KVH INDUSTRIES INC \DE\
Form 10-Q
November 05, 2009
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended: September 30, 2009

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ______ to ______

Commission File Number 0-28082

KVH Industries, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware	**05-0420589**
(State or Other Jurisdiction of	**(I.R.S. Employer**
Incorporation or Organization)	**Identification Number)**

50 Enterprise Center, Middletown, RI 02842

(Address of Principal Executive Offices) (Zip Code)

(401) 847-3327

(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 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** x **No** ¨

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

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

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

Date	**Class**	**Outstanding shares**
November 2, 2009	Common Stock, par value $0.01 per share	14,004,421

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Form 10-Q

INDEX

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

KVH INDUSTRIES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share amounts, unaudited)

	September 30, 2009	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 4,103	$ 4,979
Marketable securities	37,400	37,681
Accounts receivable, net of allowance for doubtful accounts of approximately $901 as of September 30, 2009 and $333 as of December 31, 2008	12,342	13,960
Inventories	14,762	15,484
Prepaid expenses and other assets	1,272	731
Costs and estimated earnings in excess of billings on uncompleted contracts	76	44
Deferred income taxes	32	32
Total current assets	69,987	72,911
Property and equipment, less accumulated depreciation of $20,712 as of September 30, 2009 and $19,050 as of December 31, 2008	15,564	13,286
Other non-current assets	5,913	4,226
Deferred income taxes	3,334	3,334
Total assets	**$ 94,798**	**$ 93,757**
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 3,713	$ 5,488
Accrued compensation and employee-related expenses	3,537	3,013
Accrued other	3,347	2,400
Deferred sales	866	366
Accrued product warranty costs	1,149	1,139
Accrued professional services	379	256
Current portion of long-term debt	116	2,026
Total current liabilities	13,107	14,688
Other long-term liabilities	82	
Long-term debt excluding current portion	3,837	
Total liabilities	**17,026**	**14,688**

Commitments and contingencies (notes 3 and 10)		
Stockholders equity:		
Preferred stock, $0.01 par value. Authorized 1,000,000 shares; none issued		
Common stock, $0.01 par value. Authorized 20,000,000 shares, 15,191,644 and 15,127,327 shares issued at September 30, 2009 and December 31, 2008; 13,990,320 and 14,049,047 shares outstanding at September 30, 2009 and December 31, 2008, respectively	152	151
Additional paid-in capital	94,263	92,932
Accumulated deficit	(7,253)	(5,273)
Accumulated other comprehensive income	81	129
Less: treasury stock at cost, common stock, 1,201,324 shares as of September 30, 2009 and 1,078,280 shares as of December 31, 2008	(9,471)	(8,870)
Total stockholders equity	**77,772**	**79,069**
Total liabilities and stockholders equity	**$ 94,798**	**$ 93,757**

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

3

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except share amounts, unaudited)

	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Sales:				
Product	$ 18,620	$ 12,325	$ 52,314	$ 52,734
Service	4,023	3,415	10,461	8,454
Net sales	22,643	15,740	62,775	61,188
Costs and expenses:				
Costs of product sales	10,663	7,693	33,139	31,754
Costs of service sales	3,044	1,571	7,422	3,893
Sales, marketing and support	4,241	3,573	12,371	11,830
Research and development	2,292	1,813	6,265	5,804
General and administrative	1,943	1,992	5,723	5,280
Total costs and expenses	22,183	16,642	64,920	58,561
Income (loss) from operations	460	(902)	(2,145)	2,627
Interest income	74	278	279	1,037
Interest expense	26	36	63	118
Other expense, net	29	42	21	236
Income (loss) before income taxes	479	(702)	(1,950)	3,310
Income tax expense	94	110	30	558
Net income (loss)	**$ 385**	**$ (812)**	**$ (1,980)**	**$ 2,752**
Per share information:				
Net income (loss) per share, basic and diluted	**$ 0.03**	**$ (0.06)**	**$ (0.14)**	**$ 0.19**
Number of shares used in per share calculation:				
Basic	**13,978**	**14,251**	**13,981**	**14,461**
Diluted	**14,241**	**14,251**	**13,981**	**14,474**

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands, unaudited)

	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Cash flows from operating activities:		
Net (loss) income	$ (1,980)	$ 2,752
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation	1,872	1,659
Compensation expense related to stock options and employee stock purchase plan	1,248	1,171
Provision for doubtful accounts, net	612	122
Loss on foreign currency forward exchange contracts		302
Gain on sale of fixed assets	(10)	
Changes in operating assets and liabilities:		
Accounts receivable	1,006	3,645
Costs and estimated earnings in excess of billings on uncompleted contracts	(32)	(45)
Inventories	722	(5,902)
Prepaid expenses and other assets	(541)	90
Other non-current assets	(1,687)	(3,303)
Accounts payable	(1,775)	2,524
Accrued expenses	1,603	1,002
Deferred sales	500	213
Other long-term liabilities	82	(9)
Net cash provided by operating activities	**1,620**	**4,221**
Cash flows from investing activities:		
Purchase of marketable securities	(32,214)	(22,438)
Maturities and sales of marketable securities	32,447	21,584
Capital expenditures, net	(4,168)	(2,070)
Proceeds from the sale of fixed assets	29	
Net cash used in investing activities	**(3,906)**	**(2,924)**
Cash flows from financing activities:		
Repayments of mortgage loan	(2,073)	(98)
Borrowings from mortgage loan	4,000	
Proceeds from stock options and employee stock purchase plan	135	207
Payment of employee restricted stock withholdings	(47)	
Payment of stock registration fees	(4)	
Repurchase of common stock	(601)	(6,148)
Net cash provided by (used in) financing activities	**1,410**	**(6,039)**
Net decrease in cash and cash equivalents	**(876)**	**(4,742)**
Cash and cash equivalents at beginning of period	**4,979**	**12,284**
Cash and cash equivalents at end of period	**$ 4,103**	**$ 7,542**

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements

(Unaudited, all amounts in thousands except share and per share amounts)

(1) Description of Business

KVH Industries, Inc. (the Company or KVH) develops, manufactures and markets mobile communications products for the marine, land mobile and in-flight markets, and navigation, guidance and stabilization products for both the defense and commercial markets.

KVH s mobile communications products enable customers to receive live digital television, telephone and Internet services in automobiles, recreational vehicles, marine vessels, and commercial airplanes while in motion via satellite services. KVH sells its mobile communications products through an extensive international network of retailers, distributors and dealers. KVH also leases products directly to end users.

KVH offers precision fiber optic gyro-based systems that enable platform and optical stabilization, navigation, pointing and guidance. KVH s guidance and stabilization products also include tactical navigation systems that provide uninterrupted access to navigation and pointing information in a variety of military vehicles, including tactical trucks and light armored vehicles. KVH s guidance and stabilization products are sold directly to U.S. and allied governments and government contractors, as well as through an international network of authorized independent sales representatives. In addition, KVH s guidance and stabilization products have numerous commercial applications such as precision mapping, autonomous vehicles, train location control and track geometry measurement systems, industrial robotics and optical stabilization.

KVH s mobile communications service sales includes sales earned from product repairs, sales from satellite telephone and Internet airtime services, and certain DIRECTV and DISH Network account subsidies and referral fees earned in conjunction with the sale of its products. KVH provides, for monthly usage fees, third-party satellite connectivity for voice, data and Internet services to its Inmarsat TracPhone customers who choose to activate their subscriptions with KVH. KVH also earns monthly fixed and usage fees for satellite connectivity sales from broadband Internet, data and Voice over Internet Protocol (VOIP) service to its TracPhone V7 customers. Under current DIRECTV and DISH Network programs, KVH is eligible to receive a one-time subsidy for each receiver activated for service and a new mobile account activation fee from DIRECTV and DISH Network for each customer who activates their DIRECTV or DISH Network service directly through KVH. In addition, KVH sells extended warranty programs primarily for its mobile communications products.

KVH s guidance and stabilization service sales include product repairs and engineering services provided under development contracts.

(2) Basis of Presentation

The accompanying condensed consolidated financial statements of KVH Industries, Inc. and its wholly owned subsidiary, KVH Europe A/S (collectively, KVH or the Company), have been prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission regarding interim financial reporting. The Company has evaluated all subsequent events through the date the financial statements were issued on November 5, 2009. Given that KVH Europe A/S operates as the Company s European and international distributor, all of its operating expenses are reflected within sales, marketing and support within the accompanying condensed consolidated statements of operations. All significant intercompany accounts and transactions have been eliminated in consolidation. The condensed consolidated financial statements have not been audited by our independent registered public accounting firm, but include all adjustments (consisting of only normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial condition, results of operations, and cash flows for the periods presented. These condensed consolidated financial statements do not include all disclosures associated with annual financial statements and accordingly should be read in conjunction with the Company s consolidated financial statements and related notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2008 filed on March 13, 2009 with the Securities and Exchange Commission. The results for the three and nine months ended September 30, 2009 are not necessarily indicative of operating results for the remainder of the year.

(3) Significant Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of sales and expenses during the reporting periods. Significant estimates and assumptions by management affect the Company s revenue recognition, valuation of accounts receivable, valuation of inventory, valuation of deferred tax assets, certain accrued expenses and accounting for contingencies.

6

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

Although the Company regularly assesses these estimates, actual results could differ materially from these estimates. Changes in estimates are recorded in the period in which they become known. The Company bases its estimates on historical experience and various other assumptions that it believes to be reasonable under the circumstances.

(4) Stock-Based Compensation

The Company recognizes stock-based compensation in accordance with the provisions of Accounting Standards Codification (ASC) 718, *Compensation-Stock Based Compensation*. Stock-based compensation expense was $452 and $382 for the three months ended September 30, 2009 and September 30, 2008, respectively and $1,248 and $1,171 for the nine months ended September 30, 2009 and September 30, 2008, respectively. As of September 30, 2009, there was $781 of total unrecognized compensation expense related to stock options, which is expected to be recognized over a weighted-average period of 1.95 years. As of September 30, 2009, there was $2,579 of total unrecognized compensation expense related to restricted stock awards, which is expected to be recognized over a weighted-average period of 3.17 years.

The Company granted 88,668 and 566,768 restricted stock awards to employees under the terms of the Amended and Restated 2006 Stock Incentive Plan during the three and nine months ended September 30, 2009, respectively. The restricted stock awards vest ratably over four years from the date of grant subject to the recipient remaining employed through the applicable vesting dates. Compensation expense for restricted stock awards is measured at fair value on the date of grant based on the number of shares granted and the quoted market closing price of the Company s common stock. Such value is recognized as expense over the vesting period of the award, net of estimated forfeitures.

A total of 210,000 of the restricted stock awards granted during the nine months ended September 30, 2009 were performance-based awards granted to executives. Of these restricted stock awards, 105,000 will vest ratably over four years from date of grant provided that the Company achieves two specific mini-VSAT sales objectives in 2009 and the remaining 105,000 will vest ratably over four years from date of grant provided that the Company achieves certain fiber optic gyro production output targets in 2009. As of June 30, 2009, the fiber optic gyro production output targets were achieved. As a result, the Company recorded expense for the three and nine months ended September 30, 2009 related to the performance-based restricted stock awards, the amount of which was not material.

