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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2023

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 **(State or other Jurisdiction of Incorporation or Organization)**	**59-3157093** **(I.R.S. Employer Identification No.)**

250 Technology Park, **(Address of Principal Executive Offices)**	**Lake Mary, Florida**	**32746** **(Zip Code)**

(407) 333-9911
(Registrant’s Telephone Number, including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value $.001	FARO	Nasdaq Global Select Market LLC

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 every Interactive Data File required to be submitted 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 such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐	Smaller reporting company	☐
Emerging growth company	☐		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

There were 18,902,121 shares of the registrant’s common stock outstanding as of May 4, 2023.

FARO TECHNOLOGIES, INC.

Quarterly Report on Form 10-Q
Quarter Ended March 31, 2023

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)	March 31, 2023 (unaudited)	December 31, 2022
ASSETS		
Current assets:		
Cash and cash equivalents	$ 68,564	$ 37,812
Short-term investments	20,024	—
Accounts receivable, net	90,238	90,326
Inventories, net	50,886	50,026
Prepaid expenses and other current assets	45,830	41,201
Total current assets	275,542	219,365
Non-current assets:		
Property, plant and equipment, net	19,505	19,720
Operating lease right-of-use assets	17,605	18,989
Goodwill	108,051	107,155
Intangible assets, net	48,793	48,978
Service and sales demonstration inventory, net	30,917	30,904
Deferred income tax assets, net	24,271	24,192
Other long-term assets	4,044	4,044
Total assets	$ 528,728	$ 473,347
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 22,888	$ 27,286
Accrued liabilities	26,180	23,345
Income taxes payable	7,282	6,767
Current portion of unearned service revenues	36,792	36,407
Customer deposits	6,389	6,725
Lease liabilities	5,479	5,709
Total current liabilities	105,010	106,239
Loan - 5.50% convertible Senior Notes	72,379	—
Unearned service revenues - less current portion	21,101	20,947
Lease liabilities - less current portion	13,287	14,649
Deferred income tax liabilities	11,897	11,708
Income taxes payable - less current portion	8,718	8,706
Other long-term liabilities	23	49
Total liabilities	232,415	162,298
Commitments and contingencies - See Note 12		
Shareholders' equity:		
Common stock - par value $0.001, 50,000,000 shares authorized; 20,276,813 and 20,156,233 issued, respectively; 18,902,121 and 18,780,013 outstanding, respectively	20	20
Additional paid-in capital	331,875	328,227
Retained earnings	25,624	46,788
Accumulated other comprehensive loss	(30,551)	(33,331)
Common stock in treasury, at cost - 1,374,692 and 1,376,220 shares held, respectively	(30,655)	(30,655)
Total shareholders' equity	296,313	311,049
Total liabilities and shareholders' equity	$ 528,728	$ 473,347

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

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

(in thousands, except share and per share data)	Three Months Ended March 31, 2023	Three Months Ended March 31, 2022
Sales		
Product	$ 65,240	$ 56,730
Service	19,727	19,926
Total sales	84,967	76,656
Cost of sales		
Product	33,957	24,333
Service	11,294	11,297
Total cost of sales	45,251	35,630
Gross profit	39,716	41,026
Operating expenses		
Selling, general and administrative	41,376	35,490
Research and development	12,718	12,128
Restructuring costs	4,238	600
Total operating expenses	58,332	48,218
Loss from operations	(18,616)	(7,192)
Other (income) expense		
Interest expense	835	8
Other income, net	(220)	(13)
Loss before income tax expense	(19,231)	(7,187)
Income tax expense	1,933	2,500
Net loss	$ (21,164)	$ (9,687)
Net loss per share - Basic	$ (1.12)	$ (0.53)
Net loss per share - Diluted	$ (1.12)	$ (0.53)
Weighted average shares - Basic	18,816,110	18,240,299
Weighted average shares - Diluted	18,816,110	18,240,299

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(UNAUDITED)

	Three Months Ended	
(in thousands)	March 31, 2023	March 31, 2022
Net loss	$ (21,164)	$ (9,687)
Currency translation adjustments, net of income taxes	2,780	(1,984)
Comprehensive loss	$ (18,384)	$ (11,671)

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

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

(in thousands)	Three Months Ended March 31, 2023	Three Months Ended March 31, 2022
Cash flows from:		
Operating activities:		
Net loss	$ (21,164)	$ (9,687)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	4,413	3,012
Stock-based compensation	3,634	2,867
Deferred income tax expense (benefit)	562	66
Provision for excess and obsolete inventory	344	229
Loss on disposal of assets	69	112
Provisions for bad debts, net of recoveries	33	16
Change in operating assets and liabilities:		
Decrease (Increase) in:		
Accounts receivable	2,378	1,449
Inventories	(1,530)	(2,065)
Prepaid expenses and other current assets	(4,219)	(3,313)
(Decrease) Increase in:		
Accounts payable and accrued liabilities	(2,450)	(1,682)
Income taxes payable	(102)	1,261
Customer deposits	(433)	492
Unearned service revenues	121	206
Net cash used in operating activities	(18,344)	(7,037)
Investing activities:		
Purchases of property and equipment	(1,688)	(2,442)
Purchases of short-term investments	(20,024)	—
Cash paid for technology development, patents and licenses	(1,820)	(2,612)
Net cash used in investing activities	(23,532)	(5,054)
Financing activities:		
Payments on finance leases	(44)	(58)
Payments for taxes related to net share settlement of equity awards	14	(916)
Proceeds from issuance of 5.50% Convertible Senior Notes, due 2028, net of discount, issuance cost and accrued interest	72,310	—
Net cash provided by (used in) financing activities	72,280	(974)
Effect of exchange rate changes on cash and cash equivalents	348	(1,732)
Increase (Decrease) in cash and cash equivalents	30,752	(14,797)
Cash and cash equivalents, beginning of period	37,812	121,989
Cash and cash equivalents, end of period	$ 68,564	$ 107,192

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(UNAUDITED)

(in thousands, except share data)	Common Stock Shares	Common Stock Amounts	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Common Stock in Treasury	Total
BALANCE JANUARY 1, 2023	18,780,013	$ 20	$ 328,227	$ 46,788	$ (33,331)	$ (30,655)	$ 311,049
Net loss	—	—	—	(21,164)	—	—	(21,164)
Currency translation adjustment	—	—	—	—	2,780	—	2,780
Stock-based compensation	—	—	3,634	—	—	—	3,634
Common stock issued, net of shares withheld for employee taxes	122,108	—	14	—	—	—	14
BALANCE MARCH 31, 2023	18,902,121	$ 20	$ 331,875	$ 25,624	$ (30,551)	$ (30,655)	$ 296,313

(in thousands, except share data)	Common Stock Shares	Common Stock Amounts	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Common Stock in Treasury	Total
BALANCE JANUARY 1, 2022	18,205,636	$ 20	$ 301,061	$ 73,544	$ (17,374)	$ (30,792)	$ 326,459
Net loss	—	—	—	(9,687)	—	—	(9,687)
Currency translation adjustment	—	—	—	—	(1,984)	—	(1,984)
Stock-based compensation	—	—	2,867	—	—	—	2,867
Common stock issued, net of shares withheld for employee taxes	55,041	—	(1,051)	—	—	135	(916)
BALANCE MARCH 31, 2022	18,260,677	$ 20	$ 302,877	$ 63,857	$ (19,358)	$ (30,657)	$ 316,739

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
(in thousands, except share and per share data, or as otherwise noted)

NOTE 1 – DESCRIPTION OF BUSINESS

FARO Technologies, Inc. and its subsidiaries (collectively "FARO," the "Company," "us," "we" or "our") design, develop, manufacture, market and support software driven, three-dimensional ("3D") measurement, imaging, and realization solutions for the 3D metrology, architecture, engineering and construction ("AEC"), Operations and Maintenance ("O&M") and public safety analytics markets. We enable our customers to capture, measure, manipulate, interact with and share 3D and 2D data from the physical world in a virtual environment and then translate this information back into the physical domain. Our broad technology set equips our customers with a wide range of 3D capture technologies that range from ultra-high accuracy laser-scanner-based technology to lower accuracy, photogrammetry-based technology. Our FARO suite of 3D products and software solutions are used for inspection of components and assemblies, rapid prototyping, reverse engineering, documenting large volume or structures in 3D, surveying and construction, construction management, assembly layout, machine guidance as well as in investigation and reconstructions of crash and crime scenes. We sell the majority of our solutions through a direct sales force, with an increasing volume being sold through an indirect channel across a range of industries including automotive, aerospace, metal and machine fabrication, surveying, architecture, engineering and construction, public safety forensics and other industries.

NOTE 2 – PRINCIPLES OF CONSOLIDATION

Our consolidated financial statements include the accounts of FARO Technologies, Inc. and its subsidiaries, all of which are wholly owned. All intercompany transactions and balances have been eliminated. The financial statements of our 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 loss. Foreign currency transaction gains and losses are included in net income (loss).

NOTE 3 – BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements and notes thereto have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") for interim financial information and with the instructions of Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. These condensed consolidated financial statements include all normal recurring accruals and adjustments considered necessary by management for a fair presentation in conformity with 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 condensed consolidated results of operations for the three months ended March 31, 2023, are not necessarily indicative of results that may be expected for the year ending December 31, 2023, or any future period.

The information included in this Quarterly Report on Form 10-Q, including the interim condensed consolidated financial statements and the accompanying notes, should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2022. The accompanying December 31, 2022, condensed consolidated balance sheet has been derived from those audited consolidated financial statements.

