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

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2009

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number 0-23081

FARO TECHNOLOGIES, INC.

(Exact name of Registrant as Specified in Its Charter)

Florida

*(State or Other Jurisdiction
of Incorporation or Organization)*

250 Technology Park, Lake Mary, FL

(Address of Principal Executive Offices)

59-3157093

(I.R.S. Employer Identification Number)

32746

(Zip Code)

(Registrant's telephone number, including area code): (407) 333-9911

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$.001	NASDAQ Global Market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definite proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer Non-accelerated filer

Smaller Reporting Company

(Do not check if a smaller reporting company)

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

The aggregate market value of the Registrant's common stock held by non-affiliates of the Registrant on July 3, 2009, the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$386 million (based on the last sale on such date on the NASDAQ Global Market).

As of February 23, 2010, there were outstanding 16,119,044 shares of the Registrant's common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's proxy statement for the 2010 Annual Meeting of Shareholders are incorporated by reference in Part III of this Annual Report on Form 10-K.

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PART I

CAUTIONARY STATEMENTS FOR FORWARD-LOOKING INFORMATION

Some of the statements made in this Annual Report on Form 10-K are “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, or the Exchange Act. Statements that are not historical facts or that describe our plans, beliefs, goals, intentions, objectives, projections, expectations, assumptions, strategies, or future events are forward-looking statements. In addition, words such as “may,” “will,” “believe,” “plan,” “should,” “could,” “seek,” “expect,” “anticipate,” “intend,” “estimate,” “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, and other factors that could cause actual results to differ materially from those expressed or implied by such forward-looking statements. Consequently, undue reliance should not be placed on these forward-looking statements. The Company does not intend to update any forward-looking statements, whether as a result of new information, future events, or otherwise, unless otherwise required by law. Important factors that could cause actual results to differ materially from those contemplated in such forward-looking statements include, among others, the following:

- the slowdown in the manufacturing industry or the domestic and international economies in the regions of the world where the Company operates;
- the Company’s inability to further penetrate its customer base;
- development by others of new or improved products, processes or technologies that make the Company’s products obsolete or less competitive;
- the Company’s inability to maintain its technological advantage by developing new products and enhancing its existing products;
- the Company’s inability to successfully identify and acquire target companies or achieve expected benefits from acquisitions that are consummated;
- the cyclical nature of the industries of the Company’s customers and material adverse changes in its customers access to liquidity and capital;
- the market potential for the computer-aided measurement (“CAM2”) market and the potential adoption rate for the Company’s products are difficult to quantify and predict;
- the inability to protect the Company’s patents and other proprietary rights in the United States and foreign countries;
- fluctuations in the Company’s annual and quarterly operating results and the inability to achieve its financial operating targets as a result of a number of factors including, without limitation (i) litigation and regulatory action brought against the Company, (ii) quality issues with its products, (iii) excess or obsolete inventory, (iv) raw material price fluctuations, (v) expansion of the Company’s manufacturing capability and other inflationary pressures, (vi) the size and timing of customer orders, (vii) the amount of time that it takes to fulfill orders and ship the Company’s products, (viii) the length of the Company’s sales cycle to new customers and the time and expense incurred in further penetrating its existing customer base, (ix) increases in operating expenses required for product development and new product marketing, (x) costs associated with new product introductions, such as product development, marketing, assembly line start-up costs and low introductory period production volumes, (xi) the timing and market acceptance of new products and product enhancements, (xii) customer order deferrals in anticipation of new products and product enhancements, (xiii) the Company’s success in expanding its sales and marketing programs, (xiv) start-up costs associated with opening new sales offices outside of the United States, (xv) fluctuations in revenue without proportionate adjustments in

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fixed costs, (xvi) the efficiencies achieved in managing inventories and fixed assets, (xvii) investments in potential acquisitions or strategic sales, product or other initiatives, (xviii) shrinkage or other inventory losses due to product obsolescence, scrap or material price changes, (xix) adverse changes in the manufacturing industry and general economic conditions, (xx) compliance with government regulations including health, safety, and environmental matters, (xxi) the ultimate costs of the Company's monitoring obligations in respect of the Foreign Corrupt Practices Act ("FCPA") matter; and (xxii) other factors noted herein;