The Company also granted 42,045 and 44,545 stock options to employees under the terms of the Amended and Restated 2003 Incentive and Nonqualified Stock Option Plan during the three and nine months ended September 30, 2009, respectively.

The fair value of stock options granted for the nine months ended September 30, 2009 was estimated as of the date of grant using the Black-Scholes option-pricing model. The weighted-average fair value per share for all options granted during the three months ended September 30, 2009 and 2008 was $2.85 and $2.92, respectively. The weighted-average fair value per share for all options granted during the nine months ended September 30, 2009 and 2008 was $2.79 and $2.93 respectively. The weighted-average assumptions used to value options as of their grant date were as follows:

	Nine months ended September 30,	
	2009	2008
Risk-free interest rate	2.28%	3.13%
Expected volatility	44.24%	36.11%
Expected life (in years)	4.07	4.09
Dividend yield	0%	0%

(5) Net Income (Loss) per Common Share

Basic net income (loss) per share is calculated based on the weighted average number of common shares outstanding during the period. Diluted net income per share incorporates the dilutive effect of common stock equivalent options, restricted stock awards, warrants and other convertible securities, if any, as determined with the treasury stock accounting method. Common stock equivalents related to options and restricted stock awards for 1,027,603 and 1,178,701 shares of common stock for the three and nine months ended September 30, 2009, respectively, have been excluded from the fully diluted calculation of net income (loss) per share, as inclusion would be anti-dilutive. Common stock equivalents related to options and restricted stock awards for 1,293,183 and 1,300,784 shares of common stock for the three and nine months ended September 30, 2008, respectively, have been excluded from the fully diluted calculation of net income per share, as inclusion would be anti-dilutive.

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

A reconciliation of the basic and diluted weighted average common shares outstanding is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
Weighted average common shares outstanding basic	13,978,456	14,251,003	13,980,727	14,460,550
Dilutive common shares issuable in connection with stock plans	262,056			13,009
Weighted average common shares outstanding diluted	14,240,512	14,251,003	13,980,727	14,473,559

(6) Inventories

Inventories are stated at the lower of cost or market using the first-in first-out costing method. Inventories as of September 30, 2009 and December 31, 2008 include the costs of material, labor, and factory overhead. Components of inventories consist of the following:

	September 30, 2009	December 31, 2008
Raw materials	$ 10,086	$ 10,084
Work in process	1,687	1,385
Finished goods	2,989	4,015
	$ 14,762	$ 15,484

(7) Comprehensive Income (Loss)

Comprehensive income (loss) includes net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) includes the effects of unrealized gains or losses on available-for-sale marketable securities that are separately included in accumulated other comprehensive income within stockholders equity. The Company s comprehensive income (loss) for the periods presented is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
Net income (loss)	$ 385	$ (812)	$ (1,980)	$ 2,752
Unrealized gain (loss) on available-for-sale securities	13	28	(48)	31
Total comprehensive income (loss)	$ 398	$ (784)	$ (2,028)	$ 2,783

(8) Product Warranty

The Company s products carry limited warranties that range from one to three years and vary by product. The warranty period begins on the date of retail purchase by the original purchaser. The Company accrues estimated product warranty costs at the time of sale and any additional amounts are recorded when such costs are probable and can be reasonably estimated. Factors that affect the Company s warranty liability include the number of units sold, historical and anticipated rates of warranty repairs and the estimated cost per repair. Warranty and related costs are reflected within sales, marketing and support in the accompanying statements of operations. As of September 30, 2009 and December 31, 2008, the Company had accrued product warranty costs of $1,149 and $1,139, respectively. The following table summarizes product warranty activity for the periods presented:

	Nine months ended September 30,	
	2009	**2008**
Beginning balance	$ 1,139	$ 778
Charges to expense	598	1,067
Costs incurred	(588)	(739)
Ending balance	$ 1,149	$ 1,106

8

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

(9) Segment Reporting

Under common operational management, the Company designs, develops, manufactures and markets its navigation, guidance and stabilization and mobile communication products for use in a wide variety of applications. Products are generally sold directly to third-party consumer electronic dealers and retailers, consumer product manufacturers, government contractors or directly to U.S. and other foreign government agencies. Primarily, sales originating in North America consist of sales within the United States and Canada and, to a lesser extent, Mexico, Asia/Pacific and some Latin and South American countries. North American sales also include all guidance and stabilization product sales throughout the world. Sales originating from the Company s Denmark subsidiary principally consist of sales into all European countries, both inside and outside the European Union, as well as Africa, the Middle East, India and all countries in Asia.

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

The Company operates in two geographic segments, exclusively in the mobile communications, navigation and guidance equipment industry, which it considers to be a single business activity. The Company has two primary industry categories: mobile communication and guidance and stabilization. Mobile communication sales include marine, aeronautical and land mobile communication equipment, product repairs, satellite-based telephone and Internet airtime services, television account subsidies and referral fees earned in conjunction with the sale of the Company s products, and Broadband Internet connectivity and VOIP services sold with the Company s mini-VSAT product. Guidance and stabilization product sales include sales of commercial and defense-related navigation, guidance and stabilization equipment based upon digital compass and fiber optic sensor technology. Guidance and stabilization sales also include product repairs and engineering services provided under development contracts.

The following table summarizes information regarding the Company s operations by geographic segment:

	Sales Originating From		
	North America	Europe	Total
Three months ended September 30, 2009			
Mobile communication sales to the United States	$ 8,008	$	$ 8,008
Mobile communication sales to Canada	180		180
Mobile communication sales to Europe	181	2,909	3,090
Mobile communication sales to other geographic areas	140	742	882
Guidance and stabilization sales to the United States	4,641		4,641
Guidance and stabilization sales to Canada	808		808
Guidance and stabilization sales to Europe	3,461		3,461
Guidance and stabilization sales to other geographic areas	1,573		1,573
Intercompany sales	1,089		1,089
Subtotal	20,081	3,651	23,732
Eliminations	(1,089)		(1,089)
Net sales	$ 18,992	$ 3,651	$ 22,643
Segment net income	$ 69	$ 316	$ 385
Depreciation	$ 646	$ 9	$ 655
Total assets	$ 88,787	$ 6,011	$ 94,798
Three months ended September 30, 2008			
Mobile communication sales to the United States	$ 8,040	$	$ 8,040
Mobile communication sales to Canada	183		183
Mobile communication sales to Europe		2,924	2,924
Mobile communication sales to other geographic areas	162	960	1,122
Guidance and stabilization sales to the United States	1,111		1,111
Guidance and stabilization sales to Canada	794		794
Guidance and stabilization sales to Europe	1,327		1,327
Guidance and stabilization sales to other geographic areas	239		239
Intercompany sales	1,861		1,861
Subtotal	13,717	3,884	17,601
Eliminations	(1,861)		(1,861)

Net sales	$ 11,856	$ 3,884	$ 15,740
Segment net (loss) income	$ (1,179)	$ 367	$ (812)
Depreciation	$ 518	$ 9	$ 527
Total assets	$ 89,086	$ 4,431	$ 93,517

	Sales Originating From		
	North America	**Europe**	**Total**
Nine months ended September 30, 2009			
Mobile communication sales to the United States	$ 22,330	$	$ 22,330
Mobile communication sales to Canada	439		439
Mobile communication sales to Europe	1,158	8,984	10,142

10

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

	Sales Originating From		
	North America	Europe	Total
Mobile communication sales to other geographic areas	410	2,418	2,828
Guidance and stabilization sales to the United States	12,346		12,346
Guidance and stabilization sales to Canada	2,061		2,061
Guidance and stabilization sales to Europe	9,521		9,521
Guidance and stabilization sales to other geographic areas	3,108		3,108
Intercompany sales	4,379		4,379
Subtotal	55,752	11,402	67,154
Eliminations	(4,379)		(4,379)
Net sales	$ 51,373	$ 11,402	$ 62,775
Segment net (loss) income	$ (2,798)	$ 818	$ (1,980)
Depreciation	$ 1,847	$ 25	$ 1,872
Total assets	$ 88,787	$ 6,011	$ 94,798
Nine months ended September 30, 2008			
Mobile communication sales to the United States	$ 30,378	$	$ 30,378
Mobile communication sales to Canada	805		805
Mobile communication sales to Europe	456	12,292	12,748
Mobile communication sales to other geographic areas	672	3,996	4,668
Guidance and stabilization sales to the United States	7,955		7,955
Guidance and stabilization sales to Canada	1,156		1,156
Guidance and stabilization sales to Europe	2,628		2,628
Guidance and stabilization sales to other geographic areas	850		850
Intercompany sales	10,037		10,037
Subtotal	54,937	16,288	71,225
Eliminations	(10,037)		(10,037)
Net sales	$ 44,900	$ 16,288	$ 61,188
Segment net income	$ 1,650	$ 1,102	$ 2,752
Depreciation	$ 1,630	$ 29	$ 1,659
Total assets	$ 89,086	$ 4,431	$ 93,517

(10) Legal Matters

From time to time, the Company is involved in litigation incidental to the conduct of its business. In the ordinary course of business, the Company is a party to inquiries, legal proceedings and claims including, from time to time, disagreements with vendors and customers. The Company is not a party to any lawsuit or proceeding that, in management s opinion, is likely to materially harm the Company s business, results of operations, financial condition or cash flows.

(11) Recent Accounting Pronouncements

During the third quarter of 2009, the Company adopted the new Accounting Standards Codification (ASC) as issued by the Financial Accounting Standards Board (FASB). The ASC has become the source of authoritative U.S. generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. The ASC is not intended to change or alter existing GAAP. The adoption of the ASC did not have a material impact on the Company s financial position or results of operations.

In June 2009, the FASB issued new accounting guidance which amends the evaluation criteria to identify the primary beneficiary of a variable interest entity (VIE) and requires ongoing reassessment of whether an enterprise is the primary beneficiary of the VIE. The new guidance significantly changes the consolidation rules for VIEs including the consolidation of common structures, such as joint ventures, equity method investments and collaboration arrangements. The guidance is applicable to all new and existing VIEs. The provisions of this new accounting guidance is effective for interim and annual reporting periods ending after November 15, 2009 and will become effective for the Company beginning in the first quarter of 2010. The Company does not expect the adoption will have a material impact on the Company s financial position or results of operations.

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

In September 2009, the FASB issued new accounting guidance related to the revenue recognition of multiple element arrangements. The new guidance states that if vendor specific objective evidence or third party evidence for deliverables in an arrangement cannot be determined, companies will be required to develop a best estimate of the selling price for separate deliverables and allocate arrangement consideration using the relative selling price method. The accounting guidance will be applied prospectively and will become effective during the first quarter of 2011. Early adoption is allowed. The Company does not expect the adoption will have a material impact on the Company s financial position or results of operations.