Stock-based compensation expense is allocated to the applicable departmental cost in our condensed consolidated financial statements. The following table summarizes total stock-based compensation expense for each of the line items on our condensed consolidated statements of operations:

	Three Months Ended			
	March 31, 2023		March 31, 2022	
Cost of sales				
Product	$	240	$	160
Service		32		39
Total cost of sales	$	272	$	199
Operating expenses				
Selling, general and administrative	$	2,568	$	2,221
Research and development		794		447
Total operating expenses	$	3,362	$	2,668
Total stock-based compensation	$	3,634	$	2,867

NOTE 4 – IMPACT OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Impact of Recently Adopted Accounting Standards

In October 2021, the FASB issued ASU No. 2021-08, Business Combinations (Topic 805): Accounting for Contract Asset and Contract Liabilities from Contracts with Customers, which intends to simplify the accounting for acquired revenue contracts with customers in a business combination and to also remove inconsistencies in this topic related to recognition of an acquired contract liability and payment terms and their effect on subsequent revenue recognized by the acquirer. ASU No. 2021-08 allows an acquirer to recognize and measure contract assets and contract liabilities acquired in a business combination in a similar manner to how they are recorded on the acquiree’s financial statements at book value. Early adoption is permitted and we early adopted ASU No. 2021-08 in the fourth quarter of 2021. As a result of the early adoption of ASU No.2021-08, we recorded the deferred revenue associated with the acquisition of Holobuilder in 2021 at its book value of approximately $4.0 million. Further, we recorded the deferred revenue associated with the acquisition of GeoSLAM in 2022 at its book value of approximately $1.3 million.

In August 2020, the FASB issued ASU No. 2020-06—Debt - Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging - Contracts in Entity's Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity's Own Equity. The update simplifies the accounting for convertible instruments that were previous separated into a debt component and an equity component, and our convertible debt was already determined to be a single debt instrument that did not require bifurcation. The Company adopted ASU 2020-06 as of January 1, 2022, and therefore, the Notes (as defined below) would not be subject any beneficial conversion or cash conversion guidance. Moreover, the Company did not elect the fair value option - as defined in ASC 825 and 815 - to present the Notes on its financial statements.

NOTE 5 – REVENUES

The following tables present our revenues by sales type as presented in our condensed consolidated statements of operations disaggregated by the timing of transfer of goods or services:

	For the Three Months Ended March 31,			
	2023		2022	
Product sales				
Product transferred to customers at a point in time	$	59,892	$	51,480
Product transferred to customers over time		5,348		5,250
Total product sales	$	65,240	$	56,730

	For the Three Months Ended March 31,	
	2023	2022
Service sales		
Service transferred to customers at a point in time	$ 8,390	$ 8,703
Service transferred to customers over time	11,337	11,223
Total service sales	$ 19,727	$ 19,926

The following table presents our revenues disaggregated by geography, based on the billing addresses of our customers:

	For the Three Months Ended March 31,	
	2023	2022
Total sales to external customers		
Americas [1]	$ 42,343	$ 36,677
EMEA [1]	24,165	22,136
APAC [1]	18,459	17,843
	$ 84,967	$ 76,656

[1] Regions represent North America and South America (the “Americas”); Europe, the Middle East, and Africa (“EMEA”); and Asia-Pacific (“APAC”).

For revenue related to our measurement and imaging equipment and related software, we allocate the contract price to performance obligations based on our best estimate of the standalone selling price. We make this allocation estimate utilizing data from the sale of our applicable products and services to customers separately in similar circumstances. Revenue related to our measurement and imaging equipment and related software is generally recognized upon shipment from our facilities or when delivered to the customer location, as determined by the agreed upon shipping terms, at which time we are entitled to payment and title and control has passed to the customer. Software arrangements generally include short-term maintenance that is considered post-contract support (“PCS”), which is considered to be product transferred to the customer over time and a separate performance obligation. We generally establish a standalone sales price for this PCS component based on our maintenance renewal rate. Maintenance renewals are recognized on a straight-line basis over the term of the maintenance agreement. Payments for products and services are collected within a short period of time following transfer of control or commencement of delivery of services, as applicable.

Further, customers frequently purchase extended hardware service contracts with the purchase of measurement equipment and related software. Hardware service contracts are considered a performance obligation when services are transferred to a customer over time, and, as such, we recognize revenue on a straight-line basis over the contractual term. Hardware service contracts include contract periods that extend between one month to three years.

We capitalize commission expenses related to deliverables transferred to a customer over time and amortize such costs ratably over the term of the contract. As of March 31, 2023, the deferred cost asset related to deferred commissions was approximately $3.0 million. For classification purposes, $2.1 million and $1.0 million are comprised within the Prepaid expenses and other current assets and Other long-term assets, respectively, on our condensed consolidated balance sheet as of March 31, 2023. As of December 31, 2022, the deferred cost asset related to deferred commissions was approximately $3.0 million. For classification purposes, $2.0 million and $1.0 million were comprised within the Prepaid expenses and other current assets and Other long-term assets, respectively, on our condensed consolidated balance sheet as of December 31, 2022.

The unearned service revenue liabilities reported on our condensed consolidated balance sheets reflect the contract liabilities to satisfy the remaining performance obligations for extended warranties, subscription-based software and software maintenance. The current portion of unearned service revenues on our condensed consolidated balance sheets is what we expect to recognize as revenue within twelve months after the applicable balance sheet date relating to extended warranties, subscription-based software and software maintenance contract liabilities. The unearned service revenues less the current portion on our condensed consolidated balance sheets is what we expect to recognize as revenue extending beyond twelve months after the applicable balance sheet date relating to extended warranties, subscription-based software and software maintenance contract liabilities. Customer deposits on our condensed consolidated balance sheets represent customer prepayments on contracts for performance obligations that we must satisfy in the future to recognize the related contract revenue. These amounts are generally related to performance obligations which are delivered in less than 12 months. During the three months ended March 31, 2023, we recognized $11.4 million of revenue that was deferred on our condensed consolidated balance sheet as of December 31, 2022. During the three ended March 31, 2022, we recognized $10.9 million of revenue that was deferred on our condensed consolidated balance sheet as of December 31, 2021.

The nature of certain of our contracts gives rise to variable consideration, primarily related to an allowance for sales returns. We are required to estimate the contract asset related to sales returns and record a corresponding adjustment to Cost of Sales. Our allowance for sales returns for March 31, 2023 and March 31, 2022 was approximately $0.2 million, and $0.2 million, respectively.

Shipping and handling fees billed to customers in a sales transaction are recorded in Product Sales and shipping and handling costs incurred are recorded in Cost of Sales. We exclude from Sales any value-added sales and other taxes that we collect concurrently with revenue-producing activities.

NOTE 6 – ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

	As of March 31, 2023	As of December 31, 2022
Accounts receivable	$ 92,466	$ 92,611
Allowance for credit losses	(2,228)	(2,285)
Total	$ 90,238	$ 90,326

Activity related to the allowance for credit losses was as follows:

	Three Months Ended March 31, 2023
Beginning balance of the allowance for credit losses	$ 2,285
Current period provision for expected credit losses, net of recoveries	33
Charge-offs of amounts previously expensed	(90)
Ending balance of the allowance for credit losses	$ 2,228

NOTE 7 – INVENTORIES

Inventories are stated at the lower of cost or net realizable value using the first-in first-out (FIFO) method. We have three principal categories of inventory: 1) manufactured product to be sold; 2) sales demonstration inventory - completed product used to support our sales force for demonstrations and held for sale; and 3) service inventory - completed product and parts used to support our service department and held for sale. Shipping and handling costs are classified as a component of Cost of Sales in our condensed consolidated statements of operations. Sales demonstration inventory is held by our sales representatives for up to three years, at which time it would be refurbished and transferred to finished goods as used equipment, stated at the lower of cost or net realizable value. We expect these refurbished units to remain in finished goods inventory and sold within 12 months at prices that produce reduced gross margins. Service inventory is used to provide a temporary replacement product to a customer covered by a premium warranty when the customer's unit requires service or repair and as training equipment. Service inventory is available for sale; however, management does not expect service inventory to be sold within 12 months and, as such, classifies this inventory as a long-term asset. Service inventory that we utilize for training or repairs and which we deem as no longer available for sale is transferred to fixed assets at the lower of cost or net realizable value and depreciated over the remaining life, typically three years.

Inventories consist of the following:

	As of March 31, 2023	As of December 31, 2022
Raw materials	$ 30,960	$ 33,076
Finished goods	19,926	16,950
Inventories, net	$ 50,886	$ 50,026
Service and sales demonstration inventory, net	$ 30,917	$ 30,904

NOTE 8 – NET LOSS PER SHARE

Basic net loss per share is computed by dividing net loss by the weighted average number of shares outstanding. Diluted net loss per share is computed by also considering the impact of potential common stock on both net loss and the weighted average number of shares outstanding. Our potential common stock consists of employee stock options, time-based restricted stock units, market-based restricted stock unit awards, and common stock issued for settlement of Notes (as defined in Note 16). Our potential common stock is included in the diluted earnings per share calculation when adding such potential common stock would not be anti-dilutive. Market-based awards are included in the computation of diluted earnings per share only to the extent that the underlying conditions (and any applicable market condition) (i) are satisfied as of the end of the reporting period or (ii) would be considered satisfied if the end of the reporting period were the end of the related contingency period and the result would be dilutive under the treasury stock method. When we report a net loss for the period presented, the calculation of diluted net loss per share excludes our potential common stock, as the effect would be anti-dilutive.

For the three months ended March 31, 2023, there were approximately 1,077,583 shares issuable upon the exercise of options, the vesting of time-based restricted stock and the contingent vesting of market-based restricted stock units that were excluded from the dilutive calculations, as they were anti-dilutive. For the three months ended March 31, 2022, there were approximately 599,083 issuable upon the exercise of options that were excluded from the dilutive calculations, as they were anti-dilutive. In addition, the Company has issued $75 million aggregate principal amount of Notes on January 24, 2023, which, if converted, would result in the issuance of a maximum of 2,124,645 shares of common stock. These shares were excluded from the dilutive calculations, as their effect would have been anti-dilutive.

