# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION
**WASHINGTON, DC 20549**

# FORM 10-Q

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

**For the quarterly period ended April 2, 2011**

**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: 0-23081**

# FARO TECHNOLOGIES, INC.
**(Exact name of Registrant as specified in its charter)**

| | |
|---|---|
| **Florida**<br>**(State or other Jurisdiction of Incorporation or Organization)** | **59-3157093**<br>**(I.R.S. Employer Identification No.)** |
| **250 Technology Park, Lake Mary, Florida**<br>**(Address of Principal Executive Offices)** | **32746**<br>**(Zip Code)** |

**Registrant's Telephone Number, including area code: (407) 333-9911**

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

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

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

| | | | |
|---|---|---|---|
| Large accelerated filer | ☐ | Accelerated filer | ☒ |
| Non-accelerated filer | ☐ 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 ☒

There were outstanding 16,338,708 shares of the registrant's common stock as of April 22, 2011.

**FARO TECHNOLOGIES, INC.**

Quarterly Report on Form 10-Q
Quarter Ended April 2, 2011

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**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**FARO TECHNOLOGIES, INC. AND SUBSIDIARIES**
CONSOLIDATED BALANCE SHEETS

| (in thousands, except share data) | April 2, 2011 (unaudited) | December 31, 2010 |
|---|---|---|
| **ASSETS** | | |
| Current Assets: | | |
| Cash and cash equivalents | $ 53,282 | $ 50,722 |
| Short-term investments | 64,987 | 64,986 |
| Accounts receivable, net | 47,533 | 51,862 |
| Inventories, net | 36,932 | 28,242 |
| Deferred income taxes, net | 4,161 | 4,455 |
| Prepaid expenses and other current assets | 8,821 | 8,045 |
| Total current assets | 215,716 | 208,312 |
| Property and Equipment: | | |
| Machinery and equipment | 26,267 | 24,840 |
| Furniture and fixtures | 6,121 | 5,700 |
| Leasehold improvements | 9,977 | 9,682 |
| Property and equipment at cost | 42,365 | 40,222 |
| Less: accumulated depreciation and amortization | (26,631) | (24,982) |
| Property and equipment, net | 15,734 | 15,240 |
| Goodwill | 19,781 | 19,015 |
| Intangible assets, net | 7,363 | 7,204 |
| Service inventory | 13,795 | 13,726 |
| Deferred income taxes, net | 2,640 | 2,522 |
| Total Assets | $275,029 | $ 266,019 |
| **LIABILITIES AND SHAREHOLDERS’ EQUITY** | | |
| Current Liabilities: | | |
| Accounts payable | $ 10,199 | $ 12,025 |
| Accrued liabilities | 15,113 | 15,208 |
| Income taxes payable | 93 | 1,138 |
| Current portion of unearned service revenues | 14,437 | 13,357 |
| Customer deposits | 4,522 | 3,679 |
| Current portion of obligations under capital leases | 67 | 91 |
| Total current liabilities | 44,431 | 45,498 |
| Unearned service revenues - less current portion | 7,569 | 6,758 |
| Deferred tax liability, net | 1,184 | 1,161 |
| Obligations under capital leases - less current portion | 144 | 125 |
| Total Liabilities | 53,328 | 53,542 |
| Commitments and contingencies - See Note R | | |
| Shareholders’ Equity: | | |
| Common stock - par value $.001, 50,000,000 shares authorized; 17,018,943 and 16,894,374 issued; 16,338,708 and 16,214,139 outstanding, respectively | 17 | 17 |
| Additional paid-in capital | 159,719 | 156,310 |
| Retained earnings | 61,227 | 57,983 |
| Accumulated other comprehensive income | 9,813 | 7,242 |
| Common stock in treasury, at cost - 680,235 shares | (9,075) | (9,075) |
| Total Shareholders’ Equity | 221,701 | 212,477 |
| Total Liabilities and Shareholders’ Equity | $275,029 | $ 266,019 |

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

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**FARO TECHNOLOGIES, INC. AND SUBSIDIARIES**
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

| (in thousands, except share and per share data) | Three Months Ended April 2, 2011 | Three Months Ended April 3, 2010 |
|---|---|---|
| SALES | | |
| Product | $ 42,958 | $ 33,938 |
| Service | 9,608 | 8,331 |
| Total Sales | 52,566 | 42,269 |
| COST OF SALES | | |
| Product | 15,573 | 11,275 |
| Service | 6,721 | 5,603 |
| Total Cost of Sales (exclusive of depreciation and amortization, shown separately below) | 22,294 | 16,878 |
| GROSS PROFIT | 30,272 | 25,391 |
| OPERATING EXPENSES: | | |
| Selling | 14,152 | 11,235 |
| General and administrative | 6,590 | 6,247 |
| Depreciation and amortization | 1,614 | 1,540 |
| Research and development | 3,632 | 2,989 |
| Total operating expenses | 25,988 | 22,011 |
| INCOME FROM OPERATIONS | 4,284 | 3,380 |
| OTHER (INCOME) EXPENSE | | |
| Interest income | (26) | (19) |
| Other (income) expense, net | (129) | 505 |
| Interest expense | 29 | 27 |
| INCOME BEFORE INCOME TAX EXPENSE | 4,410 | 2,867 |
| INCOME TAX EXPENSE | 1,167 | 803 |
| NET INCOME | $ 3,243 | $ 2,064 |
| NET INCOME PER SHARE - BASIC | $ 0.20 | $ 0.13 |
| NET INCOME PER SHARE - DILUTED | $ 0.20 | $ 0.13 |
| Weighted average shares - Basic | 16,253,121 | 16,124,886 |
| Weighted average shares - Diluted | 16,598,797 | 16,267,231 |

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

**FARO TECHNOLOGIES, INC. AND SUBSIDIARIES**
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

| (in thousands) | Three Months Ended April 2, 2011 | Three Months Ended April 3, 2010 |
|---|---|---|
| CASH FLOWS FROM: | | |
| OPERATING ACTIVITIES: | | |
| Net income | $ 3,243 | $ 2,064 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,614 | 1,540 |
| Compensation for stock options and restricted stock units | 642 | 564 |
| Provision for bad debts | 329 | 348 |
| Deferred income tax expense | 291 | 34 |
| Change in operating assets and liabilities: | | |
| Decrease (increase) in: | | |
| Accounts receivable | 5,412 | 506 |
| Inventories, net | (7,525) | (2,748) |
| Prepaid expenses and other current assets | (509) | (3,039) |
| Income tax benefit from exercise of stock options | (237) | (6) |
| Increase (decrease) in: | | |
| Accounts payable and accrued liabilities | (2,447) | 2,199 |
| Income taxes payable | (742) | (234) |
| Customer deposits | 762 | (540) |
| Unearned service revenues | 1,389 | 348 |
| Net cash provided by operating activities | 2,222 | 1,036 |
| INVESTING ACTIVITIES: | | |
| Purchases of property and equipment | (1,183) | (613) |
| Payments for intangible assets | (294) | (205) |
| Net cash used in investing activities | (1,477) | (818) |
| FINANCING ACTIVITIES: | | |
| Proceeds from notes payable | — | 2,490 |
| Payments on capital leases | (22) | (19) |
| Income tax benefit from exercise of stock options | 237 | 6 |
| Proceeds from issuance of stock, net | 2,529 | 275 |
| Net cash provided by financing activities | 2,744 | 2,752 |
| EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS | (929) | 283 |
| INCREASE IN CASH AND CASH EQUIVALENTS | 2,560 | 3,253 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 50,722 | 35,078 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | $ 53,282 | $ 38,331 |

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

**FARO TECHNOLOGIES, INC. AND SUBSIDIARIES**
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Three Months Ended April 2, 2011 and April 3, 2010
(Unaudited)
(in thousands, except share and per share data, or as otherwise noted)

NOTE A – DESCRIPTION OF BUSINESS

FARO Technologies, Inc. and subsidiaries (collectively the "Company" or "FARO") design, develop, manufacture, market and support software-based three-dimensional measurement devices for manufacturing, industrial, building construction and forensic applications. The Company's principal products include the FaroArm, FARO Laser Scan Arm and FARO Gage, all articulated electromechanical measuring devices, and the FARO Laser Tracker ION, FARO Focus 3D and FARO 3D Imager AMP, both laser-based measuring devices. Primary markets for the Company's products include automobile, aerospace, heavy equipment, light manufacturing and machine shops. The Company sells the vast majority of its products through a direct sales force located in many of the world's largest industrialized countries.

