

COGNEX CORP  
Form 10-Q  
November 01, 2010

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

(Mark One)

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended October 3, 2010 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 001-34218**

**COGNEX CORPORATION**

(Exact name of registrant as specified in its charter)

**Massachusetts**  
(State or other  
jurisdiction of  
incorporation or  
organization)

**04-2713778**  
(I.R.S. Employer  
Identification No.)

**One Vision Drive  
Natick, Massachusetts 01760-2059  
(508) 650-3000**

(Address, including zip code, and telephone number, including area code, of principal executive offices)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  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

As of October 3, 2010, there were 40,035,145 shares of Common Stock, \$.002 par value, of the registrant outstanding.



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CONSOLIDATED STATEMENTS OF OPERATIONS**

(In thousands, except per share amounts)

	<b>Three-months Ended October</b>		<b>Nine-months Ended October</b>	
	<b>3, 2010 (unaudited)</b>	<b>October 4, 2009</b>	<b>3, 2010 (unaudited)</b>	<b>October 4, 2009</b>
Revenue				
Product	\$ <b>69,288</b>	\$ 37,429	\$ <b>190,968</b>	\$ 112,185
Service	<b>5,705</b>	3,749	<b>14,803</b>	12,248
	<b>74,993</b>	41,178	<b>205,771</b>	124,433
Cost of revenue				
Product	<b>15,537</b>	9,589	<b>44,362</b>	31,893
Service	<b>3,376</b>	2,449	<b>9,209</b>	8,585
	<b>18,913</b>	12,038	<b>53,571</b>	40,478
Gross margin				
Product	<b>53,751</b>	27,840	<b>146,606</b>	80,292
Service	<b>2,329</b>	1,300	<b>5,594</b>	3,663
	<b>56,080</b>	29,140	<b>152,200</b>	83,955
Research, development, and engineering expenses	<b>7,961</b>	6,756	<b>24,140</b>	23,295
Selling, general, and administrative expenses	<b>25,857</b>	21,281	<b>75,217</b>	69,826
Restructuring charges (Note 14)	<b>(13)</b>	223	<b>75</b>	4,258
Operating income (loss)	<b>22,275</b>	880	<b>52,768</b>	(13,424)
Foreign currency gain (loss)	<b>102</b>	1	<b>(71)</b>	(813)
Investment income	<b>384</b>	419	<b>949</b>	1,875
Other income (expense)	<b>(129)</b>	(158)	<b>(531)</b>	1,517
Income (loss) before income tax expense (benefit)	<b>22,632</b>	1,142	<b>53,115</b>	(10,845)
Income tax expense (benefit)	<b>4,487</b>	(3,359)	<b>11,498</b>	(5,517)
Net income (loss)	\$ <b>18,145</b>	\$ 4,501	\$ <b>41,617</b>	\$ (5,328)

Earnings (loss) per weighted-average common and common-equivalent share:

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Basic	\$	<b>0.46</b>	\$	0.11	\$	<b>1.05</b>	\$	(0.13)
Diluted	\$	<b>0.45</b>	\$	0.11	\$	<b>1.05</b>	\$	(0.13)

Weighted-average common and common-equivalent shares  
outstanding:

Basic	<b>39,729</b>	39,662	<b>39,693</b>	39,658
Diluted	<b>39,917</b>	39,666	<b>39,792</b>	39,658

Cash dividends per common share	\$	<b>0.06</b>	\$	0.05	\$	<b>0.17</b>	\$	0.25
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The accompanying notes are an integral part of these consolidated financial statements.

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**COGNEX CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**  
(In thousands)

	<b>October 3, 2010 (unaudited)</b>	December 31, 2009
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 38,213	\$ 119,831
Short-term investments	113,516	55,563
Accounts receivable, less reserves of \$1,318 and \$1,358 in 2010 and 2009, respectively	47,202	30,964
Inventories	23,867	16,832
Deferred income taxes	7,951	7,693
Prepaid expenses and other current assets	26,640	18,471
 Total current assets	 257,389	 249,354
Long-term investments	88,590	26,633
Property, plant, and equipment, net	28,316	28,576
Deferred income taxes	17,149	14,643
Intangible assets, net	24,480	28,337
Goodwill	82,313	82,604
Other assets	1,501	9,722
	\$ 499,738	\$ 439,869
 <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 6,336	\$ 4,959
Accrued expenses	26,492	18,811
Accrued income taxes	10,299	2
Deferred revenue and customer deposits	16,234	14,908
 Total current liabilities	 59,361	 38,680
Reserve for income taxes	4,954	6,741
Commitments and contingencies (Note 8)		
Shareholders' equity:	80	79