A reconciliation of the number of common shares used in the calculation of basic and diluted net loss per share is presented below:

	Three Months Ended			
	March 31, 2023		March 31, 2022	
	Shares	Per-Share Amount	Shares	Per-Share Amount
Basic net loss per share	18,816,110	$(1.12)	18,240,299	$(0.53)
Effect of dilutive securities	—	—	—	—
Diluted net loss per share	18,816,110	$(1.12)	18,240,299	$(0.53)

NOTE 9 – ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	As of March 31, 2023	As of December 31, 2022
Accrued compensation and benefits	$ 11,910	$ 12,483
Accrued restructuring costs	3,970	528
Accrued warranties	2,682	2,610
Professional and legal fees	2,516	1,662
Taxes other than income	2,459	3,737
Other accrued liabilities	2,643	2,325
Total accrued liabilities	$ 26,180	$ 23,345

Activity related to accrued warranties was as follows:

	Three Months Ended	
	March 31, 2023	March 31, 2022
Balance, beginning of period	$ 2,610	$ 1,880
Provision for warranty expense	736	618
Fulfillment of warranty obligations	(664)	(750)
Balance, end of period	$ 2,682	$ 1,748

NOTE 10 – FAIR VALUE MEASUREMENTS

Our financial instruments include cash and cash equivalents, accounts receivable, customer deposits, accounts payable and accrued liabilities. The carrying amounts of such financial instruments approximate their fair value due to the short-term nature of these instruments.

Liabilities measured at fair value on a recurring basis are categorized in the tables below based upon the lowest level of significant input to the valuations:

	As of March 31, 2023		
	Level 1	Level 2	Level 3
Assets:			
U.S. Treasury securities (due in 6 months) (1)	20,024	$ —	$ —
Liabilities:			
Contingent consideration (2)	$ —	$ —	$ 1,043
Total	$ 20,024	$ —	$ 1,043

	As of December 31, 2022		
	Level 1	Level 2	Level 3
Liabilities:			
Contingent consideration (2)	$ —	$ —	$ 1,043
Total	$ —	$ —	$ 1,043

(1) As of March 31, 2023, the Company held U.S. Treasury securities with a total fair value of $35.0 million. Of this amount, $20.0 million represents Treasury bills with a 6-month maturity, and are included as short-term investments on the Condensed Consolidated Balance Sheets. These securities were classified as Level 1 investments in the above fair value hierarchy. The remaining $15.0 million represents Treasury bills with a 3-month maturity, which were included in Cash and Cash Equivalents on the Condensed Consolidated Balance Sheets. The fair value of the U.S. Treasury securities with 6-months maturity was determined using quoted market prices in active markets, which represents Level 1 inputs in the fair value hierarchy.

(2) Contingent consideration liability represents arrangements to pay the former owners of certain companies we acquired based on the attainment of future product release milestones and is reported in Other long-term liabilities. We use a probability-weighted discounted cash flow model to estimate the fair value of contingent consideration liabilities. These probability weightings are developed internally and assessed on a quarterly basis. The remaining undiscounted maximum payment under these arrangements was approximately $1.0 million as of March 31, 2023. We expect to make payments earned by former owners under these arrangements on August 31, 2023.

NOTE 11 – RESTRUCTURING

In the first quarter of 2020, our Board of Directors approved a global restructuring plan (the “Restructuring Plan”), which is intended to support our strategic plan in an effort to improve operating performance and ensure that we are appropriately structured and resourced to deliver increased and sustainable value to our shareholders and customers. Key activities under the Restructuring Plan include a continued focus on efficiency and cost-saving efforts, which included a planned decrease of total headcount.

On July 15, 2021, we entered into a manufacturing services agreement (the “Agreement”) with Sanmina, in connection with the Restructuring Plan. Under the Agreement, Sanmina will provide manufacturing services for the Company’s measurement device products manufactured by the Company at the Company’s Lake Mary, Florida, Exton, Pennsylvania, and Stuttgart, Germany manufacturing sites. This phased transition to a Sanmina production facility was completed at the beginning of the third quarter of 2022 as part of our cost reduction initiative. We are currently evaluating the Lake Mary, Florida and Stuttgart, Germany manufacturing sites with the intention to reduce our leased floor space. However, all of these facilities are mixed-use spaces shared with our service, research and development, or sales teams who continue to use these spaces. The Company, in collaboration with third-party lessors and architectural resources, intends to conduct studies over the feasibility of abandoning or demising leased floor space against our current needs. Our current needs continue to include access to existing spaces previously constructed to closely monitor temperature and vibration for our service and research and development teams. The conclusion of this evaluation and any subsequent approval to abandon or reduce these leased spaces would be considered as a change in the manner of the use of these corresponding assets, and thereby will be evaluated for impairment. We expect to complete this evaluation before the first half of fiscal year 2023. We have completed this evaluation for the Exton, Pennsylvania manufacturing site and entered into an agreement to sublease 17,000 square feet of unused space. As of March 31, 2023, the remaining value of leasehold improvements for the remaining facilities under evaluation is approximately $0.6 million and a portion of this may be impaired, if the Company decides to reduce or abandon the leased space. Since the approval of the Restructuring Plan, we have paid $24.8 million, primarily consisting of severance and related benefits. As of March 31, 2023, we have completed all of our planned activities under the 2020 restructuring plan and have rolled forward the $0.5 million in remaining amounts payable to the Integration Plan discussed below.

On February 7, 2023, our Board of Directors approved an integration plan (the "Integration Plan"), which is intended to streamline and simplify operations, particularly around our recent acquisitions and the resulting redundant operations and offerings. Key activities under the Integration Plan include a planned decrease in headcount, consolidation of our cloud-based offerings from 3 platforms (2 acquired, 1 organic) into a single customer offering, and the optimization of our facility assets to align with current and expected future utilization. As of March 31, 2023, we expected to incur total pre-tax charges in the range of $10 million to $16 million through the end of fiscal year 2023, and expected to realize approximately $10 million in annualized cost savings when this plan is complete. The Integration Plan was amended on May 3, 2023, and the Board approved increases to both the expected pre-tax charges and the annualized cost savings (see Note 17 - Subsequent Events, for further details). In the first quarter of 2023, we have recognized $4.2 million in restructuring costs associated with the Integration Plan, and paid $0.8 million during the same period; primarily consisting of severance and related benefits.

Activity related to the accrued restructuring charges for the Integration Plan and cash payments during the first quarter ended March 31, 2023 is as follows:

	Severance and other benefits	Professional fees and other related charges	Total
Balance at January 1, 2023	$ 318	$ 210	$ 528
Additions charged to expense	4,118	120	4,238
Cash payments	(796)		(796)
Balance at March 31, 2023	$ 3,640	$ 330	$ 3,970

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Purchase Commitments — We enter into purchase commitments for products and services in the ordinary course of business. These purchases generally cover production requirements for 60 to 120 days as well as materials necessary to service customer units through the product lifecycle and for warranty commitments. As of March 31, 2023, we had approximately $29.7 million in purchase commitments that are expected to be delivered within the next 12 months. To ensure adequate component availability, as of March 31, 2023, we also had $23.9 million in long-term commitments for purchases to be delivered after 12 months.

Legal Proceedings — We are not involved in any legal proceedings other than routine litigation arising in the normal course of business, none of which we believe will have a material adverse effect on our business, financial condition or results of operations.

NOTE 13 – LEASES

We have operating and finance leases for manufacturing facilities, corporate offices, research and development facilities, sales and training facilities, vehicles, and certain equipment under which we assume the role of lessee. We do not lease assets as a lessor. Our leases have remaining lease terms of less than one year to approximately ten years, some of which include options to extend the leases for up to fifteen years, and some of which include options to terminate the leases within three months. We do not participate in any material subleasing.

We determine if an arrangement is a lease at inception. Operating leases are included in Operating lease right-of-use (“ROU”) asset, Lease liability, and Lease liability - less current portion in our condensed consolidated balance sheets. Finance leases are included in Property and equipment, net, Lease liability, and Lease liability - less current portion in our condensed consolidated balance sheets.

ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Operating lease ROU assets and lease liabilities are recognized on the commencement date of the lease based on the present value of lease payments over the lease term. Variable lease payments that depend on an index or rate include the variable portion when calculating ROU assets and lease liabilities. Variable lease payments that do not depend on an index or rate are expensed as incurred. As most of our leases do not provide an implicit rate, we use our incremental borrowing rate based on the information available on the commencement date of the lease to determine the present value of lease payments. We use the implicit rate when readily determinable. The operating lease ROU assets also include any lease payments made and lease incentives. Our lease terms may include options to extend or terminate the lease when it is reasonably certain that we will exercise that option at the time the lease is commenced. Lease expense for lease payments is recognized on a straight-line basis over the lease term.

While we have lease agreements with lease and non-lease components, we account for the lease and non-lease components as a single lease component.

The components of lease expense were as follows:

	Three Months Ended March 31, 2023	Three Months Ended March 31, 2022
Operating lease cost	$ 1,730	$ 1,806
Finance lease cost:		
Amortization of ROU assets	15	48
Interest on lease liabilities	3	5
Total finance lease cost	$ 18	$ 53

We recognize lease payments made for short-term leases where terms are 12 months or less as the payments are incurred. Our short-term lease costs for the three months ended March 31, 2023 and March 31, 2022 were both less than $0.1 million.

Supplemental balance sheet information related to leases was as follows:

	As of March 31, 2023	As of December 31, 2022
Operating leases:		
Operating lease right-of-use assets	$ 17,605	$ 18,989
Current operating lease liabilities	$ 5,479	$ 5,535
Operating lease liabilities - less current portion	13,287	14,532
Total operating lease liabilities	$ 18,766	$ 20,067
Finance leases:		
Property and equipment, at cost	$ 1,523	$ 1,523
Accumulated amortization	(1,402)	(1,387)
Property and equipment, net	$ 121	$ 136
Current finance lease liabilities	$ 160	$ 174
Finance lease liabilities - less current portion	86	117
Total finance lease liabilities	$ 246	$ 291
Weighted Average Remaining Lease Term (in years):		
Operating leases	4.89	4.97
Finance leases	2.12	2.24
Weighted Average Discount Rate:		
Operating leases	5.70 %	5.67 %
Finance leases	5.30 %	5.31 %

Supplemental cash flow information related to leases was as follows:

	Three Months Ended March 31, 2023	Three Months Ended March 31, 2022
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from operating leases	$ 1,773	$ 1,853
Operating cash flows from finance leases	$ 3	$ 5
Financing cash flows from finance leases	$ 44	$ 58
ROU assets obtained in exchange for lease obligations:		
Operating leases	$ —	$ —

Maturities of lease liabilities are as follows:

Year Ending December 31,	Operating leases	Finance leases
2023 (excluding the first 6 months)	$ 4,911	$ 137
2024	5,247	73
2025	3,422	23
2026	2,392	18
2027	1,579	9
Thereafter	4,052	—
Total lease payments	$ 21,603	$ 260
Less imputed interest	(2,837)	(14)
Total	$ 18,766	$ 246

NOTE 14 – INCOME TAXES

For the three months ended March 31, 2023, we recorded an income tax expense of $1.9 million compared with an income tax benefit of $2.5 million for the three months ended March 31, 2022. Our effective tax rate was -10.1% for the three months ended March 31, 2023, compared with -34.8% in the prior year period. The tax rate for 2023 reflects a tax expense on a pre-tax loss consistent with the prior year period. The change in our income tax expense and our effective tax rate were primarily due to the continued impact of the capitalization of research and development ("R&D") expenditures for income tax purposes. The Tax Cuts and Jobs Act (the "Act") requires the capitalization and amortization of R&D costs incurred after December 31, 2021. We have considered the continued effects of the Act on the forecasted domestic taxable income for the year ending December 31, 2023. Our entity in the United States remains in a full valuation allowance position, hence we were not able to recognize the tax benefits associated with the capitalization of these R&D expenditures.