In September 2009, the FASB issued new accounting guidance related to certain revenue arrangements that include software elements. Previously, companies that sold tangible products with more than incidental software were required to apply software revenue recognition guidance. This guidance often delayed revenue recognition for the delivery of the tangible product. Under the new guidance, tangible products that have software components that are essential to the functionality of the tangible product will be excluded from the software revenue recognition guidance. The new guidance will include factors to help companies determine what is essential to the functionality. Software-enabled products will now be subject to other revenue guidance and will likely follow the guidance for multiple element arrangements issued by the FASB in September 2009. The new guidance is to be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with earlier application permitted. If a vendor elects earlier application and the first reporting period of adoption is not the first reporting period in the vendor s fiscal year, the guidance must be applied through retrospective application from the beginning of the vendor s fiscal year and the vendor must disclose the effect of the change to those previously reported periods. The Company does not expect the adoption will have a material impact on the Company s financial position or results of operations.

(12) Share Buyback Program

On November 26, 2008, the Company s Board of Directors authorized a program to repurchase up to one million shares of the Company s common stock. As of September 30, 2009, 798,676 shares of the Company s common stock remain available for repurchase under the authorized program. The repurchase program is funded using the Company s existing cash, cash equivalents, marketable securities and future cash flows. Under the repurchase program, the Company, at management s discretion, may repurchase shares on the open market from time to time, in privately negotiated transactions or block transactions, or through an accelerated repurchase agreement. The timing of such repurchases depends on availability of shares, price, market conditions, alternative uses of capital, and applicable regulatory requirements. The program may be modified, suspended or terminated at any time without prior notice. The repurchase program has no expiration date. There were no other repurchase programs outstanding during the nine months ended September 30, 2009, and no repurchase programs expired during the period.

The Company repurchased zero and 123,044 shares of its common stock in the three and nine months ended September 30, 2009, respectively, at a cost of $601.

(13) Long-Term Aviation Antenna Development and Production Agreement

On February 18, 2008, the Company entered into a $20,896 long-term antenna development and production agreement (the Agreement). Under the terms of the Agreement, the Company has designed, developed, and manufactured DIRECTV-compatible satellite television antennas to be used on narrowbody commercial aircraft operating in the United States. In accordance with ASC 730, *Research & Development*, and the Agreement, the Company has capitalized a net amount of $4,430 in related development costs, which the Company has a contractual right to recover, and which are reflected in other non-current assets as of September 30, 2009. These costs are expensed into cost of sales as antennas are sold in proportion to the number of antennas delivered versus the total contractual antenna production requirement. The Company began shipment of the antennas in the second quarter of 2009.

(14) Fair Value Measurements

Effective January 1, 2008, the Company adopted the required provisions of ASC 820, *Fair Value Measurements and Disclosures*. ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an 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. ASC 820 also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. ASC 820 describes three levels of inputs that may be used to measure fair value:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. The Company s Level 1 assets are investments in money market mutual funds, government agency bonds, United States treasuries and certificates of deposit.

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

Level 2: Quoted prices for similar assets or liabilities in active markets; or observable prices that are based on observable market data, based on directly or indirectly market-corroborated inputs. The Company has no Level 2 inputs.

Level 3: Unobservable inputs that are supported by little or no market activity, and are developed based on the best information available given the circumstances. The Company has no Level 3 inputs.

13

Table of Contents

KVH INDUSTRIES, INC. AND SUBSIDIARY

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited, all amounts in thousands except share and per share amounts)

The following table presents financial assets at September 30, 2009 for which the Company measures fair value on a recurring basis, by level, within the fair value hierarchy:

	Level 1	Level 2	Level 3	Total
Assets				
Money market mutual funds	$ 7,950			$ 7,950
Government agency bonds	15,562			15,562
United States treasuries	11,667			11,667
Certificates of deposit	2,221			2,221

Certain financial instruments are carried at cost on the condensed consolidated balance sheets, which approximates fair value due to their short-term, highly liquid nature. These instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued expenses.

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

The statements included in this quarterly report on Form 10-Q, other than statements of historical fact, are forward-looking statements. Examples of forward-looking statements include statements regarding our future financial results, operating results, business strategies, projected costs, products, competitive positions and plans, customer preferences, consumer trends, anticipated product development, and objectives of management for future operations. In some cases, forward-looking statements can be identified by terminology such as may, will, should, would, expects, plans, anticipates, believes, estimates, predicts, potential, continue, or the negative of these terms or other comparable terminology. Any expectations based on these forward-looking statements are subject to risks and uncertainties and other important factors, including those discussed in the section entitled Risk Factors in Item 1A of Part II of this quarterly report. These and many other factors could affect our future financial and operating results, and could cause actual results to differ materially from expectations based on forward-looking statements made in this document or elsewhere by us or on our behalf. For example, our expectations regarding certain items as a percentage of sales assume that we will achieve our anticipated sales goals. The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this report.

Overview

We are a leading manufacturer of solutions that provide global high-speed internet, television, and voice services via satellite to mobile users at sea, on land, and in the air. We are also a premier manufacturer of high-performance navigational sensors and integrated inertial systems for defense and commercial guidance and stabilization applications.

Our mobile satellite business includes receive-only TracVision satellite TV systems, 2-way TracPhone satellite communications systems, and the mini-VSAT Broadband airtime service. Our TracVision mobile satellite TV systems enable mobile reception in vehicles or vessels of most leading satellite TV services, such as DIRECTV, DISH Network, and ExpressVu in North America, and Astra and Eutelsat in Europe. In February 2008, we entered the aviation market with a development and production contract for a satellite TV antenna that is sold on an OEM basis by LiveTV. Our TracPhone satellite communications systems enable reception of Inmarsat L-Band MSS services or our own mini-VSAT Broadband Ku-band FSS service, and are sold primarily to mariners. We sell our mobile satellite products and airtime services through our direct sales force and an extensive international network of independent sales representatives, distributors and retailers to leisure, commercial, and government customers.

Our guidance and stabilization products use our precision fiber optic gyro (FOG) and digital compass technologies to help stabilize platforms such as antennas, gun turrets, optical systems, material handling equipment, and radar units and to provide guidance for torpedoes and other munitions. These products are either integrated within our own navigation and antenna systems or sold as modules to other manufacturers. We also use our FOG and digital compass technology to produce some variants of our TACNAV line of navigation systems for military vehicles. We sell our guidance and stabilization products to commercial and military customers either directly to U.S. and allied governments and government contractors or through an international network of authorized independent sales representatives.

Table of Contents

We generate sales primarily from the sale of our mobile satellite systems and services and our guidance and stabilization products and services. The following table provides, for the periods indicated, our sales by industry category:

	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
	(in thousands)			
Mobile communications	$ 12,160	$ 12,269	$ 35,739	$ 48,599
Guidance and stabilization	10,483	3,471	27,036	12,589
Net sales	$ 22,643	$ 15,740	$ 62,775	$ 61,188

Our mobile communications service sales include sales earned from product repairs, sales of satellite telephone and Internet usage services, and certain DIRECTV and DISH Network account referral fees earned in conjunction with the sale of our products. We provide, for a fee, third-party satellite telephone and Internet airtime to our TracPhone and Internet customers who choose to activate their subscriptions with us. We also earn service sales from broadband Internet and VOIP service sold with our mini-VSAT product. Under current DIRECTV and DISH Network programs, we are eligible to receive a one-time subsidy for each receiver activated and a new mobile account activation fee from DIRECTV and DISH Network for each customer who activates their DIRECTV or DISH Network service directly through us. Our guidance and stabilization service sales include product repairs and engineering services provided under development contracts.

Our guidance and stabilization business is characterized by a small number of customers who place a small number of relatively large dollar value orders. Orders for our guidance and stabilization products typically vary in size and are sometimes in the range of several hundred thousand dollars to over one million dollars. Each order can have a significant impact on our sales, and because our guidance and stabilization products generally have higher gross margins than our mobile communications products, each order can have an impact on our net income that is disproportionately large relative to the sales generated by the order.

We have historically derived a substantial portion of our sales from sales to customers located outside the United States. Note 9 of the notes to the condensed consolidated financial statements provides information regarding our sales to specific geographic regions.

Critical Accounting Policies and Estimates

The 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 and liabilities, sales and expenses, and related disclosure at the date of our financial statements. Our significant accounting policies are summarized in note 1 of the notes to the consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2008.

As described in our Form 10-K for the year ended December 31, 2008, our most critical accounting policies and estimates upon which our consolidated financial statements were prepared were those relating to revenue recognition, allowances for accounts receivable, inventories, income taxes and deferred income tax assets and liabilities and warranty. We have reviewed our policies and determined that these remain our most critical accounting policies for the quarter ended September 30, 2009. Readers should refer to our 2008 Form 10-K under Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies for the detailed descriptions of these policies.

Results of Operations

The following table provides, for the periods indicated, certain financial data expressed as a percentage of sales:

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
Sales:				
Product	82.2%	78.3%	83.3%	86.2%
Service	17.8	21.7	16.7	13.8
Net sales	100.0	100.0	100.0	100.0
Costs and expenses:				
Costs of product sales	47.1	48.9	52.8	51.9
Costs of service sales	13.5	10.0	11.8	6.4
Sales, marketing and support	18.7	22.7	19.7	19.3

Table of Contents

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
Research and development	10.1	11.5	10.0	9.5
General and administrative	8.6	12.6	9.1	8.6
Total costs and expenses	98.0	105.7	103.4	95.7
Income (loss) from operations	2.0	(5.7)	(3.4)	4.3
Interest income	0.3	1.8	0.4	1.7
Interest expense	0.1	0.2	0.1	0.2
Other expense, net	0.1	0.3	0.0	0.4
Income (loss) before income taxes	2.1	(4.4)	(3.1)	5.4
Income tax expense	0.4	0.7	0.0	0.9
Net income (loss)	1.7%	(5.1)%	(3.1)%	4.5%

Three Months Ended September 30, 2009 and 2008

Net Sales

Product sales for the three months ended September 30, 2009 increased $6.3 million, or 51%, to $18.6 million from $12.3 million for the three months ended September 30, 2008. The primary reason for the increase was a $7.3 million, or 264%, increase in sales of our guidance and stabilization products. Specifically, sales of our FOG products increased $7.0 million, or 767%, driven largely by increased sales in support of remotely operated weapons station programs. However, although our expectation is that FOG product sales will continue to increase in support of remotely operated weapons station programs in 2010, we do not expect such a level of growth rate to continue. Also contributing to the increase was a $0.4 million increase in sales related to our TACNAV defense products. Partially offsetting the increase was a decrease in sales of our marine products of $0.7 million, or 9%, compared with the three months ended September 30, 2008. This decrease was principally the result of decreases in the sales of our marine consumer products, including the TracVision M-series satellite television products and Inmarsat-compatible TracPhone products. In addition, sales of our land mobile products decreased by $0.3 million, or 16%, compared to the three months ended September 30, 2008. Mobile communications product sales originating from our Danish subsidiary decreased $0.2 million, or 8%, from the three months ended September 30, 2008 to the three months ended September 30, 2009. Mobile communications product sales originating from North America decreased $0.7 million, or 11%, from the three months ended September 30, 2008 to the three months ended September 30, 2009.

