the risk factors set forth in “*Part II. Item 1A. Risk Factors.*”

Consequently, such forward-looking statements should be regarded solely as the current plans, estimates and beliefs of Veeco Instruments Inc. (together with its consolidated subsidiaries, “Veeco”, the “Company”, “we”, “us”, and “our”, unless the context indicates otherwise). The Company does not undertake any obligation to update any forward-looking statements to reflect future events or circumstances after the date of such statements.

Explanatory Note

Although this Report relates to the three months ended March 31, 2013, certain information is presented as of the time this Report is being filed, rather than as of March 31, 2013. Our business and financial condition as of the date this Report is filed is different from what our business and financial condition was as of March 31, 2013. We intend to file our quarterly report on Form 10-Q for the three and six months ended June 30, 2013 as soon as it is practical.

During 2012, the Company commenced an internal investigation in response to information it received concerning certain issues, including contract documentation issues, related to a limited number of customer transactions in South Korea. During the review of information in connection with the internal investigation, questions were raised that prompted the Company to conduct a comprehensive and extensive review of its revenue recognition accounting for certain multiple element arrangements. The Company retained experienced counsel, assisted by an experienced outside accounting consulting firm, to oversee the accounting review undertaken by the Company. The Company completed that review in October 2013.

The delay in filing our periodic reports began with an announcement, on November 15, 2012, regarding our accounting review of our application of accounting principles related to the Company’s sales of multiple element arrangements of MOCVD systems in certain transactions originating in 2009 and 2010. We conducted examinations of our MOCVD transactions to determine whether the revenue and related expenses were recognized in the appropriate accounting period. Subsequently, we expanded our accounting review to other relevant transactions of similar multiple element arrangements arising since 2009. In the course of our accounting review, we have examined more than 100 multiple element arrangements.

The primary focus of the Company’s accounting review concerned whether the Company correctly interpreted and applied generally accepted accounting principles in the United States (“U.S. GAAP”) relating to revenue recognition for multiple element arrangements as set forth in Securities and Exchange Commission Staff Accounting Bulletin No. 104: Revenue Recognition, and ASC 605-25 - Revenue Recognition: Multiple Element Arrangements (formerly known as EITF 00-21 and EITF 08-01), to certain sales of Veeco products.

We often enter into large orders with our customers consisting of several elements. For accounting purposes, these are called multiple element arrangements, and can include systems, upgrades, spare parts, service, as well as certain other items. Our accounting review examined the selected sales transactions to determine whether the Company appropriately: (1) identified all of the elements in its arrangements with customers; (2) determined the proper units of accounting as part of the arrangements; and (3) allocated the arrangements’ consideration to each of the units of accounting under the applicable accounting standards. As a result of our accounting review we identified errors in the consolidated financial statements related to prior periods. The errors were primarily attributable to the misapplication of U.S. GAAP for recognizing revenue and related costs under multiple element arrangements and accounting for warranties. We assessed the materiality of these errors, both quantitatively and qualitatively, and concluded that these errors were not material, individually or in the aggregate, to our consolidated financial statements in 2012 or any other prior periods.

While performing the foregoing accounting review, our Chief Executive Officer and the Chief Financial Officer supervised and participated in conducting an evaluation of the effectiveness of our internal control over financial reporting based on the criteria in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). Based upon that evaluation, management identified material weaknesses in the Company’s internal control over financial reporting and therefore management concluded that we did not maintain effective internal control over financial reporting through the date of this Report based on the criteria established by COSO.

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Notwithstanding the material weaknesses discussed in “ *Part I. Item 4. Controls and Procedures* ” in this report and based upon our accounting review performed during the delayed filing periods, our management has concluded that our condensed consolidated financial statements included in this report on Form 10-Q have been prepared in accordance with U.S. GAAP for interim financial information.

Available Information

We file annual, quarterly and current reports, information statements and other information with the SEC. The public may obtain information by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is *www.sec.gov* . For quarterly and annual reports, only those reports that were required to be filed through March 31, 2013 are available as of the date of this Report.

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 website as soon as reasonably practicable after we electronically file such material with the SEC. For quarterly and annual reports, only those reports that were required to be filed through March 31, 2013 are available as of the date of this Report.

VEECO INSTRUMENTS INC.

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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)

	For the three months ended March 31,	
	2013	2012
Net sales	\$ 61,781	\$ 139,909
Cost of sales	39,229	74,641
Gross profit	<u>22,552</u>	<u>65,268</u>
Operating expenses (income):		
Selling, general and administrative	19,648	19,773
Research and development	20,737	23,306
Amortization	856	1,215
Restructuring	531	63
Other, net	404	(35)
Total operating expenses	<u>42,176</u>	<u>44,322</u>
Operating (loss) income	(19,624)	20,946
Interest income, net	192	203
(Loss) income from continuing operations before income taxes	(19,432)	21,149
Income tax (benefit) provision	(9,361)	4,687
(Loss) income from continuing operations	<u>(10,071)</u>	<u>16,462</u>
Discontinued operations:		
Loss from discontinued operations before income taxes	—	(81)
Income tax benefit	—	(31)
Loss from discontinued operations	<u>—</u>	<u>(50)</u>
Net (loss) income	<u>\$ (10,071)</u>	<u>\$ 16,412</u>
(Loss) income per common share:		
Basic:		
Continuing operations	\$ (0.26)	\$ 0.43
Discontinued operations	—	—
(Loss) income	<u>\$ (0.26)</u>	<u>\$ 0.43</u>
Diluted:		
Continuing operations	\$ (0.26)	\$ 0.42
Discontinued operations	—	—
(Loss) income	<u>\$ (0.26)</u>	<u>\$ 0.42</u>
Weighted average shares outstanding:		
Basic	38,716	38,261
Diluted	38,716	38,863

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

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

	For the three months ended March 31,	
	2013	2012
Net (loss) income	\$ (10,071)	\$ 16,412
Other comprehensive (loss) income, net of tax		
Unrealized gain (loss) on available-for-sale securities (net of taxes of \$16 and \$(43) for 2013 and 2012, respectively)	43	(118)
Less: Reclassification adjustments for gains included in net (loss) income	(59)	(10)
Net unrealized loss on available-for-sale securities	(16)	(128)
Foreign currency translation (net of taxes of \$(13) and \$7 for 2013 and 2012, respectively)	(763)	(489)
Comprehensive (loss) income	\$ (10,850)	\$ 15,795

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

Veeco Instruments Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(In thousands, except share data)

	March 31, 2013 (Unaudited)	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	\$ 223,121	\$ 384,557
Short-term investments	362,747	192,234
Restricted cash	2,061	2,017
Accounts receivable, net	42,912	63,169
Inventories	67,689	59,807
Prepaid expenses and other current assets	30,582	32,155
Deferred income taxes	13,171	10,545
Total current assets	<u>742,283</u>	<u>744,484</u>
Property, plant and equipment at cost, net	96,714	98,302
Goodwill	55,828	55,828
Deferred income taxes	4,505	935
Intangible assets, net	20,118	20,974
Other assets	16,435	16,781
Total assets	<u>\$ 935,883</u>	<u>\$ 937,304</u>
Liabilities and equity		
Current liabilities:		
Accounts payable	\$ 32,503	\$ 26,087
Accrued expenses and other current liabilities	76,132	74,260
Deferred revenue	9,216	9,380
Income taxes payable	697	2,292
Current portion of long-term debt	274	268
Total current liabilities	<u>118,822</u>	<u>112,287</u>
Deferred income taxes	7,137	7,137
Long-term debt	2,067	2,138
Other liabilities	4,737	4,530
Total liabilities	<u>132,763</u>	<u>126,092</u>
Equity:		
Preferred stock, 500,000 shares authorized; no shares issued and outstanding	—	—
Common stock; \$.01 par value; authorized 120,000,000 shares; 39,304,294 and 39,328,503 shares issued and outstanding in 2013 and 2012, respectively	393	393
Additional paid-in capital	711,481	708,723
Retained earnings	86,052	96,123
Accumulated other comprehensive income	5,194	5,973
Total equity	<u>803,120</u>	<u>811,212</u>
Total liabilities and equity	<u>\$ 935,883</u>	<u>\$ 937,304</u>

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

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

	For the three months ended March 31,	
	2013	2012
Cash Flows from Operating Activities		
Net (loss) income	\$ (10,071)	\$ 16,412
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	3,927	3,715
Deferred income taxes	(6,215)	674
Non-cash equity-based compensation	2,579	3,130
Provision for bad debt	16	—
Excess tax benefits from stock option exercises	(31)	(91)
Other, net	—	14
Changes in operating assets and liabilities:		
Accounts receivable	20,004	5,079
Inventories	(8,395)	10,599
Accounts payable	6,458	(2,179)
Accrued expenses, deferred revenue and other current liabilities	1,764	(7,169)
Income taxes payable	(1,555)	(1,556)
Other, net	2,005	13,007
Net cash provided by operating activities	<u>10,486</u>	<u>41,635</u>
Cash Flows from Investing Activities		
Capital expenditures	(1,619)	(8,455)
Proceeds from sales of short-term investments	101,236	43,569
Payments for purchases of short-term investments	(271,713)	(18,503)
Net cash (used in) provided by investing activities	<u>(172,096)</u>	<u>16,611</u>
Cash Flows from Financing Activities		
Proceeds from stock option exercises	280	537
Restricted stock tax withholdings	(132)	(95)
Excess tax benefits from stock option exercises	31	91
Repayments of long-term debt	(65)	(60)
Net cash provided by financing activities	<u>114</u>	<u>473</u>
Effect of exchange rate changes on cash and cash equivalents	60	(1,309)
Net (decrease) increase in cash and cash equivalents	(161,436)	57,410
Cash and cash equivalents as of beginning of period	384,557	217,922
Cash and cash equivalents as of end of period	<u>\$ 223,121</u>	<u>\$ 275,332</u>
Non-cash investing and financing activities		
Transfers from property, plant and equipment to inventory	\$ 135	\$ —

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

Veeco Instruments Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1—Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Veeco Instruments Inc. (together with its consolidated subsidiaries, “Veeco”, the “Company”, “we”, “us”, and “our”, unless the context indicates otherwise) have been prepared in accordance with accounting principles generally accepted in the United States (“U.S.”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles (“U.S. GAAP”) 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 ended March 31, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. For further information, refer to the consolidated financial statements and footnotes thereto included in our annual report on Form 10-K for the year ended December 31, 2012.