NOTE B – PRINCIPLES OF CONSOLIDATION

The consolidated financial statements of the Company include the accounts of FARO Technologies, Inc. and all of the Company's subsidiaries. All intercompany transactions and balances have been eliminated. The financial statements of the Company's foreign subsidiaries are translated into U.S. dollars using exchange rates in effect at period-end for assets and liabilities and average exchange rates during each reporting period for results of operations. Adjustments resulting from financial statement translations are reflected as a separate component of accumulated other comprehensive income.

NOTE C – BASIS OF PRESENTATION

The consolidated financial statements of the Company include all normal recurring accruals and adjustments considered necessary by management for their fair presentation in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates. The consolidated results of operations for the three months ended April 2, 2011 are not necessarily indicative of results that may be expected for the year ending December 31, 2011 or any future period.

The information included in this Quarterly Report on Form 10-Q, including the interim consolidated financial statements and the accompanying notes, should be read in conjunction with the audited consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

NOTE D – RECLASSIFICATIONS

From time to time the Company may reclassify certain amounts to conform to the current period presentation.

NOTE E – IMPACT OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In October 2009, the FASB issued Accounting Standards Update, or ASU No. 2009-13, *Multiple-Delivery Revenue Arrangements*. ASU 2009-13 establishes the accounting and reporting guidance for arrangements, including multiple revenue-generating activities, and provides amendments to the criteria for separating deliverables and measuring and allocating arrangement consideration to one or more units of accounting. The amendments of ASU 2009-13 also establish a selling price hierarchy for determining the selling price of a deliverable. Significantly enhanced disclosures are also required by ASU 2009-13 to provide information about a vendor's multiple-deliverable revenue arrangements, including information about the nature and terms, significant deliverables, and its performance within arrangements. The amendments also require a reporting company to provide information about the significant judgments made and changes to those judgments and about how the application of the relative selling-price method affects the timing or amount of revenue recognition. The amendments in ASU 2009-13 are effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with early application permitted. The Company implemented this new standard on January 1, 2011 and the adoption of ASU 2009-13 did not have a material impact on its consolidated financial statements nor is it expected to have a material impact in future periods.

In January 2010, the FASB issued ASU 2010-6, *Improving Disclosures About Fair Value Measurements* or ASU 2010-6, which requires reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements, including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information on purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair-value measurements. ASU 2010-6 is effective for annual reporting periods beginning after December 15, 2009, except for Level 3 reconciliation disclosures, which are effective for annual periods beginning after December 15, 2010. The adoption of ASU 2010-6 did not have a material impact on the Company's consolidated financial statements nor is it expected to have a material impact in future periods.

In July 2010, the FASB issued guidance to enhance disclosures about the credit quality of a creditor's financing receivables and the adequacy of its allowance for credit losses. The amended guidance is effective for period-end balances beginning with the first interim or annual reporting period ending on or after December 15, 2010. The amended guidance is effective for activity during a reporting period beginning with the first interim or annual reporting period beginning on or after December 15, 2010. The adoption of the amended guidance had no impact on the Company's disclosure or on its consolidated financial statements.

In October 2009, the FASB issued ASU 2009-13, which amends ASC Topic 605, "Revenue Recognition". The guidance relates to the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting and modifies the manner in which the transaction consideration is allocated across the individual deliverables. Also, the guidance expands the disclosure requirements for revenue arrangements with multiple deliverables. ASU 2009-13 was effective beginning January 1, 2011, and may be applied retrospectively for all periods presented or prospectively to arrangements entered into or materially modified after the adoption date. The adoption of ASU 2009-13 did not have a material impact on the Company's consolidated financial statements.

In December 2010, the Financial Accounting Standards Board ("FASB") issued accounting standard ASU 2010-28, "Intangibles-Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts (a consensus of the FASB Emerging Issues Task Force)." ASU 2010-28 provides amendments to Topic 350 that modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. As a result, goodwill impairments may be reported sooner than under current practice. ASU 2010-28 is effective for fiscal years and interim periods within those years, beginning after December 15, 2010, with early adoption not permitted. The adoption of ASU 2010-28 did not have a material impact on our consolidated results of operation and financial condition.

NOTE F – SHARE-BASED COMPENSATION

Share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized over the service period, typically the vesting period. The vesting period for the share-based compensation awarded by the Company is generally three years. The Company uses the Black-Scholes option pricing model to determine the fair value of stock option grants. The Company uses the closing market price of its common stock on the date of grant to determine the fair value of restricted stock and restricted stock units.

The Company used the following assumptions for the Black-Scholes option-pricing model to determine the fair value of options granted during the three months ended April 2, 2011 and April 3, 2010:

| | For the Three Months Ended | |
|---|---|---|
| | April 2, 2011 | April 3, 2010 |
| Risk-free interest rate | 1.55% and 1.69% | 1.85% |
| Expected dividend yield | 0% | 0% |
| Expected option life | 4 years | 4 years |
| Expected volatility | 48.7% | 43.5% and 46.5% |
| Weighted-average expected volatility | 48.7% | 46.5% |

Historical information was the primary basis for the selection of the expected dividend yield, expected volatility and the expected lives of the options. The risk-free interest rate was based on yields of U.S. zero coupon issues and U.S. Treasury issues, with a term equal to the expected life of the option being valued.

The Company recorded total share-based compensation expense of $671 and $587 for the three months ended April 2, 2011 and April 3, 2010, respectively.

A summary of stock option activity and weighted average exercise prices for the three months ended April 2, 2011 follows:

| | Options | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value as of April 2, 2011 |
|---|---|---|---|---|
| Outstanding at January 1, 2011 | 1,098,859 | $ 21.37 | | |
| Granted | 257,261 | 35.85 | | |
| Forfeited | (2,469) | 23.43 | | |
| Exercised | (121,005) | 20.92 | | |
| Outstanding at April 2, 2011 | 1,232,646 | $ 24.42 | 5.0 | $ 19,354 |
| Options exercisable at April 2, 2011 | 783,235 | $ 21.55 | 4.1 | $ 14,548 |

The weighted-average grant-date fair value of the stock options granted during the three months ended April 2, 2011 and April 3, 2010 was $14.15 and $9.29 per option, respectively. The total intrinsic value of stock options exercised during the three months ended April 2, 2011 and April 3, 2010 was $1.85 million and $0.1 million, respectively. The fair value of stock options vested during the three months ended April 2, 2011 and April 3, 2010 was $1.6 million and $1.7 million, respectively.

