CYBEROPTICS CORP
Form 10-Q
November 12, 2013

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Check One)

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

For the quarterly period ended September 30, 2013

o **TRANSITION PURSUANT TO SECTION 13 OR 15(D)**
OF THE SECURITIES EXCHANGE ACT

For the transition period from ______ to ______

COMMISSION FILE NO. (0-16577)

CYBEROPTICS CORPORATION

(Exact name of registrant as specified in its charter)

Minnesota (State or other jurisdiction of incorporation or organization)	**41-1472057** (I.R.S. Employer Identification No.)
5900 Golden Hills Drive **MINNEAPOLIS, MINNESOTA** (Address of principal executive offices)	**55416** (Zip Code)

(763) 542-5000
(Registrant s telephone number,
including area code)

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 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 þ No o

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

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 definition of accelerated filer or large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller Reporting Company þ
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date. At October 31, 2013, there were 6,556,131 shares of the registrant s Common Stock, no par value, issued and outstanding.

PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED BALANCE SHEETS
CYBEROPTICS CORPORATION
(Unaudited)

(In thousands, except share information)	September 30, 2013	December 31, 2012
ASSETS		
Cash and cash equivalents	$ 4,524	$ 7,340
Marketable securities	7,801	11,438
Accounts receivable, less allowance for doubtful accounts of $740 at September 30, 2013 and $775 at December 31, 2012	7,548	6,129
Inventories	12,457	12,533
Income tax refunds receivable	789	1,325
Other current assets	1,407	1,338
Deferred tax assets	100	100
Total current assets	34,626	40,203
Marketable securities, long-term	11,445	10,435
Equipment and leasehold improvements, net	1,438	1,719
Intangible and other assets, net	133	189
Goodwill	569	569
Other assets	195	142
Deferred tax assets	197	363
Total assets	$ 48,603	$ 53,620
LIABILITIES AND STOCKHOLDERS EQUITY		
Accounts payable	$ 4,124	$ 2,476
Advance customer payments	283	563
Accrued expenses	1,882	1,840
Deferred tax liability	29	29
Total current liabilities	6,318	4,908
Deferred rent	383	408
Deferred warranty revenue	197	146
Reserve for income taxes	244	686
Total liabilities	7,142	6,148
Commitments and contingencies		
Stockholders equity:		
Preferred stock, no par value, 5,000,000 shares authorized, none outstanding		
Common stock, no par value, 25,000,000 shares authorized, 6,666,984 shares issued and outstanding at September 30, 2013 and 6,969,772 shares issued and outstanding at December 31, 2012	29,815	31,410
Accumulated other comprehensive loss	(453)	(157)
Retained earnings	12,099	16,219
Total stockholders equity	41,461	47,472
Total liabilities and stockholders equity	$ 48,603	$ 53,620

SEE THE ACCOMPANYING NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
CYBEROPTICS CORPORATION
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands, except per share amounts)	**2013**	**2012**	**2013**	**2012**
Revenues	$ 8,726	$ 11,558	$ 24,756	$ 35,841
Cost of revenues	4,720	6,477	13,737	19,996
Gross margin	4,006	5,081	11,019	15,845
Research and development expenses	1,978	2,129	5,835	6,108
Selling, general and administrative expenses	2,989	3,324	9,340	9,919
Restructuring and severance costs		217		217
Loss from operations	(961)	(589)	(4,156)	(399)
Interest income and other	(107)	94	(184)	53
Loss before income taxes	(1,068)	(495)	(4,340)	(346)
Income tax provision (benefit)	(294)	(48)	(220)	(134)
Net loss	$ (774)	$ (447)	$ (4,120)	$ (212)
Net loss per share Basic	$ (0.11)	$ (0.06)	$ (0.60)	$ (0.03)
Net loss per share Diluted	$ (0.11)	$ (0.06)	$ (0.60)	$ (0.03)
Weighted average shares outstanding Basic	6,784	6,951	6,883	6,940
Weighted average shares outstanding Diluted	6,784	6,951	6,883	6,940