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 of each period. The interim quarter ends are determined at the beginning of each year based on the 13-week quarters. The 2013 interim quarter ends are March 31, June 30 and September 29. The 2012 interim quarter ends were April 1, July 1 and September 30. 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. We have reclassified certain amounts previously reported in our financial statements to conform to the current presentation, including amounts related to discontinued operations.

Accounting Review

During 2012, the Company commenced an internal investigation in response to information it received concerning certain issues, including contract documentation issues, related to a limited number of customer transactions in South Korea. During the review of information in connection with the internal investigation, questions were raised that prompted the Company to conduct a comprehensive and extensive review of its revenue recognition accounting for certain multiple element arrangements. The Company retained experienced counsel, assisted by an experienced outside accounting consulting firm, to oversee the accounting review undertaken by the Company. The Company completed that review in October 2013.

The delay in filing our periodic reports began with an announcement, on November 15, 2012, regarding our accounting review of our application of accounting principles related to the Company’s sales of multiple element arrangements of Metal Organic Chemical Vapor Deposition (“MOCVD”) systems in certain transactions originating in 2009 and 2010. We conducted examinations of our MOCVD transactions to determine whether the revenue and related expenses were recognized in the appropriate accounting period. Subsequently, we expanded our accounting review to other relevant transactions of similar multiple element arrangements arising since 2009. In the course of our accounting review, we have examined more than 100 multiple element arrangements.

The primary focus of the Company’s accounting review concerned whether the Company correctly interpreted and applied generally accepted accounting principles relating to revenue recognition for multiple element arrangements as set forth in Securities and Exchange Commission Staff Accounting Bulletin No. 104: Revenue Recognition, and ASC 605-25 - Revenue Recognition: Multiple Element Arrangements (formerly known as EITF 00-21 and EITF 08-01), to certain sales of Veeco products.

We often enter into large orders with our customers consisting of several elements. For accounting purposes, these are called multiple element arrangements, and can include systems, upgrades, spare parts, services, as well as certain other items. Our accounting review examined the selected sales transactions to determine whether the Company appropriately: (1) identified all of the elements in its arrangements with customers; (2) determined the proper units of accounting as part of the arrangements; and (3) allocated the arrangements’ consideration to each of the units of accounting under the applicable accounting standards. As a result of our accounting review we identified errors in the consolidated financial statements related to prior periods. The errors were primarily attributable to the misapplication of U.S. GAAP for recognizing revenue and related costs under multiple element arrangements and accounting for warranties. We assessed the materiality of these errors, both quantitatively and qualitatively, and concluded that these errors were not material, individually or in the aggregate, to our consolidated financial statements in 2012 or any other prior periods.

Notwithstanding the material weaknesses discussed in “*Part I. Item 4. Controls and Procedures*” and based upon the accounting review discussed above, our management has concluded that our consolidated financial statements are fairly stated in all material respects in accordance with U.S. GAAP for interim financial statements.

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Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates made by management include: the best estimate of selling price for our products and services; allowance for doubtful accounts; inventory valuation; recoverability and useful lives of property, plant and equipment and identifiable intangible assets; investment valuations; fair value of derivatives; recoverability of goodwill and long lived assets; recoverability of deferred tax assets; liabilities for product warranty; accruals for contingencies; equity-based payments, including forfeitures and performance based vesting; and liabilities for tax uncertainties. Actual results could differ from those estimates.

(Loss) Income Per Common Share

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

	Three months ended	
	March 31,	
	2013	2012
Basic weighted average shares outstanding	38,716	38,261
Dilutive effect of stock options and restricted stock	—	602
Diluted weighted average shares outstanding	38,716	38,863

Basic (loss) income per common share is computed using the weighted average number of common shares outstanding during the period. Diluted (loss) income per common share is computed using the weighted average number of common shares and common equivalent shares outstanding during the period. Potentially dilutive securities attributable to outstanding stock options and restricted stock were approximately 1.4 million and 1.2 million common equivalent shares during the three months ended March 31, 2013 and 2012. Approximately 0.5 million common equivalent shares were excluded from the calculation of diluted net loss per share during the three months ended March 31, 2013, because their effect on loss per share was anti-dilutive due to the net loss sustained during the period.

Revenue Recognition

We recognize revenue when all of the following criteria have been met: persuasive evidence of an arrangement exists with a customer; delivery of the specified products has occurred or services have been rendered; prices are contractually fixed or determinable; and collectability is reasonably assured. Revenue is recorded including shipping and handling costs and excluding applicable taxes related to sales. A significant portion of our revenue is derived from contractual arrangements with customers that have multiple elements, such as systems, upgrades, components, spare parts, maintenance and service plans. For sales arrangements that contain multiple elements, we split the arrangement into separate units of accounting if the individually delivered elements have value to the customer on a standalone basis. We also evaluate whether multiple transactions with the same customer or related party should be considered part of a multiple element arrangement, whereby we assess, among other factors, 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 each other. When we have separate units of accounting, we allocate revenue to each element based on the following selling price hierarchy: vendor-specific objective evidence (“VSOE”) if available; third party evidence (“TPE”) if VSOE is not available; or our best estimate of selling price (“BESP”) if neither VSOE nor TPE is available. For the majority of the elements in our arrangements we utilize BESP. The accounting guidance for selling price hierarchy did not include BESP for arrangements entered into prior to January 1, 2011, and as such we recognized revenue for those arrangements as described below.

We consider many facts when evaluating each of our sales arrangements to determine the timing of revenue recognition, including the contractual obligations, the customer's creditworthiness and the nature of the customer's post-delivery acceptance provisions. Our system sales arrangements, including certain upgrades, generally include field acceptance provisions that may include functional or mechanical test procedures. For the majority of our arrangements, a customer source inspection of the system is performed in our 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 will be performed at the customer's site prior to final acceptance of the system. As such, we objectively demonstrate that the criteria specified in the contractual acceptance provisions are achieved prior to delivery and, therefore, we recognize revenue upon delivery since there is no substantive contingency remaining related to the acceptance provisions as of that date, subject to the retention amount constraint described below. For new products, new applications of existing products or for products with substantive customer acceptance provisions where we cannot objectively demonstrate that the criteria specified in the contractual acceptance provisions have been achieved prior to delivery, revenue and the associated costs are deferred and fully recognized upon the receipt of final customer acceptance, assuming all other revenue recognition criteria have been met.

Our system sales arrangements, including certain upgrades, generally do not contain provisions for right of return or forfeiture, refund, or other purchase price concessions. In the rare instances where such provisions are included, we defer all revenue until such rights expire. In many cases our products are sold with a billing retention, typically 10% of the sales price (the "retention amount"), which is typically payable by the customer when field acceptance provisions are completed. The amount of revenue recognized upon delivery of a system or upgrade is limited to the lower of i) the amount that is not contingent upon acceptance provisions or ii) the value allocated to the delivered elements, if such sale is part of a multiple-element arrangement.

For transactions entered into prior to January 1, 2011, under the accounting rules for multiple-element arrangements in place at that time, we deferred the greater of the retention amount or the relative fair value of the undelivered elements based on VSOE. When we could not establish VSOE or TPE for all undelivered elements of an arrangement, revenue on the entire arrangement was deferred until the earlier of the point when we did have VSOE for all undelivered elements or the delivery of all elements of the arrangement.

Our sales arrangements, including certain upgrades, generally include installation. The installation process is not deemed essential to the functionality of the equipment since it is not complex; that is, it does not require significant changes to the features or capabilities of the equipment or involve building elaborate interfaces or connections subsequent to factory acceptance. We have a demonstrated history of consistently completing installations in a timely manner and can reliably estimate the costs of such activities. Most customers engage us to perform the installation services, although there are other third-party providers with sufficient knowledge who could complete these services. Based on these factors, we deem the installation of our systems to be inconsequential and perfunctory relative to the system as a whole, and as a result, do not consider such services to be a separate element of the arrangement. As such, we accrue the cost of the installation at the time of revenue recognition for the system.

In Japan, where our contractual terms with customers generally specify title and risk and rewards of ownership transfer upon customer acceptance, revenue is recognized and the customer is billed upon the 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 are recognized at the time of delivery in accordance with the terms of the applicable sales arrangement.

Note 2—Discontinued Operations

We recorded a \$0.1 million loss from discontinued operations with no sales recorded for the three months ended March 31, 2012.