The following table summarizes the restricted stock and restricted stock unit activity and weighted average grant-date fair values for the three months ended April 2, 2011:

| | Shares | Weighted-Average Grant Date Fair Value |
|---|---|---|
| Non-vested at beginning of period | 40,313 | $ 23.53 |
| Granted | 6,642 | 35.90 |
| Forfeited | (624) | 18.96 |
| Vested | (5,479) | 21.24 |
| Non-vested at April 2, 2011 | 40,852 | $ 25.91 |

As of April 2, 2011, there was $5.4 million of total unrecognized stock-based compensation expense related to non-vested stock-based compensation arrangements. The expense is expected to be recognized over a weighted average period of 2.5 years.

NOTE G – SUPPLEMENTAL CASH FLOW INFORMATION

Selected cash payments and non-cash activity were as follows:

| | Three Months Ended April 2, 2011 | Three Months Ended April 3, 2010 |
|---|---|---|
| Cash paid for interest | $ 11 | $ 27 |
| Cash paid for income taxes | $ 1,270 | $ 2,534 |

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## NOTE H – CASH AND CASH EQUIVALENTS

The Company considers cash on hand and all short-term, highly liquid investments that have maturities of three months or less at the time of purchase to be cash and cash equivalents.

## NOTE I – SHORT-TERM INVESTMENTS

Short-term investments at April 2, 2011 and December 31, 2010 include U.S. Treasury Bills totaling $65.0 million that mature through September 15, 2011. The interest rate on the U.S. Treasury bills is less than one percent. The investments are classified as held-to-maturity and recorded at cost. The fair value of the U.S. Treasury Bills at April 2, 2011 approximated cost.

## NOTE J – ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

| | As of April 2, 2011 | As of December 31, 2010 |
|---|---|---|
| Accounts receivable | $ 52,494 | $ 56,562 |
| Allowance for doubtful accounts | (4,962) | (4,700) |
| Total | $ 47,532 | $ 51,862 |

## NOTE K – INVENTORIES

Inventories consist of the following:

| | As of April 2, 2011 | As of December 31, 2010 |
|---|---|---|
| Raw materials | $ 20,061 | $ 12,743 |
| Finished goods | 4,960 | 3,441 |
| Sales demonstration inventory | 14,459 | 14,662 |
| Reserve for excess and obsolete | (2,548) | (2,604) |
| Inventory | $ 36,932 | $ 28,242 |
| Service inventory | $ 13,795 | $ 13,726 |

NOTE L – EARNINGS PER SHARE

A reconciliation of the number of common shares used in the calculation of basic and diluted earnings per share (EPS) is presented below:

| | Three Months Ended | | | |
|---|---|---|---|---|
| | April 2, 2011 | | April 3, 2010 | |
| | Shares | Per-Share Amount | Shares | Per-Share Amount |
| Basic EPS | 16,253,121 | $ 0.20 | 16,124,886 | $ 0.13 |
| Effect of dilutive securities | 345,676 | — | 142,345 | — |
| Diluted EPS | 16,598,797 | $ 0.20 | 16,267,231 | $ 0.13 |

The effect of 253,961 and 718,325 securities were not included for the three months ended April 2, 2011 and April 3, 2010, respectively, as they were antidilutive.

NOTE M – ACCRUED LIABILITIES

Accrued liabilities consist of the following:

| | As of April 2, 2011 | As of December 31, 2010 |
|---|---|---|
| Accrued compensation and benefits | $ 7,863 | $ 8,303 |
| Accrued warranties | 1,827 | 1,857 |
| Professional and legal fees | 1,080 | 1,000 |
| Other accrued liabilities | 4,343 | 4,048 |
| | $15,113 | $ 15,208 |

NOTE N – INCOME TAXES

Total deferred tax assets for the Company's foreign subsidiaries relating to net operating loss carryforwards were $14.6 million and $14.1 million at April 2, 2011 and December 31, 2010, respectively. The related valuation allowance was $11.6 million and $11.1 million at April 2, 2011 and December 31, 2010, respectively. The Company's effective tax rate was 26.5% for the three months ended April 2, 2011 and 28.0% for the three months ended April 3, 2010. The Company's tax rate continues to be lower than the statutory tax rate in the United States primarily as a result of favorable tax rates in foreign jurisdictions. Significant judgment is required in determining the Company's worldwide provision for income taxes. In the ordinary course of a global business, there are many transactions for which the ultimate tax outcome is uncertain. The Company reviews its tax contingencies on a regular basis and makes appropriate accruals as necessary.

The effective income tax rate for 2011 and 2010 includes a reduction in the statutory corporate tax rates for the Company's operations in Switzerland. The favorable tax rate ruling requires the Company to maintain a certain level of manufacturing operations in Switzerland. The aggregate dollar effect of this favorable tax rate was approximately $0.0 million, or $0.0 per share, in the three month period ended April 2, 2011, and $0.1 million, or $0.01 per share, in the three month period ended April 3, 2010.

In 2005, the Company opened a regional headquarters and began to manufacture its products in Singapore. In the third quarter of 2006, the Company received confirmation of a tax holiday for its operations from the Singapore Economic Development Board for a period of four years commencing January 1, 2006 and an additional six year extension at favorable tax rates subject to certain terms and conditions including employment, spending, and capital investment. The aggregate dollar effect of this favorable tax rate was approximately $0.1 million, or $0.01 per share, during the three month period ended April 2, 2011, and $0.3 million, or $0.01 per share, in the three month period ended April 3, 2010.

NOTE O – FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company's financial instruments include cash and cash equivalents, short-term investments, accounts receivable and accounts payable and accruals. The carrying amounts of such financial instruments approximate their fair value due to the short-term nature of these instruments.

NOTE P – SEGMENT REPORTING

The Company has three reportable segments based upon geographic regions: Americas, Europe/Africa and Asia Pacific. The Company does not allocate corporate expenses to Europe/Africa or Asia Pacific regions. These corporate expenses are included in the Americas region. The Company does not incur R&D expenses in its Asia Pacific region.

The Company develops, manufactures, markets, supports and sells Computer-Aided Design ("CAD")-based quality assurance products integrated with CAD-based inspection and statistical process control software in each of these regions. These activities represent approximately 99% of consolidated sales. The Company evaluates performance and allocates resources based upon profitable growth and assets deployed.

The following table presents information about the Company's reportable segments:

| | Three Months Ended April 2, 2011 | Three Months Ended April 3, 2010 |
|---|---|---|
| **Americas Region** | | |
| Net sales to external customers | $ 19,327 | $ 16,278 |
| Operating income (loss) | 467 | (267) |
| Long-lived assets | 22,645 | 22,620 |
| Capital expenditures | 885 | 91 |
| Total assets | 140,772 | 126,877 |
| **Europe/Africa Region** | | |
| Net sales to external customers | $ 19,022 | $ 16,113 |
| Operating (loss) income | (308) | 1,409 |
| Long-lived assets | 18,203 | 16,903 |
| Capital expenditures | 270 | 302 |
| Total assets | 87,547 | 73,621 |
| **Asia Pacific Region** | | |
| Net sales to external customers | $ 14,217 | $ 9,878 |
| Operating income | 4,125 | 2,238 |
| Long-lived assets | 2,030 | 1,791 |
| Capital expenditures | 287 | 168 |
| Total assets | 46,710 | 38,292 |
| **Totals** | | |
| Net sales to external customers | $ 52,566 | $ 42,269 |
| Operating income | 4,284 | 3,380 |
| Long-lived assets | 42,878 | 41,314 |
| Capital expenditures | 1,442 | 561 |
| Total assets | 275,029 | 238,790 |

The geographical sales information presented above represents sales to customers located in each respective region, whereas the long-lived assets information represents assets held in the respective regions. There were no customers that individually accounted for 10% or more of total revenue in each of the periods presented above.