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Common stock, \$.002 par value

Authorized: 140,000 shares, issued: 40,035 and 39,665 shares in 2010 and 2009,  
respectively

Additional paid-in capital

**78,347** 69,271

Retained earnings

**363,329** 328,459

Accumulated other comprehensive loss

**(6,333)** (3,361)

Total shareholders equity

**435,423** 394,448

**\$ 499,738** \$ 439,869

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

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**COGNEX CORPORATION**  
**CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY AND COMPREHENSIVE INCOME**  
(In thousands)

	<b>Common Stock</b>		<b>Additional</b>		<b>Accumulated</b>		<b>Total</b>
	<b>Shares</b>	<b>Par Value</b>	<b>Paid-in Capital</b>	<b>Retained Earnings</b>	<b>Other Comprehensive Loss</b>	<b>Comprehensive Income</b>	<b>Shareholders Equity</b>
Balance as of December 31, 2009	39,665	\$ 79	\$ 69,271	\$ 328,459	\$ (3,361)		\$ 394,448
Issuance of common stock under stock option plans	370	1	7,323	-	-		7,324
Stock-based compensation expense	-	-	1,672	-	-		1,672
Excess tax benefit from stock option exercises	-	-	81	-	-		81
Payment of dividends	-	-	-	(6,747)	-		(6,747)
Comprehensive income:							
Net income	-	-	-	41,617	-	\$ 41,617	41,617
Net unrealized loss on available-for-sale investments, net of tax of \$92	-	-	-	-	(314)	(314)	(314)
Foreign currency translation adjustment, net of tax benefit of \$122	-	-	-	-	(2,658)	(2,658)	(2,658)
Comprehensive income						<b>\$ 38,645</b>	
Balance as of October 3, 2010 (unaudited)	<b>40,035</b>	<b>\$ 80</b>	<b>\$ 78,347</b>	<b>\$ 363,329</b>	<b>\$ (6,333)</b>		<b>\$ 435,423</b>

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

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**COGNEX CORPORATION**  
**CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**  
(In thousands)

	<b>Nine-months Ended</b>	
	<b>October 3, 2010</b>	<b>October 4, 2009</b>
	<b>(unaudited)</b>	
Cash flows from operating activities:		
Net income (loss)	\$ 41,617	\$ (5,328)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Stock-based compensation expense	1,672	5,088
Depreciation and amortization	9,201	8,269
Intangible asset impairment charge (Note 6)	-	1,000
Provision for excess and obsolete inventory	1,361	3,033
Excess tax benefit from stock option exercises	(81)	467
Change in deferred income taxes	(2,397)	(2,651)
Change in operating assets and liabilities	(4,625)	(9,456)
Net cash provided by operating activities	<b>46,748</b>	422
Cash flows from investing activities:		
Purchase of investments	(178,080)	(24,045)
Maturity and sale of investments	58,676	37,970
Purchase of property, plant, and equipment	(3,307)	(4,512)
Cash paid for business acquisition (Note 17)	-	(4,500)
Cash received related to disposition	315	-
Net cash provided by (used in) investing activities	<b>(122,396)</b>	4,913
Cash flows from financing activities:		
Issuance of common stock under stock option plans	7,324	80
Stock option buyback	(83)	-
Payment of dividends	(6,747)	(9,914)
Excess tax benefit from stock option exercises	81	(467)
Net cash provided by (used in) financing activities	<b>575</b>	(10,301)
Effect of foreign exchange rate changes on cash	<b>(6,545)</b>	4,990
Net increase (decrease) in cash and cash equivalents	<b>(81,618)</b>	24
Cash and cash equivalents at beginning of period	<b>119,831</b>	127,138
Cash and cash equivalents at end of period	<b>\$ 38,213</b>	\$ 127,162

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

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**COGNEX CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**NOTE 1: Summary of Significant Accounting Policies**

As permitted by the rules of the Securities and Exchange Commission applicable to Quarterly Reports on Form 10-Q, these notes are condensed and do not contain all disclosures required by generally accepted accounting principles. Reference should be made to the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

In the opinion of the management of Cognex Corporation (the Company), the accompanying consolidated unaudited financial statements contain all adjustments, consisting of normal, recurring adjustments, restructuring charges (Note 14), business acquisitions (Note 17), and intangible asset impairment charges (Note 6), necessary to present fairly the Company's financial position as of October 3, 2010, and the results of its operations for the three-month and nine-month periods ended October 3, 2010 and October 4, 2009, and changes in shareholders' equity and cash flows for the periods presented.