SEE THE ACCOMPANYING NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
CYBEROPTICS CORPORATION
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	**2013**	**2012**	**2013**	**2012**
Net loss	$ (774)	$ (447)	$ (4,120)	$ (212)
Other comprehensive income (loss), before tax:				
Foreign currency translation adjustments	115	212	(140)	344
Unrealized gains (losses) on available-for-sale securities:				
Unrealized gains (losses)	24	(72)	30	(73)
Reclassification adjustment for (gains) losses included in net loss		(2)	21	(6)
Total unrealized gains (losses) on available-for-sales securities	24	(74)	51	(79)
Unrealized gains (losses) on foreign exchange forward contracts:				
Unrealized gains (losses)	61	290	(231)	544
Reclassification adjustment for losses included in net loss	71		24	170
Total unrealized gains (losses) on foreign exchange forward contracts	132	290	(207)	714
Other comprehensive income (loss), before tax	271	428	(296)	979
Income tax provision related to items of other comprehensive income (loss)		93		235
Other comprehensive income (loss), net of tax	271	335	(296)	744
Total comprehensive income (loss)	$ (503)	$ (112)	$ (4,416)	$ 532

SEE THE ACCOMPANYING NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
CYBEROPTICS CORPORATION
(Unaudited)

(In thousands)	Nine Months Ended September 30, 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (4,120)	$ (212)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,292	1,368
Provision for doubtful accounts	(22)	(95)
Deferred taxes	43	
Foreign currency transaction (gains) losses	151	(19)
Realized (gains) losses on available-for-sale securities	21	(6)
Stock compensation costs	330	349
Changes in operating assets and liabilities:		
Accounts receivable	(1,397)	2,943
Inventories	(399)	(1,435)
Income tax refunds receivable	536	(185)
Other assets	(271)	(79)
Accounts payable	1,671	95
Advance customer payments	(229)	(224)
Accrued expenses	(339)	(810)
Net cash provided by (used in) operating activities	(2,733)	1,690
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from maturities of available-for-sale marketable securities	6,294	10,584
Proceeds from sales of available-for-sale marketable securities	4,340	2,936
Purchases of available-for-sale marketable securities	(7,996)	(18,681)
Additions to equipment and leasehold improvements	(610)	(1,086)
Additions to patents	(39)	(95)
Net cash provided by (used in) investing activities	1,989	(6,342)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from exercise of stock options	25	
Common stock repurchases	(2,014)	
Proceeds from issuance of common stock under employee stock purchase plan	64	139
Net cash provided by (used in) financing activities	(1,925)	139
Effects of exchange rate changes on cash and cash equivalents	(147)	104
Net decrease in cash and cash equivalents	(2,816)	(4,409)
Cash and cash equivalents beginning of period	7,340	13,791
Cash and cash equivalents end of period	$ 4,524	$ 9,382

SEE THE ACCOMPANYING NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

NOTES TO THE (UNAUDITED) INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CYBEROPTICS CORPORATION

1. INTERIM REPORTING:

The interim condensed consolidated financial statements presented herein as of September 30, 2013, and for the three and nine month periods ended September 30, 2013 and 2012, are unaudited, but in the opinion of management, include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of financial position, results of operations and cash flows for the periods presented.

The results of operations for the three and nine month periods ended September 30, 2013 do not necessarily indicate the results to be expected for the full year. The December 31, 2012 consolidated balance sheet data was derived from audited consolidated financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. These unaudited interim condensed consolidated financial statements should be read in conjunction with our consolidated financial statements and notes thereto, contained in our Annual Report on Form 10-K for the year ended December 31, 2012.

2. MARKETABLE SECURITIES:

Our investments in marketable securities are classified as available-for-sale and consist of the following:

	September 30, 2013			
(In thousands)	**Cost**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
Short-Term				
U.S. government and agency obligations	$ 5,965	$ 9	$	$ 5,974
Corporate debt securities and certificates of deposit	1,825	2		1,827
Marketable securities short-term	$ 7,790	$ 11	$	$ 7,801
Long-Term				
U.S. government and agency obligations	$ 6,752	$ 12	$ (2)	$ 6,762
Corporate debt securities and certificates of deposit	3,004	4	(5)	3,003
Asset backed securities	1,623	1		1,624
Equity security	42	14		56
Marketable securities long-term	$ 11,421	$ 31	$ (7)	$ 11,445

	December 31, 2012			
(In thousands)	**Cost**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
Short-Term				
U.S. government and agency obligations	$ 7,358	$ 10	$ (35)	$ 7,333
Corporate debt securities and certificates of deposit	4,100	5		4,105
Marketable securities short-term	$ 11,458	$ 15	$ (35)	$ 11,438
Long-Term				
U.S. government and agency obligations	$ 9,033	$ 23	$ (23)	$ 9,033
Corporate debt securities and certificates of deposit	1,192	4	(1)	1,195
Asset back securities	165			165
Equity security	42			42
Marketable securities long-term	$ 10,432	$ 27	$ (24)	$ 10,435