- changes in gross margins due to changing product mix of products sold and the different gross margins on different products;
- the Company's inability to successfully maintain the requirements of Restriction of use of Hazardous Substances ("RoHS") and Waste Electrical and Electronic Equipment ("WEEE") compliance into its products;
- the inability of the Company's products to displace traditional measurement devices and attain broad market acceptance;
- the impact of competitive products and pricing in the CAM2 market and the broader market for measurement and inspection devices;
- the effects of increased competition as a result of recent consolidation in the CAM2 market;
- risks associated with expanding international operations, such as fluctuations in currency exchange rates, difficulties in staffing and managing foreign operations, political and economic instability, compliance with import and export regulations, and the burdens and potential exposure of complying with a wide variety of U.S. and foreign laws and labor practices;
- the loss of the Company's Chief Executive Officer or other key personnel;
- difficulties in recruiting research and development engineers, and application engineers;
- the failure to effectively manage the Company's growth;
- variations in the effective income tax rate and the difficulty in predicting the tax rate on a quarterly and annual basis; and
- the loss of key suppliers and the inability to find sufficient alternative suppliers in a reasonable period or on commercially reasonable terms;

as well as other risks and uncertainties discussed in Part I. Item 1A. Risk Factors in this Annual Report on Form 10-K. Moreover, new risks and uncertainties emerge from time to time, and we undertake no obligation to update publicly or review the risks and uncertainties included in this Annual Report on Form 10-K.

ITEM 1. BUSINESS.

The Company designs, develops, manufactures, markets and supports portable, software driven, 3-D measurement and imaging systems used in a broad range of manufacturing, industrial, building construction and forensic applications. The Company's FaroArm[®], FARO Laser ScanArm[®] and FARO Gage articulated measuring devices, the FARO Laser Scanner Photon, the FARO Laser Tracker ION[™], and their companion CAM2 software, provide for Computer-Aided Design, or CAD, based inspection and/or factory-level statistical process control and high-density surveying. Together, these products integrate the measurement, quality inspection, and reverse engineering functions with CAD software to improve productivity, enhance product quality and decrease rework and scrap in the manufacturing process. The Company uses the acronym "CAM2" for this process, which stands for computer-aided measurement. As of December 2009, the Company's products have been purchased by approximately 10,000 customers worldwide, ranging from small machine shops to such large manufacturing and industrial companies as Audi, Boeing, Bombardier, FORD, General Electric, General Motors, Honda, Johnson Controls, Komatsu America International, Lockheed Martin, NASA, Northrup Grumman, Siemens and Volkswagen, among many others.

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The Company was founded in 1982 and re-incorporated in Florida in 1992. The Company's worldwide headquarters are located at 250 Technology Park, Lake Mary, Florida 32746, and its telephone number is (407) 333-9911.

Industry Background

The Company believes that there are four principal forces driving the need for its products and services: 1) the widespread use by manufacturers of CAD in product development, which shortens product cycles; 2) the adoption by manufacturers of quality standards such as Six Sigma and ISO-9000 (and its offshoot QS-9000), which stress the measurement of every step in a manufacturing process to reduce or eliminate defects, 3) the inability of traditional measurement devices to address many manufacturing problems such as throughput, efficiency, and accuracy, especially those related to large components for products such as automobiles, aircraft, heavy duty construction equipment, and factory retrofits, and 4) the growing demand to capture large volumes of three-dimensional data for modeling and analysis.

CAD improves the manufacturing process. The creation of physical products involves the processes of design, engineering, production and measurement and quality inspection. These basic processes have been profoundly affected by the computer hardware and software revolution that began in the 1980s. CAD software was developed to automate the design process, providing manufacturers with computerized 3-D design capability and shortening the time between design changes. Today, most manufacturers use some form of CAD software to create designs and engineering specifications for new products and to quantify and modify designs and specifications for existing products. While manufacturers previously designed their products to be in production for longer periods of time, current manufacturing practices must accommodate more frequent product introductions and modifications, while satisfying more stringent quality and safety standards. Assembly fixtures and measurement tools must be linked to the CAD design to enable production to keep up with the rate of design change.