The results disclosed in the Consolidated Statements of Operations for the three-month and nine-month periods ended October 3, 2010 are not necessarily indicative of the results to be expected for the full year.

**NOTE 2: Revenue Recognition**

The Company's product revenue is derived from the sale of machine vision systems, which can take the form of hardware with embedded software or software-only, and related accessories. The Company also generates revenue by providing maintenance and support, training, consulting, and installation services to its customers. Certain of the Company's arrangements include multiple deliverables that provide the customer with a combination of products or services. In order to recognize revenue, the Company requires that a signed customer contract or purchase order is received, the fee from the arrangement is fixed or determinable, and collection of the resulting receivable is probable. Assuming that these criteria have been met, product revenue is recognized upon delivery, revenue from maintenance and support programs is recognized ratably over the program period, revenue from training and consulting services is recognized over the period that the services are provided, and revenue from installation services is recognized when the customer has signed off that the installation is complete.

The Company has historically applied the software revenue recognition rules as prescribed by Accounting Standards Codification (ASC) Subtopic 985-605. In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) Number 2009-14, Certain Revenue Arrangements That Include Software Elements, which amended ASC Subtopic 985-605. This ASU removes tangible products containing software components and non-software components that function together to deliver the product's essential functionality from the scope of the software revenue recognition rules. In the case of the Company's hardware products with embedded software, the Company has determined that the hardware and software components function together to deliver the product's essential functionality, and therefore, the revenue from the sale of these products no longer falls within the scope of the software revenue recognition rules. Revenue from the sale of software-only products remains within the scope of the software revenue recognition rules. Maintenance and support, training, consulting, and installation services no longer fall within the scope of the software revenue recognition rules, except when they are sold with and relate to a software-only product. Revenue recognition for products that no longer fall under the scope of the software revenue recognition rules is similar to that for other tangible products. ASU Number 2009-13, Multiple-Deliverable Revenue Arrangements, which amended ASC Topic 605 and was also issued in October 2009, is applicable for multiple-deliverable revenue arrangements. ASU 2009-13 allows companies to allocate revenue in a multiple-deliverable arrangement in a manner that better reflects the transaction's economics. ASU 2009-13 and 2009-14 are effective for revenue arrangements entered into or materially modified in the Company's fiscal year 2011, however early adoption is permitted and the Company has elected to adopt the provisions of these amendments as of January 1, 2010.

Under the software revenue recognition rules, the fee from a multiple-deliverable arrangement is allocated to each of the undelivered elements based upon vendor-specific objective evidence (VSOE), which is limited to the price charged when the same deliverable is sold separately, with the residual value from the arrangement allocated to the delivered element. The portion of the fee that is allocated to each deliverable is then recognized as revenue when the

criteria for revenue recognition are met with respect to that deliverable. If VSOE does not exist for all of the undelivered elements, then all revenue from the

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**COGNEX CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

arrangement is typically deferred until all elements have been delivered to the customer. All revenue arrangements negotiated prior to January 1, 2010 and the sale of all software-only products and associated services have been accounted for under this guidance during the nine-month period ended October 3, 2010.

Under the revenue recognition rules for tangible products as amended by ASU 2009-13, the fee from a multiple-deliverable arrangement is allocated to each of the deliverables based upon their relative selling prices as determined by a selling-price hierarchy. A deliverable in an arrangement qualifies as a separate unit of accounting if the delivered item has value to the customer on a stand-alone basis. A delivered item that does not qualify as a separate unit of accounting is combined with the other undelivered items in the arrangement and revenue is recognized for those combined deliverables as a single unit of accounting. The selling price used for each deliverable is based upon VSOE if available, third-party evidence (TPE) if VSOE is not available, and best estimate of selling price (BESP) if neither VSOE nor TPE are available. TPE is the price of the Company's or any competitor's largely interchangeable products or services in stand-alone sales to similarly situated customers. BESP is the price at which the Company would sell the deliverable if it were sold regularly on a stand-alone basis, considering market conditions and entity-specific factors. All revenue arrangements negotiated after January 1, 2010, excluding the sale of all software-only products and associated services, have been accounted for under this guidance during the nine-month period ended October 3, 2010.