NOTE Q – COMPREHENSIVE INCOME (LOSS)

| | Three Months Ended April 2, 2011 | Three Months Ended April 3, 2010 |
|---|---|---|
| NET INCOME | $ 3,243 | $ 2,064 |
| OTHER COMPREHENSIVE INCOME (LOSS) | | |
| Currency translation adjustments | 2,571 | (3,174) |
| COMPREHENSIVE INCOME (LOSS) | $ 5,814 | $ (1,110) |

Other comprehensive income (loss) results from the effect of currency translation adjustments on the investments in (capitalization of) foreign subsidiaries, combined with their accumulated earnings or losses.

NOTE R – COMMITMENTS AND CONTINGENCIES

***Leases***—The Company is a party to leases arising in the normal course of business that expire on or before 2019. Total obligations under these leases are approximately $5.0 million for 2011.

***Purchase Commitments***—The Company enters into purchase commitments for products and services in the ordinary course of business. These purchases generally cover production requirements for 60 to 90 days. As of April 2, 2011, the Company does not have any long-term commitments for purchases.

***Patent Matters*** — On July 11, 2008, Metris USA, Inc. and its affiliates, Metris N.V., Metris IPR N.V. and 3-D Scanners Ltd., filed a complaint against the Company for patent infringement in the U.S. District Court for the District of Massachusetts (the "Massachusetts Court") concerning U.S. Patent Nos. 6,611,617 and 7,313,264 (hereinafter, the "patents-in-suit"). Following an acquisition by Nikon Corporation in late 2009, Metris USA, Inc. subsequently changed its name to Nikon Metrology, Inc., Metris N.V. changed its name to Nikon Metrology NV, and Metris IPR N.V. was dissolved and merged into Nikon Metrology NV. We refer to each of Nikon Metrology, Inc., Nikon Metrology NV, and 3-D Scanners Ltd. as "Plaintiffs" or "Nikon".

The Company responded to the complaint with counterclaims alleging that the patents-in-suit, which are generally directed to laser scanning devices, are invalid, non-infringed, and unenforceable due to fraud during prosecution of the patents in the U.S. Patent and Trademark Office. On August 31, 2009, the Massachusetts Court granted the Company's motion to add counterclaims and defenses for violation of federal and state antitrust and unfair competition laws based on the alleged knowing assertion of invalid and fraudulent patents. The Company also filed an amended counterclaim to add the Plaintiff's parent company, Nikon Corporation, as a counterclaim defendant.

On January 29, 2010, the Company filed a motion for summary judgment that the patents-in-suit are unenforceable due to inequitable conduct during patent prosecution. Evidentiary hearings on the issue of inequitable conduct commenced on July 19, 2010, and concluded on October 22, 2010. Post-trial briefing concluded on December 10, 2010. The Court has not yet issued a decision. On July 14, 2010, the Company filed a motion for summary judgment of non-infringement of both patents-in-suit. In addition, during the first quarter of 2010, Nikon served a supplemental interrogatory answer revising its alleged date of conception of the patents-in-suit to an earlier date. The Company filed a motion to strike the supplemental interrogatory answer, and the parties are waiting for the hearing date on the motion. On August 31, 2010, Nikon filed a motion for summary judgment against the Company's counterclaims for antitrust violations and unfair trade practices. The Company filed its opposition on October 12, 2010.

On February 22, 2011, the Court denied Nikon's Motion for Summary Judgment on the Company's counterclaims for anti-trust violations and unfair trade practices without prejudice. On February 24, 2011, the Court denied the Company's Motion for Summary Judgment of non-infringement without prejudice. The parties may renew their respective motions for summary judgment after the Court issues a decision on inequitable conduct, if necessary. No further motions for summary judgment are expected to be filed. A mediation hearing held on February 18, 2011 to settle the matter was unsuccessful.

The Company believes that it does not infringe the patents-in-suit and/or that the patents-in-suit are invalid and unenforceable. The Company does not anticipate this lawsuit will have a material impact on the Company; however, the outcome is difficult to predict, and an adverse determination could have a material impact on the Company's business, financial condition or results of operations.

Other than the litigation mentioned above, the Company is not involved in any other legal proceedings, other than routine litigation arising in the normal course of business, none of which the Company believes will have a material adverse effect on the Company's business, financial condition or results of operations.

NOTE S – LINES OF CREDIT

On July 11, 2006, the Company entered into a loan agreement providing for an available line of credit of $30.0 million, which was most recently amended on June 18, 2009. Loans under the Amended and Restated Loan Agreement, as amended, bear interest at the rate of LIBOR plus a fixed percentage between 2.25% - 2.50% and require the Company to maintain a minimum cash balance and tangible net worth measured at the end of the Company's fiscal quarters. As of April 2, 2011, the Company was in compliance with all of the covenants under the Amended and Restated Loan Agreement, as amended. The term of the Amended and Restated Loan Agreement, as amended, extends to March 31, 2012. The Company has not drawn on this line of credit.

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

*The following information should be read in conjunction with the Consolidated Financial Statements, including the notes thereto, included elsewhere in this Form 10-Q, and Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.*

FARO Technologies, Inc. ("FARO", the "Company", "us", "we", or "our") has made "forward-looking statements" in this report (within the meaning of the Private Securities Litigation Reform Act of 1995). Statements that are not historical facts or that describe our plans, beliefs, goals, intentions, objectives, projections, expectations, assumptions, strategies, or future events are forward-looking statements. In addition, words such as "may," "will," "believe," "plan," "should," "could," "seek," "expect," "anticipate," "intend," "estimate," "project" and similar words, or discussions of our strategy or other intentions identify forward-looking statements. Specifically, this Quarterly Report on Form 10-Q contains, among others, forward-looking statements regarding:

- the Company's ability to achieve and maintain profitability;
- the impact of fluctuations in exchange rates;
- the effect of estimates and assumptions with respect to critical accounting policies and the impact of the adoption of recently issued accounting pronouncements;
- the impact of changes in technologies on the competitiveness of the Company's products or their components;
- the magnitude of increased warranty costs from new product introductions and enhancements to existing products;
- the sufficiency of the Company's plants to meet its manufacturing requirements;
- the outcome of litigation and its effect on the Company's business, financial condition or results of operations;
- the continuation of the Company's share repurchase program;
- the sufficiency of the Company's working capital, cash flow from operations, and credit facility to fund its long-term liquidity requirements;
- the impact of geographic changes in the manufacturing or sales of the Company's products on its tax rate; and
- the imposition of penalties against the Company for failure to comply with its continuing obligations with respect to the FCPA Matter.