The weakening of the recreational vehicle market commencing in the second quarter of 2008 due in part to increased fuel prices, and the crisis of consumer confidence in the general economy during the second half of 2008 and in the first, second and third quarter of 2009, caused declines in demand for our land mobile products and our marine consumer products.

Our operating performance depends significantly on general economic conditions, which have worsened dramatically in recent periods. Net sales of our mobile communications products are largely generated by discretionary consumer spending, and demand for these products is likely to demonstrate slower growth or decline as a result of weak regional and global economic conditions. Consumer spending tends to decline during recessionary periods and may decline at other times. Consumers may choose not to purchase our mobile communications products due to a perception that they are luxury items. As global and regional economic conditions change, including the general level of interest rates, fluctuating oil prices and demand for durable consumer products, demand for our products could be materially and adversely affected. As a result of these and other factors, customers could slow or suspend spending on our products and services. We may also be forced to further increase our allowance for doubtful accounts, which would have a negative impact on our earnings and financial condition. During the first nine months of 2009, we recorded an additional $0.6 million to our allowance for doubtful accounts. The increase was largely driven by the increase in revenue of our airtime services business and the financial deterioration of a few of our mobile communication product distributors. We cannot predict the timing, duration or ultimate impact of the current economic downturn. We expect our business to continue to be adversely impacted by this downturn.

Governments are experiencing significant declines in tax receipts, which may cause them to curtail spending significantly or reallocate funds away from defense programs. There can be no assurances that government responses to the disruptions in the economy will remedy these problems.

Service sales for the three months ended September 30, 2009 increased $0.6 million, or 18%, to $4.0 million from $3.4 million for the three months ended September 30, 2008. The primary reason for the increase was a $1.0 million increase in airtime sales for our mini-VSAT Broadband service that we launched in the fourth quarter of 2007, which was partially offset by a decline in service repair sales of $0.4 million.

Table of Contents

Cost of Sales

For the three months ended September 30, 2009, costs of product sales increased by $3.0 million, or 39%, to $10.7 million for the three month ended September 30, 2009 from $7.7 million for the three months ended September 30, 2008. The primary reason for the increase in dollar amount was the increase in unit sales of higher priced FOG products, partially offset by a decline in unit sales of mobile communications products and a shift in the sales mix of mobile communications products toward lower priced marine products.

Costs of service sales increased by $1.5 million, or 94%, to $3.0 million for the three month ended September 30, 2009 from $1.6 million for the three months ended September 30, 2008. This increase was driven by increased airtime usage of our mini-VSAT Broadband service as well as by increased costs related to the build out and operation of the network and support infrastructure for our mini-VSAT Broadband service as part of our initiative for the global expansion of that service. We expect these costs to continue to increase substantially during the fourth quarter of 2009 and at least during the first half of 2010 as we complete the initial build out of the global mini-VSAT infrastructure.

Gross margin from product sales for the three months ended September 30, 2009 increased to 43% from 38% in the year-ago period. The primary reason for the increase in gross margin was a 264% increase in our relatively higher margin guidance and stabilization product sales resulting in improved utilization of production capacity for fiber optic gyros for the three-month period ended September 30, 2009. Also contributing to the gross margin improvement was a 10% decrease in our relatively lower margin mobile communication product sales.

Gross margin from service sales for the three months ended September 30, 2009 decreased to 24% from 54% in the year-ago period, primarily as a result of increased costs related to the build out and operations of the network and support infrastructure for our mini-VSAT Broadband service. In the near term, we expect these costs to continue to grow more rapidly than the number of subscribers for, and revenues from, our mini-VSAT Broadband service.

Operating Expenses

Sales, marketing and support expense for the three months ended September 30, 2009 increased by $0.7 million, or 19%, to $4.2 million from $3.6 million for the three months ended September 30, 2008. The primary reason for the increase in 2009 was a $0.4 million increase in commission expense as a result of the increased product and airtime sales discussed above. Also contributing to the increase was a $0.2 million increase in employee compensation for sales, marketing and support, primarily as a result of an increase in stock compensation expense and accrued performance based incentive compensation, and a $0.1 million increase in bad debt expense. As a percentage of sales, sales, marketing and support expense decreased during the quarter ended September 30, 2009 to 19% from 23% for the quarter ended September 30, 2008, due primarily to the increase in overall product and service sales discussed above.

Research and development expense for the three months ended September 30, 2009 increased by $0.5 million, or 26%, to $2.3 million from $1.8 million for the three months ended September 30, 2008. The primary reason for the increase in 2009 expense was the core completion of the development project for the DIRECTV-compatible satellite television antenna to be used on narrowbody commercial aircraft. The project was substantially complete in the second quarter of 2009 and resulted in a $0.9 million decrease in the capitalization of aviation antenna development costs (see note 13 to the condensed consolidated financial statements) during the third quarter of 2009 versus the third quarter of 2008 and a corresponding increase in research and development expense. Partially offsetting this increase was a decrease in engineering related employee compensation and material costs. As a percentage of sales, research and development expense decreased during the quarter ended September 30, 2009 to 10% from 12% for the quarter ended September 30, 2008, due primarily to the increase in overall product and service sales discussed above.

General and administrative expense for the three months ended September 30, 2009 was $1.9 million, which was generally consistent with the general and administrative expense for the three months ended September 30, 2008. As a percentage of sales, general and administrative expense decreased during the quarter ended September 30, 2009 to 9% from 13% for the quarter ended September 30, 2008, due primarily to the increase in overall product and service sales discussed above.

Interest Income and Other Expense

Interest income and other expense for the three months ended September 30, 2009 decreased by $0.2 million to $0.0 million from $0.2 million for the three months ended September 30, 2008. The primary reason for the decrease was a $0.2 million decrease in interest income in the 2009 period resulting from lower interest rates and a lower average amount of cash, cash equivalents and marketable securities invested during the three months ended September 30, 2009.

Income Tax Expense

Income tax expense for the three months ended September 30, 2009 was $0.1 million, which was consistent with income tax expense for the three months ended September 30, 2008. Our effective tax rate was 19.6% for the three months ended September 30, 2009

Table of Contents

compared to 15.7% for the year-ago period. We expect that substantially all of our 2009 taxable income generated from our U.S. operations will be offset by federal net operating losses generated by us in prior years. Accordingly, we expect that any tax expense generated by our U.S. operations in 2009 will be made up primarily of federal alternative minimum tax and to a lesser extent certain state tax expense. Taxable income generated by our subsidiary in Denmark will be subject to taxation at the Danish statutory rates as we have no net operating loss carry-forwards or tax credits available to offset current or future taxable income in that jurisdiction. The consistency in income tax expense in 2009 is attributed to the similar level of taxable income generated by our Danish subsidiary for the three months ended September 30, 2009 from the three months ended September 30, 2008.

We regularly evaluate our valuation allowance recorded against our net deferred tax assets. Should we generate net income in 2009 and project net income for 2010 and beyond, we may determine, after considering all available evidence, that it is more likely than not that all or some additional portion of our net deferred tax assets would be realized. Should that determination be made, we would reverse all or a portion of the valuation allowance at such time and recognize a reduction of income tax expense (as of September 30, 2009, the maximum amount of reduction which could impact income tax expense totaled approximately $5.3 million). In addition, as a portion of our deferred tax assets were generated from excess tax deductions from share-based payment awards, pursuant to ASC 718, *Compensation-Stock Compensation*, a portion of any such valuation allowance reversal would be recorded to additional paid-in capital when the deduction reduces tax payable (as of September 30, 2009, such amount would total approximately $1.9 million).

Nine Months Ended September 30, 2009 and 2008

Net Sales

Product sales for the nine months ended September 30, 2009 decreased $0.4 million, or 1%, to $52.3 million from $52.7 million for the nine months ended September 30, 2008. The weakening of the recreational vehicle market commencing in the second quarter of 2008 due in part to increased fuel prices, and the crisis of consumer confidence in the general economy during the second half of 2008 and the first, second and third quarters of 2009, caused declines in demand for our land mobile products and our marine consumer products. Sales of our marine products decreased by $10.7 million, or 32%, compared with the nine months ended September 30, 2008. This decrease was principally the result of decreases in the sales of our marine consumer products, including the TracVision M-series satellite television products and Inmarsat-compatible TracPhone products. In addition, sales of our land mobile products decreased by $5.3 million, or 60%, compared to the nine months ended September 30, 2008. Mobile communications product sales originating from our Danish subsidiary decreased $5.2 million, or 36%, from the nine months ended September 30, 2008 to the nine months ended September 30, 2009. Mobile communications product sales originating from North America decreased $10.7 million, or 38%, from the nine months ended September 30, 2008 to the nine months ended September 30, 2009.

Sales of our guidance and stabilization products increased by $15.5 million, or 152%, from the nine months ended September 30, 2008 to the nine months ended September 30, 2009. Specifically, sales of our FOG products increased $15.2 million, or 323%, driven largely by increased sales in support of remotely operated weapons station programs.

Service sales for the nine months ended September 30, 2009 increased $2.0 million, or 24%, to $10.5 million from $8.5 million for the nine months ended September 30, 2008. The primary reason for the increase was a $3.4 million increase in airtime sales for our mini-VSAT Broadband service that we launched in the fourth quarter of 2007, which was partially offset by a decline in service repair and extended warranty sales of $1.1 million.

Table of Contents

Cost of Sales

For the nine months ended September 30, 2009, costs of product sales increased by $1.4 million, or 4%, to $33.1 million for the nine months ended September 30, 2009 from $31.8 million for the nine months ended September 30, 2008. The primary reason for the increase was the increase in unit sales of higher priced FOG products, which was partially offset by a decline in unit sales of mobile communication products and a shift in the sales mix of mobile communications products towards lower priced marine products.

Costs of service sales increased by $3.5 million, or 91%, to $7.4 million for the nine months ended September 30, 2009 from $3.9 million for the nine months ended September 30, 2008. This increase was driven by increased airtime usage of our mini-VSAT Broadband service as well as by increased costs related to the build out and operation of the network and support infrastructure for our mini-VSAT Broadband service as part of our initiative for the global expansion of that service.

Gross margin from product sales for the nine months ended September 30, 2009 decreased to 37% from 40% in the year-ago period. The deterioration in our gross margin from product sales was attributable to under-utilization of our production capacity earlier in 2009 due to reduced unit sales of mobile communications products, a higher level of price discounts to maintain our competitive position in the mobile communications marketplace and a $1.1 million increase in our inventory reserves primarily related to certain military components and the introduction of new mobile communication products.

Gross margin from service sales for the nine months ended September 30, 2009 decreased to 29% from 54% in the year-ago period, as a result of increased costs related to the build out and operations of the network and support infrastructure for our mini-VSAT Broadband service.

Operating Expenses

Sales, marketing and support expense for the nine months ended September 30, 2009 increased by $0.5 million, or 5%, to $12.4 million from $11.8 million for the nine months ended September 30, 2008. As a percentage of sales, year-to-date sales, marketing and support expense increased to 20% in 2009 from 19% in 2008. The primary reason for the increase in 2009 was a $0.6 million increase in commission expense as a result of the increase in selected product sales and airtime sales discussed above. Also contributing to the increase was a $0.5 million increase in bad debt expense. Partially offsetting the increase was a $0.5 million decrease in warranty and service-related expenses.