The selling prices used in the relative selling price allocation method (1) for certain of the Company's services are based upon VSOE, (2) for third-party accessories available from other vendors are based upon TPE, and (3) for hardware products with embedded software, custom accessories, and services for which VSOE does not exist are based upon BESP. The Company does not believe TPE exists for these products and services because they are differentiated from competing products and services in terms of functionality and performance and there are no competing products or services that are largely interchangeable. For the Company's Modular Vision Systems Division (MVSD), BESP has been established for each product line within each major region, and for the Company's Surface Inspection Systems Division (SISD), BESP has been established for each major industry. Management establishes BESP with consideration for market conditions, such as the impact of competition and geographic considerations, and entity-specific factors, such as the cost of the product and the division's profit objectives. Management believes that BESP is reflective of reasonable pricing of that deliverable as if priced on a stand-alone basis.

Since all of the Company's revenue prior to the adoption of ASU 2009-14 fell within the scope of the software revenue recognition rules and the Company has only established VSOE for certain services, revenue in a multiple-deliverable arrangement involving products was frequently deferred until the last item was delivered. The adoption of ASU 2009-13 and 2009-14 results in earlier revenue recognition in multiple-deliverable arrangements involving the Company's hardware products with embedded software because revenue can be recognized for each of these deliverables based upon their relative selling prices as defined above. In the three-month and nine-month periods ended October 3, 2010, revenue was \$926,000 and \$3,284,000 higher, respectively, than it would have been if ASU 2009-13 and 2009-14 had not been adopted.

**NOTE 3: Fair Value Measurements**

**Financial Assets and Liabilities that are Measured at Fair Value on a Recurring Basis**

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The following table summarizes the financial assets and liabilities measured at fair value on a recurring basis as of October 3, 2010 (in thousands):

	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>
Assets:		
Short-term investments	\$ -	\$ 113,516
Long-term investments	-	82,415
Currency forward contracts	334	-
Liabilities:		
Currency forward contracts	13	-

The Company's investments are reported at fair value based upon model-driven valuations in which all significant inputs are observable or can be derived from or corroborated by observable market data for substantially the full term of the asset, and are therefore classified as Level 2 investments. The Company's investments are priced daily by a large, third-party pricing service. The service maintains regular contact with market makers, brokers, dealers, and analysts to gather information on market movement, direction, trends, and other specific data. They use this information to structure yield curves for various types of debt securities and arrive at the current day's valuations. The Company did not record an other-than-temporary impairment charge during the nine-month period ended October 3, 2010.

The Company's forward contracts are reported at fair value based upon quoted U.S. Dollar foreign currency exchange rates, and are therefore classified as Level 1.

**Financial Assets that are Measured at Fair Value on a Non-recurring Basis**

The Company has an interest in a limited partnership, which is accounted for using the cost method and is measured at fair value on a non-recurring basis. Management monitors the carrying value of this investment compared to its fair value to determine if an other-than-temporary impairment has occurred. If a decline in fair value is considered to be other-than-temporary, an impairment charge would be recorded to reduce the carrying value of the asset to its fair value. The fair value of this investment is based upon valuations of the partnership's investments as determined by the General Partner. The portfolio consists of securities of public and private companies, and consequently, inputs used in the fair value calculation are classified as Level 3. The Company did not record an other-than-temporary impairment charge during the nine-month period ended October 3, 2010.

**Non-financial Assets that are Measured at Fair Value on a Non-recurring Basis**

Non-financial assets such as goodwill, intangible assets, and property, plant, and equipment are measured at fair value only when an impairment loss is recognized. The Company did not record an impairment charge related to these assets during the nine-month period ended October 3, 2010.

**NOTE 4: Cash, Cash Equivalents, and Investments**

Cash, cash equivalents, and investments consisted of the following (in thousands):

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