Our quarterly estimate of our annual effective tax rate, and our quarterly provision for income tax (benefit) expense, are subject to significant variation due to numerous factors, including variability in accurately predicting our pretax and taxable income or loss and the mix of jurisdictions to which they relate, as well as the amount of pretax income or loss recognized during the quarter.

NOTE 15 - BUSINESS COMBINATIONS

On September 1, 2022, we completed the acquisition of UK-based GeoSLAM, a leading provider of mobile scanning solutions with proprietary high-productivity simultaneous localization and mapping (SLAM) software. We believe this acquisition enables the Company to provide mobile scanning solutions using SLAM software to create 3D models for use in Digital Twin applications. We believe these newly acquired capture technologies integrate into our 4D digital reality-based SaaS offering that will allow customers to access multiple 4D data sources for visualization and analysis through a single user experience. We acquired all voting equity interests of GeoSLAM held by the previous owners. The results of GeoSLAM's operations as of and after the date of acquisition have been included in our condensed consolidated financial statements as of and for the period ended March 31, 2023. The total purchase price included $29 million of cash paid, net of cash acquired and a non-cash payment of 495,562 shares of FARO stock valued at $15.9 million that is subject to customary lock-up provisions for a total purchase price of $44.9 million.

The acquisition of GeoSLAM constitutes a business combination as defined by ASC Topic 805, *Business Combinations*. Accordingly, the assets acquired and liabilities assumed were recorded at their fair values on the date of acquisition. The purchase price allocations below represent our determination of the fair value of the assets acquired and liabilities assumed for the acquisitions.

Following is a summary of our allocations of the purchase price to the fair values of the assets acquired and liabilities assumed as of the date of the acquisition:

		Fair Value
Tangible assets acquired:		
Accounts receivable	$	2,452
Inventory		6,576
Property, plant and equipment, net		270
Other assets		505
Total assets acquired		9,803
Liabilities assumed:		
Accounts payable and accrued liabilities		(2,187)
Deferred revenue		(1,282)
Other current liabilities		(289)
Total liabilities assumed		(3,758)
Intangible assets		18,610
Net assets acquired		24,655
Deferred income tax liability		4,472
Goodwill		24,763
Purchase price paid, net of cash acquired	$	44,946

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations as well as the value of the workforce. This goodwill is not tax deductible. Acquisition and integration costs are not included as components of consideration transferred, but are recorded as expense in the period in which such costs are incurred. As of March 31, 2023, we have incurred $2.1 million of acquisition or integration costs for the GeoSLAM acquisition. Accounts receivable acquired represent a gross contractual amount of $2.6 million of which we expect to collect $2.5 million. We believe that the fair value of these receivables approximates the net book value given their short term nature. Pro forma financial results for GeoSLAM have not been presented because the effects of these transactions, individually and in the aggregate, were not material to our condensed consolidated financial results.

Following are the details of the purchase price allocated to the intangible assets acquired for the GeoSLAM acquisition:

		Amount	Weighted Average Life (Years)
Brand	$	466	3
Technology		3,828	5
Customer relationships		14,316	15
Fair value of intangible assets acquired	$	18,610	13

On December 1, 2022, we completed the acquisition of SiteScape, an innovator in LiDAR 3D scanning software solutions for the AEC and O&M markets. SiteScape enables LiDAR equipped mobile devices to easily capture indoor spaces digitally, providing a readily available entry-point to scanning physical spaces for a broad range of applications. We believe integrating SiteScape's iOS-enabled low-resolution LiDAR capture capability into the FARO Sphere Platform will allow streamlining multiple capture methods into a single centralized environment on a single coordinate system. We believe this enables FARO's construction and facilities customers to access a portfolio which now contains low-resolution Lidar, 360° photo, video, mobile mapping and terrestrial laser scanning. The total purchase price included $1.9 million of cash paid, net of cash acquired. The results of SiteScape's operations as of and after the date of acquisition have been included in our consolidated financial statements as of and for the period ended December 31, 2022.

The acquisition of SiteScape constitutes a business combination as defined by ASC Topic 805, *Business Combinations*. Accordingly, the assets acquired and liabilities assumed were recorded at their fair values on the date of acquisition. The purchase price allocations below represent our determination of the fair value of the assets acquired and liabilities assumed for the acquisitions.

Following is a summary of our allocations of the purchase price to the fair values of the assets acquired and liabilities assumed as of the date of the acquisition:

	Fair Value
Intangible assets	807
Goodwill	1,109
Purchase price paid, net of cash acquired	1,916

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations as well as the value of the workforce. This goodwill is not tax deductible. Acquisition and integration costs are not included as components of consideration transferred, but are recorded as expense in the period in which such costs are incurred. As of March 31, 2023, we have incurred $0.2 million of acquisition or integration costs for the SiteScape acquisition. Pro forma financial results for SiteScape have not been presented because the effects of these transactions, individually and in the aggregate, were not material to our condensed consolidated financial results.

Following are the details of the purchase price allocated to the intangible assets acquired for the SiteScape acquisition:

	Amount	Weighted Average Life (Years)
Technology	$ 807	3
Fair value of intangible assets acquired	$ 807	3

NOTE 16 - DEBT

On January 24, 2023, the Company issued $75 million aggregate principal amount of 5.50% Convertible Senior Notes due 2028 (the “Notes”). The Notes are general senior unsecured obligations of the Company and will mature on February 1, 2028, unless earlier redeemed, repurchased or converted. The Notes will bear interest from January 24, 2023, at a rate of 5.50% per annum payable semiannually in arrears on February 1 and August 1 of each year, beginning August 1, 2023.

The Notes are convertible into shares of the Company’s common stock at an initial conversion price of approximately $42.36 per share, which represents a premium of approximately 20% to the $35.30 per share closing market price of the common stock on January 19, 2023.

The proceeds from the issuance of the Notes are presented under the long term liabilities of our condensed consolidated balance sheet. The net proceeds from the issuance of the Notes were approximately $72.2 million, after deducting underwriting discounts and other offering expenses. The Company intends to use the net proceeds from this offering to fund working capital needs and for general corporate purposes. As of March 31, 2023, the outstanding principal balance of the Notes was $75 million. The Company is in compliance with all covenants under the indenture governing the Notes.

As of March 31, 2023, the future minimum payments for interest on our outstanding convertible debt for the next five years are as follows:

Year Ending	Minimum Interest Payments
2023	$ 2,154
2024	$ 4,125
2025	$ 4,125
2026	$ 4,125
2027	$ 4,125

NOTE 17 - SUBSEQUENT EVENTS

Subsequent to the quarter-end, the Company announced the retirement of its President and Chief Executive Officer, Michael Burger, to be effective on July 1, 2023, and an amendment to the Integration Plan approved on February 7, 2023.

A. The Company announced on May 3, 2023 that Michael Burger, its President and Chief Executive Officer, has informed the Company of his intention to retire as President and Chief Executive Officer of the Company, with the retirement to be effective July 1, 2023. The Company and Mr. Burger intend to enter into a transition agreement relating to Mr. Burger’s retirement and continuing service as an advisor to the Company for a period of time thereafter.

The Company also announced the appointment of Yuval Wasserman, the Company’s current Chairman of the Board, as the Company’s Executive Chairman, effective May 4, 2023. As of such date, Mr. Wasserman will be, on an interim basis, the most senior executive officer of the Company, and the Company’s principal executive officer for purposes of the rules and regulations of the Securities and Exchange Commission. Upon Mr. Burger’s retirement, Mr. Wasserman will also assume the role of Interim Chief Executive Officer.

B. On May 3, 2023, an amendment to the Integration Plan was approved by our Board of Directors. The original approval anticipated pre-tax charges in the range of $10 million to $16 million, along with an anticipated annualized savings of approximately $10 million. The amendment approves pre-tax charges in the range of $22 million to $28 million, with a targeted annualized savings of approximately $20 million to $30 million. The increase in expected savings reflects our revised growth expectations for the remainder of 2023.

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

The following information should be read in conjunction with the condensed consolidated financial statements, including the notes thereto, included elsewhere in this Quarterly Report on Form 10-Q (the "Quarterly Report") and Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2022, as filed with the Securites and Exchange Commission on February 15, 2023 (the Annual Report").

Amounts reported in millions within this Quarterly Report on Form 10-Q are computed based on the amounts in thousands. As a result, the sum of the components reported in millions may not equal the total amount reported in millions due to rounding. Certain columns and rows within the tables that follow may not add due to the use of rounded numbers. Percentages presented are calculated based on the respective amounts in thousands.

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," "might," "would," "will," "will be," "future," "strategy," "believe," "plan," "should," "could," "seek," "expect," "anticipate," "intend," "estimate," "goal," "objective," "project," "forecast," "target" and similar words identify forward-looking statements.