Research and development expense for the nine months ended September 30, 2009 increased by $0.5 million, or 8%, to $6.3 million from $5.8 million for the nine months ended September 30, 2008. The primary reason for the increase in 2009 expense was the core completion of the development project for the DIRECTV-compatible satellite television antenna to be used on narrowbody commercial aircraft. The project was substantially complete in the second quarter of 2009 and resulted in a $1.2 million decrease in the capitalization of aviation antenna development costs (see note 13 to the condensed consolidated financial statements) during the nine months end September 30, 2009 versus the nine months ended September 30, 2008 and a corresponding increase in research and development expense. Partially offsetting this increase was a decrease in engineering related employee compensation and material costs. As a percentage of sales, year-to-date research and development expense remained fairly consistent on a year-over-year basis at 10%.

General and administrative expense for the nine months ended September 30, 2009 increased by $0.4 million, or 8%, to $5.7 million from $5.3 million for the nine months ended September 30, 2008. The primary reason for the increase in 2009 expense was a $0.3 million increase in legal and consulting fees. As a percentage of sales, year-to-date general and administrative expense remained fairly consistent on a year-over-year basis at 9%.

Interest Income and Other Expense

Interest income and other expense for the nine months ended September 30, 2009 decreased by $0.5 million to $0.2 million from $0.7 million for the nine months ended September 30, 2008. The primary reason for the decrease was a $0.8 million decrease in interest income in the 2009 period resulting from lower interest rates and a lower average amount of cash, cash equivalents and marketable securities invested during the nine months ended September 30, 2009. Also contributing to the decrease was a $0.1 million decrease in currency gains driven by a decrease in gains from remeasurement of transactions at our Danish subsidiary, which has the U.S. dollar as its functional currency. Partially offsetting these factors was a $0.3 million decrease in losses related to foreign currency exchange contracts.

Income Tax Expense

Income tax expense for the nine months ended September 30, 2009 decreased by $0.5 million to $0.0 million from $0.6 million for the nine months ended September 30, 2008. Our effective tax rate was 1.5% for the nine months ended September 30, 2009 compared to 16.9% for the year-ago period. The primary reason for the decrease in 2009 was our $2.0 million pre-tax loss versus a net profit in 2008. Also contributing to the decrease was a decrease of $0.2 million in federal income tax expense resulting from an adjustment recorded to reconcile our previously recorded estimates of federal income tax expense to our 2008 federal income tax return that was completed and filed in June 2009 and a $0.1 million federal income tax benefit recorded in 2009 from the monetization of research and development tax credits.

Table of Contents

Liquidity and Capital Resources

We have historically funded our operations primarily from operating cash flows, net proceeds from public and private equity offerings, bank financings and proceeds received from exercises of stock options. As of September 30, 2009, we had $41.5 million in cash, cash equivalents and marketable securities and $56.9 million in working capital.

Net cash provided by operations was $1.6 million for the nine months ended September 30, 2009 as compared to net cash provided by operations of $4.2 million for the nine months ended September 30, 2008. The decrease is primarily due to a $4.7 million decrease in net income, coupled with a $3.7 million increase in cash outflows related to accounts payable and accrued expenses, a $2.6 million decrease in cash inflows attributable to changes in accounts receivable, and a $0.6 million increase in cash outflows related to prepaid expenses and other assets. This increase in cash outflows was partially offset by a $6.6 million decrease in cash outflows related to decreased inventory levels, coupled with a $1.6 million decrease in cash outflows related to other non-current assets, consisting primarily of a reduction in capitalized development costs related to our aviation antenna program, and a $0.3 million increase in cash inflows related to deferred revenue, consisting primarily of increased customer advances for marine airtime services.

Net cash used in investing activities was $3.9 million for the nine months ended September 30, 2009 as compared to net cash used in investing activities of $2.9 million for the nine months ended September 30, 2008. The increase is primarily due to a $2.1 million increase in our capital expenditures. This increase in capital expenditures was due primarily to our initiative for the global expansion of our min-VSAT Broadband satellite communication products and service. The increase in cash outflows was partially offset by a $1.1 million decrease in our net investment in marketable securities.

Net cash provided by financing activities was $1.4 million for the nine months ended September 30, 2009 as compared to net cash used in financing activities of $6.0 million for the nine months ended September 30, 2008. The increase is primarily due to a $4.0 million mortgage loan entered into in 2009, partially offset by a $2.0 million balloon payment to pay off our former mortgage loan. Also contributing to the increase in net cash provided by financing activities was a $5.5 million decrease in repurchases of common stock in 2009.

On April 6, 2009, we entered into a mortgage loan in the amount of $4.0 million related to our headquarters facility in Middletown, Rhode Island. The loan term is 10 years, with a principal amortization of 20 years, and the interest rate will be a rate per year adjusted periodically based on a defined interest period equal to the BBA Libor Rate plus 2.25 percentage points. Land, building and improvements with an approximate carrying value of $5.3 million as of September 30, 2009 secure the mortgage loan. The monthly mortgage payment is approximately $9,400 plus interest and increases in increments of approximately $1,000 each year throughout the life of the mortgage. Due to the difference in the term of the loan and amortization of the principal, a balloon payment of $2.6 million is due on April 1, 2019. The loan contains one financial covenant, a Fixed Charge Coverage Ratio, which applies in the event that our consolidated cash, cash equivalents and marketable securities balance falls below $25.0 million at any time. We were compliant with this financial covenant as of September 30, 2009. Under the mortgage loan we may prepay our outstanding loan balance subject to certain early termination charges as defined in the mortgage loan agreement. If we were to default on our mortgage loan, the land, building and improvements would be used as collateral.

Currently, we have a revolving loan agreement with a bank that provides for a maximum available credit of $15.0 million and will expire on December 31, 2011. We pay interest on any outstanding amounts at a rate equal to, at our option, BBA LIBOR Daily Floating Rate plus 1.75%, or the Eurodollar Rate plus 1.75%. The line of credit contains two financial covenants, a Leverage Ratio and a Fixed Charge Coverage Ratio, that apply in the event that our consolidated cash, cash equivalents and marketable securities balance falls below $25.0 million at any time. We were compliant with these two financial covenants throughout the nine months ended September 30, 2009. We may terminate the loan agreement prior to its full term without penalty, provided we give 30 days advance written notice to the bank. As of September 30, 2009, no borrowings were outstanding under the facility.

On November 26, 2008, our Board of Directors authorized a program to repurchase up to one million shares of our common stock. The share repurchase program is funded using our existing cash, cash equivalents, marketable securities and future cash flows. We repurchased 123,044 shares of our common stock in the nine months ended September 30, 2009 under the program at a cost of approximately $0.6 million.

On September 25, 2008, we entered into a ten-year agreement with ViaSat, Inc. to begin a global expansion of our mini-VSAT Broadband satellite communication service, including an initial purchase of three new regional satellite hubs. On October 3, 2008, we entered into a 5-year agreement with GE International Holdings, Inc. (also known as SAT-GE) to lease satellite capacity in order to provide coverage in the Pacific Ocean. In 2009, we also entered into several agreements in order to provide satellite coverage to African, Asia-Pacific, Indian Ocean, Australian and New Zealand waters. In addition to these agreements, as part of the coverage expansion, we plan to seek to acquire additional satellite capacity from Ku-band satellite operators, expend funds to seek regulatory approvals and permits, develop product enhancements in anticipation of the expansion and hire additional personnel. We anticipate these costs will be funded by cash, cash equivalents and marketable securities on hand, as well as cash flows from operations.

Table of Contents

We believe that the $41.5 million we held in cash, cash equivalents and marketable securities at September 30, 2009, together with our other working capital and cash flows from operations, will be adequate to meet planned operating and capital requirements for at least the next twelve months. However, as the need or opportunity arises, we may seek to raise additional capital through public or private sales of securities or through additional debt financing. There are no assurances that we will be able to obtain any additional funding or that such funding will be available on terms acceptable to us.

As of September 30, 2009, we had a standby letter of credit in the amount of approximately $0.2 million outstanding in support of a customer deposit. We had not entered into any other off-balance sheet commitments, guarantees, or standby repurchase obligations as of September 30, 2009.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our primary market risk exposure is in the area of foreign currency exchange risk. We are exposed to currency exchange rate fluctuations related to our subsidiary operations in Denmark. Certain transactions originating from our Danish subsidiary that are made in the Danish Krone or in Euros are reported in the U.S. dollar, the subsidiary s functional currency. For foreign currency exposures existing at September 30, 2009, a 10% unfavorable movement in the foreign exchange rates for the Krone or the Euro would not expose us to material losses in earnings or cash flows.

From time to time, we purchase foreign currency forward contracts generally having durations of no more than five months. These forward contracts are intended to offset the impact of exchange rate fluctuations on cash flows of our Danish subsidiary. Foreign currency forward contracts are recorded on the balance sheet at fair value until executed. Changes in the fair value are recognized in earnings. As of September 30, 2009, we had no foreign currency forward contracts outstanding.

The primary objective of our investment activities is to preserve principal and maintain liquidity, while at the same time maximize income. We have not entered into any instruments for trading purposes. Some of the securities that we invest in may have market risk. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities that can include commercial paper, United States treasuries, certificates of deposit, investment grade asset-backed corporate securities, money market mutual funds and government agency and non-government debt securities. As of September 30, 2009, a hypothetical 100 basis-point increase in interest rates would result in an immaterial decrease in the fair value of our investments that have maturities of greater than one year. Due to the conservative nature of our investments and the relatively short duration of their maturities, we believe interest rate risk is substantially mitigated. As of September 30, 2009, 73% of the $37.4 million classified as available-for-sale marketable securities will mature or reset within one year. Accordingly, long-term interest rate risk is not considered material. We do not invest in any financial instruments denominated in foreign currencies.

To the extent that we borrow against our variable-rate credit facility, we will be subject to interest rate risk. There were no borrowings outstanding at September 30, 2009.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act, which are designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, and that such information is accumulated and communicated to our management, including our President, Chief Executive Officer and Chairman of the Board, or CEO, and Chief Financial and Accounting Officer, or CFO, as appropriate to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our CEO and CFO, our management has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this interim report. Based on that evaluation, our CEO and CFO concluded that our disclosure controls and procedures were effective as of September 30, 2009.

Evaluation of Changes in Internal Control over Financial Reporting

Under the supervision and with the participation of our CEO and CFO, our management has evaluated our internal control over financial reporting during the third quarter of 2009. Based on that evaluation, our CEO and CFO did not identify any change in our internal control over financial reporting during the third quarter of 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we are involved in litigation incidental to the conduct of our business. In the ordinary course of business, we are a party to inquiries, legal proceedings and claims including, from time to time, disagreements with vendors and customers. We are not a party to any lawsuit or proceeding that, in our opinion, is likely to materially harm our business, results of operations, financial condition or cash flows.