Forward-looking statements are not guarantees of future performance and are subject to a number of known and unknown risks, uncertainties, and other factors that could cause actual results to differ materially from those expressed or implied by such forward-looking statements. Consequently, undue reliance should not be placed on these forward-looking statements. The Company does not intend to update any forward-looking statements, whether as a result of new information, future events, or otherwise, unless otherwise required by law. Important factors that could cause actual results to differ materially from those contemplated in such forward-looking statements include, among others, the following:

- economic downturn in the manufacturing industry or the domestic and international economies in the regions of the world where the Company operates;
- the Company's inability to further penetrate its customer base and target markets;
- development by others of new or improved products, processes or technologies that make the Company's products obsolete or less competitive;

- the Company’s inability to maintain its technological advantage by developing new products and enhancing its existing products;
- the Company’s inability to successfully identify and acquire target companies or achieve expected benefits from acquisitions that are consummated;
- the cyclical nature of the industries of the Company’s customers and material adverse changes in its customers’ access to liquidity and capital;
- the market potential for the computer-aided measurement (“CAM2”) market and the potential adoption rate for the Company’s products are difficult to quantify and predict;
- the inability to protect the Company’s patents and other proprietary rights in the United States and foreign countries;
- fluctuations in the Company’s annual and quarterly operating results and the inability to achieve its financial operating targets as a result of a number of factors including, without limitation (i) litigation and regulatory action brought against the Company, (ii) quality issues with its products, (iii) excess or obsolete inventory, (iv) raw material price fluctuations, (v) expansion of the Company’s manufacturing capability and other inflationary pressures, (vi) the size and timing of customer orders, (vii) the amount of time that it takes to fulfill orders and ship the Company’s products, (viii) the length of the Company’s sales cycle to new customers and the time and expense incurred in further penetrating its existing customer base, (ix) increases in operating expenses required for product development and new product marketing, (x) costs associated with new product introductions, such as product development, marketing, assembly line start-up costs and low introductory period production volumes, (xi) the timing and market acceptance of new products and product enhancements, (xii) customer order deferrals in anticipation of new products and product enhancements, (xiii) the Company’s success in expanding its sales and marketing programs, (xiv) start-up costs associated with opening new sales offices outside of the United States, (xv) fluctuations in revenue without proportionate adjustments in fixed costs, (xvi) the efficiencies achieved in managing inventories and fixed assets, (xvii) investments in potential acquisitions or strategic sales, product or other initiatives, (xviii) shrinkage or other inventory losses due to product obsolescence, scrap or material price changes, (xix) adverse changes in the manufacturing industry and general economic conditions, (xx) compliance with government regulations including health, safety, and environmental matters, (xxi) the ultimate costs of the Company’s monitoring obligations in respect of the Foreign Corrupt Practices Act (“FCPA”) matter; and (xxii) other factors noted herein;
- changes in gross margins due to changing product mix of products sold and the different gross margins on different products;
- the Company’s inability to successfully maintain the requirements of Restriction of use of Hazardous Substances (“RoHS”) and Waste Electrical and Electronic Equipment (“WEEE”) compliance in its products;
- the inability of the Company’s products to displace traditional measurement devices and attain broad market acceptance;
- the impact of competitive products and pricing in the CAM2 market and the broader market for measurement and inspection devices;
- the effects of increased competition as a result of recent consolidation in the CAM2 market;
- risks associated with expanding international operations, such as fluctuations in currency exchange rates, difficulties in staffing and managing foreign operations, political and economic instability, compliance with import and export regulations, and the burdens and potential exposure of complying with a wide variety of U.S. and foreign laws and labor practices;
- the loss of the Company’s Chief Executive Officer or other key personnel;
- difficulties in recruiting research and development engineers and application engineers;
- the failure to effectively manage the effects of the Company’s growth;
- variations in the effective income tax rate and the difficulty in predicting the tax rate on a quarterly and annual basis;

- the loss of key suppliers and the inability to find sufficient alternative suppliers in a reasonable period or on commercially reasonable terms; and

other risks and uncertainties discussed in Part I, Item 1A. Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

**Overview**

The Company designs, develops, manufactures, markets and supports portable, software driven, 3-D measurement and imaging systems that are used in a broad range of manufacturing, industrial, building construction and forensic applications. The Company's FaroArm®, FARO Laser ScanArm® and FARO Gage articulated measuring devices, the FARO Laser Tracker ION™, the FARO Focus$^{3D}$, the FARO 3D Imager AMP and their companion CAM2® software, provide for Computer-Aided Design, or CAD-based inspection and/or factory-level statistical process control, and high-density surveying. Together, these products integrate the measurement, quality inspection, and reverse engineering functions with CAD software to improve productivity, enhance product quality and decrease rework and scrap in the manufacturing process. The Company uses the acronym "CAM2" for this process, which stands for computer-aided measurement. As of April 2, 2011, the Company's products have been purchased by approximately 11,000 customers worldwide, ranging from small machine shops to such large manufacturing and industrial companies as Audi, Bell Helicopter, Boeing, British Aerospace, Caterpillar, Daimler Chrysler, General Electric, General Motors, Honda, Johnson Controls, Komatsu America International, Lockheed Martin, Nissan, Siemens and Volkswagen, among many others.

The Company derives revenues primarily from the sale of its FaroArm, FARO Laser ScanArm, FARO Gage, FARO Laser Tracker ION and FARO Focus$^{3D}$ measurement equipment, and their related multi-faceted software. Revenue related to these products is generally recognized upon shipment. In addition, the Company sells one and three-year extended warranties and training and technology consulting services relating to its products. The Company recognizes the revenue from extended warranties on a straight-line basis. The Company also receives royalties from licensing agreements for its historical medical technology and recognizes the revenue from these royalties as licensees use the technology.

The Company operates in international markets throughout the world. It maintains sales offices in China, France, Germany, Great Britain, Italy, India, Japan, Malaysia, Netherlands, Poland, Spain, Singapore and Vietnam. The Company manages and reports its global sales in three regions: the Americas, Europe/Africa and Asia/Pacific. In the first quarter of 2011, 36.8% of the Company's sales were in the Americas compared to 38.5% in the first three months of 2010, 36.2% were in the Europe/Africa region compared to 38.1% in the first quarter of 2010 and 27.0% were in the Asia/Pacific region compared to 23.4% in the same prior year period. In the first quarter of 2011, new order bookings increased $16.1 million, or 40.5%, to $55.9 million from $39.8 million in the prior year period. New orders in the first quarter of 2011 increased $3.8 million, or 22.9%, in the Americas to $20.4 million from $16.6 million in the prior year period. New orders increased $7.7 million, or 56.2%, to $21.4 million in Europe/Africa from $13.7 million in the first quarter of 2010. In Asia/Pacific, new orders increased $4.6 million, or 48.4% to $14.1 million from $9.5 million in the first quarter of 2010.

The Company manufactures its FaroArm, FARO Gage, FARO 3D Imager AMP, and FARO Laser Tracker ION products in the Company's manufacturing facilities located in Florida and Pennsylvania for customer orders from the Americas, in its manufacturing facility located in Switzerland for customer orders from the Europe/Africa region and in its manufacturing facility located in Singapore for customer orders from the Asia/Pacific region. The Company manufactures its FARO Focus$^{3D}$ product in its facility located in Stuttgart, Germany. The Company expects all its existing plants to have the production capacity necessary to support its volume requirements through 2011.

The Company accounts for wholly owned foreign subsidiaries in the currency of the respective foreign jurisdiction; therefore, fluctuations in exchange rates may have an impact on inter-company accounts reflected in the Company's consolidated financial statements. The Company is aware of the availability of off-balance sheet financial instruments to hedge exposure to foreign currency exchange rates, including cross-currency swaps, forward contracts and foreign currency options (see Foreign Exchange Exposure below). However, it does not regularly use such instruments, and none were utilized in 2010 or the three months ended April 2, 2011.

The Company incurred a net loss in each of the four quarters of fiscal 2009, primarily as a result of a decrease in product sales, due to the deterioration of the global economy. Prior to the first quarter of 2009, the Company had a history of sales and earnings growth and 26 consecutive profitable quarters through December 31, 2008. The Company was profitable in each quarter in the year ended December 31, 2010. Its historical sales and earnings growth were the result of a number of factors, including: continuing market demand for and acceptance of the Company's products; increased sales activity in part through additional sales staff worldwide, new products and product enhancements such as the FARO Gage and Laser Scanner; and the effect of acquisitions. However, the Company's historical financial performance is not indicative of its future financial performance.