Note 3—Balance Sheet Information

Cash and Cash Equivalents

Cash and cash equivalents include cash and certain highly liquid investments. Highly liquid investments with maturities of three months or less when purchased may be classified as cash equivalents. Such items may include liquid money market accounts, treasury bills, government agency securities and corporate debt. The investments that are classified as cash equivalents are carried at cost, which approximates fair value.

Short-Term Investments

Available-for-sale securities consist of the following (*in thousands*):

	March 31, 2013			
	Amortized Cost	Gains in Accumulated Other Comprehensive Income	Losses in Accumulated Other Comprehensive Income	Estimated Fair Value
Treasury bills	\$ 271,168	\$ 33	\$ —	\$ 271,201
Government agency securities	8,055	—	—	8,055
Corporate bonds	63,488	38	(27)	63,499
Commercial paper	19,992	—	—	19,992
Total available-for-sale securities	<u>\$ 362,703</u>	<u>\$ 71</u>	<u>\$ (27)</u>	<u>\$ 362,747</u>

	December 31, 2012			
	Amortized Cost	Gains in Accumulated Other Comprehensive Income	Losses in Accumulated Other Comprehensive Income	Estimated Fair Value
Treasury bills	\$ 184,102	\$ 76	\$ —	\$ 184,178
Government agency securities	8,056	—	—	8,056
Total available-for-sale securities	<u>\$ 192,158</u>	<u>\$ 76</u>	<u>\$ —</u>	<u>\$ 192,234</u>

During the three months ended March 31, 2013 and 2012, available-for-sale securities were liquidated for total proceeds of \$101.2 million and \$43.6 million, respectively. The gross realized gains and losses on these sales were \$0.1 million for the three months ended March 31, 2013 and minimal gross realized gains for the three months ended March 31, 2012. The cost of securities sold is based on specific identification.

The table below shows the fair value of short-term investments that have been in an unrealized loss position for less than 12 months as of March 31, 2013 (*in thousands*):

	Estimated Fair value	Unrealized Losses
Corporate bonds	\$ 28,491	\$ (27)
Total	<u>\$ 28,491</u>	<u>\$ (27)</u>

We did not hold any short-term investments that have been in an unrealized loss position for 12 months or longer for the period noted in the preceding table.

The Company regularly reviews its investment portfolio to identify and evaluate investments that have indications of possible impairment. Factors considered in determining whether an unrealized loss was considered to be temporary or other-than-temporary and therefore impaired include: the length of time and extent to which fair value has been lower than the cost basis; the financial condition and near-term prospects of the investee; and whether it is more likely than not that the Company will be required to sell the security prior to recovery. The Company believes the gross unrealized losses on the Company's short-term investments as of March 31, 2013 were temporary in nature and therefore did not recognize any impairment. As of December 31, 2012 we did not hold any short-term investments that were in a loss position.

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Contractual maturities of available-for-sale securities are as follows (*in thousands*):

	March 31, 2013
	Estimated Fair Value
Due in one year or less	\$ 288,752
Due in 1—2 years	32,811
Due in 2—3 years	41,184
Total available-for-sale securities	<u>\$ 362,747</u>

Actual maturities may differ from contractual maturities because some borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

Restricted Cash

As of March 31, 2013 and December 31, 2012, restricted cash consisted of \$2.1 million and \$2.0 million, respectively, which serves as collateral for bank guarantees that provide financial assurance that the Company will fulfill certain customer obligations. This cash is held in custody by the issuing bank and is restricted as to withdrawal or use while the related bank guarantees are outstanding.

Accounts Receivable, Net

Accounts receivable are shown net of the allowance for doubtful accounts of \$0.5 million as of March 31, 2013 and December 31, 2012.

Inventories

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

	March 31,	December 31,
	2013	2012
Materials	\$ 44,219	\$ 36,523
Work in process	17,248	13,363
Finished goods	6,222	9,921
	<u>\$ 67,689</u>	<u>\$ 59,807</u>

Cost Method Investment

As of March 31, 2013 and December 31, 2012 we have recorded a total investment of \$14.5 million in a rapidly developing organic light emitting diode (“OLED”) equipment company (the “Investment”). Our ownership in the Investment is approximately 15.3% of the preferred shares and a 12.0% interest in the total company. Since we do not exert significant influence on the Investment, this investment is treated under the cost method in accordance with applicable accounting guidance. The fair value of this investment is not estimated because there are no identified events or changes in circumstances that may indicate an other-than-temporary decline in the fair value of the investment and we are exempt from estimating interim fair values because the investment does not meet the definition of a publicly traded company. This investment is recorded in other assets in our Condensed Consolidated Balance Sheets. Subsequently, during the second and third quarters of 2013, we invested an additional \$0.8 million in the Investment each quarter.

Customer Deposits

As of March 31, 2013 and December 31, 2012, we had customer deposits of \$38.4 million and \$32.7 million, respectively, which are recorded as a component of accrued expenses and other current liabilities.

Accrued Warranty

We estimate the costs that may be incurred under the warranties we provide and record a liability in the amount of such costs at the time the related revenue is recognized. Factors that affect our warranty liability include product failure rates, material usage and labor costs incurred in correcting product failures during the warranty period. This accrual is recorded in accrued expense and other current liabilities in our Condensed Consolidated Balance Sheets. We periodically assess the adequacy of our recognized warranty liability and adjust the amount as necessary. Changes in our warranty liability during the period are as follows (*in thousands*):

	Three months ended March 31,	
	2013	2012
Balance as of the beginning of period	\$ 4,942	\$ 8,731
Warranties issued during the period	478	696
Settlements made during the period	(1,341)	(1,840)
Changes in estimate during the period	—	327
Balance as of the end of period	<u>\$ 4,079</u>	<u>\$ 7,914</u>

In the current year's presentation we no longer include installation in the accrued warranty balance; therefore, in order to conform the balance to current year presentation, we have reclassified \$1.047 million from the beginning balance of 2012 accrued warranty to accrued installation which, along with accrued warranty, is also a component of Accrued expenses and other current liabilities.

Mortgage Payable

We have a mortgage payable with approximately \$2.3 million outstanding as of March 31, 2013 and \$2.4 million outstanding as of December 31, 2012. The mortgage accrues interest at an annual rate of 7.91%, and the final payment is due on January 1, 2020. The fair value of the mortgage as of March 31, 2013 was approximately \$2.5 million and \$2.6 million as of December 31, 2012.

Accumulated Other Comprehensive Income

The components of accumulated other comprehensive income are (*in thousands*):

As of March 31, 2013	Gross	Taxes	Net
Translation adjustments	\$ 6,290	\$ (352)	\$ 5,938
Minimum pension liability	(1,285)	510	(775)
Unrealized gain on available-for-sale securities	44	(13)	31
Accumulated other comprehensive income	<u>\$ 5,049</u>	<u>\$ 145</u>	<u>\$ 5,194</u>
As of December 31, 2012	Gross	Taxes	Net
Translation adjustments	\$ 7,040	\$ (339)	\$ 6,701
Minimum pension liability	(1,285)	510	(775)
Unrealized gain on available-for-sale securities	76	(29)	47
Accumulated other comprehensive income	<u>\$ 5,831</u>	<u>\$ 142</u>	<u>\$ 5,973</u>

Note 4—Segment Information

We manage the business, review operating results and assess performance, as well as allocate resources, based upon four reporting units that are aggregated into two segments: the VIBE and Mechanical reporting units which are reported in our Data Storage segment; and the MOCVD and molecular beam epitaxy (“MBE”) reporting units which are reported in our Light Emitting Diode (“LED”) and Solar 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. Our LED & Solar segment consists of MOCVD systems, MBE systems and thermal deposition sources. These systems are primarily sold to customers in the LED, wireless devices and solar industries, as well as to scientific research customers. This segment has manufacturing, product development and marketing sites in Somerset, New Jersey; Poughkeepsie, New York; and St. Paul, Minnesota. Our Data Storage 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 manufacturing, product development and marketing sites in Plainview, New York; Camarillo, California; and Ft. Collins, Colorado. We evaluate the performance of our reportable segments based on income (loss) from continuing operations before interest, income taxes, amortization and certain items (in the aggregate “segment profit (loss)”), which is the primary indicator used to plan and forecast future periods. The presentation of this financial measure facilitates meaningful comparison with prior periods, as management believes segment profit (loss) reports baseline performance and thus provides useful information. Certain items include restructuring charges and equity-based compensation expense. The accounting policies of the reportable segments are the same as those described in the summary of critical accounting policies.