Quality standards dictate measurement to reduce defects. QS-9000 is the name given to the Quality System Requirements of the automotive industry developed by Chrysler, Ford, General Motors and major truck manufacturers. Companies registered under QS-9000 are considered to have higher standards and better quality products. Six Sigma embodies the principles of total quality management that focus on measuring results and reducing product or service failure rates to 3.4 per million. All aspects of a Six Sigma company's infrastructure must be analyzed, and if necessary, restructured to increase revenues and raise customer satisfaction levels. The all-encompassing nature of these and other quality standards has resulted in manufacturers measuring every aspect of their process, including stages of product assembly that may never have been measured before, in part because of the lack of suitable measurement equipment.

Traditional products do not measure up. A significant aspect of the manufacturing process is measurement and quality inspection. Historically, manufacturers have measured and inspected products using hand-measurement tools such as scales, calipers, micrometers and plumb lines for simple measuring tasks, test (or check) fixtures for certain large manufactured products, and traditional (or fixed) coordinate measurement machines, or CMM, for objects that require higher precision measurement. However, the broader utility of each of these measurement methods is limited.

Although hand-measurement tools are often appropriate for simple geometric measurements, including hole diameters or length and width of a rectangular component, their use for complex part measurements, such as the fender of a car, is limited. Also, these devices do not allow for the measurements to be directly compared electronically to the CAD model of the part. Test fixtures (customized fixed tools used to make comparative measurements of complex production parts to "master parts") are relatively expensive and must be reworked or discarded each time a dimensional change is made in the part being measured. In addition, these manual measuring devices do not permit the manufacturer to electronically compare the dimensions of an object with its CAD model.

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Conventional CMMs are generally large, fixed-base machines that provide very high levels of precision and provide a link to the CAD model of the object being measured. However, fixed-base CMMs require the object being measured be brought to the CMM and the object fit within the CMMs measurement grid. As manufactured subassemblies increase in size and become integrated into even larger assemblies, they become less transportable, thus diminishing the utility of a conventional CMM. Consequently, manufacturers must continue to use hand-measuring tools, or expensive customized test fixtures, in order to measure large or unconventionally shaped objects. In addition, some parts or assemblies are not easily accessible and cannot be measured using traditional devices.

Manufacturing demands three-dimensional data. Conventional surveying equipment is limited to single-point measurements and does not have the capacity to capture and analyze large volumes of three-dimensional data. As data requirements for construction, civil engineering and forensic inspection projects become more complex, single-point measurement devices will become increasingly more difficult to utilize in those applications.

Escalating global competition has created a demand for higher quality products with shorter life cycles. Customers require more rapid design, greater control of the manufacturing process, tools to compare components to their CAD specifications and the ability to precisely measure components that cannot be measured or inspected by conventional devices, and the ability to capture and analyze large volumes of three-dimensional data. Moreover, they increasingly require measurement capabilities to be integrated into manufacturing processes and to be available on the factory floor.

FARO Products

The FaroArm. The FaroArm is a combination of a portable, six or seven-axis, instrumented articulated measurement arm, a computer, and CAM2 software programs, which are described below under “CAM2 Software”.

- **Articulated Arm**—Each articulated arm is comprised of three major joints, each of which may consist of one, two or three axes of motion. The articulated arm is available in a variety of sizes, configurations and precision levels suitable for a broad range of applications. To take a measurement, the operator simply touches the object to be measured with a probe at the end of the arm and presses a button. Data can be captured at either individual points or a series of points. Digital rotational transducers located at each of the joints of the arm measure the angles at those joints, and this rotational measurement data is transmitted to an on-board controller that converts the arm angles to precise locations in 3-D space using “xyz” position coordinates and “ijk” orientation coordinates.
- **Computer**—The Company pre-installs its CAM2 software on either a notebook or desktop style computer, depending on the customer’s need, and the measuring device, computer and installed software are sold as a system. The Company purchases the computers sold with its products from various suppliers.

The FARO Laser ScanArm. The FARO Laser ScanArm is a FaroArm equipped with a combination of a hard probe (like that in the FaroArm) and a non-contact line laser probe. This product provides the Company’s customers the ability to measure products without touching them and offers a seven-axis contact/non-contact measurement device with a fully integrated laser scanner. The ScanArm is used for non-contact measurement applications, including inspection, cloud-to-CAD comparison, rapid prototyping, reverse engineering and 3-D modeling.