FCPA Update

As previously reported by the Company, the Company conducted an internal investigation in 2006 into certain payments made by its China subsidiary that may have violated the Foreign Corrupt Practices Act or the FCPA and other applicable laws, which we refer to as the FCPA Matter, and entered into settlement agreements and documents with the SEC and the U.S. Department of Justice or the "DOJ", in 2008 related to the FCPA Matter. Under the terms of the agreements with the SEC and the DOJ, the Company assumed a two-year monitoring obligation and other continuing obligations with respect to compliance with the FCPA and other laws, including full cooperation with the U.S. government and the adoption of a compliance code containing specific provisions intended to prevent violations of the FCPA. During the second quarter of 2010, the Company, in conjunction with the SEC and the DOJ, completed the selection of the FCPA monitor. As a result of delays in the SEC/DOJ approval of the monitor, the Company is currently still in the monitoring period, which otherwise would have already expired. The Company is cooperating with the monitor as the monitor implements a work plan to assess the Company's compliance with the requirements of the settlement agreements. Failure to comply with any continuing obligations with respect to the FCPA Matter could result in the SEC and the DOJ seeking to impose penalties against the Company in the future.

**Results of Operations**

**Three Months Ended April 2, 2011 Compared to the Three Months Ended April 3, 2010**

Sales increased by $10.3 million, or 24.4%, to $52.6 million in the three months ended April 2, 2011 from $42.3 million for the three months ended April 3, 2010. This increase resulted primarily due to an increase in unit sales in all regions related to the continuing recovery in the global economy. Product sales increased by $9.0 million, or 26.6%, to $43.0 million for the three months ended April 2, 2011 from $34.0 million for the first quarter of 2010. Service revenue increased by $1.3 million, or 15.3%, to $9.6 million for the three months ended April 2, 2011 from $8.3 million in the same period during the prior year, primarily due to an increase in warranty revenue.

Sales in the Americas region increased $3.0 million, or 18.4%, to $19.3 million for the three months ended April 2, 2011 from $16.3 million in the three months ended April 3, 2010. Product sales in the Americas region increased by $2.6 million, or 20.6%, to $15.2 million for the three months ended April 2, 2011 from $12.6 million in the first quarter of the prior year. Service revenue in the Americas region increased by $0.4 million, or 10.8%, to $4.1 million for the three months ended April 2, 2011 from $3.7 million in the same period during the prior year, primarily due to an increase in Customer Service revenue.

Sales in the Europe/Africa region increased $3.0 million, or 18.6%, to $19.1 million for the three months ended April 2, 2011 from $16.1 million in the three months ended April 3, 2010. Product sales in the Europe/Africa region increased by $2.3 million, or 17.7%, to $15.3 million for the three months ended April 2, 2011 from $13.0 million in the first quarter of the prior year. Service revenue in the Europe/Africa region increased $0.7 million, or 22.6%, to $3.8 million for the three months ended April 2, 2011 from $3.1 million in the same period during the prior year.

Sales in the Asia/Pacific region increased $4.3 million, or 43.4%, to $14.2 million for the three months ended April 2, 2011 from $9.9 million in the three months ended April 3, 2010. Product sales in the Asia/Pacific region increased by $4.1 million, or 48.8%, to $12.5 million for the three months ended April 2, 2011 from $8.4 million in the first quarter of the prior year. Service revenue in the Asia/Pacific region increased by $0.2 million, or 13.3%, to $1.7 million for the three months ended April 2, 2011 from $1.5 million in the same period during the prior year.

Gross profit increased by $4.9 million, or 19.2%, to $30.3 million for the three months ended April 2, 2011 from $25.4 million for the three months ended April 3, 2010. Gross margin decreased to 57.6% for the three months ended April 2, 2011 from 60.1% for the three months ended April 3, 2010. The decrease in gross margin is primarily due to a decrease in gross margin from product sales to 63.7% in the three months ended April 2, 2011 from 66.8% for the three months ended April 3, 2010, primarily as a result of a change in the sales mix resulting from an increase in sales of product lines with lower gross margins. Gross margin from service revenues decreased to 30.0% in the three months ended April 2, 2011 from 32.7% for the three months ended April 3, 2010, primarily due to an increase in customer service costs.

Selling expenses increased by $3.0 million, or 26.0%, to $14.2 million for the three months ended April 2, 2011 from $11.2 million for three months ended April 3, 2010. This increase was primarily due to an increase in compensation expense of $2.1 million, an increase in marketing and advertising costs of $0.3 million and an increase in travel related costs of $0.7 million.

Worldwide sales and marketing headcount increased by 25, or 8.4%, to 323 at April 2, 2011 from 298 at April 3, 2010. Regionally, the Company's sales and marketing headcount increased by 7, or 8.7%, to 87 from 80 for the Americas; increased by 4, or 3.6%, in Europe/Africa to 117 from 113; and increased by 14, or 13.3%, in Asia/Pacific to 119 from 105.

As a percentage of sales, selling expenses increased to 26.9% of sales in the three months ended April 2, 2011 from 26.6% in the three months ended April 3, 2010. Regionally, selling expenses were 22.9% of sales in the Americas for the quarter, compared to 22.1% of sales in the first quarter of 2010; 32.4% of sales for Europe/Africa compared to 29.2% of sales from the same period in the prior year; and 25.1% of sales compared to 29.6% of sales for Asia/Pacific from the same period in the prior year.

General and administrative expenses increased by $0.4 million, or 5.5%, to $6.6 million for the three months ended April 2, 2011 from $6.2 million for the three months ended April 3, 2010, primarily due to an increase in compensation costs of $0.6 million, offset by a decrease in professional and legal fees of $0.2 million.

Depreciation and amortization expenses increased slightly to $1.6 million for the three months ended April 2, 2011 from $1.5 million for the three months ended April 3, 2010.

Research and development expenses increased to $3.6 million for the three months ended April 2, 2011 from $3.0 million for the three months ended April 3, 2010, primarily as a result of an increase in compensation expense of $0.6 million. Research and development expenses as a percentage of sales decreased to 6.9% for the three months ended April 2, 2011 from 7.1% for the three months ended April 3, 2010.

Other (income) expense, net increased by $0.6 million to $0.1 million of income for the three months ended April 2, 2011, from expense of $0.5 million for the three months ended April 3, 2010, primarily as a result of changes in foreign exchange rates that created net foreign currency transaction gains in the intercompany account balances of the Company's subsidiaries denominated in different currencies.

Income tax expense increased by $0.4 million to $1.2 million for the three months ended April 2, 2011 from $0.8 million for the three months ended April 3, 2010. This increase was primarily due to an increase in pretax income. Total deferred taxes for the Company's foreign subsidiaries relating to net operating loss carryforwards were $14.6 million and $14.1 million at April 2, 2011 and December 31, 2010, respectively. The related valuation allowance was $11.6 million and $11.1 million at April 2, 2011 and December 31, 2010, respectively. The Company's effective tax rate decreased to 26.5% for the three months ended April 2, 2011 from 28.0% in the prior year period, primarily as a result of a decrease in taxable income in jurisdictions with higher tax rates. The Company's tax rate continues to be lower than the statutory tax rate in the United States primarily as a result of favorable tax rates in foreign jurisdictions. However, the Company's tax rate could be impacted positively or negatively by geographic changes in the manufacturing or sales of its products and the resulting effect on taxable income in each jurisdiction.