ITEM 1A. Risk Factors

An investment in our common stock involves a high degree of risk. You should carefully consider the following risk factors in evaluating our business. If any of these risks, or other risks not presently known to us or that we currently believe are not significant, develops into an actual event, then our business, financial condition and results of operations could be adversely affected. If that happens, the market price of our common stock could decline.

Our revenues and results of operations have been and may continue to be adversely impacted by worldwide economic turmoil and credit tightening.

Worldwide economic conditions have experienced a significant downturn over the last two years, including slower economic activity, tightened credit markets, inflation and deflation concerns, decreased consumer confidence, reduced corporate profits, reduced or canceled capital spending, adverse business conditions and liquidity concerns. These conditions make it difficult for businesses, governments and consumers to accurately forecast and plan future activities. Governments are experiencing significant declines in tax receipts, which may cause them to curtail spending significantly or reallocate funds away from defense programs. There can be no assurances that government responses to the disruptions in the economy will remedy these problems. As a result of these and other factors, customers could slow or suspend spending on our products and services. We may also be forced to increase our allowance for doubtful accounts, which would have a negative impact on our earnings and financial condition. We cannot predict the timing, duration or ultimate impact of this downturn. We expect our business to continue to be adversely impacted by this downturn.

Our revenues and results of operations have been and may continue to be adversely impacted by the current recession or associated declines in consumer spending.

Net sales of our mobile communications products are largely generated by discretionary consumer spending, and demand for these products is likely to demonstrate slower growth or decline as a result of worsening regional and global economic conditions. Consumer spending tends to decline during recessionary periods and may decline at other times. For example, sales of our mobile satellite communications products declined approximately 37% from the nine months ended September 30, 2008 to the nine months ended September 30, 2009. Consumers may choose not to purchase our mobile communications products due to a perception that they are luxury items. As global and regional economic conditions change, including the general level of interest rates, fluctuating oil prices and demand for durable consumer products, demand for our products could be materially and adversely affected.

We have a history of variable operating results and may not be profitable in the future.

Although we generated net income during 2006, 2007, and 2008 and in twenty of the last twenty-seven fiscal quarters, at times our profitability has fluctuated significantly on both a sequential and comparable quarter-to-quarter basis during 2006, 2007 and 2008 and during the first three quarters of 2009. As of September 30, 2009, we had an accumulated deficit of $7.3 million.

Our inventory levels could require an inventory write-down if our inventory reduction and rebalancing efforts are ineffective.

Our net inventory level at December 31, 2008 increased by $6.2 million, or 66% compared to the prior year and decreased by only $0.7 million in the first nine months of 2009. The increase was largely the result of two factors. First, commencing during the second quarter of 2008 we began to build up inventory levels of fiber optic gyro materials in anticipation of large orders for remote weapon stations and MK54 torpedo programs. Second, the dramatic weakening of the RV market commencing in the first half of 2008, particularly during the second quarter, and the crisis of consumer confidence in the general economy during the second half of the year, caused precipitous declines in demand for our RV products and substantial reductions in demand for our marine consumer products. While shipments of fiber optic gyros for remote weapon stations are now underway, we anticipate that it will take several quarters to reduce other product inventories to more normal levels if the current weak level of demand continues. We currently anticipate receiving a large order for the MK54 torpedo program during the fourth quarter of 2009, but there can be no assurance that the order will not be delayed or cancelled. As of September 30, 2009 we had approximately $0.4 million of inventory, primarily made up of raw materials for military products whose utilization will be dependent upon the receipt of additional sales orders in the future. If we do not receive such sales orders, and we are unable to redeploy the components of such inventory for other product sales, we may be required to record additional write-downs to inventory which would negatively impact both gross margins and net income in the period when such write-downs are recorded. During the first nine months of 2009, we recorded an additional $1.1 million in inventory reserves in order to account for the risk of excess inventory due to weak consumer demand. However, if our future

Table of Contents

inventory reduction and rebalancing efforts are unsuccessful or take an extended period of time, we may have to consider additional, more sizeable inventory reserves or write-downs to address potential excess and obsolete inventory, or our gross margins may fall below historical levels, which would adversely affect our financial results.

Adverse economic conditions could result in financial difficulties or bankruptcy for any of our suppliers, which could adversely affect our business and results of operations.

The significant downturn in worldwide economic conditions and credit tightening could present challenges to our suppliers, which could result in disruptions to our business, increase our costs, delay shipment of our products and impair our ability to generate and recognize revenue. To address their own business challenges, our suppliers may increase prices, reduce the availability of credit, require deposits or advance payments or take other actions that may impose a burden on us. They may also reduce production capacity, slow or delay delivery of products, face challenges meeting our specifications or otherwise fail to meet our requirements. In some cases, our suppliers may face bankruptcy. We may be required to identify, qualify and engage new suppliers, which would require time and the attention of management. Any of these events could impair our ability to deliver our products to customers in a timely and cost-effective manner, cause us to breach our contractual commitments or result in the loss of customers.

Shifts in our product sales mix toward our mobile communications products may reduce our overall gross margins.

Our mobile communications products historically have had lower product gross margins than our guidance and stabilization products. During 2007 and the first three quarters of 2008, sales of our guidance and stabilization products either declined or grew at a substantially lower rate than our overall sales growth. During the fourth quarter of 2008 and the first three quarters of 2009, we experienced a significant increase in sales of our guidance and stabilization products, primarily due to an increase in our FOG product sales. A shift in our product sales mix toward mobile communications products would likely cause lower gross margins in the future.

We must increase sales of the TracPhone V7 and our mini-VSAT Broadband service in order to improve our service gross margins.

As a result of our continued build-out of the mini-VSAT Broadband network infrastructure, our cost of service sales includes certain fixed costs that do not vary with the volume of service sales. If sales of our TracPhone V7 and the mini-VSAT Broadband service do not increase as we expect or decline, our service gross margins may remain below historical levels or decline. For example, our service gross margin declined modestly from the second quarter of 2009 to the third quarter of 2009. Any such decline in service gross margins could have a material adverse effect on our net income.

Competition may limit our ability to sell our mobile communications products and guidance and stabilization products.

The mobile communications markets and defense navigation, guidance and stabilization markets in which we participate are very competitive, and we expect this competition to persist and intensify in the future. We may not be able to compete successfully against current and future competitors, which could impair our ability to sell our products. For example, improvements in the performance of lower cost gyros by competitors could potentially jeopardize sales of our fiber optic gyros.

In the guidance and stabilization markets, we compete primarily with Honeywell International Inc., Kearfott Guidance & Navigation Corporation, Northrop Grumman Corporation, Smiths Group plc, Tamam, and Fizoptica.

In the market for marine satellite TV equipment, we compete with NaviSystem Marine Electronic Systems Srl, King Controls, Cobham Sea Tel, Inc., Raymarine, Thrane & Thrane A/S and Intellian. In the market for maritime broadband service we compete with Speedcast, SeaMobile, CapRock, Schlumberger, Thrane & Thrane A/S, Ship Equip, Vizada and Stratos. In the marine market for satellite communications equipment, we compete with Cobham Sea Tel, Inc., Furuno Electric Co., Ltd., Globalstar LP, Iridium Satellite LLC, EMS and Japan Radio Company.

In the market for land mobile satellite TV equipment, we compete with King Controls, MotoSAT, TracStar Systems, Inc., Winegard Company, and Sirius Satellite Radio.

Among the factors that may affect our ability to compete in our markets are the following:

many of our primary competitors are well-established companies that could have substantially greater financial, managerial, technical, marketing, personnel and other resources than we do;

product improvements, new product developments or price reductions by competitors may weaken customer acceptance of, and reduce demand for, our products;

new technology or market trends may disrupt or displace a need for our products; and

Table of Contents

- our competitors may have lower production costs than we do, which may enable them to compete more aggressively in offering discounts and other promotions.

The emergence of a competing small maritime VSAT antenna and complementary service or other, similar service could reduce the competitive advantage we believe we currently enjoy with our 24-inch diameter TracPhone V7 antenna and integrated mini-VSAT Broadband service.

Our TracPhone V7 system offers customers a range of benefits due to its integrated design, hardware costs that are lower than existing maritime VSAT systems, and spread spectrum technology. We anticipate competition from companies like Cobham Sea Tel and MTN, both of which have previously announced their intent to offer similar systems and services. We also compete against companies like MTN and Speedcast that offer established maritime VSAT service using, in some cases, antennas 1 meter in diameter or larger. In addition, other companies could replicate the distinguishing features of our TracPhone V7, which could potentially reduce the appeal of our solution and adversely affect sales. Moreover, consumers may choose other services such as Inmarsat Fleet or FleetBroadband for their global service coverage and potentially lower hardware costs despite higher service costs and slower data rates.

Our ability to compete in the maritime airtime services market may be impaired if we are unable to complete the expansion of coverage of our mini-VSAT Broadband service to offer service around the globe or with sufficient service capacity to meet customer demand.

The TracPhone V7 and mini-VSAT Broadband service offer a range of benefits to mariners, especially in commercial markets, due to the smaller size antenna and faster, more affordable airtime. However, to support these customers, we need to complete the expansion of the coverage areas of the mini-VSAT Broadband service, which is currently offered in the north Pacific Ocean, the Americas, Caribbean, North Atlantic, Europe, the Persian Gulf, Asia-Pacific, Australia, and New Zealand waters with agreements in place to support service in the Indian Ocean and around Africa. If we are unable to reach agreement with third-party satellite providers to support the mini-VSAT Broadband service and its spread spectrum technology around South America or transponder space is is unavailable should we need to increase our capacity to meet growing demand in a given region, our ability to support vessels and aeronautical applications globally will be at risk and reduce the attractiveness of the product and service to these customers.

Customers for our fiber optic gyro products and TACNAV include the U.S. military and foreign governments, whose purchasing and delivery schedules and priorities are often unpredictable.

We sell our fiber optic gyro systems as well as vehicle navigation products to U.S. and foreign military and government customers, either directly or as a subcontractor to other manufacturers. These customers often use a competitive bidding process and have unique purchasing and delivery requirements, which often makes the timing of sales to these customers unpredictable. Factors that affect their purchasing and delivery decisions include:

- changes in modernization plans for military equipment;
- changes in tactical navigation requirements;
- global conflicts impacting troop deployment;
- priorities for current battlefield operations;
- allocation of funding for military programs;
- new military and operational doctrines that affect military equipment needs;

sales cycles that are long and difficult to predict;

shifting response time and/or delays in the approval process associated with the export licenses we must obtain prior to the international shipment of certain of our military products;

delays in military procurement schedules; and

delays in the testing and acceptance of our products, including delays resulting from changes in customer specifications.

These factors can cause substantial fluctuations in sales of fiber optic gyros and TACNAV products from period to period. For example, sales of our TACNAV products declined from 2006 to 2007, but increased from 2007 to 2008 and again from the nine months ended September 30, 2008 to the nine months ended September 30, 2009. The Obama administration and the new Congress may change defense spending priorities, either in conjunction with the decision to commence troop withdrawals from Iraq or for other reasons. Moreover, government customers and their contractors can generally cancel orders for our products for convenience or decline to exercise previously disclosed contract options. Even under firm orders with government customers, funding must usually be appropriated in the budget process in order for the government to complete the contract. The cancellation of or failure to fund orders for our products could substantially reduce our net sales and results of operations.