The FARO Gage. Sold as a combination of an articulated arm device with a computer and software, the FARO Gage is a smaller, higher accuracy version of the FaroArm. The FARO Gage is also distinguished from the FaroArm by the special mounting features and software unique to the FARO Gage. The FARO Gage is targeted at machine tools, and bench tops around machine tools, where basic measurements of smaller machined parts must be measured. As such, the CAM2 FARO Gage software developed for this device, described below, features basic 2-D and 3-D measurements common to these applications.

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The FARO Laser Tracker ION. The FARO Laser ION combines a portable, large-volume laser measurement tool, a computer, and CAM2 software programs.

- **Laser Tracker**—The FARO Laser Tracker ION utilizes an ultra-precise laser beam to measure objects of up to 230 feet. It enables manufacturing, engineering, and quality control professionals to measure and inspect large parts, machine tools and other large objects on-site and in-process. With its greater angular resolution, repeatability, and accuracy, the FARO Laser Tracker ION advances already-proven tracker technology. Among its many enhanced features is AgilrADM, which improves upon existing Absolute Distance Measurement technology by providing the time-saving ability to reacquire the laser beam without the need to return to a known reference point or the need to hold the target stationary.
- **Computer**—The FARO Laser Tracker ION includes a notebook or desktop style computer, depending on the customer's requirements, that includes the pre-installed CAM2 Software.

The FARO Laser Scanner Photon. The FARO Laser Scanner Photon utilizes laser technology to measure and collect a cloud of data points, allowing for the detailed and precise three-dimensional rendering of an object or an area as large as a factory. This technology is currently used for factory planning, facility life-cycle management, quality control, forensic analysis and capturing large volumes of three-dimensional data. Laser scanning technology simplifies modeling, reduces project time and maintains or increases the accuracy of the image. The resulting data is used with major CAD systems or FARO's own proprietary CAM2 software.

CAM2 Software. CAM2 is the Company's family of proprietary CAD-based measurement and statistical process control software used with the Company's measurement devices. The CAM2 product line includes the following software programs, many of which are translated into multiple languages:

- **CAM2 Q** allows the FARO Laser ScanArm to automatically recognize geometric features for non-contact inspection. Customers can measure with multiple FaroArms and FARO Laser Tracker IONs simultaneously to achieve geometry calculations accurate to one half-micron. CAM2 Q also contains a new fully customizable user interface, allowing users to create and organize a work environment that best meets the user's needs.
- **CAM2 Measure X** allows customers to compare measurements of manufactured components or assemblies with the corresponding CAD data for the components or assemblies. CAM2 Measure X is offered with the FaroArm and the FARO Laser Tracker ION.
- **Soft Check Tool** is a custom software program designed to lead an operator through a measurement process on the FaroArm or FARO Laser Tracker ION with minimal training. These programs are created by the Company from specifications provided by the customer.
- **FARO Gage Software**, used with the FARO Gage, includes a dedicated graphical interface designed for the ease of use of the operator. Capable of producing graphical and tabular reports, the software runs a library of gauging and Soft Check tools.
- **Laser Scanner Photon Software.** The Company has a number of programs available for use with its Laser Scanner Photon product, as follows:
 - **FARO Scout** is a software tool for displaying 3-D measurements and navigation in huge pointclouds.
 - **FARO Scene** displays, analyzes, administers and edits 3-D measurements in pointclouds, including registration of multiple pointclouds.
 - **FARO Cloud for AutoCAD** supports the visualization and analysis of millions of 3-D points in the well known AutoCAD software environment and makes possible as-built documentation of industrial structures, historic buildings or many more applications.
 - **FARO Works** is a web-based tool for the administration of complex projects and navigation from floor plan to scan with links to measurements.

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Customers

As of December 2009, the Company's products have been purchased by approximately 10,000 customers worldwide, ranging from small machine shops to such large manufacturing and industrial companies as Audi, Bell Helicopter, Boeing, British Aerospace, Caterpillar, Daimler AG, General Electric, General Motors, Honda, Johnson Controls, Komatsu America International, Lockheed Martin, Nissan, Siemens and Volkswagen, among many others, as well as universities and law enforcement agencies. The Company's ten largest customers by revenue represented an aggregate of approximately 5.2% of the Company's total revenues in 2009. No customer represented more than 0.9% of the Company's sales in 2009.