Net income increased by $1.1 million to $3.2 million for the three months ended April 2, 2011 from $2.1 million for the three months ended April 3, 2010 as a result of the factors described above.

**Liquidity and Capital Resources**

Cash and cash equivalents increased by $2.6 million to $53.3 million at April 2, 2011 from $50.7 million at December 31, 2010. The increase was primarily attributable to increase in net income and non-cash expenses of $6.1 million and proceeds from stock option exercises of $2.7 million, offset by an increase in working capital of $3.9 million, purchases of equipment and intangible assets of $1.5 million, and the effect of exchange rate changes on cash of $0.9 million.

On July 11, 2006, the Company entered into a loan agreement providing for an available line of credit of $30.0 million, which was most recently amended on June 18, 2009. Loans under the Amended and Restated Loan Agreement, as amended, bear interest at the rate of LIBOR plus a fixed percentage between 2.25% and 2.50% and require the Company to maintain a minimum cash balance and tangible net worth measured at the end of each of the Company's fiscal quarters. As of April 2, 2011, the Company was in compliance with all of the covenants under the Amended and Restated Loan Agreement, as amended. The term of the Amended and Restated Loan Agreement, as amended, expires on March 31, 2012. The Company has not drawn on this line of credit.

The Company believes that its working capital, anticipated cash flow from operations, and credit facility will be sufficient to fund its long-term liquidity requirements for the foreseeable future.

The Company has no off balance sheet arrangements.

**Critical Accounting Policies**

The preparation of the Company's consolidated financial statements requires the Company's management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, as well as disclosure of contingent assets and liabilities. The Company bases its estimates on historical experience, along with various other factors believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Some of these judgments can be subjective and complex and, consequently, actual results may differ from these estimates under different assumptions or conditions. While for any given estimate or assumption made by the Company's management there may be other estimates or assumptions that are reasonable, the Company believes that, given the current facts and circumstances, it is unlikely that applying any such other reasonable estimate or assumption would materially impact the financial statements.

In response to the SEC's financial reporting release, FR-60, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies," the Company has selected its critical accounting policies for purposes of explaining the methodology used in its calculation, in addition to any inherent uncertainties pertaining to the possible effects on its financial condition. The critical policies discussed below are the Company's processes of recognizing revenue, the reserve for excess and obsolete inventory, income taxes, the reserve for warranties and goodwill impairment. These policies affect current assets and operating results and are therefore critical in assessing the Company's financial and operating status. These policies involve certain assumptions that, if incorrect, could have an adverse impact on the Company's operations and financial position.

Revenue Recognition

Revenue related to the Company's measurement equipment and related software is generally recognized upon shipment, as the Company considers the earnings process substantially complete as of the shipping date. Revenue from sales of software only is recognized when no further significant production, modification or customization of the software is required and where persuasive evidence of a sales agreement exists, delivery has occurred, and the sales price is fixed or determinable and deemed collectible. Revenues resulting from sales of comprehensive support, training and technology consulting services are recognized as such services are performed. Extended maintenance plan revenues are recognized on a straight-line basis over the life of the plan. The Company warrants its products against defects in design, materials and workmanship for one year. A provision for estimated future costs relating to warranty expense is recorded when products are shipped. Costs relating to extended maintenance plans are recognized as incurred. Revenue from the licensing agreements for the use of the Company's historical technology for medical applications is recognized when the technology is sold by the licensees.

Reserve for Excess and Obsolete Inventory

Since the value of inventory that will ultimately be realized cannot be known with exact certainty, the Company relies upon both past sales history and future sales forecasts to provide a basis for the determination of the reserve. Inventory is considered obsolete if the Company has withdrawn those products from the market or had no sales of the product for the past 12 months and has no sales forecasted for the next 12 months. Inventory is considered excess if the quantity on hand exceeds 12 months of expected remaining usage. The resulting obsolete and excess parts are then reviewed to determine if a substitute usage or a future need exists. Items without an identified current or future usage are reserved in an amount equal to 100% of the FIFO cost of such inventory. The Company's products are subject to changes in technologies that may make certain of its products or their components obsolete or less competitive, which may increase its historical provisions to the reserve.

Income Taxes

The Company reviews its deferred tax assets on a regular basis to evaluate their recoverability based upon expected future reversals of deferred tax liabilities, projections of future taxable income over a two-year period, and tax planning strategies that it might employ to utilize such assets, including net operating loss carryforwards. Based on the positive and negative evidence of recoverability, the Company establishes a valuation allowance against the net deferred assets of a taxing jurisdiction in which it operates unless it is "more likely than not" that it will recover such assets through the above means. In the future, the Company's evaluation of the need for the valuation allowance will be significantly influenced by its ability to achieve profitability and its ability to predict and achieve future projections of taxable income.

Significant judgment is required in determining the Company's worldwide provision for income taxes. In the ordinary course of global business, there are many transactions for which the ultimate tax outcome is uncertain. The Company establishes provisions for income taxes when, despite the belief that tax positions are fully supportable, there remain certain positions that do not meet the minimum probability threshold as described by ASC 740, which is a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority. In the ordinary course of business, the Company and its subsidiaries are examined by various federal, state, and foreign tax authorities. The Company regularly assesses the potential outcomes of these examinations and any future examinations for the current or prior years in determining the adequacy of its provision for income taxes. The Company assesses the likelihood and amount of potential adjustments and adjusts the income tax provision, the current tax liability and deferred taxes in the period in which the facts that gave rise to a revision become known.

Reserve for Warranties

The Company establishes at the time of sale a liability for the one year warranty included with the initial purchase price of equipment, based upon an estimate of the repair expenses likely to be incurred for the warranty period. The warranty period is measured in installation-months for each major product group. The warranty reserve is reflected in accrued liabilities in the accompanying consolidated balance sheets. The warranty expense is estimated by applying the actual total repair expenses for each product group in the prior period and determining a rate of repair expense per installation-month. This repair rate is multiplied by the number of installation-months of warranty for each product group to determine the provision for warranty expenses for the period. The Company evaluates its exposure to warranty costs at the end of each period using the estimated expense per installation-month for each major product group, the number of units remaining under warranty and the remaining number of months each unit will be under warranty. The Company has a history of new product introductions and enhancements to existing products, which may result in unforeseen issues that increase its warranty costs. While such expenses have historically been within expectations, the Company cannot guarantee this will continue in the future.

Goodwill Impairment

Goodwill represents the excess cost of a business acquisition over the fair value of the net assets acquired. Indefinite-life identifiable intangible assets and goodwill are not amortized but are tested for impairment. The Company performs an annual review in the fourth quarter of each year, or more frequently if indicators of potential impairment exist, to determine if the carrying value of the recorded goodwill is impaired. If an asset is impaired, the difference between the value of the asset reflected on the financial statements and its current fair value is recognized as an expense in the period in which the impairment occurs.

The goodwill impairment test is applied using a two-step approach. In performing the first step, the company calculates the fair values of the reporting units using discounted cash flows (“DCF”) of each reporting unit. If the carrying amount of the reporting unit exceeds the fair market value, the second step is performed to measure the amount of the impairment loss, if any. In the second step, the implied fair value of the goodwill is estimated as the fair value of the reporting unit as calculated in the first step, less the fair values of the net tangible and intangible assets of the reporting unit other than goodwill. If the carrying amount of goodwill exceeds its implied fair market value, an impairment loss is recognized in an amount equal to that excess, not to exceed the carrying amount of the goodwill. Management has concluded there was no goodwill impairment in the year ended December 31, 2010.