Table of Contents

Sales of our fiber optic gyro systems and TACNAV products generally consist of a few large orders, and the delay or cancellation of a single order could substantially reduce our net sales.

KVH products sold to customers in the defense industry are purchased through orders that can generally range in size from several hundred thousand dollars to more than one million dollars. As a result, the delay or cancellation of a single order could materially reduce our net sales and results of operations. We continue to experience unanticipated delays in defense orders, which make our revenues and operating results less predictable. Because our guidance and stabilization products typically have relatively higher product gross margins than our mobile communications products, the loss of an order for guidance and stabilization products could have a disproportionately adverse effect on our results of operations.

Only a few customers account for a substantial portion of our guidance and stabilization revenues, and the loss of any of these customers could substantially reduce our net sales.

We derive a significant portion of our guidance and stabilization revenues from a small number of customers, including the U.S. Government. The loss of business from any of these customers could substantially reduce our net sales and results of operations and could seriously harm our business. Since we are often awarded a contract as a subcontractor to a major defense supplier that is engaged in a competitive bidding process as prime contractor for a major weapons procurement program, our revenues depend significantly on the success of the prime contractors with which we align ourselves.

Our mobile satellite products currently depend on satellite services provided by third parties, and any disruption in those services could adversely affect sales.

Our satellite products include only the equipment necessary to receive satellite services; we do not broadcast satellite television programming or own the satellites to directly provide two-way satellite communications. We currently offer satellite television products compatible with the DIRECTV and DISH Network services in the United States, the ExpressVu service in Canada, the Sky Mexico service and various other regional services in other parts of the world.

We rely on Inmarsat for satellite communications services for our mini-M, Fleet and FleetBroadband compatible TracPhone products. SES AMERICOM, Eutelsat, SP-JSAT, SAT-GE, and Intelsat currently provide the satellite network to support the mini-VSAT Broadband service and our TracPhone V7.

If customers become dissatisfied with the programming, pricing, service, availability or other aspects of any of these satellite services, or if any one or more of these services becomes unavailable for any reason, we could suffer a substantial decline in sales of our satellite products. There may be no alternative service provider available in a particular geographic area, and our technology may not be compatible with that of any alternative service provider that may be available. In addition, the unexpected failure of a satellite could disrupt the availability of programming and services, which could reduce the demand for, or customer satisfaction with, our products.

We rely upon spread spectrum communications technology developed by ViaSat and fielded by third-party satellite providers to permit two-way broadband Internet via our 24-inch diameter TracPhone V7, and any disruption in the availability of this technology could adversely affect sales.

Our mini-VSAT Broadband service relies on spread spectrum technology developed with ViaSat, Inc. for use with satellite networks controlled by SES World Skies, Eutelsat, Sky Perfect-JSAT, SAT-GE, and Intelsat. Our TracPhone V7 two-way broadband satellite terminal combines our stabilized antenna technology with ViaSat s ArcLight spread spectrum mobile broadband technology, along with a new maritime version of ViaSat s ArcLight spread spectrum modem. The ArcLight technology is also integrated within the satellite hubs that support this service. Sales of the TracPhone V7 and our mini-VSAT Broadband service could be disrupted if we fail to receive approval from regulatory authorities to provide our spread spectrum service in various countries where our customers operate or if there are issues with the availability of the ArcLight maritime modems.

Investment in the global deployment of the mini-VSAT Broadband service will require significant capital investment and initial operating expenses that may not be recouped if we fail to meet the subscriber levels necessary to cover those costs on an ongoing basis.

It is our intent to invest in and deploy the mini-VSAT Broadband network on a global basis in cooperation with ViaSat under the terms of a 10-year agreement announced in July 2008. As part of the coverage expansion, we agreed to acquire satellite capacity from Ku-band satellite operators and purchased three new regional satellite hubs from ViaSat. We have also made prepayments to ViaSat on two additional regional satellite hubs. During the deployment period, we expect to see a substantial increase in costs associated with the build out of the mini-VSAT

Broadband global infrastructure and support capability. In the short term KVH and ViaSat will be covering the operational cost per transponder access until sufficient subscribers join the network and allow us to reach a breakeven point on our transponder cost, which may not occur. We currently estimate that, on average, it will require at least nine months to reach the breakeven point once the service is turned on for a new coverage region. However, should an insufficient number of subscribers activate within a region, our operations may continue below the breakeven level for a longer duration and adversely affect our operating results and cash levels.

Table of Contents

High fuel prices, high interest rates, tight credit availability and environmental concerns are adversely affecting sales of our mobile communications products.

Factors such as historically high fuel prices, interest rates, tight credit and environmental protection laws are continuing to materially and adversely affect sales or use of larger vehicles and vessels for which our mobile satellite communications products are designed. Many customers finance their purchases of these vehicles and vessels, and higher interest rates and/or tightened credit availability has reduced demand for both these vehicles and vessels and our mobile communications products. Moreover, in the current credit markets financing for these purchases has been unavailable or more difficult to obtain. The increased cost of operating these vehicles and vessels is adversely affecting and may continue to adversely affect demand for our mobile satellite communications products.

We may continue to increase the use of international suppliers to source components for our manufacturing operations, which could disrupt our business.

Although we have historically manufactured and sourced raw materials for the majority of our products in the U.S., in order for us to compete with lower priced competitive products while also improving our profitability, we have found it desirable to source raw materials and manufactured components from foreign countries such as China and Mexico. Our increased reliance on foreign manufacturing and/or raw material supply has lengthened our supply chain and increased the risk that a disruption in that supply chain could have a material adverse affect on our operations and financial performance.

We have single dedicated manufacturing facilities for each of our mobile communications and guidance and stabilization product categories, and any significant disruption to a facility could impair our ability to deliver our products.

We currently manufacture all of our mobile communications products at our headquarters in Middletown, Rhode Island, and the majority of our guidance and stabilization products at our facility in Tinley Park, Illinois. Some of our production processes are complex, and we may be unable to respond rapidly to the loss of the use of either production facility. For example, our production facilities use some specialized equipment that may take time to replace if they are damaged or become unusable for any reason. In that event, shipments would be delayed, which could result in customer or dealer dissatisfaction, loss of sales and damage to our reputation. Finally, we have only a limited capability to increase our manufacturing capacity in the short term. If short-term demand for our products exceeds our manufacturing capacity, our inability to fulfill orders in a timely manner could also lead to customer or dealer dissatisfaction, loss of sales and damage to our reputation.

We depend on sole or limited source suppliers, and any disruption in supply could impair our ability to deliver our products on time or at expected cost.

We obtain many key components for our products from third-party suppliers, and in some cases we use a single or a limited number of suppliers. Any interruption in supply could impair our ability to deliver our products until we identify and qualify a new source of supply, which could take several weeks, months or longer and could increase our costs significantly. Suppliers might change or discontinue key components, which could require us to modify our product designs. For example, we have experienced changes in the chemicals used to coat our optical fiber, which changed its characteristics and thereby necessitated design modifications. In general, we do not have written long-term supply agreements with our suppliers but instead purchase components through purchase orders, which expose us to potential price increases and termination of supply without notice or recourse. It is generally not our practice to carry significant inventories of product components, and this could magnify the impact of the loss of a supplier. If we are required to use a new source of materials or components, it could also result in unexpected manufacturing difficulties and could affect product performance and reliability.

Any failure to maintain and expand our third-party distribution relationships may limit our ability to penetrate markets for mobile communications products.

We market and sell our mobile communications products through an international network of independent retailers, chain stores and distributors, as well as to manufacturers of marine vessels and recreational vehicles. If we are unable to maintain or improve our distribution relationships, it could significantly limit our sales. In addition, our distribution partners may sell products of other companies, including competing products, and are not required to purchase minimum quantities of our products.

If we are unable to improve our existing mobile communications and guidance and stabilization products and develop new, innovative products, our sales and market share may decline.

The markets for mobile communications products and guidance and stabilization products are each characterized by rapid technological change, frequent new product innovations, changes in customer requirements and expectations and evolving industry standards. If we fail to make innovations in our existing products and reduce the costs of our products, our market share may decline. Products using new technologies, or emerging industry standards, could render our products obsolete. If our competitors successfully introduce new or enhanced products that eliminate technological advantages our products may have in a market or otherwise outperform our products, or are perceived by consumers as doing so, we may be unable to compete successfully in the markets affected by these changes.

Table of Contents

If we cannot effectively manage changes in our rate of growth, our business may suffer.

We have previously expanded our operations to pursue existing and potential market opportunities. This growth placed a strain on our personnel, management, financial and other resources. More recently, our mobile communications revenue have declined in response to economic conditions, weak consumer demand and other factors and our guidance and stabilization revenue has increased dramatically. If, in the future, we grow more rapidly than we anticipate and fail to manage that growth properly, we may incur unnecessary expenses, and the efficiency of our operations may decline. If we are unable to adjust our operating expenses on a timely basis in response to changes in revenue cycles, our results of operations may be harmed. To manage changes in our rate of growth effectively, we must, among other things:

- match our manufacturing facilities and capacity to demand for our products in a timely manner;
- successfully attract, train, motivate and manage appropriate numbers of employees for manufacturing, sales and customer support activities;
- effectively manage our inventory and working capital; and
- improve the efficiencies within our operating, administrative, financial and accounting systems, and our procedures and controls.

We may be unable to hire and retain the skilled personnel we need to expand our operations.

To meet our growth objectives, we must attract and retain highly skilled technical, operational, managerial and sales and marketing personnel. If we fail to attract and retain the necessary personnel, we may be unable to achieve our business objectives and may lose our competitive position, which could lead to a significant decline in net sales. We face significant competition for these skilled professionals from other companies, research and academic institutions, government entities and other organizations.

Our success depends on the services of our executive officers and key employees.

Our future success depends to a significant degree on the skills and efforts of Martin Kits van Heyningen, our co-founder, President, Chief Executive Officer, and Chairman of the Board. If we lost the services of Mr. Kits van Heyningen, our business and operating results could be seriously harmed. We also depend on the ability of our other executive officers and members of senior management to work effectively as a team. None of our senior management or other key personnel is bound by an employment agreement. The loss of one or more of our executive officers or senior management members could impair our ability to manage our business effectively.

Our international business operations expose us to a number of difficulties in coordinating our activities abroad and in dealing with multiple regulatory environments.