Our investments in marketable debt securities all have maturities of less than three years. At September 30, 2013, marketable debt securities valued at $15,208,000 were in an unrealized gain position totaling $28,000 and marketable debt securities valued at $3,982,000 were in an unrealized loss position totaling $7,000 (all had been in an unrealized loss position for less than twelve months). At December 31, 2012, marketable debt securities valued at $19,012,000 were in an unrealized gain position totaling $42,000 and marketable debt securities valued at $2,819,000 were in an unrealized loss position totaling $59,000 (all had been in an unrealized loss position for less than twelve months).

Net pre-tax unrealized gains for marketable securities of $35,000 at September 30, 2013 and net pre-tax unrealized losses for marketable securities of $17,000 at December 31, 2012 were recorded as a component of accumulated other comprehensive income (loss) in stockholders equity. In the three months ended September 30, 2013, we received proceeds of $818,000 from the sale of marketable securities. In the nine months ended September 30, 2013, we received proceeds of $4,340,000 from the sale of marketable securities. In the three months ended September 30, 2012, we received proceeds of $632,000 from the sale of marketable securities. In the nine months ended September 30, 2012 we received proceeds of $2,936,000 from the sale of marketable securities. We recognized a $21,000 loss from the sale of marketable securities in the nine months ended September 30, 2013 and a $6,000 gain from the sale of marketable securities in the nine months ended September 30, 2012.

Investments in marketable securities classified as cash equivalents of $886,000 at September 30, 2013 and $2,824,000 at December 31, 2012 consist of the following:

	September 30, 2013			
(In thousands)	**Cost**	**Unrealized Gains**	**Unrealized Losses**	**Recorded Basis**
Corporate debt securities and certificates of deposit	$ 886	$	$	$ 886
	$ 886	$	$	$ 886

	December 31, 2012			
(In thousands)	**Cost**	**Unrealized Gains**	**Unrealized Losses**	**Recorded Basis**
Corporate debt securities and certificates of deposit	$ 2,824	$	$	$ 2,824
	$ 2,824	$	$	$ 2,824

Cash and marketable securities held in foreign accounts totaled $1,180,000 at September 30, 2013 and $3,585,000 at December 31, 2012.

3. DERIVATIVES:

We enter into foreign exchange forward contracts to hedge against the effect of exchange rate fluctuations on cash flows denominated in foreign currencies associated with our subsidiary in Singapore. These transactions are designated as cash flow hedges. The effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income (loss) and reclassified into earnings in the same period during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. Hedge ineffectiveness and the amounts excluded from effectiveness testing recognized in income on cash flow hedges were not material for the three and nine month periods ended September 30, 2013 and September 30, 2012.

The maximum length of time over which we hedge our exposure to the variability in future cash flows is 12 months. Accordingly, at September 30, 2013 and September 30, 2012, all of our open foreign exchange forward contracts had maturities of one year or less. The dollar equivalent gross notional amount of our foreign exchange forward contracts designated as cash flow hedges was approximately $6.2 million at September 30, 2013 and $9.6 million at September 30, 2012.

Reclassifications of amounts from accumulated other comprehensive income (loss) into earnings include accumulated gains (losses) at the time earnings are impacted by the forecasted transaction. The location in the consolidated statements of operations and comprehensive income (loss) and amounts of gains and losses related to derivative instruments designated as cash flow hedges are as follows:

	Three Months Ended September 30, 2013		
(In thousands)	Pretax Gain (Loss) Recognized in Other Comprehensive Income (Loss) on Effective Portion of Derivative	Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income (Loss)	Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income (Loss)
Cost of revenues	$ 31	$ (41)	$
Research and development	16	(17)	
Selling, general and administrative	14	(13)	
Total	$ 61	$ (71)	$

	Three Months Ended September 30, 2012		
(In thousands)	Pretax Gain (Loss) Recognized in Other Comprehensive Income (Loss) on Effective Portion of Derivative	Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income (Loss)	Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income (Loss)
Cost of revenues	$ 200	$ 2	$
Research and development	51	(2)	
Selling, general and administrative	39		
Total	$ 290	$	$