Forward-looking statements are not guarantees of future performance and are subject to a number of known and unknown risks, uncertainties, assumptions, including those described in the section titled "Risk Factors" and elsewhere in this Quarterly Report, 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. These forward-looking statements speak only as of the date of this Quarterly Report. We do 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:

- an economic downturn or other adverse changes in the industries that we serve or the domestic and international economies in the regions of the world where we operate and other general economic, business, and financial conditions;
- the effects of the ongoing COVID-19 pandemic, including on our business operations, as well as its impact on general economic and financial market conditions;
- the effects of shipping and other supply chain disruptions caused by the ongoing COVID-19 pandemic and its impact on our ability to deliver our products to customers;
- our inability to realize the intended benefits of reorganizing our business functions to improve the efficiency of our sales organization and to improve operational effectiveness;
- our inability to realize the intended benefits of our undertaking to transition to a subscription-based business model to deliver new and existing software offerings on a cloud-computing-based platform, including but not limited to impairment charges of capitalized expenditures related to the development of Sphere, our cloud-computing-based platform, and our inability to realize the expected benefits;
- our inability to successfully execute our strategic plan, Integration Plan (defined below) and Restructuring Plan (defined below), including but not limited to additional impairment charges including existing leasehold improvements and/or higher than expected severance costs and exit costs, and our inability to realize the expected benefits of such plans;
- our inability to realize the anticipated benefits of our partnership with Sanmina (defined below);
- our inability to reasonably source essential equipment and materials to manufacture our products as a result of global supply shortages;
- the effect of inflationary pressures, rising interest rates, and instability in the banking sector, and its impact on our business operations;
- our inability to successfully realize changes to the pricing of our products and services;
- our inability to achieve and maintain profitability to fully realize the economic benefit of recorded deferred tax assets;
- our inability to further penetrate our customer base and target markets;

- development by others of new or improved products, processes or technologies that make our products less competitive or obsolete;
- our inability to maintain what we believe to be our technological advantage by developing new products and enhancing our existing products;
- risks associated with expanding international operations, such as difficulties in staffing and managing foreign operations, increased political and economic instability, compliance with potentially evolving 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;
- changes in trade regulation, which result in rising prices of imported steel, steel byproducts, aluminum and aluminum byproducts and various other raw materials that we use in the production of measurement devices, and our ability to pass those costs on to our customers or require our suppliers to absorb such costs;
- changes in foreign regulation which may result in rising prices of our measurement devices sold as exports to our international customers, our customers' willingness to absorb incremental import tariffs, and the corresponding impact on our profitability;
- our inability to successfully identify and acquire target companies and achieve expected benefits from, and effectively integrate, acquisitions that are consummated, including the operations from Holobuilder, Inc., UK-based NGH Holdings Limited and its subsidiaries (collectively, "GeoSLAM") and US-based SiteScape Inc., and the intellectual property acquired;
- our inability to realize the intended benefits of the technology, products, operations, contracts, and personnel of our acquisitions;
- the cyclical nature of the industries of our customers and material adverse changes in our customers' access to liquidity and capital;
- changes in the potential for the computer-aided measurement market and the potential adoption rate for our products, which are difficult to quantify and predict;
- our inability to protect our patents and other proprietary rights in the United States and foreign countries;
- our inability to defend against a cyberattack, security or other data breach of our systems may compromise the confidentiality, integrity, or availability of our internal data and the availability of our products and websites designed to support our customers or their data;
- our inability to adequately maintain effective internal controls over financial reporting;
- fluctuations in our annual and quarterly operating results and the inability to achieve our financial operating targets as a result of a number of factors including, without limitation (i) litigation and regulatory action brought against us, (ii) quality issues with our products, (iii) excess or obsolete inventory, shrinkage or other inventory losses due to product obsolescence, change in demand for our products, scrap or material price changes, (iv) raw material price fluctuations and other inflationary pressures, (v) expansion of our manufacturing capability, (vi) the size and timing of customer orders, (vii) the amount of time that it takes to fulfill orders and ship our products, (viii) the length of our sales cycle to new customers and the time and expense incurred in further penetrating our existing customer base, (ix) manufacturing inefficiencies associated with new product introductions, (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 inability of our sales and marketing programs to achieve their sales targets, (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) inefficiencies in the management of our inventories and fixed assets, (xvii) compliance with government regulations including health, safety, and environmental matters, and (xviii) costs associated with the training and ramp-up time for new sales people;
- changes in gross margins due to a changing mix of products sold and the different gross margins on different products and sales channels;
- changes in applicable laws, rules or regulations, or their interpretation or enforcement, or the enactment of new laws, rules or regulations that apply to our business operations or require us to incur significant expenses for compliance;
- our inability to successfully comply with the requirements of the Restriction of Hazardous Substances Directive and the Waste Electrical and Electronic Equipment Directive in the European Union;
- the inability of our products to displace traditional measurement devices and attain broad market acceptance;

- the impact of competitive products and pricing on our current offerings;
- the loss or change of any of our executive officers or other key personnel, which may be impacted by factors such as our inability to competitively address inflationary pressures on employee compensation and flexibility in employee work arrangements;
- difficulties in recruiting research and development engineers, application engineers, or other key personnel;
- the failure to effectively manage the effects of any future growth;
- the impact of reductions or projected reductions in government spending, or uncertainty regarding future levels of government expenditures, particularly in the defense sector;
- variations in our effective income tax rate, which makes it difficult to predict our effective income tax rate on a quarterly and annual basis, and the impact of the U.S. Tax Cuts and Jobs Act of 2017 on the global intangible low-taxed income of foreign subsidiaries;
- the loss of key suppliers and the inability to find sufficient alternative suppliers in a reasonable period of time or on commercially reasonable terms;
- the impact of fluctuations in exchange rates on non-U.S. dollar-denominated revenues and expenses;
- the effect of estimates and assumptions with respect to critical accounting policies and the impact of the adoption of recently issued accounting pronouncements;
- the effect of changes in political conditions in the U.S. and other countries in which we operate, including the effect of changes in U.S. trade policies or the United Kingdom’s withdrawal from the European Union, on general market conditions, global trade policies and currency exchange rates;
- the magnitude of increased warranty costs from new product introductions and enhancements to existing products;
- the sufficiency of our plants and third-party resources to meet manufacturing requirements;
- the continuation of our share repurchase program;
- the sufficiency of our working capital and cash flows from operations to fund our short- and long-term liquidity requirements;
- the impact of geographic changes in the manufacturing or sales of our products on our effective income tax rate;
- our ability to comply with the requirements for favorable tax rates in foreign jurisdictions; and
- other risks and uncertainties discussed in Part I, Item 1A. Risk Factors in our Annual Report, elsewhere in this Quarterly Report on Form 10-Q, and in other SEC filings.

Moreover, new risks and uncertainties emerge from time to time, and we undertake no obligation to update publicly or review such risks and uncertainties included in this Quarterly Report, unless otherwise required by law.

Overview

We are a global technology company that designs, develops, manufactures, markets and supports software driven, three-dimensional (“3D”) measurement, imaging, and realization solutions for the 3D metrology, architecture, engineering and construction (“AEC”), Operations and Maintenance (“O&M”) and public safety analytics markets. We enable our customers to capture, measure, manipulate, interact with and share 3D and 2D data from the physical world in a virtual environment and then translate this information back into the physical domain. Our broad technology set equips our customers with a wide range of 3D capture technologies that range from ultra-high accuracy laser-scanner-based technology to lower accuracy, photogrammetry-based technology. Our FARO suite of 3D products and software solutions are used for inspection of components and assemblies, rapid prototyping, reverse engineering, documenting large volume or structures in 3D, surveying and construction, construction management, assembly layout, machine guidance as well as in investigation and reconstructions of crash and crime scenes. We sell the majority of our solutions through a direct sales force, with an increasing volume being sold through an indirect channel across a range of industries including automotive, aerospace, metal and machine fabrication, surveying, architecture, engineering and construction, public safety forensics and other industries.

We derive our revenues primarily from the sale of our measurement equipment and related multi-faceted software programs. Revenue related to these products is generally recognized upon shipment. In addition, we sell extended warranties and training and technology consulting services relating to our products. We recognize the revenue from hardware service contracts and software maintenance contracts on a straight-line basis over the contractual term, and revenue from training and technology consulting services when the services are provided.

We operate in international markets throughout the world and maintain sales offices in Australia, Brazil, Canada, China, France, Germany, India, Italy, Japan, Malaysia, Mexico, the Netherlands, Poland, Singapore, South Korea, Spain, Switzerland, Thailand, the United Kingdom and the United States.

Sanmina currently manufactures our FARO Quantum Max Arm, FARO Focus Laser Scanner, FARO Laser Tracker and our FARO Laser Projector products in their facility located in Thailand. We expect these third-party manufacturing facilities to have the production capacity necessary to support our volume requirements during 2023.

We account for wholly-owned foreign subsidiaries in the currency of the respective foreign jurisdiction; therefore, fluctuations in exchange rates may have an impact on the value of the intercompany account balances denominated in different currencies and reflected in our consolidated financial statements. We are 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. No such instruments were utilized by the Company in 2023, 2022 or 2021. We have not used hedging instruments in the past as fluctuations in exchange rate on our revenue were mostly offset by those same fluctuations in exchange rate on our expenses, providing a natural hedge in foreign jurisdictions. Our exchange rate exposure may change as a result of our current or future operational strategies and we will continue assessing the appropriateness of hedging for our business.

Restructuring Plan and Integration Plan

In the first quarter of 2020, our Board of Directors approved a global restructuring plan (the “Restructuring Plan”), which is intended to support our strategic plan in an effort to improve operating performance and ensure that we are appropriately structured and resourced to deliver increased and sustainable value to our shareholders and customers. Key activities under the Restructuring Plan include a continued focus on efficiency and cost-saving efforts, which included a planned decrease of total headcount upon the completion of the Restructuring Plan.