Historically, sales to customers outside the United States and Canada have accounted for a significant portion of our net sales. We have only one foreign sales office, which is located in Denmark, and we otherwise support our international sales from our operations in the United States. Our limited operations in foreign countries may impair our ability to compete successfully in international markets and to meet the service and support needs of our customers in countries where we have no infrastructure. We are subject to a number of risks associated with our international business activities, which may increase our costs and require significant management attention. These risks include:

- technical challenges we may face in adapting our mobile communication products to function with different satellite services and technology in use in various regions around the world;
- satisfaction of international regulatory requirements and delays and costs associated with procurement of any necessary licenses or permits;

restrictions on the sale of certain guidance and stabilization products to foreign military and government customers;

increased costs of providing customer support in multiple languages;

potentially adverse tax consequences, including restrictions on the repatriation of earnings;

protectionist laws and business practices that favor local competitors, which could slow our growth in international markets;

potentially longer sales cycles, which could slow our revenue growth from international sales;

potentially longer accounts receivable payment cycles and difficulties in collecting accounts receivable;

losses arising from foreign currency exchange rate fluctuations; and

economic and political instability in some international markets.

Table of Contents

Exports of certain guidance and stabilization products are subject to the International Traffic in Arms Regulations and require a license from the U.S. Department of State prior to shipment.

We must comply with the United States Export Administration Regulations and the International Traffic in Arms Regulations, or ITAR. Certain of our products have military or strategic applications and are on the munitions list of the ITAR and require an individual validated license in order to be exported to certain jurisdictions. Any changes in export regulations may further restrict the export of our products, and we may cease to be able to procure export licenses for our products under existing regulations. The length of time required by the licensing process can vary, potentially delaying the shipment of products and the recognition of the corresponding revenue. Any restriction on the export of a product line or any amount of our products could cause a significant reduction in net sales.

Our business may suffer if we cannot protect our proprietary technology.

Our ability to compete depends significantly upon our patents, our source code and our other proprietary technology. The steps we have taken to protect our technology may be inadequate to prevent others from using what we regard as our technology to compete with us. Our patents could be challenged, invalidated or circumvented, and the rights we have under our patents could provide no competitive advantages. Existing trade secrets, copyright and trademark laws offer only limited protection. In addition, the laws of some foreign countries do not protect our proprietary technology to the same extent as the laws of the United States, which could increase the likelihood of misappropriation. Furthermore, other companies could independently develop similar or superior technology without violating our intellectual property rights. Any misappropriation of our technology or the development of competing technology could seriously harm our competitive position, which could lead to a substantial reduction in net sales.

If we resort to legal proceedings to enforce our intellectual property rights, the proceedings could be burdensome, disruptive and expensive, distract the attention of management, and there can be no assurance that we would prevail.

Also, we have delivered certain technical data and information to the U.S. government under procurement contracts, and it may have unlimited rights to use that technical data and information. There can be no assurance that the U.S. government will not authorize others to use that data and information to compete with us.

Claims by others that we infringe their intellectual property rights could harm our business and financial condition.

Our industries are characterized by the existence of a large number of patents and frequent claims and related litigation regarding patent and other intellectual property rights. We cannot be certain that our products do not and will not infringe issued patents, patents that may be issued in the future, or other intellectual property rights of others.

We do not generally conduct exhaustive patent searches to determine whether the technology used in our products infringes patents held by third parties. In addition, product development is inherently uncertain in a rapidly evolving technological environment in which there may be numerous patent applications pending, many of which are confidential when filed, with regard to similar technologies.

From time to time we have faced claims by third parties that our products or technology infringe their patents or other intellectual property rights, and we may face similar claims in the future. Any claim of infringement could cause us to incur substantial costs defending against the claim, even if the claim is invalid, and could distract the attention of our management. If any of our products are found to violate third-party proprietary rights, we may be required to pay substantial damages. In addition, we may be required to re-engineer our products or obtain licenses from third parties to continue to offer our products. Any efforts to re-engineer our products or obtain licenses on commercially reasonable terms may not be successful, which would prevent us from selling our products, and, in any case, could substantially increase our costs and have a material adverse effect on our business, financial condition and results of operations.

Fluctuations in our quarterly net sales and results of operations could depress the market price of our common stock.

We have at times experienced significant fluctuations in our net sales and results of operations from one quarter to the next. Our future net sales and results of operations could vary significantly from quarter to quarter due to a number of factors, many of which are outside our control. Accordingly, you should not rely on quarter-to-quarter comparisons of our results of operations as an indication of future performance. It is possible that our net sales or results of operations in a quarter will fall below the expectations of securities analysts or investors. If this occurs, the market price of our common stock could fall significantly. Our results of operations in any quarter can fluctuate for many reasons, including:

changes in demand for our mobile communications products and guidance and stabilization products;

the timing and size of individual orders from military customers;

the mix of products we sell;

Table of Contents

- our ability to manufacture, test and deliver products in a timely and cost-effective manner, including the availability and timely delivery of components and subassemblies from our suppliers;
- our success in winning competitions for orders;
- the timing of new product introductions by us or our competitors;
- expense incurred in pursuing acquisitions, such as during the third quarter of 2006;
- market and competitive pricing pressures;
- general economic climate; and
- seasonality of pleasure boat and recreational vehicle usage.

A large portion of our expenses, including expenses for facilities, equipment, and personnel, are relatively fixed. Accordingly, if our net sales decline or do not grow as much as we anticipate, we might be unable to maintain or improve our operating margins. Any failure to achieve anticipated net sales could therefore significantly harm our operating results for a particular fiscal period.

Our tax planning strategy involves assumptions that may cause our annual provision for income tax expense or benefit to fluctuate materially. Moreover, our tax planning strategy is based upon our ability to sell our manufacturing and corporate headquarters facility located in Middletown, Rhode Island, as may be necessary.

We rely upon a tax planning strategy to support the realizability of certain of our deferred tax assets. The strategy represents an action that we ordinarily would not take, but would take, if necessary, to realize an estimated $3.3 million in U.S. deferred tax assets. The strategy depends upon our ability to sell our Middletown, Rhode Island headquarters facility in order to generate taxable income for the purpose of utilizing our U.S. net operating tax loss carry-forwards before they expire. Our estimate of the taxable income that would result from any such sale, and therefore the supportable deferred tax asset value, is based upon the difference between the property s estimated fair market value and our tax basis. Accordingly, the estimated net realizable value of our deferred tax asset is highly correlated to property values in and around the Middletown, Rhode Island area and therefore subject to changes in property value and or assumptions used in the valuation process. Changes in these property values or assumptions could cause us to revise our estimates and to record significant increases or decreases to our deferred tax assets during the year that could materially affect our results of operations.

The market price of our common stock may be volatile.

Our stock price has historically been volatile. From January 1, 2006 to September 30, 2009, the trading price of our common stock ranged from $14.48 to $2.81. Many factors may cause the market price of our common stock to fluctuate, including:

- variations in our quarterly results of operations;
- the introduction of new products by us or our competitors;
- changing needs of military customers;

- changes in estimates of our performance or recommendations by securities analysts;
- the hiring or departure of key personnel;
- acquisitions or strategic alliances involving us or our competitors;
- market conditions in our industries; and
- the global macroeconomic and geopolitical environment.

In addition, the stock market can experience extreme price and volume fluctuations. Major stock market indices experienced dramatic declines in 2008 and in the first quarter of 2009. These fluctuations are often unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the market price of our common stock. When the market price of a company s stock drops significantly, stockholders often institute securities litigation against that company. Any such litigation could cause us to incur significant expenses defending against the claim, divert the time and attention of our management and result in significant damages.

Table of Contents

Acquisitions may disrupt our operations or adversely affect our results.

We evaluate strategic acquisition opportunities to acquire other businesses as they arise. The expenses we incur evaluating and pursuing acquisitions could have a material adverse effect on our results of operations. If we acquire a business, we may be unable to manage it profitably or successfully integrate its operations with our own. Moreover, we may be unable to realize the financial, operational and other benefits we anticipate from any acquisition. Competition for acquisition opportunities could increase the price we pay for businesses we acquire and could reduce the number of potential acquisition targets. Further, our approach to acquisitions may involve a number of special financial and business risks, such as:

- charges related to any potential acquisition from which we may withdraw;
- diversion of our management s time, attention, and resources;
- loss of key acquired personnel;
- increased costs to improve or coordinate managerial, operational, financial, and administrative systems, including compliance with the Sarbanes-Oxley Act of 2002;
- dilutive issuances of equity securities;
- the assumption of legal liabilities; and
- amortization of acquired intangible assets.

Our charter and by-laws and Delaware law may deter takeovers.

Our certificate of incorporation, by-laws and Delaware law contain provisions that could have an anti-takeover effect and discourage, delay or prevent a change in control or an acquisition that many stockholders may find attractive. These provisions may also discourage proxy contests and make it more difficult for our stockholders to take some corporate actions, including the election of directors. These provisions relate to:

- the ability of our Board of Directors to issue preferred stock, and determine its terms, without a stockholder vote;
- the classification of our Board of Directors, which effectively prevents stockholders from electing a majority of the directors at any one annual meeting of stockholders;
- the limitation that directors may be removed only for cause by the affirmative vote of the holders of two-thirds of our shares of capital stock entitled to vote;
- the prohibition against stockholder actions by written consent;

the inability of stockholders to call a special meeting of stockholders; and

advance notice requirements for stockholder proposals and director nominations.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On November 26, 2008, our Board of Directors authorized a program to repurchase up to one million shares of our common stock. The repurchase program is funded using our existing cash, cash equivalents, marketable securities and future cash flows. Under the repurchase program, at management s discretion, we may repurchase shares on the open market from time to time, in privately negotiated transactions or block transactions, or through an accelerated repurchase agreement. The timing of such repurchases depends on availability of shares, price, market conditions, alternative uses of capital, and applicable regulatory requirements. The program may be modified, suspended or terminated at any time without prior notice. The repurchase program has no expiration date. There were no other repurchase programs outstanding during the three months ended September 30, 2009, and no repurchase programs expired during the period.

Period	Total Number of Shares Purchased	Average Cost Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs
July 1, 2009 July 31, 2009		$		798,676
August 1, 2009 August 31, 2009				798,676
September 1, 2009 September 30, 2009				798,676
Total		$		

30

Table of Contents

ITEM 6. EXHIBITS

Exhibits:

Exhibit No.	Description	Filed with this Form 10-Q	Incorporated by Reference Form	Filing Date	Exhibit No.
3.1	Amended and Restated Certificate of Incorporation		S-1	February 16, 1996	3.3
3.2	Certificate of Amendment of Certificate of Incorporation		S-3	November 26, 2003	4.2
3.3	Amended, Restated and Corrected Bylaws of KVH Industries, Inc.		8-K	July 31, 2007	3
4.1	Specimen certificate for the common stock		S-1/A	March 22, 1996	4.1
10.24	Loan Agreement dated as of April 6, 2009 between Bank of America, N. A. and KVH Industries, Inc.		8-K	April 8, 2009	10.1
31.1	Rule 13a-14(a)/15d-14(a) certification of principal executive officer	X			
31.2	Rule 13a-14(a)/15d-14(a) certification of principal financial officer	X			
32.1	Section 1350 certification of principal executive officer	X			
32.2	Section 1350 certification of principal financial officer	X			

Table of Contents

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: November 5, 2009

KVH Industries, Inc.

By: /s/ Patrick J. Spratt

Patrick J. Spratt

(Duly Authorized Officer and Chief Financial and Accounting Officer)

32

Table of Contents

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32.2	Section 1350 certification of principal financial officer	X			