The following tables present certain data pertaining to our reportable segments and a reconciliation of segment (loss) profit to (loss) income from continuing operations before income taxes for the three months ended March 31, 2013 and 2012, respectively, and goodwill and total assets as of March 31, 2013 and December 31, 2012 (*in thousands*):

	<u>LED & Solar</u>	<u>Data Storage</u>	<u>Unallocated Corporate</u>	<u>Total</u>
Three months ended March 31, 2013				
Net sales	\$ 42,307	\$ 19,474	\$ —	\$ 61,781
Segment (loss) profit	\$ (11,222)	\$ 375	\$ (4,811)	\$ (15,658)
Interest income, net	—	—	192	192
Amortization	(532)	(324)	—	(856)
Equity-based compensation	(710)	(130)	(1,739)	(2,579)
Restructuring	(423)	(50)	(58)	(531)
Loss from continuing operations before income taxes	<u>\$ (12,887)</u>	<u>\$ (129)</u>	<u>\$ (6,416)</u>	<u>\$ (19,432)</u>
Three months ended March 31, 2012				
Net sales	\$ 95,574	\$ 44,335	\$ —	\$ 139,909
Segment profit (loss)	\$ 17,486	\$ 8,953	\$ (1,085)	\$ 25,354
Interest income, net	—	—	203	203
Amortization	(863)	(352)	—	(1,215)
Equity-based compensation	(1,006)	(411)	(1,713)	(3,130)
Restructuring	(58)	(5)	—	(63)
Income (loss) from continuing operations before income taxes	<u>\$ 15,559</u>	<u>\$ 8,185</u>	<u>\$ (2,595)</u>	<u>\$ 21,149</u>
As of March 31, 2013				
Goodwill	\$ 55,828	\$ —	\$ —	\$ 55,828
Total assets	\$ 256,616	\$ 38,465	\$ 640,802	\$ 935,883
As of December 31, 2012				
Goodwill	\$ 55,828	\$ —	\$ —	\$ 55,828
Total assets	\$ 276,352	\$ 38,664	\$ 622,288	\$ 937,304

Note 5—Fair Value Measurements

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

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

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

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

The major categories of assets and liabilities measured on a recurring basis, at fair value, as of March 31, 2013 and December 31, 2012, are as follows (*in thousands*):

	March 31, 2013			
	Level 1	Level 2	Level 3	Total
Treasury bills	\$ 271,201	\$ —	\$ —	\$ 271,201
Government agency securities	—	48,054	—	48,054
Corporate bonds	—	63,499	—	63,499
Commercial paper	—	19,992	—	19,992
Total	<u>\$ 271,201</u>	<u>\$ 131,545</u>	<u>\$ —</u>	<u>\$ 402,746</u>

	December 31, 2012			
	Level 1	Level 2	Level 3	Total
Treasury bills	\$ 278,698	\$ —	\$ —	\$ 278,698
Government agency securities	—	123,054	—	123,054
Total	<u>\$ 278,698</u>	<u>\$ 123,054</u>	<u>\$ —</u>	<u>\$ 401,752</u>

Consistent with Level 1 measurement principles, treasury bills are priced using active market prices of identical securities. Consistent with Level 2 measurement principles, government agency securities, commercial paper and corporate bonds are priced with matrix pricing.

Government agency securities and treasury bills that are classified as cash equivalents are carried at cost, which approximates market value. Accordingly, no gains or losses (realized/unrealized) have been incurred for cash equivalents. All investments classified as available-for-sale are recorded at fair value within short-term investments in the Condensed Consolidated Balance Sheets.

In determining the fair value of its investments and levels, the Company uses pricing information from pricing services that value securities based on quoted market prices in active markets and matrix pricing. Matrix pricing is a mathematical valuation technique that does not rely exclusively on quoted prices of specific investments, but on the investment's relationship to other benchmarked quoted securities. The Company has a review process in place for investment valuations to facilitate identification and resolution of potentially erroneous prices. The Company reviews the information provided by the third-party service provider to record the fair value of its portfolio.

Note 6—Derivative Financial Instruments

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

March 31, 2013

<u>Not Designated as Hedges under ASC 815</u>	<u>Component of</u>	<u>Maturity</u>	<u>Notional Amount</u>	<u>Estimated Fair Value</u>
Foreign currency exchange forwards	Accrued expenses and other current liabilities	April 2013	\$ 3,715	\$ (21)
Total Derivative Instruments			<u>\$ 3,715</u>	<u>\$ (21)</u>

December 31, 2012

<u>Not Designated as Hedges under ASC 815</u>	<u>Component of</u>	<u>Maturity</u>	<u>Notional Amount</u>	<u>Estimated Fair Value</u>
Foreign currency exchange forwards	Prepaid expenses and other current assets	January 2013	\$ 9,590	\$ 244
Total Derivative Instruments			<u>\$ 9,590</u>	<u>\$ 244</u>

	<u>Location of Realized Net (Loss) Gain and Changes in the Fair Value of Derivatives</u>	<u>For the three months ended March 31,</u>	
		<u>2013</u>	<u>2012</u>
Foreign currency exchange forwards	Other, net	<u>\$ 228</u>	<u>\$ 80</u>
Weighted average notional amount of derivatives outstanding		<u>\$ 2,400</u>	<u>\$ 2,405</u>

Note 7—Commitments, Contingencies and Other Matters

Restructuring

During the three months ended March 31, 2013, we took measures to improve profitability. As a result of these actions, we recorded a restructuring charge of \$0.5 million. During the three months ended March 31, 2012, we recorded \$0.4 million in personnel severance and related costs and \$0.1 million in other associated costs resulting from a headcount reduction of approximately 20 employees.

A summary of restructuring expense is as follows (*in thousands*):

	For the three months ended	
	March 31,	
	2013	2012
Personnel severance and related costs	\$ 435	\$ 63
Other associated costs	96	—
Restructuring expense	\$ 531	\$ 63

Restructuring Liability

The following is a reconciliation of the restructuring liability through March 31, 2013 (*in thousands*):

	LED & Solar	Data Storage	Unallocated Corporate	Total
Short-term liability				
Balance as of January 1, 2013	\$ 448	\$ 1,308	\$ 119	\$ 1,875
Restructuring	422	51	58	531
Cash payments	(602)	(672)	(152)	(1,426)
Balance as of March 31, 2013	\$ 268	\$ 687	\$ 25	\$ 980

The balance of the short-term liability will be paid over the next 12 months.

The following is a reconciliation of the restructuring liability through December 31, 2012 (*in thousands*):

	LED & Solar	Data Storage	Unallocated Corporate	Total
Short-term liability				
Balance as of January 1, 2012	\$ 534	\$ 128	\$ 294	\$ 956
Restructuring	874	1,684	135	2,693
Cash payments	(960)	(504)	(310)	(1,774)
Balance as of December 31, 2012	\$ 448	\$ 1,308	\$ 119	\$ 1,875

Note 8—Subsequent Events

Notice of Potential De-Listing : During our internal control evaluation and accounting review, we were unable to timely file our periodic statements with the SEC and, as of the date of this Report, have yet to become current with all of our required filings. We have been notified by the NASDAQ Stock Market that our common stock listing will be suspended if we have not filed all of our outstanding periodic reports with the SEC on or before November 4, 2013. If our stock is delisted, then it will no longer be traded on the NASDAQ Global Select Market, however, it would continue to trade in the over-the-counter market, which may have an adverse effect on the trading price of our stock.

Colbus: Veeco and certain other parties were named as defendants in a lawsuit filed on April 25, 2013 in the Superior Court of California, County of Sonoma. The plaintiff in the lawsuit, Patrick Colbus, seeks unspecified damages and asserts claims that he suffered burns and other injuries while he was cleaning a molecular beam epitaxy system alleged to have been manufactured by Veeco. The lawsuit alleges, among other things, that the molecular beam epitaxy system was defective and that Veeco failed to adequately warn of the potential risks of the system. Veeco believes this lawsuit is without merit and intends to defend vigorously against the claims and Veeco maintains insurance which may apply to this matter. Because the Company believes that this potential loss is not probable or estimable, it has not recorded any reserves related to this legal matter.

Acquisition of Synos Technology, Inc. (“Synos”) : On October 1, 2013, we acquired Synos, which designs and manufactures Fast Array Scanning™ Atomic Layer Deposition systems (“ALD”) that are enabling the production of flexible organic light-emitting diode (“OLED”) displays for mobile devices. The initial purchase price is \$70 million. The agreement also includes an earn-out feature that would require an additional payment of up to \$115 million if future performance milestones are achieved prior to December 31, 2014. With the earn-out feature, the total maximum potential purchase price is \$185 million. Synos is headquartered in Fremont, California and has approximately 50 employees. Preliminary purchase accounting allocations for Synos are not yet available.

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

Executive Summary

Veeco Instruments Inc. (together with its consolidated subsidiaries, "Veeco", the "Company", "we", "us", and "our", unless the context indicates otherwise) creates Process Equipment that enables technologies for a cleaner and more productive world. We design, manufacture and market equipment to make light emitting diodes ("LED"s) and hard-disk drives, as well as for concentrator photovoltaics, power semiconductors, wireless components, and micro-electromechanical systems ("MEMS").

Veeco develops highly differentiated, "best-in-class" Process Equipment for critical performance steps. Our products feature leading technology, low cost-of-ownership and high throughput. Core competencies in advanced thin film technologies, over 200 patents, and decades of specialized process know-how helps us to stay at the forefront of these demanding industries.

Veeco's LED & Solar segment designs and manufactures metal organic chemical vapor deposition ("MOCVD") and molecular beam epitaxy ("MBE") systems and components sold to manufacturers of LEDs, wireless components, power semiconductors, and concentrator photovoltaics, as well as to R&D applications.

Veeco's Data Storage segment designs and manufactures systems used to create thin film magnetic heads ("TFMH"s) that read and write data on hard disk drives. These include ion beam etch, ion beam deposition, diamond-like carbon, physical vapor deposition, chemical vapor deposition, and slicing, dicing and lapping systems. While our systems are primarily sold to hard drive customers, they also have applications in optical coatings, MEMS and magnetic sensors, and extreme ultraviolet ("EUV") lithography.