On July 15, 2021, we entered into a manufacturing services agreement (the “Agreement”) with Sanmina Corporation (Nasdaq: SANM) (“Sanmina”), in connection with the Restructuring Plan. Under the Agreement, Sanmina will provide manufacturing services for the Company’s measurement device products previously manufactured by the Company at the Company’s Lake Mary, Florida, Exton, Pennsylvania, and Stuttgart, Germany manufacturing sites. This phased transition to a Sanmina production facility was completed at the beginning of the third quarter of 2022 as part of our cost reduction initiative. We are currently evaluating these manufacturing sites with the intention to reduce our leased floor space. However, all of these facilities are mixed-use spaces shared with our service, research and development, or sales teams who continue to use these spaces. The Company, in collaboration with third party lessors and architectural resources, intends to conduct studies over the feasibility of abandoning or demising leased floor space against our current needs. Our current needs continue to include access to existing spaces previously constructed to closely monitor temperature and vibration for our service and research and development teams. The conclusion of this evaluation and any subsequent approval to abandon or reduce these leased spaces would be considered as a change in the manner of the use of these corresponding assets, and thereby will be evaluated for impairment. We expect to complete this evaluation before the first half of fiscal year 2023. As of March 31, 2023, the remaining value of leasehold improvements for these facilities is approximately $0.6 million and a portion of this may be impaired, if the Company decides to reduce or abandon the leased space. Separately, we may also incur additional charges for the modification of leases for these facilities.

Substantially all of our planned activities under the Restructuring Plan are complete and any final steps will be performed as a part of the Integration Plan discussed below.

On February 7, 2023, our Board of Directors approved an integration plan (the "Integration Plan"), which is intended to streamline and simplify operations, particularly around our recent acquisitions and the resulting redundant operations and offerings. Key activities under the Integration Plan include a planned decrease in headcount, consolidation of our cloud-based offerings from 3 platforms (2 acquired, 1 organic) into a single customer offering, and the optimization of our facility assets to align with current and expected future utilization. As of March 31, 2023, we expected to incur total pre-tax charges in the range of $10 million to $16 million through the end of fiscal year 2023, and expected to realize $10 million in annualized cost savings when this plan is complete. This plan was amended on May 3, 2023. As of the date of this filing and per the amendment on May 3, 2023, the total expected pre-tax charges are in the range of $22 million to $28 million. We now expect to realize annualized cost savings in the range of $20 million to $30 million when this plan is complete. In the first quarter of 2023, we have recognized $4.2 million in restructuring costs associated with the Integration Plan, and paid $0.8 million during the same period; primarily consisting of severance and related benefits. Also, in the fourth quarter of 2022, we’ve taken a $1.1 million asset impairment charge to fully expense the net book value of certain software assets. These costs were included in the financial results of the fourth quarter of 2022.

Faro Sphere and the Unified Software Environment

FARO Sphere is our new cloud-based platform that is the foundation to our new software and solution strategy. Our objective is to provide differentiated value by offering workflow enhancements which include data uploads from any location, access to our existing suite of 3D software applications, cloud-based data analysis and global user access. FARO Sphere represents the first step into expansion of our cloud-based software offerings that we believe will deliver greater value to our customers and to our shareholders. The FARO Sphere environment could be adopted globally across a wide range of markets, including construction management, facilities, operations and maintenance, robotic simulation and incident preplanning. This potential adoption would lead to an increase in the number of users and thus enable revenue growth of our software and a shift toward increased levels of recurring revenue over time. We have released the first phase of FARO Sphere to our customers during the second quarter of 2022. A key aspect our our Integration Plan is to consolidate our cloud-based offerings into a single Unified Software Environment.

Revenue from our current software products was $10.3 million and $10.3 million for the three months ended March 31, 2023 and March 31, 2022, respectively. Our recurring revenue which is comprised of hardware service contracts, software maintenance contracts, and subscription-based software applications was $16.7 million and $16.5 million for the three months ended March 31, 2023 and March 31, 2022, respectively.

Research and development costs incurred relating to the development of internal-use software and website development, including software used to upgrade and enhance our websites and applications to be sold as a service are capitalized in the period incurred and amortized over 1 year to 5 years. These costs include external direct costs of materials and services and internal costs such as payroll and benefits of those employees directly associated with the development of new functionality in internal use software to be sold as a service. The amount of costs capitalized relating to internally developed computer software to be sold as a service was $1.3 million and $1.5 million for the three months ended March 31, 2023 and March 31, 2022, respectively. Cash paid relating to these development costs are included as an investing activity within the Cash paid for technology development, patents and licenses line of our condensed consolidated statement of cash flows.

Acquisitions

On September 1, 2022, we acquired UK-based GeoSLAM, a leading provider of mobile scanning solutions with proprietary high-productivity simultaneous localization and mapping (“SLAM”) software. GeoSLAM's software enables mobile 3D documentation of indoor or enclosed environments without the need for global positioning system (“GPS”). GeoSLAM’s products and solutions are primarily used today in the geospatial and mining markets. However, there is a growing demand for high productivity mobile scanning in the construction, operations and maintenance markets as well.

On December 1, 2022, we acquired SiteScape, an innovator in light detecting and ranging (“LiDAR”) 3D scanning software solutions for the architecture, engineering and construction (“AEC”) and operations and maintenance (“O&M”) markets. SiteScape enables LiDAR equipped mobile devices to easily capture indoor spaces digitally, providing a readily available entry-point to scanning physical spaces for a broad range of applications. The SiteScape software is available for all LiDAR equipped iPhone operating system (“iOS”) devices, which enables quick and easily accessible data capture to be available to the consumer-based market.

Sanmina Relationship Components: As presented on our Condensed Consolidated Balance Sheets

In order to provide greater transparency on our financial transactions with Sanmina, the following table presents the components of Sanmina relationship with the Company, as presented on our Condensed Consolidated Balance Sheets as of March 31, 2023 and December 31, 2022.

	March 31, 2023	December 31, 2022
Current Assets:		
Prepaid expenses and other current assets	$ 13,816	$ 14,674
Current Liabilities:		
Accounts payable [1]	$ 3,250	$ 5,137

(1) As of March 31, 2023, we had a net payable balance of $3.3 million, which includes $8.7 million of accounts receivable due from Sanmina and $11.9 million of accounts payable owed to Sanmina. As of December 31, 2022, we had a net payable balance of $5.1 million, which included $10.6 million of accounts receivable due from Sanmina and $15.7 million of accounts payable owed to Sanmina.

The amounts presented in the table above are based on the balances in the above captions, as of the dates indicated, and do not reflect our entire financial relationship with Sanmina.

Results of Operations

The following table sets forth, for the periods indicated, our unaudited results of operations expressed as dollar amounts and as a percentage of total sales.

	Three months ended March 31,			
(dollars in thousands)	2023	% of Sales	2022	% of Sales
Sales				
Product	$ 65,240	76.8 %	$ 56,730	74.0 %
Service	19,727	23.2 %	19,926	26.0 %
Total sales	84,967	100.0 %	76,656	100.0 %
Cost of sales				
Product	33,957	40.0 %	24,333	31.7 %
Service	11,294	13.3 %	11,297	14.7 %
Total cost of sales	45,251	53.3 %	35,630	46.5 %
Gross profit	39,716	46.7 %	41,026	53.5 %
Operating expenses				
Selling, general and administrative	41,376	48.7 %	35,490	46.3 %
Research and development	12,718	15.0 %	12,128	15.8 %
Restructuring costs	4,238	5.0 %	600	0.8 %
Total operating expenses	58,332	68.7 %	48,218	62.9 %
Loss from operations	(18,616)	(21.9)%	(7,192)	(9.4)%
Other (income) expense				
Interest (income) expense, net	835	1.0 %	8	— %
Other (income) expense, net	(220)	(0.3)%	(13)	— %
Loss before income tax benefit	(19,231)	(22.6)%	(7,187)	(9.4)%
Income tax expense (benefit)	1,933	2.3 %	2,500	3.3 %
Net loss	$ (21,164)	(24.9)%	$ (9,687)	(12.6)%

Consolidated Results

Three Months Ended March 31, 2023 Compared to the Three Months Ended March 31, 2022

Sales. Total sales increased by $8.3 million, or 10.8%, to $85.0 million for the three months ended March 31, 2023 from $76.7 million for the three months ended March 31, 2022. The increase was primarily driven by our product sales, as our service sales remained consistent with the comparable period. Total product sales increased by $8.5 million, or 15.0%, to $65.2 million for the three months ended March 31, 2023 from $56.7 million for the three months ended March 31, 2022. Total product sales increased due to an increased global demand for our Focus Laser Scanner and Quantum Max Arm, combined with the addition of GeoSLAM product sales of $4.0 million.

Gross profit. Gross profit decreased by $1.3 million, or 3.2%, to $39.7 million for the three months ended March 31, 2023 from $41.0 million for the three months ended March 31, 2022, and gross margin decreased by 6.8 percentage points to 46.7% for the three months ended March 31, 2023 from 53.5% for the three months ended March 31, 2022. Gross margin from product revenue decreased by 9.1 percentage points to 48.0% for the three months ended March 31, 2023 from 57.1% for the prior year period primarily due to unfavorable price variances due to global supply shortages. The higher cost of raw materials primarily stems from sourcing semiconductor components in an extremely tight broker market, where we had to make large payments to secure delivery in advance of receiving certain components, since the third quarter of 2023. As of March 31, 2023, these advance payments included in Inventories, net, on our Consolidate Balance Sheets accounts for $8.6 million. We expect amortizing these amounts in the second and third quarters of 2023, in correlation with the receipt and consumption of the associated materials. We anticipate continued unfavorable price variances until global supply and cost conditions normalize. However, we are expecting our continued shift in supply chain sourcing to Southeast Asia to positively impact gross margins in 2024. Gross margin from service revenue decreased by 0.6 percentage points to 42.7% for the three months ended March 31, 2023 from 43.3% for the prior year period, primarily due to higher service component pricing with a relatively consistent fixed cost structure.

Selling, general and administrative expenses. Selling, general and administrative expenses increased by $5.9 million, or 16.6%, to $41.4 million for the three months ended March 31, 2023 from $35.5 million for the three months ended March 31, 2022. This increase was primarily driven by higher personnel costs resulting from additional headcount obtained primarily from both of our recent acquisitions of GeoSLAM and SiteScape, and base compensation increases. Selling, general and administrative expenses as a percentage of sales increased by 2.4 percentage points to 48.7% for the three months ended March 31, 2023 from 46.3% for the three months ended March 31, 2022. Our worldwide period-ending selling, general and administrative headcount increased by 42, or 5.6%, to 795 at March 31, 2023, from 753 at March 31, 2022.