Sales and Marketing

The Company conducts its sales and marketing efforts on a decentralized basis in three main regions around the world: Americas, Europe/Africa and Asia/Pacific. The regional headquarters for the Americas is located in the Company's headquarters in Lake Mary, Florida; the Europe/Africa regional headquarters is located in Stuttgart, Germany; and the regional headquarters for the Asia/Pacific region is located in Singapore. At December 31, 2009, the Company employed 90, 112, and 104 sales and marketing specialists in the Americas, Europe/Africa, and Asia/Pacific regions, respectively. The Company has direct sales representation in the United States, Canada, Mexico, Brazil, Germany, the United Kingdom, France, Spain, Italy, Poland, Turkey, the Netherlands, India, China, Singapore, Malaysia, Vietnam, Thailand, and Japan. Note 17 to the Company's Notes to Consolidated Financial Statements included in Part II. Item 7 of this Annual Report on Form 10-K includes financial information about the Company's foreign and domestic operations and export sales.

The Company's sales and marketing efforts use a process of integrated lead qualification and sales demonstration. Once a customer opportunity is identified, the Company employs a team-based sales approach involving inside and outside sales personnel who are supported by application engineers. Each team has the ability to sell multiple product lines. The Company employs a variety of marketing techniques to promote brand awareness and customer identification.

Research and Development

The Company believes that its future success depends on its ability to maintain technological leadership, which will require ongoing enhancements of its products and the development of new applications and products that provide 3-D measurement solutions. Accordingly, the Company intends to continue to make substantial investments in the development of new technologies, the commercialization of new products that build on the Company's existing technological base and the enhancement and development of additional applications for its products.

The Company's research and development efforts are directed primarily at enhancing the functional adaptability of its current products and developing new and innovative products that respond to specific requirements of the emerging market for 3-D measurement systems. The Company's research and development efforts have been devoted primarily to mechanical hardware, electronics and software. The Company's engineering development efforts will continue to focus on enhancing its existing products and developing new products for the CAM2 market. The field of CAM2 and more broadly, 3-D measurement, continues to expand and new technologies and applications will be essential to competing in this market. Research and development activities, especially with respect to new products and technologies, are subject to significant risks, and there can be no assurance that any of the Company's research and development activities will be completed successfully or on schedule, or, if completed, will be commercially accepted.

At December 31, 2009, the Company employed 83 scientists and technicians in its research and development efforts. Research and development expenses were approximately \$12.6 million in each of 2009 and 2008, compared to \$10.3 million in 2007.

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Intellectual Property

The Company holds or has pending 83 patents in the United States and related patents worldwide. The Company also has 23 registered or pending trademarks in the United States and worldwide.

The Company relies on a combination of contractual provisions and trade secret laws to protect its proprietary information. There can be no assurance that the steps taken by the Company to protect its trade secrets and proprietary information will be sufficient to prevent misappropriation of its proprietary information or preclude third-party development of similar intellectual property.

Despite the Company's efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of the Company's products or to obtain and use information that the Company regards as proprietary. The Company intends to vigorously defend its proprietary rights against infringement by third parties. However, policing unauthorized use of the Company's products is difficult, particularly overseas, and the Company is unable to determine the extent to which piracy of its software products exists. In addition, the laws of some foreign countries do not protect the Company's proprietary rights to the same extent as the laws of the United States. The Company's success and its ability to maintain its competitive position depends, in large part, on its ability to protect its intellectual property.

The Company does not believe that any of its products infringe on the proprietary rights of third parties. There can be no assurance, however, that third parties will not claim infringement by the Company with respect to current or future products. Any such claims, with or without merit, could be time-consuming, result in costly litigation, cause product shipment delays or require the Company to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to the Company, which could have a material adverse effect upon the Company's business, operating results and financial condition.

Manufacturing and Assembly

The Company manufactures its FaroArm, FARO Gage, and FARO Laser Tracker products in the Company's manufacturing facilities located in Florida and Pennsylvania for customer orders from the Americas, in its manufacturing facility located in Switzerland for customer orders from the Europe/Africa region, and in its manufacturing facility located in Singapore for customer orders from the Asia/Pacific region. The Company manufactures its FARO Laser Scanner Photon product in its facility located in Stuttgart, Germany. The Company expects all its existing plants to have the production capacity necessary to support its volume requirements through 2010.