As of September 30, 2013, Veeco's approximately 780 employees support our customers through product and process development, training, manufacturing, and sales and service sites in the U.S., South Korea, Taiwan, China, Singapore, Japan, Europe and other locations.

Veeco Instruments was organized as a Delaware corporation in 1989.

Highlights of the First Quarter of 2013

- Revenue was \$61.8 million, a 55.8% decrease from the first quarter of 2012.
- Bookings were \$70.4 million, a 37.9% decrease from the first quarter of 2012.
- Net loss from continuing operations was \$(10.1) million, or \$(0.26) per share, compared to net income from continuing operations of \$16.5 million, or \$0.42 per share, in the first quarter of 2012.
- Gross margins were 36.5%, compared to 46.7% in the first quarter of 2012.

Outlook

Through the first nine months of 2013, we have not seen any clear signs that customer overcapacity in our MOCVD business and weak end-market demand in our Data Storage segment will improve in the near term. Our customers continue to guard spending tightly and limit capacity expansions. The LED industry is still in an equipment digestion period and near term visibility remains limited. With few MOCVD deals available, we have also experienced increased pricing pressure. In our Data Storage segment, our hard drive customers are experiencing weak end-market demand which has resulted in excess manufacturing capacity, therefore they are only making select technology purchases. While our overall bookings have continued to decline in 2013, bookings in our Data Storage segment have been relatively flat for the first nine months of 2013 compared to the first nine months of 2012.

While the Company has been actively working to reduce costs during this extended business downturn, pricing pressure and persistent low volumes in MOCVD represent significant headwinds and have caused the Company to move to a loss in 2013.

Our outlook discussion above constitutes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Our expectations regarding future results are subject to risks and uncertainties. Our actual results may differ materially from those anticipated.

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

Results of Operations:

Three Months Ended March 31, 2013 and 2012

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 2013 interim quarter ends are March 31, June 30 and September 29. The 2012 interim quarter ends were April 1, July 1 and September 30. For ease of reference, we report these interim quarter ends as March 31, June 30 and September 30 in our interim condensed consolidated financial statements.

The following table shows our Condensed Consolidated Statements of Operations, percentages of sales, and comparisons between the three months ended March 31, 2013 and 2012 (*dollars in thousands*):

	Three months ended March 31,				Dollar and Percentage Change Period to Period	
	2013		2012			
Net sales	\$ 61,781	100.0%	\$ 139,909	100.0%	\$ (78,128)	(55.8)%
Cost of sales	39,229	63.5%	74,641	53.3%	(35,412)	(47.4)%
Gross profit	22,552	36.5%	65,268	46.7%	(42,716)	(65.4)%
Operating expenses (income):						
Selling, general and administrative	19,648	31.8%	19,773	14.1%	(125)	(0.6)%
Research and development	20,737	33.6%	23,306	16.7%	(2,569)	(11.0)%
Amortization	856	1.4%	1,215	0.9%	(359)	(29.5)%
Restructuring	531	0.9%	63	0.0%	468	742.9%
Other, net	404	0.7%	(35)	(0.0)%	439	*
Total operating expenses	42,176	68.4%	44,322	31.7%	(2,146)	(4.8)%
Operating (loss) income	(19,624)	(31.9)%	20,946	15.0%	(40,570)	*
Interest income, net	192	0.3%	203	0.1%	(11)	(5.4)%
(Loss) income from continuing operations before income taxes	(19,432)	(31.6)%	21,149	15.1%	(40,581)	*
Income tax (benefit) provision	(9,361)	(15.2)%	4,687	3.4%	(14,048)	*
(Loss) income from continuing operations	(10,071)	(16.4)%	16,462	11.8%	(26,533)	*
Discontinued operations:						
Loss from discontinued operations before income taxes	—	0.0%	(81)	(0.1)%	81	*
Income tax benefit	—	0.0%	(31)	(0.0)%	31	*
Loss from discontinued operations	—	0.0%	(50)	(0.0)%	50	*
Net (loss) income	\$ (10,071)	(16.4)%	\$ 16,412	11.7%	\$ (26,483)	*

* Not Meaningful

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Net Sales and Bookings

The following is an analysis of net sales by segment and by region (*dollars in thousands*):

	Sales				Dollar and Percentage Change Period to Period	
	Three months ended March 31,					
	2013	Percent of Total	2012	Percent of Total		
Segment Analysis						
LED & Solar	\$ 42,307	68.5%	\$ 95,574	68.3%	\$ (53,267)	(55.7)%
Data Storage	19,474	31.5%	44,335	31.7%	(24,861)	(56.1)%
Total	\$ 61,781	100.0%	\$ 139,909	100.0%	\$ (78,128)	(55.8)%
Regional Analysis						
Americas	\$ 12,433	20.1%	\$ 20,216	14.4%	\$ (7,783)	(38.5)%
Europe, Middle East and Africa	4,550	7.4%	5,231	3.7%	(681)	(13.0)%
Asia Pacific	44,798	72.5%	114,462	81.8%	(69,664)	(60.9)%
Total	\$ 61,781	100.0%	\$ 139,909	100.0%	\$ (78,128)	(55.8)%

Our LED & Solar segment sales decreased 55.7% in 2013, principally due to a decline in MOCVD resulting from industry overcapacity. MBE sales also declined meaningfully from the prior year due to the lack of production buys from wireless customers. Our Data Storage segment sales decreased 56.1% in 2013 due to customer fabrication facility overcapacity and weak hard drive demand. Our Data Storage sales in 2012 were favorably impacted by the replacement of equipment at one of our customer's site that was damaged by the floods in Thailand. By region, net sales decreased in Asia Pacific, primarily due to a significant decrease in MOCVD sales in China resulting from industry overcapacity. Net sales in the Americas (less than 1% is outside U.S.) and Europe, Middle East and Africa "EMEA" also decreased, due to reduced end-market demand resulting from the weak global economy. We believe that there will continue to be period-to-period variations in the geographic distribution of sales.

Bookings decreased 37.9% to \$70.4 million from \$113.4 million in the comparable prior period, primarily attributable to a 49.5% decrease in LED & Solar bookings, principally driven by a decline in MOCVD bookings due to industry overcapacity. Since hitting a peak in second quarter of 2011, Veeco's bookings have slowed dramatically over the past two years. While Data Storage bookings decreased 3.7% from the comparable prior period, customers remain hesitant to make further investments as end-user hard drive demand has slowed and orders remain at low levels. We continue to experience weak overall market conditions due to overcapacity in all of our businesses.

Our book-to-bill ratio for the three months ended March 31, 2013, which is calculated by dividing bookings recorded in a given time period by revenue recognized in the same time period, was 1.14 to 1. Our backlog as of March 31, 2013 was \$156.7 million, compared to \$150.2 million as of December 31, 2012. During the three months ended March 31, 2013, we recorded backlog adjustments of approximately \$2.2 million, consisting of a \$1.0 million adjustment related to orders that no longer met our booking criteria as well as an adjustment related to foreign currency translation of \$1.2 million. Our backlog consists of orders for which we received a firm purchase order, a customer-confirmed shipment date within twelve months and a deposit, where required. As of March 31, 2013, we had customer deposits of \$38.4 million.

Gross Profit

Gross profit in dollars and gross margin for the periods indicated were as follows (*dollars in thousands*):

	Three months ended March 31,		Dollar and Percentage Change Period to Period	
	2013	2012		
Gross profit - LED & Solar	\$ 13,985	\$ 45,185	\$ (31,200)	(69)%
<i>Gross margin</i>	33.1%	47.3%		
Gross profit - Data Storage	\$ 8,567	\$ 20,083	\$ (11,516)	(57.3)%
<i>Gross margin</i>	44.0%	45.3%		
Gross profit - Total Veeco	\$ 22,552	\$ 65,268	\$ (42,716)	(65.4)%
<i>Gross margin</i>	36.5%	46.7%		

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Our LED & Solar segment gross margins decreased to 33.1% from 47.3% in the comparable prior year period, primarily due to a significant decrease in sales volume, lower average selling prices and fewer final acceptances partially offset by lower warranty, plant and service spending associated with reduced volumes and cost reductions in response to lower business levels. We anticipate a continuing weak business environment resulting in persistent selling price pressure in our MOCVD business. Data Storage gross margins decreased to 44.0% from 45.3% in the comparable prior period, primarily due to a decrease in volume partially offset by lower plant spending.

Selling, General and Administrative

Selling, general and administrative expenses for the periods indicated were as follows (*dollars in thousands*):

	Three months ended March 31,		Dollar and Percentage Change Period to Period	
	2013	2012		
Selling, general and administrative	\$ 19,648	\$ 19,773	\$ (125)	(0.6)%
<i>Percentage of sales</i>	31.8%	14.1%		

Selling, general and administrative expenses decreased primarily due to a reduction in bonus, profit sharing and commission expense from the reduced level of business in each of our segments and cost control measures put into place in response to weak market conditions resulting in lower personnel-related costs and other discretionary expenses. These savings were offset by increased professional fees associated with our accounting review.

Research and Development

Research and development expenses for the periods indicated were as follows (*dollars in thousands*):

	Three months ended March 31,		Dollar and Percentage Change Period to Period	
	2013	2012		
Research and development	\$ 20,737	\$ 23,306	\$ (2,569)	(11.0)%
<i>Percentage of sales</i>	33.6%	16.7%		

Research and development expense decreased as the Company strategically focuses on product development in areas of high-growth for future end-market opportunities in our LED & Solar segment.