	Nine Months Ended September 30, 2013		
(In thousands)	Pretax Gain (Loss) Recognized in Other Comprehensive Income (Loss) on Effective Portion of Derivative	Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income (Loss)	Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income (Loss)
Cost of revenues	$ (139)	$ (2)	$
Research and development	(53)	(12)	
Selling, general and administrative	(39)	(10)	
Total	$ (231)	$ (24)	$

(In thousands)	Nine Months Ended September 30, 2012 Pretax Gain (Loss) Recognized in Other Comprehensive Income on Effective Portion of Derivative	Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income (Loss)	Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income
Cost of revenues	$ 379	$ (119)	$
Research and development	93	(30)	
Selling, general and administrative	72	(21)	
Total	$ 544	$ (170)	$

We expect to reclassify the September 30, 2013 pretax unrealized loss recorded in accumulated other comprehensive income (loss) of $40,000 to earnings over the next 12 months with the impact offset by cash flows from underlying hedged items. The fair value of our foreign exchange forward contracts representing a loss in the amount of $38,000 as of September 30, 2013 has been recorded in accrued expenses. The fair value of our foreign exchange forward contracts representing a gain in the amount of $153,000 as of December 31, 2012 has been recorded in other current assets.

Additional information with respect to the impact of derivative instruments on other comprehensive income (loss) is included in Note 12. Additional information with respect to the fair value of derivative instruments is included in Note 4.

Our foreign exchange forward contracts contain credit risk to the extent that our bank counter-parties may be unable to meet the terms of the agreements. We minimize such risk by limiting our counter-parties to major financial institutions. We do not expect material losses as a result of defaults by other parties.

4. FAIR VALUE MEASUREMENTS:

We determine the fair value of our assets and liabilities based on the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value maximize the use of observable inputs and minimize the use of unobservable inputs. We use a fair value hierarchy with three levels of inputs, of which the first two are considered observable and the last unobservable, to measure fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1). The next highest priority is based on quoted prices for similar assets or liabilities in active markets or quoted prices for identical or similar assets or liabilities in non-active markets or other observable inputs (Level 2). The lowest priority is given to unobservable inputs (Level 3). The following provides information regarding fair value measurements for our marketable securities and foreign exchange forward contracts as of September 30, 2013 and December 31, 2012 according to the three-level fair value hierarchy:

		Fair Value Measurements at September 30, 2013 Using		
(In thousands)	Balance September 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Marketable securities:				
U.S. government and agency obligations	$ 12,736	$	$ 12,736	$
Corporate debt securities and certificates of deposit	4,830		4,830	
Asset backed securities	1,624		1,624	
Equity security	56	56		
Total marketable securities	$ 19,246	$ 56	$ 19,190	$
Derivative instruments-liabilities:				
Foreign exchange forward contracts	$ 38	$	$ 38	$

(In thousands)	Balance December 31, 2012	Fair Value Measurements at December 31, 2012 Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Marketable securities:				
U.S. government and agency obligations	$ 16,366	$	$ 16,366	$
Corporate debt securities and certificates of deposit	5,300		5,300	
Asset backed securities	165		165	
Equity security	42	42		
Total marketable securities	$ 21,873	$ 42	$ 21,831	$
Derivative instruments-assets:				
Foreign exchange forward contracts	$ 153	$	$ 153	$

During the nine months ended September 30, 2013 there were no significant transfers within the three level hierarchy. A significant transfer is recognized when the inputs used to value a security have been changed which merit a transfer between the disclosed levels of the valuation hierarchy.

The fair value for our U.S. government and agency obligations, corporate debt securities and certificates of deposit and asset backed securities are determined based on valuations provided by external investment managers who obtain them from a variety of industry standard data providers. The fair value for our equity security is based on a quoted market price obtained from an active market.

The fair value for our foreign exchange forward contracts is based on foreign currency spot and forward rates obtained from reputable financial institutions with resulting valuations periodically validated by obtaining foreign currency spot rate and forward quotes from other industry standard sources, third party or counterparty quotes. The fair value of our foreign exchange forward contracts representing a loss in the amount of $38,000 as of September 30, 2013 has been recorded in accrued expenses. The fair value of our foreign exchange forward contracts representing a gain in the amount of $153,000 as of December 31, 2012 has been recorded in other current assets.