Research and development expenses. Research and development expenses increased by $0.6 million, or 4.9%, to $12.7 million for the three months ended March 31, 2023 from $12.1 million for the three months ended March 31, 2022. Research and development expenses as a percentage of sales decreased to 15.0% for the three months ended March 31, 2023 from 15.8% for the three months ended March 31, 2022.

Restructuring costs. In February 2023, we initiated the Integration Plan to streamline and simplify operations, particularly around our recent acquisitions and the resulting redundant operations and offerings. Restructuring costs included in operating expenses increased by $3.6 million to $4.2 million for the three months ended March 31, 2023 from $0.6 million for the three months ended March 31, 2022 primarily consisting of accrued severance and related benefits charges and professional fees.

Interest (income) expense, net. We recorded net interest expense of $0.8 million for the three months ended March 31, 2023 and net interest expense of less than $0.1 million for the three months ended March 31, 2022.

Other income, net. For the three months ended March 31, 2023, other income was $0.2 million compared with other expense of less than $0.1 million for the three months ended March 31, 2022.

Income tax expense (benefit). For the three months ended March 31, 2023 we recorded an income tax expense of $1.9 million compared with an income tax benefit of $2.5 million for the three months ended March 31, 2022. Our effective tax rate was -10.1% for the three months ended March 31, 2023 compared with -34.8% in the prior year period. The tax rate for 2023 reflects a tax expense on a pre-tax loss consistent with the prior year period. The change in our income tax expense and our effective tax rate were primarily due to the continued impact of the capitalization of research and development (“R&D”) expenditures for income tax purposes. The Tax Cuts and Jobs Act (the “Act”) requires the capitalization and amortization of R&D costs incurred after December 31, 2021. We have considered the continued effects of the Act on the forecasted domestic taxable income for the year ending December 31, 2023. Our entity in the United States remains in a full valuation allowance position, hence we were not able to recognize the tax benefits associated with the capitalization of these R&D expenditures.

Our quarterly estimate of our annual effective tax rate and our quarterly provision for income tax expense (benefit) are subject to significant variation due to numerous factors, including variability in accurately predicting our pretax and taxable income or loss and the mix of jurisdictions to which they relate, as well as the amount of pretax income or loss recognized during the quarter.

Net loss. Our net loss was $21.2 million for the three months ended March 31, 2023 compared with net loss of $9.7 million for the prior year period, reflecting the impact of the factors described above.

Liquidity and Capital Resources

Cash and cash equivalents increased by $30.8 million to $68.6 million at March 31, 2023, from $37.8 million at December 31, 2022. The increase was primarily driven by our issuance of the Notes.

Cash used in operating activities was $18.3 million during the three months ended March 31, 2023, compared to $7.0 million of cash used in operating activities during the three months ended March 31, 2022. The increase was due to a larger current year net loss and changes in working capital accounts, primarily consisting of an increase in other current assets originating from the timing of refunds on value-added tax payments. We received approximately $9.0 million of the aforementioned tax refunds in the first half of the second quarter of 2023.

Cash used in investing activities during the three months ended March 31, 2023, was $23.5 million compared to cash used in investing activities of $5.1 million during the three months ended March 31, 2022. The increase was primarily due to the Company's investment of $20.0 million in U.S. Treasury securities with a 6-month maturity.

Cash provided by financing activities was $72.3 million during the three months ended March 31, 2023, compared to cash used in financing activities of $1.0 million for the three months ended March 31, 2022. The increase was primarily due to the Company's issuance of the Notes. The Notes are general senior unsecured obligations of the Company.

The Notes will mature on February 1, 2028, unless earlier redeemed, repurchased or converted. The Notes bear interest from January 24, 2023, at a rate of 5.50% per annum payable semiannually in arrears on February 1 and August 1 of each year, beginning August 1, 2023. The Notes may bear additional interest under specified circumstances relating to the Company's failure to comply with its reporting obligations under the indenture governing the Notes or if the Notes are not freely tradeable as required by the indenture.

The Notes will be convertible at the option of the holders of the Notes at any time prior to November 1, 2027, only under the following circumstances: (1) during any calendar quarter commencing after the calendar quarter ending on March 31, 2023 (and only during such fiscal quarter), if the last reported sale price of the Company's common stock, par value $0.001 per share (hereinafter referred to as "common stock"), for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on and including, the last trading day of the immediately preceding calendar quarter exceeds 130% of the conversion price on each applicable trading day; (2) during the five-business day period after any ten consecutive trading day period (the "measurement period") in which the trading price per $1,000 principal amount of Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's common stock and the conversion rate for the Notes on each such trading day; (3) upon the occurrence of certain corporate events or distributions on the Company's common stock; (4) if the Company calls such Notes for redemption; or (5) upon the occurrence of specified corporate events. On or after November 1, 2027, holders may convert all or any portion of their Notes at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date regardless of the foregoing conditions. Upon conversion, the Company will satisfy its conversion obligation by paying or delivering, as the case may be, cash, shares of common stock or a combination of cash and shares of common stock, at the Company's election. The conversion rate for the Notes will initially be 23.6072 shares of the common stock per $1,000 principal amount of Notes, which is equivalent to an initial conversion price of approximately $42.36 per share of the common stock. The initial conversion price of the Notes represents a premium of approximately 20% to the $35.30 per share last reported sale price of the common stock on January 19, 2023. The conversion rate is subject to adjustment under certain circumstances in accordance with the terms of the indenture (governing the Notes).

The Company may not redeem the Notes prior to February 5, 2026. The Company may redeem for cash all or any portion of the Notes, at its option, on or after February 5, 2026, and on or before the 50th scheduled trading day immediately before the maturity date, if the last reported sale price of the common stock exceeds 130% of the conversion price on (i) each of at least 20 trading days (whether or not consecutive) during the 30 consecutive trading days ending on and including the last trading day immediately before the date on which the Company provides notice of redemption and (ii) the trading day immediately before the date the Company provides such notice. The redemption price will be equal to 100% of the principal amount of the Notes to be redeemed, plus any accrued and unpaid interest to, but excluding, the redemption date. No sinking fund is provided for the Notes, which means that the Company is not required to redeem or retire the Notes periodically.

Upon the occurrence of a fundamental change (as defined in the indenture governing the Notes) prior to the maturity date, subject to certain conditions, holders of the Notes may require the Company to repurchase all or a portion of the Notes for cash at a repurchase price equal to 100% of the principal amount of the Notes to be repurchased, plus any accrued and unpaid interest to, but excluding, the fundamental change repurchase date.

The net proceeds from this offering were approximately $72.2 million, after deducting the initial purchaser discounts and commissions and the Company's estimated offering expenses related to the offering. For the three months ended March 31, 2023, we have incurred $0.5 million in debt issuance costs primarily related to professional fees which are excluded from the discounts and commissions previously mentioned. The Company intends to use the net proceeds from this offering for working capital and other general corporate purposes.

Of our cash and cash equivalents, $31.6 million was held by foreign subsidiaries as of March 31, 2023. On December 22, 2017, the United States enacted the U.S. Tax Cuts and Jobs Act, resulting in significant modifications to existing tax law, which included a transition tax on the mandatory deemed repatriation of foreign earnings. As a result of the U.S. Tax Cuts and Jobs Act, the Company can repatriate foreign earnings and profits to the U.S. with minimal U.S. income tax consequences, other than the transition tax and global intangible low-taxed income ("GILTI") tax. We have reinvested a large portion of our undistributed foreign earnings and profits in acquisitions and other investments and intends to bring back a portion of foreign cash in certain jurisdictions where we will not be subject to local withholding taxes and which were subject already to transition tax and GILTI tax.

On November 24, 2008, our Board of Directors approved a $30.0 million share repurchase program. Acquisitions for the share repurchase program may 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 expiration date or other restriction governing the period over which we can repurchase shares under the program. In October 2015, our Board of Directors authorized an increase to the existing share repurchase program from $30.0 million to $50.0 million. We made no stock repurchases during the three-month period ended March 31, 2023, under this program. As of March 31, 2023, we had authorization to repurchase $18.3 million remaining under the repurchase program.

We believe that our working capital and anticipated cash flow from operations will be sufficient to fund our short- and long-term liquidity operating requirements for at least the next 12 months.

We have no off-balance sheet arrangements.

Contractual Obligations and Commercial Commitments

We enter into purchase commitments for products and services in the ordinary course of business. These purchases generally cover production requirements for 60 to 120 days as well as materials necessary to service customer units through the product lifecycle and for warranty commitments. As of March 31, 2023, we had $29.7 million in purchase commitments that are expected to be delivered within the next 12 months. We also had $23.9 million in long-term commitments for purchases to be delivered after 12 months. Other than as described in the preceding sentences, there have been no material changes to the contractual obligations and commercial commitments table included in Part II, Item 7 of our Annual Report.

Critical Accounting Estimates and Policies

The preparation of our condensed consolidated financial statements requires our 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. We base our 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. A discussion of our critical accounting policies is included in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report. As of March 31, 2023, our critical accounting policies have not changed from those described in our Annual Report.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Foreign Exchange Exposure

We conduct a significant portion of our business outside the United States. As of and for the three months ended March 31, 2023, 54% of our revenue was invoiced, and a significant portion of our operating expenses and manufacturing costs were paid, in foreign currencies, and 56% of our assets were denominated in foreign currencies. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material effect on our 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 our operations cannot be accurately predicted due to our constantly changing exposure to various currencies, and the fact that all foreign currencies do not react in the same manner in relation to the U.S. dollar. Our most significant exposures are to the Euro, Japanese Yen, Swiss Franc, Chinese Yuan and Brazilian Real. To the extent that the percentage of our non-U.S. dollar revenues derived from international sales increases in the future, our exposure to risks associated with fluctuations in foreign exchange rates may increase.