## Item 3. Quantitative and Qualitative Disclosures about Market Risk

***Foreign Exchange Exposure***

The Company conducts a significant portion of its business outside the United States. At present, 61.5% of its revenues are invoiced, and a significant portion of its operating expenses paid, in foreign currencies. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material adverse effect on the business, results of operations and financial condition, and could specifically result in foreign exchange gains and losses. The impact of future exchange rate fluctuations on the results of the Company’s operations cannot be accurately predicted. To the extent that the percentage of its non-U.S. dollar revenues derived from international sales increases (or decreases) in the future, the Company’s exposure to risks associated with fluctuations in foreign exchange rates may increase (or decrease).

## Item 4. Controls and Procedures

**Evaluation of Disclosure Controls and Procedures**

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act of 1934, as amended, or the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

As of the end of the period covered by this report, the Company's management carried out an evaluation, under the supervision and with the participation of its Chief Executive Officer and its Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures, as defined by Rule 13a-15(e) under the Exchange Act, were effective as of April 2, 2011.

**Changes in Internal Control Over Financial Reporting**

There were no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended April 2, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

***Patent Matters*** — On July 11, 2008, Metris USA, Inc. and its affiliates, Metris N.V., Metris IPR N.V. and 3-D Scanners Ltd., filed a complaint against the Company for patent infringement in the U.S. District Court for the District of Massachusetts (the "Massachusetts Court") concerning U.S. Patent Nos. 6,611,617 and 7,313,264 (hereinafter, the "patents-in-suit"). Following an acquisition by Nikon Corporation in late 2009, Metris USA, Inc. subsequently changed its name to Nikon Metrology, Inc., Metris N.V. changed its name to Nikon Metrology NV, and Metris IPR N.V. was dissolved and merged into Nikon Metrology NV. We refer to each of Nikon Metrology, Inc., Nikon Metrology NV, and 3-D Scanners Ltd. as "Plaintiffs" or "Nikon".

The Company responded to the complaint with counterclaims alleging that the patents-in-suit, which are generally directed to laser scanning devices, are invalid, non-infringed, and unenforceable due to fraud during prosecution of the patents in the U.S. Patent and Trademark Office. On August 31, 2009, the Massachusetts Court granted the Company's motion to add counterclaims and defenses for violation of federal and state antitrust and unfair competition laws based on the alleged knowing assertion of invalid and fraudulent patents. The Company also filed an amended counterclaim to add the Plaintiffs' parent company, Nikon Corporation, as a counterclaim defendant.

On January 29, 2010, the Company filed a motion for summary judgment that the patents-in-suit are unenforceable due to inequitable conduct during patent prosecution. Evidentiary hearings on the issue of inequitable conduct commenced on July 19, 2010, and concluded on October 22, 2010. Post-trial briefing concluded on December 10, 2010. The Court has not yet issued a decision. On July 14, 2010, the Company filed a motion for summary judgment of non-infringement of both patents-in-suit. In addition, during the first quarter of 2010, Nikon served a supplemental interrogatory answer revising its alleged date of conception of the patents-in-suit to an earlier date. The Company filed a motion to strike the supplemental interrogatory answer, and the parties are waiting for the hearing date on the motion. On August 31, 2010, Nikon filed a motion for summary judgment against the Company's counterclaims for antitrust violations and unfair trade practices. The Company filed its opposition on October 12, 2010.

On February 22, 2011, the Court denied Nikon's Motion for Summary Judgment on the Company's counterclaims for anti-trust violations and unfair trade practices without prejudice. On February 24, 2011, the Court denied the Company's Motion for Summary Judgment of non-infringement without prejudice. The parties may renew their respective motions for summary judgment after the Court issues a decision on inequitable conduct, if necessary. No further motions for summary judgment are expected to be filed. A mediation hearing held on February 18, 2011 to settle the matter was unsuccessful.

The Company believes that it does not infringe the patents-in-suit and/or that the patents-in-suit are invalid and unenforceable. The Company does not anticipate this lawsuit will have a material impact on the Company; however, the outcome is difficult to predict, and an adverse determination could have a material impact on the Company's business, financial condition or results of operations.

Other than the litigation mentioned above, the Company is not involved in any other legal proceedings, other than routine litigation arising in the normal course of business, none of which the Company believes will have a material adverse effect on the Company's business, financial condition or results of operations.

**Item 1A. Risk Factors**

In addition to the other information set forth in this Form 10-Q, you should carefully consider the factors discussed under “Risk Factors” in the Company’s Form 10-K for the year ended December 31, 2010 as filed with the Securities and Exchange Commission. These risks could materially and adversely affect the Company’s business, financial condition, and results of operations. The risks described in the Company’s Form 10-K for the year ended December 31, 2010 are not the only risks it faces. The Company’s operations could also be affected by additional factors that are not presently known to the Company or by factors that it currently considers immaterial to its business.

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

**Purchases of Equity Securities by the Issuer**

On November 24, 2008, the Company’s Board of Directors approved a $30 million share repurchase program. Acquisitions for the share repurchase program will be made from time to time at prevailing prices as permitted by securities laws and other legal requirements, and subject to market conditions and other factors. The share repurchase program may be discontinued at any time. There is no restriction date or other restriction governing the period over which the Company can repurchase shares under the program. The Company made no stock repurchases during the first quarter of fiscal 2011 under this program.

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**Item 6. Exhibits**

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|---|---|
| 3.1 | Articles of Incorporation, as amended (Filed as Exhibit 3.1 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference) |
| 3.2 | Amended and Restated Bylaws (Filed as Exhibit 3.1 to current Report on Form 8-K, dated January 28, 2010 and incorporated herein by reference) |
| 4.1 | Specimen Stock Certificate (Filed as Exhibit 4.1 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference) |
| 31-A | Certification of the President and Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31-B | Certification of the Principal Financial and Accounting Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32-A | Certification of the President and Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32-B | Certification of the Principal Financial and Accounting Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS | XBRL Instance document |
| 101.SCH | XBRL Taxonomy Extension Schema |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

## SIGNATURES

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.

**FARO Technologies, Inc.**
(Registrant)

Date: May 6, 2011

By: /s/ Keith S. Bair
Keith S. Bair
Senior Vice President and Chief Financial Officer
(Duly Authorized Officer and Principal Financial Officer)

**Exhibit 31-A**

**FARO Technologies, Inc.**
**Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Jay W. Freeland, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of FARO Technologies, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 6, 2011

/s/ Jay W. Freeland

Name: Jay W. Freeland
Title: President and Chief Executive Officer (Principal Executive Officer)

**FARO Technologies, Inc.**
**Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Keith S. Bair, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of FARO Technologies, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2011

/s/ Keith S. Bair

Name: Keith S. Bair
Title: Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

**Exhibit 32-A**

**FARO Technologies, Inc.**
**Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

Solely for the purposes of complying with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, the undersigned President and Chief Executive Officer and Director of FARO Technologies, Inc. (the Company), hereby certify that the Quarterly Report on Form 10-Q, for the quarter ended April 2, 2011 (the Report) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Jay W. Freeland

Jay W. Freeland
President and Chief Executive Officer
(Principal Executive Officer)
May 6, 2011

**FARO Technologies, Inc.**
**Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

Solely for the purposes of complying with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, the undersigned Senior Vice President and Chief Financial Officer of FARO Technologies, Inc. (the Company), hereby certify that the Quarterly Report on Form 10-Q, for the quarter ended April 2, 2011 (the Report) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Keith S. Bair

Keith S. Bair
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)
May 6, 2011