The carrying amounts of financial instruments such as cash equivalents, accounts receivable, income tax refunds receivable, other assets, accounts payable, and all current liabilities approximate their related fair values due to the short-term maturities of these instruments. Non-financial assets such as equipment and leasehold improvements, goodwill and intangible assets are subject to non-recurring fair value measurements if they are deemed impaired. We had no re-measurements of non-financial assets to fair value during the three and nine months ended September 30, 2013 or September 30, 2012.

5. ACCOUNTING FOR STOCK-BASED COMPENSATION:

All equity-based payments to employees, including grants of employee stock options and restricted stock units, are recognized as an expense in our consolidated statement of operations based on the grant date fair value of the award. We utilize the straight-line method of expense recognition over the award s service period for our graded vesting options. The fair value of stock options granted has been determined using the Black-Scholes model. The compensation expense recognized for all equity based awards is net of estimated forfeitures, which are based on historical data. We have classified equity based compensation within our statement of operations in the same manner as our cash based employee compensation costs.

Equity based compensation expense in the three months ended September 30, 2013 totaled $97,000 and includes $62,000 for stock option awards, $10,000 for our employee stock purchase plan, and $25,000 for unvested restricted stock units. Equity based compensation expense in the nine months ended September 30, 2013 totaled $330,000 and includes $192,000 for stock option awards, $34,000 for our employee stock purchase plan, $74,000 for unvested restricted stock units and $30,000 for shares issued to our non-employee directors upon their re-election to our board in May 2013.

Equity based compensation expense in the three months ended September 30, 2012 totaled $95,000 and includes $60,000 for stock option awards, $13,000 for our employee stock purchase plan, and $22,000 for unvested restricted stock units. Equity based compensation expense in the nine months ended September 30, 2012 totaled $349,000 and includes $190,000 for stock option awards, $43,000 for our employee stock purchase plan, $75,000 for unvested restricted stock units and $41,000 for shares issued to our non-employee directors upon their re-election to our board in May 2012.

At September 30, 2013, the total unrecognized compensation cost related to non-vested equity based compensation arrangements was $680,000 and the related weighted average period over which it is expected to be recognized is 1.91 years.

Stock Options

We have two stock incentive plans that are administered under the supervision of the Compensation Committee of the Board of Directors. There are 1,030,307 shares of common stock reserved in the aggregate for issuance of options and other stock based benefits under these plans, including restricted stock units and share grants to employees, officers and others. Reserved shares underlying canceled options are available for future grant under our active plan. Options are granted at an option price per share equal to or greater than the market value on the date of grant. Generally, options granted to employees vest over a four-year period and expire seven or ten years after the date of grant. As of September 30, 2013, there were 466,203 shares of common stock available under these plans for future issuance to employees, officers and others.

The following is a summary of stock option activity during the nine months ended September 30, 2013:

	Options Outstanding		Weighted Average Exercise Price Per Share
Outstanding, December 31, 2012	544,153	$	8.68
Granted			
Exercised	(5,000)		4.99
Expired	(12,500)		7.26
Forfeited	(1,250)		8.71
Outstanding, September 30, 2013	525,403	$	8.75
Exercisable, September 30, 2013	331,989	$	9.32

The intrinsic value of an option is the amount by which the fair value of the underlying stock exceeds its exercise price. At September 30, 2013, the weighted average remaining contractual term of all outstanding options was 3.60 years and their aggregate intrinsic value was $149,575. At September 30, 2013, the weighted average remaining contractual term of options that were exercisable was 2.56 years and their aggregate intrinsic value was $149,575. We received proceeds of $25,000 from the exercise of stock options in the nine months ended September 30, 2013. We received no proceeds from the exercise of stock options in the nine months ended September 30, 2012.

Restricted Stock Units

Our 1998 Stock Incentive Plan also permits our Compensation Committee to grant other stock-based benefits, including restricted stock units. Restricted stock units are valued at a price equal to the fair market value of our common stock on the date of grant, vest over a four year period provided the employee is still working for the company and entitle the holders to one share of our common stock for each restricted stock unit. The aggregate fair value of outstanding restricted stock units as of September 30, 2013 was $241,000.