Restructuring

Restructuring expenses for the periods indicated were as follows (*dollars in thousands*):

	Three months ended March 31,		Dollar and Percentage Change Period to Period	
	2013	2012		
Restructuring	\$ 531	\$ 63	\$ 468	742.9%
<i>Percentage of sales</i>	0.9%	0.0%		

Restructuring expense was \$0.5 million for the three months ended March 31, 2013 as we continue to take measures to improve profitability in a challenging business environment. The charge consists of personnel severance and related costs.

Income Taxes

Income tax (benefit) provision for the periods indicated were as follows (*dollars in thousands*):

	Three months ended March 31,		Dollar and Percentage Change Period to Period
	2013	2012	
Income tax (benefit) provision	\$ (9,361)	\$ 4,687	\$ (14,048) *
Effective tax rate	(48.2)%	22.2%	

* Not Meaningful

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

For the three months ended March 31, 2013, the Company had an effective tax benefit rate of 48.2% and recorded an income tax benefit of \$9.4 million from continuing operations. The tax benefit rate was higher than the statutory tax rate primarily due to tax rate differences in the foreign jurisdictions in which the Company operates, an income tax benefit related to the generation of current year research and development tax credits, and a discrete benefit related to legislation enacted in the first quarter of 2013 which extended the Federal Research and Development Credit for both the 2012 and 2013 tax years.

For the three months ended March 31, 2012, the Company had an effective tax rate of 22.2% and recorded a provision for income taxes of \$4.7 million from continuing operations. The effective tax rate was lower than the statutory tax rate primarily due to tax rate differences in the foreign jurisdictions in which the Company operates and an income tax benefit related to the manufacturer's deduction under IRC Section 199.

Liquidity and Capital Resources

A summary of the cash flow activity for the three months ended March 31, 2013 and 2012, respectively, is as follows (*in thousands*):

	For the three months ended March 31,	
	2013	2012
Net (loss) income	\$ (10,071)	\$ 16,412
Net cash provided by operating activities	\$ 10,486	\$ 41,635
Net cash (used in) provided by investing activities	(172,096)	16,611
Net cash provided by financing activities	114	473
Effect of exchange rate changes on cash and cash equivalents	60	(1,309)
Net (decrease) increase in cash and cash equivalents	(161,436)	57,410
Cash and cash equivalents at beginning of period	384,557	217,922
Cash and cash equivalents at end of period	\$ 223,121	\$ 275,332

Cash provided by operations during the three months ended March 31, 2013 decreased compared to the prior year period, primarily driven by the \$26.5 million reduction in net income from the prior year period. Cash provided by operations benefited from a \$0.3 million adjustment for non-cash items and a \$20.3 million net change in operating assets and liabilities, primarily driven by a \$20.0 million reduction in accounts receivable.

Cash used in investing activities during the three months ended March 31, 2013 declined by \$188.7 million from the \$16.6 million net cash provided by investing activities from the prior year period. The decrease was primarily attributable to the Company maintaining a higher short-term investment balance resulting in net purchases of short-term investment of \$170.5 million during the three months ended March 31, 2013, compared to net sales of short-term investments of \$25.1 million from the prior year period.

We generated \$0.1 million in cash from our financing activities during the three months ended March 31, 2013 compared to \$0.5 million in the prior year period primarily due to a \$0.3 million reduction in stock option exercise activity.

As of March 31, 2013, restricted cash consists of \$2.1 million which serves as collateral for bank guarantees that provide financial assurance that the Company will fulfill certain customer obligations. This cash is held in custody by the issuing bank, and is restricted as to withdrawal or use while the related bank guarantees are outstanding.

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A summary of cash and cash equivalents, restricted cash and short term investments is as follows (*in thousands*):

	September 30, 2013	March 31, 2013	December 31, 2012
Cash and cash equivalents	\$ 247,666	\$ 223,121	\$ 384,557
Restricted cash	2,850	2,061	2,017
Short-term investments	322,488	362,747	192,234
Cash and cash equivalents, restricted cash and short-term investments	<u>\$ 573,004</u>	<u>\$ 587,929</u>	<u>\$ 578,808</u>

On October 1, 2013 we utilized \$70 million of the foregoing cash balance to close on the Synos Technology, Inc. (“Synos”) acquisition. We believe that our September 30, 2013 existing cash balances and our projected cash generated from operations will be sufficient to meet our projected working capital and other cash flow requirements for the next twelve months, as well as our contractual obligations.

Contractual Obligations

There have been no significant changes to our “Contractual Obligations” table, except for purchase commitments and restructuring, in Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of our 2012 annual report on Form 10-K. The purchase commitments outstanding as of March 31, 2013 were \$89.9 million. As of September 30, 2013 our purchase commitments have been reduced to \$58.6 million. Pursuant to our agreement to acquire Synos, we may be obligated to pay up to an additional \$115 million if certain conditions are met. Please see *Note 8-Subsequent Events* in our condensed consolidated financial statements in the Report.

Application of Critical Accounting Policies

General: Our discussion and analysis of our financial condition and results of operations are based upon our Condensed 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, short-term investments, the valuation of inventories, the impairment of goodwill and indefinite-lived intangible assets, the impairment of long-lived assets, fair value measurements, warranty costs, income taxes and equity-based compensation to be critical policies due to the estimation processes involved in each. We have reclassified certain amounts previously reported in our financial statements to conform to the current presentation, including amounts related to discontinued operations.

Revenue Recognition: We recognize revenue when all of the following criteria have been met: persuasive evidence of an arrangement exists with a customer; delivery of the specified products has occurred or services have been rendered; prices are contractually fixed or determinable; and collectability is reasonably assured. Revenue is recorded including shipping and handling costs and excluding applicable taxes related to sales. A significant portion of our revenue is derived from contractual arrangements with customers that have multiple elements, such as systems, upgrades, components, spare parts, maintenance and service plans. For sales arrangements that contain multiple elements, we split the arrangement into separate units of accounting if the individually delivered elements have value to the customer on a standalone basis. We also evaluate whether multiple transactions with the same customer or related party should be considered part of a multiple element arrangement, whereby we assess, among other factors, 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 each other. When we have separate units of accounting, we allocate revenue to each element based on the following selling price hierarchy: vendor-specific objective evidence (“VSOE”) if available; third party evidence (“TPE”) if VSOE is not available; or our best estimate of selling price (“BESP”) if neither VSOE nor TPE is available. For the majority of the elements in our arrangements we utilize BESP. The accounting guidance for selling price hierarchy did not include BESP for arrangements entered into prior to January 1, 2011, and as such we recognized revenue for those arrangements as described below.

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We consider many facts when evaluating each of our sales arrangements to determine the timing of revenue recognition, including the contractual obligations, the customer's creditworthiness and the nature of the customer's post-delivery acceptance provisions. Our system sales arrangements, including certain upgrades, generally include field acceptance provisions that may include functional or mechanical test procedures. For the majority of our arrangements, a customer source inspection of the system is performed in our 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 will be performed at the customer's site prior to final acceptance of the system. As such, we objectively demonstrate that the criteria specified in the contractual acceptance provisions are achieved prior to delivery and, therefore, we recognize revenue upon delivery since there is no substantive contingency remaining related to the acceptance provisions at that date, subject to the retention amount constraint described below. For new products, new applications of existing products or for products with substantive customer acceptance provisions where we cannot objectively demonstrate that the criteria specified in the contractual acceptance provisions have been achieved prior to delivery, revenue and the associated costs are deferred and fully recognized upon the receipt of final customer acceptance, assuming all other revenue recognition criteria have been met.

Our system sales arrangements, including certain upgrades, generally do not contain provisions for right of return or forfeiture, refund, or other purchase price concessions. In the rare instances where such provisions are included, we defer all revenue until such rights expire. In many cases our products are sold with a billing retention, typically 10% of the sales price (the "retention amount"), which is typically payable by the customer when field acceptance provisions are completed. The amount of revenue recognized upon delivery of a system or upgrade is limited to the lower of i) the amount that is not contingent upon acceptance provisions or ii) the value allocated to the delivered elements, if such sale is part of a multiple-element arrangement.

For transactions entered into prior to January 1, 2011, under the accounting rules for multiple-element arrangements in place at that time, we deferred the greater of the retention amount or the relative fair value of the undelivered elements based on VSOE. When we could not establish VSOE or TPE for all undelivered elements of an arrangement, revenue on the entire arrangement was deferred until the earlier of the point when we did have VSOE for all undelivered elements or the delivery of all elements of the arrangement.

Our sales arrangements, including certain upgrades, generally include installation. The installation process is not deemed essential to the functionality of the equipment since it is not complex; that is, it does not require significant changes to the features or capabilities of the equipment or involve building elaborate interfaces or connections subsequent to factory acceptance. We have a demonstrated history of consistently completing installations in a timely manner and can reliably estimate the costs of such activities. Most customers engage us to perform the installation services, although there are other third-party providers with sufficient knowledge who could complete these services. Based on these factors, we deem the installation of our systems to be inconsequential and perfunctory relative to the system as a whole, and as a result, do not consider such services to be a separate element of the arrangement. As such, we accrue the cost of the installation at the time of revenue recognition for the system.

In Japan, where our contractual terms with customers generally specify title and risk and rewards of ownership transfer upon customer acceptance, revenue is recognized and the customer is billed upon the 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 are recognized at the time of delivery in accordance with the terms of the applicable sales arrangement.