Global Inflation Exposure

General inflation in the United States, Europe and other geographies has risen to levels not experienced in recent decades. General inflation, including rising prices for our raw materials and other inputs as well as rising salaries negatively impact our business by increasing our cost of sales and operating expenses. A period of a rising rate of inflation also negatively impacts our business by decreasing the capital for our customers to deploy to purchase our products and services. Inflation may cause our customers to reduce or delay orders for our goods and services thereby causing a decrease in sales of our products and services. The impact of future inflation fluctuations on the results of our operations cannot be accurately predicted.

Item 4. Controls and Procedures

We are responsible for establishing and maintaining disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), that are designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's (the "SEC") rules and forms. Disclosure controls and procedures also include, without limitation, controls and procedures that are designed to provide reasonable assurance that such information is accumulated and communicated to our management, including our Principal Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objective. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that our management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Principal Executive Officer and our Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of March 31, 2023. Based on that evaluation, our Principal Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2023 to provide reasonable assurance that information required to be disclosed in this Quarterly Report on Form 10-Q was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and was accumulated and communicated to our management, including our Principal Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

During the quarter ended March 31, 2023, there was no change in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are not involved in any legal proceedings, including routine litigation arising in the normal course of business, that we believe will have a material adverse effect on our business, financial condition or results of operations.

Item 1A. Risk Factors

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed under “Risk Factors” in this Item 1A and in our Annual Report, before deciding to invest in, or retain, shares of our common stock. These risks and uncertainties could materially and adversely affect our business, financial condition, and results of operations. The risks described in our Annual Report, in this Quarterly Report, and in subsequent periodic reports filed with the SEC are not the only risks we face. Our operations could also be affected by additional factors that are not presently known by us or by factors that we currently consider to be immaterial to our business. There have been no material changes in our risk factors from those set forth in our Annual Report, other than as set forth below.

Market conditions and changing circumstances, some of which may be beyond our control, could impair our ability to access our existing cash, cash equivalents and investments and to timely pay key vendors and others.

Market conditions and changing circumstances, some of which may be beyond our control, could impair our ability to access our existing cash, cash equivalents and investments and to timely pay key vendors and others. For example, in March 2023, Silicon Valley Bank (“SVB”), was placed into receivership with the FDIC, and all funds held at SVB were temporarily inaccessible to SVB’s customers and then in May 2023, First Republic Bank was also placed into receivership with the FDIC, and substantially all of its assets were sold to JPMorgan Chase Bank, National Association. If other banks and financial institutions with whom we have banking relationships enter receivership or become insolvent in the future, we may be unable to access, or we may lose, some or all of our existing cash, cash equivalents and investments, to the extent those funds are not insured or otherwise protected by the FDIC. In addition, in such circumstances we might not be able to timely pay key vendors and others. We regularly maintain cash balances that are not insured or are in excess of the FDIC’s insurance limit. Any delay in our ability to access our cash, cash equivalents and investments, or the loss of some or all of such funds, or inability to timely pay key vendors and others, could have a material adverse effect on our operations and cause us to seek additional capital sooner than planned.

Our executive management team has gone through significant changes and any failure to attract and retain qualified personnel could lead to a loss of sales or decreased profitability.

The loss of any of our current executive officers, or other key personnel, could adversely affect our sales, profitability or growth. Our executive management team has gone through a significant transition over the course of the last three years, including the hiring of a new President and Chief Executive Officer and a new Chief Financial Officer and most recently, the announcement of the retirement of our President and Chief Executive Officer and the appointment of our current Chairman, Yuval Wasserman, as our Executive Chairman, who will also assume the role of Interim Chief Executive Officer. Any changes and turnover of management could also adversely impact our stock price, and our client relationships and could make recruiting for future management positions more difficult. Moreover, we face competition for qualified personnel and we continue to rely, in part, on equity awards to attract and retain qualified personnel. Our ability to attract and retain qualified personnel could result in increased salaries and other compensation expenses and could negatively affect our profitability.

We may experience volatility in our stock price.

The price of our common stock has been, and may continue to be, highly volatile in response to various factors, many of which are beyond our control, including:

- fluctuations in demand for, and sales of, our products or prolonged downturns in the industries that we serve;
- actual or anticipated variations in quarterly or annual operating results;
- general economic uncertainties;
- issuances of shares of our common stock, whether in connection with an acquisition or upon conversion of some or all of our outstanding Notes;
- speculation in the press or investment community; and
- announcements of technological innovations or new products by us or our competitors.

The market price of our common stock may also be affected by announcements of executive leadership changes or our inability to meet analyst and investor expectations and failure to achieve projected financial results. Any failure to meet such expectations or projected financial results, even if minor, could cause the market price of our common stock to decline significantly. Volatility in our stock price may result in the inability of our shareholders to sell their shares at or above the price at which they purchased them.

Our relatively small public float and daily trading volume have in the past caused, and may in the future result in, significant volatility in our stock price. At March 31, 2023, we had approximately 20.1 million shares outstanding held by non-affiliates. Our daily trading volume for the quarter ended March 31, 2023 averaged approximately 180,034 shares.

In addition, stock markets have experienced in the past and may in the future experience a high level of price and volume volatility, and the market prices of equity securities of many companies have experienced in the past and may in the future experience wide price fluctuations not necessarily related to the operating performance of such companies. These broad market fluctuations may adversely affect the market price of our common stock. In the past, securities class action lawsuits frequently have been instituted against companies following periods of volatility in the market price of such companies' securities. If any such litigation is instigated against us, it could result in substantial costs and a diversion of management's attention and resources, which could have a material adverse effect on our results of operations and financial condition.

We may be unable to recognize the anticipated benefits of our Restructuring Plan, our new strategic plan, and any future restructuring and strategic plans.

On February 14, 2020, our Board of Directors approved a global restructuring plan, which is intended to support our new strategic plan in an effort to improve operating performance and to help ensure that we are appropriately structured and resourced to deliver sustainable value to our shareholders and customers. On February 7, 2023, our Board of Directors approved an integration plan (the "Integration Plan"), which is intended to streamline and simplify operations particularly around recent acquisitions and the resulting redundant operations and offerings, and on May 3, 2023, amended the Integration Plan, to further increase savings. Actual results, including the final costs of these restructuring plans, our new strategic plan and our ability to sustain savings, may differ materially from our expectations, resulting in our inability to realize the expected benefits of these restructuring plans and negatively impact our ability to execute our future plans and strategies, which could have a material adverse effect on our business, financial condition and results of operations.

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

Purchases of Equity Securities by the Issuer Under the Share Repurchase Plan

On November 24, 2008, our Board of Directors approved a $30.0 million share repurchase program. Acquisitions for the share repurchase program may 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 expiration date or other restriction governing the period over which we can repurchase shares under the program. In October 2015, our Board of Directors authorized an increase to the existing share repurchase program from $30.0 million to $50.0 million. We made no stock repurchases during the three month period ended March 31, 2023 under this program. As of March 31, 2023, we had authorization to repurchase $18.3 million remaining under the repurchase program.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

On May 3, 2023, an amendment to the Integration Plan was approved by our Board of Directors. The original approval anticipated pre-tax charges in the range of $10 million to $16 million, along with an anticipated annualized savings of approximately $10 million. The amendment approves pre-tax charges in the range of $22 million to $28 million, with a targeted annualized savings of approximately $20 million to $30 million.

The Integration Plan is intended to streamline and simplify operations, particularly around our recent acquisitions and the resulting redundant operations and offerings. Key activities under the Integration Plan include a planned decrease in headcount, consolidation of our cloud-based offerings from 3 platforms (2 acquired, 1 organic) into a single customer offering, and the optimization of our facility assets to align with current and expected future utilization.

Item 6. Exhibits

EXHIBIT INDEX

Exhibit Number	Exhibit Description	Incorporated by Reference				Provided Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Amended and Restated Articles of Incorporation, as amended	S-1/A	333-32983	3.1	September 10,1997	
3.2	Amended and Restated Bylaws	10-K	0-23081	3.2	February 16, 2022	
4.1	Specimen Stock Certificate	S-1/A	333-32983	4.1	September 10, 1997	
4.2	Indenture, dated as of January 24, 2023, between FARO Technologies, Inc. and U.S. Bank Trust Company, National Association	8-K	000-23081	4.1	January 24, 2023	
4.3	Form of 5.50% Convertible Senior Notes due 2028 (Included as Exhibit A to the Indenture Filed as Exhibit 4.3 to this Form 10-K)	8-K	000-23081	4.1, Exhibit A	January 24, 2023	
31.1	Certification of the Principal Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
31.2	Certification of the Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
32.1*	Certification of the Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2*	Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
101.SCH	Inline XBRL Taxonomy Extension Schema Document					X
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document					X
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document					X
101.PRE	Inline XBRL Taxonomy Presentation Linkbase Document					X
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document					X
104	Cover Page Interactive Data File (formatted as inline XBRL with applicable taxonomy extension information contained in Exhibits 101.)					X

* - The certifications attached as Exhibit 32.1 and 32.2 that accompany this Quarterly Report on Form 10-Q are deemed furnished and not filed with the Securities and Exchange Commission and are not to be incorporated by reference into any filing of the Registrant under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

SIGNATURE

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

		FARO Technologies, Inc. (Registrant)
Date: May 8, 2023	By:	/s/ Allen Muhich
		Name: Allen Muhich Title: Chief Financial Officer (Duly Authorized Officer and Principal Financial Officer)

EXHIBIT 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Yuval Wasserman, 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 8, 2023

/s/ Yuval Wasserman

Yuval Wasserman
Executive Chairman
(Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Allen Muhich, 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 8, 2023

/s/ Allen Muhich

Allen Muhich
Chief Financial Officer
(Principal Financial Officer)

EXHIBIT 32.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED 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 Executive Chairman and Principal Executive Officer of FARO Technologies, Inc. (the Company), hereby certify that the Quarterly Report on Form 10-Q for the quarter ended March 31, 2023 (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.

Date: May 8, 2023

/s/ Yuval Wasserman

Yuval Wasserman
Executive Chairman
(Principal Executive Officer)

EXHIBIT 32.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

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 Chief Financial Officer of FARO Technologies, Inc. (the Company), hereby certify that the Quarterly Report on Form 10-Q for the quarter ended March 31, 2023 (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.

Date: May 8, 2023

/s/ Allen Muhich

Allen Muhich
Chief Financial Officer
(Principal Financial Officer)