A summary of activity in non-vested restricted stock units for the nine months ended September 30, 2013 is as follows:

Non-vested restricted stock units	**Shares**		**Weighted Average Grant Date Fair Value**
Non-vested at December 31, 2012	44,555	$	7.61
Granted			
Vested	(5,438)		7.31
Forfeited	(416)		8.71
Non-vested at September 30, 2013	38,701	$	7.64

Employee Stock Purchase Plan

We have an Employee Stock Purchase Plan available to eligible U.S. employees. Under terms of the plan, eligible employees may designate from 1% to 10% of their compensation to be withheld through payroll deductions, up to a maximum of $6,500 in each plan year, for the purchase of common stock at 85% of the lower of the market price on the first or last day of the offering period. There were 12,656 shares issued under this plan in the nine months ended September 30, 2013 and 19,759 shares issued in the nine months ended September 30, 2012. As of September 30, 2013, 153,926 shares remain available for future issuance under this plan.

Stock Grant Plan for Non-Employee Directors

Our stock grant plan for non-employee directors provides for automatic grants of 1,000 shares of our common stock to each of our non-employee directors upon their re-election to the Board of Directors. The plan provides for a total of 30,000 shares of our common stock for issuance to directors and will expire on May 19, 2018. We issued a total of 5,000 shares of common stock under this plan in connection with our annual meeting in May 2013, resulting in $30,000 of stock compensation expense in the nine months ended September 30, 2013. There are presently 6,000 shares of common stock reserved in the aggregate for future issuance under this plan.

6. INVENTORIES AND WARRANTIES:

Inventories consist of the following:

(In thousands)	September 30, 2013	December 31, 2012
Raw materials and purchased parts	$ 7,287	$ 8,152
Work in process	1,549	1,322
Finished goods	3,621	3,059
Total inventories	$ 12,457	$ 12,533

Warranty costs:

We provide for the estimated cost of product warranties, which generally extend for one year after purchase, at the time revenue is recognized. While we engage in extensive product quality programs and processes, including actively monitoring and evaluating the quality of component suppliers, warranty obligations are affected by product failure rates, material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from our estimates, revisions to the estimated warranty liability would be required. Our warranty liability is included as a component of accrued expenses. At the end of each reporting period we revise our estimated warranty liability based on these factors.

A reconciliation of the changes in our estimated warranty liability is as follows:

	Nine Months Ended September 30,	
(In thousands)	2013	2012
Balance at beginning of period	$ 694	$ 985
Accrual for warranties	418	616
Warranty revision	4	(14)
Settlements made during the period	(619)	(765)
Balance at end of period	$ 497	$ 822

Deferred warranty revenue:

The current portion of our deferred warranty revenue is included as a component of advance customer payments. A reconciliation of the changes in our deferred warranty revenue is as follows:

	Nine Months Ended September 30,	
(In thousands)	2013	2012
Balance at beginning of period	$ 582	$ 806
Revenue deferrals	253	181
Amortization of deferred revenue	(355)	(336)
Total deferred warranty revenue	480	651
Current portion of deferred warranty revenue	(283)	(462)
Long-term deferred warranty revenue	$ 197	$ 189

7. INTANGIBLE ASSETS:

Intangible assets consist of the following:

	September 30, 2013			December 31, 2012		
(In thousands)	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Patents	$ 2,887	$ (2,754)	$ 133	$ 2,847	$ (2,658)	$ 189

Amortization expense for the three and nine month periods ended September 30, 2013 and 2012 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Patents	$ 30	$ 39	$ 95	$ 117

Amortization of patents has been classified as research and development expense in the accompanying statements of operations. Estimated aggregate amortization expense based on current intangibles for the next four years is expected to be as follows: $25,000 for the remainder of 2013, $71,000 in 2014, $32,000 in 2015, and $5,000 in 2016.

Intangible and other long lived assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. An impairment loss would be recognized when future undiscounted cash flows expected to result from use of the asset and eventual disposition are less than the carrying amount.

8. GOODWILL:

We assess our goodwill for impairment in the fourth quarter of each year, and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. In each quarter of 2013, our stock market capitalization fell below our net book value for a period of more than 30 days, indicating that the value of our goodwill might be impaired.

In 2013 when evaluating whether or not goodwill was impaired, we compared our fair value to our net book value or carrying value (Step 1 of the impairment test). In calculating fair value, we used the income approach. The income approach is a valuation technique under which we estimate future cash flows using financial forecasts. Future estimated cash flows are discounted to their present value to calculate fair value. When considering fair value, we also gave consideration to the control premium in excess of our current market capitalization that might be obtained from a third party acquirer. In the situation where net book value or carrying value exceeds fair value, the amount of impairment loss must be measured. The measurement of impairment (Step 2 of the impairment test) is calculated by determining the implied fair value of goodwill, which equals the excess of any remaining fair value over the fair values assigned to other assets and liabilities. Goodwill impairment is measured as the excess of the carrying amount of goodwill over its implied fair value.