Short-Term Investments: We determine the appropriate balance sheet classification of our investments at the time of purchase and evaluate the classification at each balance sheet date. As part of our cash management program, we maintain a portfolio of marketable securities which are classified as available-for-sale. These securities include corporate bonds, commercial paper, treasury bills and government agency securities with maturities of greater than three months. Securities classified as available-for-sale are carried at fair market value, with the unrealized gains and losses, net of tax, included in the determination of comprehensive (loss) income and reported in equity. Net realized gains and losses are included in net (loss) income.

Inventory Valuation: Inventories are stated at the lower of cost (principally first-in, first-out method) or market. On a quarterly basis, management assesses the valuation and recoverability of all inventories, classified as materials (which include raw materials, spare parts and service inventory), work-in-process and finished goods.

Materials inventory is used primarily to support the installed tool base and spare parts sales and is reviewed for excess quantities or obsolescence by comparing on-hand balances to historical usage, and adjusted for current economic conditions and other qualitative factors. Historically, the variability of such estimates has been impacted by customer demand and tool utilization rates.

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The work-in-process and finished goods inventory is principally used to support system sales and is reviewed for excess quantities or obsolescence by considering whether on hand inventory would be utilized to fulfill the related backlog. As the Company typically receives deposits for its orders, the variability of this estimate is reduced as customers have a vested interest in the orders they place with the Company. Management also considers qualitative factors such as future product demand based on market outlook, which is based principally upon production requirements resulting from customer purchase orders received with a customer-confirmed shipment date within the next twelve months. Historically, the variability of these estimates of future product demand has been impacted by backlog cancellations or modifications resulting from unanticipated changes in technology or customer demand.

Following identification of potential excess or obsolete inventory, management evaluates the need to write down inventory balances 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 potential excess inventory. Unanticipated changes in demand for our products may require a write down of inventory that could materially affect our operating results.

Goodwill and Indefinite-Lived Intangible Asset Impairment: The Company does not amortize goodwill or intangible assets with indefinite useful lives, but instead tests the balances in these asset accounts for impairment at least annually at the reporting unit level. Our policy is to perform this annual impairment test in the fourth quarter, using a measurement date of October 1st 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 the aforementioned guidance we are required to determine if it is appropriate to use the operating segment, as defined under guidance for segment reporting, 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 four reporting units are aggregated into two segments: the VIBE and Mechanical reporting units which are reported in our Data Storage segment; and the MOCVD and MBE reporting units which are reported in our LED & Solar segment. In identifying the reporting units management considered the economic characteristics of operating segments including the products and services provided, production processes, types or classes of customer and product distribution.

We perform this impairment test by first comparing the fair value of our reporting units to their respective carrying amount. When determining the estimated fair value of a reporting unit, we utilize a discounted future cash flow approach since reported quoted market prices are not available for our reporting units. Developing the estimate of the discounted future cash flow requires significant judgment and projections of future financial performance. The key assumptions used in developing the discounted future cash flows are the projection of future revenues and expenses, working capital requirements, residual growth rates and the weighted average cost of capital. In developing our financial projections, we consider historical data, current internal estimates and market growth trends. Changes to any of these assumptions could materially change the fair value of the reporting unit. We reconcile the aggregate fair value of our reporting units to our 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 Assets: Definite-lived intangible assets consist of purchased technology, customer-related intangible assets, patents, trademarks, covenants not-to-compete, software licenses and deferred financing costs. Purchased technology consists of the core proprietary manufacturing technologies associated with the products and offerings obtained through acquisition and are initially recorded at fair value. Customer-related intangible assets, patents, trademarks, covenants not-to-compete and software licenses that are obtained in an acquisition are initially recorded at fair value. Other software licenses and deferred financing costs are initially recorded at cost. Intangible assets with definitive useful lives are amortized using the straight-line method over their estimated useful lives for periods ranging from 2 years to 17 years.

Property, plant and equipment are recorded at cost. Depreciation is provided over the estimated useful lives of the related assets using the straight-line method for financial statement purposes. Amortization of leasehold improvements is computed using the straight-line method over the shorter of the remaining lease term or the estimated useful lives of the improvements.

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 flow expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

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

Warranty Costs: Our warranties are typically valid for one year from the date of final acceptance. We estimate the costs that may be incurred under the warranty we provide and record a liability in the amount of such costs at the time the related revenue is recognized. Estimated warranty costs are determined by analyzing specific product and historical configuration statistics and regional warranty support costs. Our warranty obligation is affected by product failure rates, material usage, and labor costs incurred in correcting product 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: 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 financial reporting purposes. These differences result in deferred tax assets and liabilities, which are included within our Condensed Consolidated Balance Sheets. The carrying value of our deferred tax assets is adjusted by a partial valuation allowance to recognize the extent to which the future tax benefits will be recognized on a more likely than not basis. Our net deferred tax assets consist primarily of tax credit carry forwards and timing differences between the book and tax treatment of inventory, acquired intangible assets and other asset valuations. Realization of these net deferred tax assets is dependent upon our ability to generate future taxable income.

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

Relevant accounting guidance addresses the determination of how tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under such guidance, we must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such uncertain tax positions are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate resolution.

Equity-Based Compensation: The Company grants equity-based awards, such as stock options and restricted stock or restricted stock units, to certain key employees to create a clear and meaningful alignment between compensation and shareholder return and to enable the employees to develop and maintain a stock ownership position. While the majority of our equity awards feature time-based vesting, performance-based equity awards, which are awarded from time to time to certain key Company executives, vest as a function of performance, and may also be subject to the recipient's continued employment which also acts as a significant retention incentive.

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

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

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

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

We settle the exercise of stock options with newly issued shares.

With respect to grants of performance based awards, we assess the probability that such performance criteria will be met in order to determine the compensation expense. Consequently, the compensation expense is recognized straight-line over the vesting period. If that assessment of the probability of the performance condition being met changes, the Company would recognize the impact of the change in estimate in the period of the change. As with the use of any estimate, and owing to the significant judgment used to derive those estimates, actual results may vary.

The Company has elected to treat awards with only service conditions and with graded vesting as one award. Consequently, the total compensation expense is recognized straight-line over the entire vesting period, so long as the compensation cost recognized at any date at least equals the portion of the grant date fair value of the award that is vested at that date.

Recent Accounting Pronouncements

In July 2013, the FASB issued ASU No. 2013-11, "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or Tax Credit Carryforward Exists." ASU 2013-11 requires entities to present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward when settlement in this manner is available under the tax law. This ASU is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The Company is evaluating the potential impact of this adoption on its consolidated financial statements.

In April 2013, the FASB issued ASU No. 2013-07, "Presentation of Financial Statements (Topic 205): Liquidation Basis of Accounting." The objective of ASU 2013-07 is to clarify when an entity should apply the liquidation basis of accounting. The update provides principles for the recognition and measurement of assets and liabilities and requirements for financial statements prepared using the liquidation basis of accounting. This ASU is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The Company does not anticipate that the adoption of this standard will have a material impact on its consolidated financial statements, absent any indications that liquidation is imminent.

In March 2013, the FASB issued ASU No. 2013-05, "Foreign Currency Matters (Topic 830): Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity." This ASU addresses the accounting for the cumulative translation adjustment when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. This ASU is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The Company is evaluating the potential impact of this adoption on its consolidated financial statements.

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In February 2013, the FASB, issued ASU No. 2013-04, “Liabilities (Topic 405): Obligations Resulting from Joint and Several Liability Arrangements for which the Total Amount of the Obligation Is Fixed at the Reporting Date.” This ASU addresses the recognition, measurement, and disclosure of certain obligations resulting from joint and several arrangements including debt arrangements, other contractual obligations, and settled litigation and judicial rulings. The ASU is effective for public entities for fiscal years, and interim periods within those years, beginning after December 15, 2013. The Company is evaluating the potential impact of this adoption on its consolidated financial statements.

In February 2013, the FASB issued ASU No. 2013-02, “Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.” The ASU requires entities to provide information about significant amounts reclassified out of accumulated other comprehensive income by component and their corresponding effect on net income. The ASU is effective for public entities for fiscal years beginning after December 15, 2012. The Company adopted this ASU in 2013.

In January 2013, the FASB issued ASU No. 2013-01, “Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities”. The ASU clarifies that ordinary trade receivables and certain other receivables are not in the scope of ASU No. 2011-11, “Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities.” Specifically, Update 2011-11 applies only to derivatives, repurchase agreements and reverse purchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria contained in FASB Accounting Standards Codification or subject to a master netting arrangement or similar agreement. The amendments in this ASU are effective for fiscal years, and interim periods within those years, beginning on or after January 1, 2013. The adoption of this standard did not have a significant effect on the Company’s consolidated financial position.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Our net sales to foreign customers represented approximately 79.9% and 85.5% of our total net sales for the three months ended March 31, 2013 and 2012, respectively. 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 3.8% and 2.7% of our total net sales for the three months ended March 31, 2013 and 2012, respectively.