In determining fair value under the income approach, our expected cash flows are affected by various assumptions. Fair value on a discounted cash flow basis uses our business plan and projections as the basis for expected future cash flow forecasts, with an estimation of residual growth rates thereafter. For each quarter of 2013 our impairment tests utilized a 15% discount rate and our terminal value was based on a multiple equal to 6 times our projected future earnings before interest, taxes, depreciation and amortization. We believe the significant assumptions used in our 2013 goodwill impairment tests, including a 15% discount rate, are reflective of the assumptions currently used in the marketplace to evaluate fair value. Our recent analyses indicate that our goodwill at September 30, 2013 and December 31, 2012 in the amount of $569,000 is not impaired.

9. SIGNIFICANT CUSTOMERS:

Export sales were 73% of revenue in the three months ended September 30, 2013 and 78% of revenue in the nine months ended September 30, 2013. Export sales were 84% of revenue in the three months ended September 30, 2012 and 86% of revenue in the nine months ended September 30, 2012. Virtually all of our export sales are negotiated, invoiced and paid in U.S. dollars. Export sales by geographic area are summarized as follows:

	Three Months Ended September 30,				Nine Months Ended September 30,			
(In thousands)		**2013**		**2012**		**2013**		**2012**
Americas	$	85	$	172	$	582	$	1,276
Europe		1,820		3,513		6,495		10,438
Asia		4,412		5,943		11,804		18,681
Other		75		79		338		455
Total export sales	$	6,392	$	9,707	$	19,219	$	30,850

Our LaserAlign sensor family has historically accounted for a significant portion of our sales and profitability. Our revenue, results of operations and cash flows would be negatively impacted if our LaserAlign customers, primarily Juki and Assembleon, are unsuccessful selling the products into which our sensors are incorporated, design their products to function without our sensors, purchase sensors from other suppliers, or otherwise terminate their relationships with us.

We are dependent upon two customers, Juki and Assembleon, for a significant portion of our total revenue. For the nine months ended September 30, 2013, sales to Juki accounted for 16% of our total revenue and sales to Assembleon accounted for 8% of our total revenue.

10. RE-ORGANIZATION AND RESTRUCTURE CHARGE:

In the third quarter of 2012, we consolidated research and development for our semiconductor products from Portland, Oregon into our Minneapolis headquarters facility. We believe this move will streamline our business and provide our sensor engineers in Minneapolis with more efficient access to our WaferSense® technology and products. The related restructure charge from this action of $217,000 was fully paid prior to December 31, 2012.

Additional severance costs of $523,000 were incurred in the fourth quarter of 2012 when we reduced our global workforce by approximately 10% or 20 employees in response to the sluggish economy and weak SMT and semiconductor market conditions. No restructuring or severance costs were incurred in the three or nine months ended September 30, 2013.

A summary of our restructuring accrual is as follows:

(In thousands)	**Fourth Quarter 2012 Workforce Reduction**	
Balance, December 31, 2012	$	192
Cost incurred		
Payments made		192
Balance, September 30, 2013	$	

11. NET LOSS PER SHARE:

Basic net loss per share is computed by dividing net loss by the weighted average number of common shares outstanding during the period. Common equivalent shares consist of common shares to be issued upon exercise of stock options, restricted stock units and from participation in our employee stock purchase plan, as calculated using the treasury stock method. All potentially dilutive common equivalent shares are excluded from the calculations of net loss per diluted share for the three and nine month periods ended September 30, 2013 and September 30, 2012 due to their anti-dilutive effect. The components of net loss per basic and diluted share are as follows:

(In thousands except per share amounts)	Net Loss	Weighted Average Shares Outstanding	Per Share Amount
Three Months Ended September 30, 2013:			
Basic	$ (774)	6,784	$ (0.11)
Dilutive effect of common equivalent shares			
Dilutive	$ (774)	6,784	$ (0.11)

(In thousands except per share amounts)	Net Loss	Weighted Average Shares Outstanding	Per Share Amount
Three Months Ended September 30, 2012:			
Basic	$ (447)	6,951	$ (0.06)
Dilutive effect of common equivalent shares			
Dilutive	$ (447)	6,951	$ (0.06)