We are exposed to financial market risks, including changes in foreign currency exchange rates. The change in currency exchange rates that have the largest impact on translating our international operating profit (loss) is the Japanese Yen. We use derivative financial instruments to mitigate these risks. We do not use derivative financial instruments for speculative or trading purposes. We generally enter into monthly forward contracts to reduce the effect of fluctuating foreign currencies on short-term foreign currency-denominated intercompany transactions and other known currency exposures. Foreign currency exchange forwards are depicted in the following tables (*in thousands*):

March 31, 2013

<u>Not Designated as Hedges under ASC 815</u>	<u>Component of</u>	<u>Maturity</u>	<u>Notional Amount</u>	<u>Estimated Fair Value</u>
Foreign currency exchange forwards	Accrued expenses and other current liabilities	April 2013	\$ 3,715	\$ (21)
Total Derivative Instruments			<u>\$ 3,715</u>	<u>\$ (21)</u>

December 31, 2012

<u>Not Designated as Hedges under ASC 815</u>	<u>Component of</u>	<u>Maturity</u>	<u>Notional Amount</u>	<u>Estimated Fair Value</u>
Foreign currency exchange forwards	Prepaid expenses and other current assets	January 2013	\$ 9,590	\$ 244
Total Derivative Instruments			<u>\$ 9,590</u>	<u>\$ 244</u>

	Location of Realized Net (Loss) Gain and Changes in the Fair Value of Derivatives	For the three months ended March 31,	
		2013	2012
Foreign currency exchange forwards	Other, net	\$ 228	\$ 80
Weighted average notional amount of derivatives outstanding		\$ 2,400	\$ 2,405

We believe that based upon our hedging strategy, a 10% change in foreign currency exchange rates would have an immaterial impact on the Condensed Consolidated Statements 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.

We centrally manage our investment portfolios considering investment opportunities and risk, tax consequences and overall financing strategies. Our investment portfolio includes fixed-income securities with a fair value of approximately \$362.7 million as of March 31, 2013. These securities are subject to interest rate risk and will decline in value if interest rates increase. Based on our investment portfolio as of March 31, 2013, an immediate 100 basis point increase in interest rates may result in a decrease in the fair value of the portfolio of approximately \$2.3 million. Our investment portfolio as of September 30, 2013 had a fair value of approximately \$322.5 million. An immediate 100 basis point increase in interest rates may result in a decrease in the fair value of the September 30, 2013 portfolio of approximately \$2.9 million. While an increase in interest rates may reduce the fair value of the investment portfolio, it is unlikely that we will realize the losses in our condensed consolidated statement of income unless the individual fixed-income securities are sold prior to recovery or the loss is determined to be other-than-temporary.

Item 4. Controls and Procedures

This Item 4 includes information concerning the controls and control evaluations referred to in the certifications of our Chief Executive Officer and Chief Financial Officer required by Rule 13a-14 of the Exchange Act included in this Report as Exhibits 32.1 and 32.2.

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) are designed to ensure that information required to be disclosed in reports filed or submitted 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 and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

Veeco's management, under the supervision and with the participation of the Chief Executive Officer and the Chief Financial Officer, conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2012 in connection with the preparation of our annual report on Form 10-K, for year ended December 31, 2012. As described below, management has identified material weaknesses in our internal control over financial reporting, which is an integral component of our disclosure controls and procedures. As a result of those material weaknesses, management has concluded that our disclosure controls and procedures were not effective as of March 31, 2013.

Management's Report on Internal Control Over Financial Reporting

Management of Veeco and its consolidated subsidiaries, under the supervision of its Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with generally accepted accounting principles in the United States ("U.S. GAAP"). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis.

Veeco management, under the supervision of its Chief Executive Officer and Chief Financial Officer, conducted an assessment of the effectiveness of its internal control over financial reporting as of December 31, 2012 based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In connection with the above assessment, Veeco management identified the following material weaknesses:

Inadequate and ineffective controls over the recognition of revenue

We did not have adequate controls to ensure that revenue was recorded in accordance with U.S. GAAP. Specifically, we noted the following with respect to our accounting for certain revenue transactions:

- We did not maintain a sufficient complement of personnel with an appropriate level of accounting knowledge, experience, and training in the application of U.S. GAAP related to revenue recognition for multiple-element arrangements.
- We did not design and maintain effective controls over the adequate review and approval of customer orders at certain of our foreign subsidiaries to ensure that the order documentation received from the customer constituted the final order documentation. Additionally, in some cases, our foreign subsidiaries did not always communicate to our corporate accounting staff all of the information necessary to make accurate revenue recognition determinations.
- We did not design and maintain adequate procedures or effective review and approval controls over the accurate recording, presentation and disclosure of revenue and related costs related to multiple-element arrangements, including ensuring that multiple-element arrangements were identified, evaluated and effectively reviewed by appropriate accounting personnel. Specifically, we did not establish adequate procedures or design effective controls to:
 - Identify the nature of contracts, capture necessary data and determine how revenue should be recognized in accordance with applicable revenue recognition guidance.
 - Ensure consistent communication and coordination between and among various finance and non-finance personnel about the scope, terms and modifications to customer arrangements.
 - Ensure that all elements included in multiple-element arrangements were identified and accounted for appropriately.
 - Assess whether vendor-specific objective evidence, third-party evidence of fair value or, for periods subsequent to January 1, 2011, adequate documentation of management's determination of best estimate of selling price existed for all the elements in the arrangement.

As a result of the material weaknesses described above, management has concluded that, as of March 31, 2013, our internal control over financial reporting was not effective.

Remediation of Material Weaknesses in Internal Control Over Financial Reporting

Management is committed to the planning and implementation of remediation efforts to address the material weakness. These remediation efforts, summarized below, which have been implemented or are in process of implementation, are intended to both address the identified material weaknesses and to enhance our overall financial control environment. In this regard, our initiatives include:

- *Organizational Enhancements*— The Company has hired a new Vice President—Global Revenue Recognition who will be responsible for all aspects of the Company's revenue recognition policies, procedures and accounting. The Company has also created three new corporate revenue recognition positions, two of which have already been filled. Additionally, the Company has replaced certain key personnel in some of its foreign subsidiaries.
- *Training*— The Company is developing a comprehensive revenue recognition training program, portions of which have already been delivered. This training is focused on senior-level management, customer-facing employees as well as business unit, finance, sales and marketing personnel, including those at our foreign subsidiaries.
- *Revenue Practices*— The Company is currently evaluating its revenue practices and has begun implementing changes in those practices. Improvements are focused in the areas of (1) development of more comprehensive revenue recognition policies and improved procedures to ensure that such policies are understood and consistently applied, (2) better communication among all functions involved in the sales process (e.g., sales, business unit, foreign subsidiaries, legal, accounting, finance), (3) more standardization of contract documentation and revenue analyses for individual transactions and (4) system improvements and automation of manual processes.

While this remediation plan is being executed, the Company has also engaged additional external resources to support and supplement the Company's existing internal resources.

When fully implemented and operational, we believe the measures described above will remediate the material weaknesses we have identified and strengthen our internal control over financial reporting. We are committed to continuing to improve our internal control processes and will continue to diligently and vigorously review our financial reporting controls and procedures. As we continue to evaluate and work to improve our internal control over financial reporting, our management may determine to take additional measures.

Changes in Internal Control Over Financial Reporting

Other than the ongoing remediation efforts described above, there have been no changes in our internal control over financial reporting during the quarter ended March 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Veeco and certain other parties were named as defendants in a lawsuit filed on April 25, 2013 in the Superior Court of California, County of Sonoma. The plaintiff in the lawsuit, Patrick Colbus, seeks unspecified damages and asserts claims that he suffered burns and other injuries while he was cleaning a molecular beam epitaxy system alleged to have been manufactured by Veeco. The lawsuit alleges, among other things, that the molecular beam epitaxy system was defective and that Veeco failed to adequately warn of the potential risks of the system. Although Veeco believes this lawsuit is without merit and intends to defend vigorously against the claims, and although Veeco maintains insurance which may apply to this matter, the lawsuit could result in substantial costs, divert management's attention and resources from our operations and negatively affect our public image and reputation. Because the Company believes that this potential loss is not probable or estimable, it has not recorded any reserves related to this legal matter.

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

Item 1A. Risk Factors

Information regarding risk factors appears in the Safe Harbor Statement at the beginning of this quarterly report on Form 10-Q, and in Part I — Item 1A of our annual report on Form 10-K for the year ended December 31, 2012. There have been no material changes from the risk factors previously disclosed in our annual report on Form 10-K for the year ended December 31, 2012.

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

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not Applicable

Item 5. Other Information

None

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.

<u>Number</u>	<u>Description</u>	<u>Incorporated by Reference to the Following Document:</u>
31.1	Certification of Chief Executive Officer pursuant to Rule 13a—14(a) or Rule 15d—14(a) of the Securities and Exchange Act of 1934.	*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a—14(a) or Rule 15d—14(a) of the Securities and Exchange Act of 1934.	*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.	*
101.INS	XBRL Instance	**
101.XSD	XBRL Schema	**
101.PRE	XBRL Presentation	**
101.CAL	XBRL Calculation	**
101.DEF	XBRL Definition	**
101.LAB	XBRL Label	**

* Filed herewith

** Filed herewith electronically

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CERTIFICATION PURSUANT TO
RULE 13a — 14(a) or RULE 15d — 14(a)
OF THE SECURITIES EXCHANGE ACT OF 1934

I, David D. Glass, certify that:

I have reviewed this quarterly report on Form 10-Q for the period ended March 31, 2013 of Veeco Instruments Inc.;

1. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
2. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
3. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
4. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ DAVID D. GLASS

By: David D. Glass
Executive Vice President and Chief Financial Officer
Veeco Instruments Inc.
November 3, 2013