(In thousands except per share amounts)	Net Loss	Weighted Average Shares Outstanding	Per Share Amount
Nine Months Ended September 30, 2013:			
Basic	$ (4,120)	6,883	$ (0.60)
Dilutive effect of common equivalent shares			
Dilutive	$ (4,120)	6,883	$ (0.60)

(In thousands except per share amounts)	Net Loss	Weighted Average Shares Outstanding	Per Share Amount
Nine Months Ended September 30, 2012:			
Basic	$ (212)	6,940	$ (0.03)
Dilutive effect of common equivalent shares			
Dilutive	$ (212)	6,940	$ (0.03)

The calculation of diluted net loss per common share excludes 589,000 and 551,000 potentially dilutive shares for the three months ended September 30, 2013 and 2012, and 598,000 and 585,000 potentially dilutive shares for the nine months ended September 30, 2013 and 2012, because their effect would be anti-dilutive.

12. COMPREHENSIVE INCOME (LOSS):

Taxes related to items of other comprehensive income (loss) are as follows:

(In thousands)	Three Months Ended September 30, 2013 Before Tax	Tax Provision /(Benefit)	Net of Tax Amount	Three Months Ended September 30, 2012 Before Tax	Tax Provision /(Benefit)	Net of Tax Amount
Foreign currency translation adjustments	$ 115	$	$ 115	$ 212	$	$ 212
Net changes related to available-for-sale securities:						
Unrealized gains (losses)	24		24	(72)	(9)	(63)
Reclassification adjustment for gains included in net loss				(2)	(1)	(1)
Total net changes related to available-for-sale securities	24		24	(74)	(10)	(64)
Net changes related to foreign exchange forward contracts:						
Unrealized gains	61		61	290	103	187
Reclassification adjustment for losses included in net loss	71		71			
Total net changes related to foreign exchange forward contracts	132		132	290	103	187
Other comprehensive income	$ 271	$	$ 271	$ 428	$ 93	$ 335

(In thousands)	Nine Months Ended September 30, 2013 Before Tax	Tax Provision /(Benefit)	Net of Tax Amount	Nine Months Ended September 30, 2012 Before Tax	Tax Provision /(Benefit)	Net of Tax Amount
Foreign currency translation adjustments	$ (140)	$	$ (140)	$ 344	$	$ 344
Net changes related to available-for-sale securities:						
Unrealized gains (losses)	30		30	(73)	(14)	(59)
Reclassification adjustment for (gains) losses included in net loss	21		21	(6)	(1)	(5)
Total net changes related to available-for-sale securities	51		51	(79)	(15)	(64)
Net changes related to foreign exchange forward contracts:						
Unrealized gains (losses)	(231)		(231)	544	192	352
Reclassification adjustment for losses included in net loss	24		24	170	58	112
Total net changes related to foreign exchange forward contracts	(207)		(207)	714	250	464
Other comprehensive income (loss)	$ (296)	$	$ (296)	$ 979	$ 235	$ 744

Reclassification adjustments are made to avoid double counting in comprehensive income (loss) items that are also recorded as part of net loss. Reclassifications to earnings related to cash flow hedging instruments are discussed in Note 3. Income taxes are not provided for foreign currency translation adjustments relating to permanent investments in international subsidiaries. We have recorded a valuation allowance against substantially all of our United States and Singapore based deferred tax assets. Accordingly, we do not expect to record a tax provision for items of other comprehensive income (loss) until such time as the valuation allowance is substantially reduced. The effect of the reclassifications from comprehensive income (loss) to earnings by line item is as follows:

Details about Accumulated Other Comprehensive Income Components	**Amount Reclassified from Accumulated Other Comprehensive Income [(a)]**				**Affected Line Item in the Statements of Operations**
	Three Months Ended September 30,		**Nine Months Ended September 30,**		
(In thousands)	**2013**	**2012**	**2013**	**2012**	
Unrealized gains (losses) on available-for-sale securities	$	$ 2	$ (21)	$ 6	Interest income and other
		1		1	Income tax provision (benefit)
	$	$ 1	$ (21)	$ 5	Net of tax
Unrealized gains (losses) on foreign exchange forward contracts	$ (41)	$ 2	$ (2)	$ (119)	Cost of revenues
	(17)	(2)	(12)	(30)	Research and development expenses
	(13)		(10)	(21)	Selling, general and administrative expenses
	(71)		(24)	(170)	Total before tax
				(58)	Income tax provision (benefit)
	$ (71)	$	$		