Manufacturing consists primarily of assembling and integrating components and subassemblies, purchased from suppliers, into finished products. The primary components, which include machined parts and electronic circuit boards, are produced by subcontractors according to the Company's specifications. All products are assembled, calibrated and tested for accuracy and functionality before shipment. The Company performs limited in-house circuit board assembly and component part machining.

The Company's manufacturing, engineering, and design headquarters have been registered to the ISO-9001 standard since July 1998. Semi-annual surveillance audits have documented continuous improvement to this multinational standard. The Company continues to examine its scope of registration as its business evolves and has chosen English as the standard business language for its operations.

This has been done in concert with the ISO9001:2000 Quality Management System Certification, and is expected to increase the quality of the Company's processes, products and services worldwide. Additionally, the Company takes a global approach to ISO17025:2005 regarding the recognition of the Competence of Calibration and Testing Laboratories, seeking to have all locations registered with identical scopes of accreditation and capabilities for the products generated and serviced.

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Currently the Company's manufacturing sites in Lake Mary, Florida, Kennett Square, Pennsylvania, Stuttgart, Germany, Schaffhausen, Switzerland and Singapore are jointly registered to ISO-9001 and ISO17025. In addition, the Company's service sites in the United States, Germany, India, Japan, China, Singapore and Brazil have joint certification and accreditation to these key standards.

Competition

The Company's portable measurement systems compete in the broad and highly competitive market for measurement devices for manufacturing and industrial applications, which, in addition to portable articulated arms, laser tracker and laser scanner products, consist of fixed-base CMMs, templates and go/no-go gages, check fixtures, handheld measurement tools, and various categories of surveying equipment. In the FARO Gage product line, the Company competes with manufacturers of handheld measurement tools and fixed-base CMMs, including some large, well-established companies. In the FaroArm, FARO Laser ScanArm, FARO Laser Tracker, and FARO Laser Scanner product lines, the Company competes primarily with Hexagon Metrology, a division of Hexagon. The Company also competes in these product lines with a number of other smaller competitors.

The Company will be required to make continued investments in technology and product development to maintain the technological advantage that it believes it currently has over its competition. Some of the Company's competitors, including some manufacturers of fixed-based CMMs and Hexagon, possess substantially greater financial, technical, and marketing resources than the Company possesses. Moreover, the Company cannot be certain that its technology or its product development efforts will allow the Company to successfully compete as the industry evolves. As the market for the Company's portable measurement systems expands, additional competition may emerge and the Company's existing and future competitors may commit more resources to the markets in which the Company participates.

Government Regulation

The Company's operations are subject to numerous governmental laws and regulations, including those governing antitrust and competition, the environment, import and export of products, currency conversions and repatriation, taxation of foreign earnings and earnings of expatriate personnel and use of local employees and suppliers. The Company's foreign operations are subject to the U.S. Foreign Corrupt Practices Act, or FCPA, which makes illegal any payments to foreign officials or employees of foreign governments that are intended to induce their influence to assist the Company or to gain any improper advantage for the Company. The Company operates in certain regions that are more highly prone to risk under the FCPA.

Manufacturers of electrical goods are subject to the European Union's RoHS and WEEE directives, which took effect during 2006. RoHS prohibits the use of lead, mercury and certain other specified substances in electronics products, and WEEE makes producers of electrical goods financially responsible for specified collection, recycling, treatment, and disposal of covered electronic products and components. Parallel initiatives are being proposed in other jurisdictions, including several states in the United States and China.

The Company currently holds WEEE registration and is in compliance with the directives of the European Union. The Company's products are currently exempt from the RoHS directive, although the Company expects to have all products in compliance in 2010. However, if the Company is unable to do so, it would be unable to sell its products in European Union countries, as well as several possible states in the United States and China, which would have a material adverse effect on its sales and results of operations.

Backlog

At December 31, 2009, the Company had orders representing approximately \$17.6 million in sales outstanding. The majority of these specific orders were shipped by February 12, 2010, and, as of February 12, 2010, the Company had orders representing approximately \$18.0 million in sales outstanding. At December 31, 2008 and 2007, the Company had orders representing approximately \$11.4 million and \$19.1 million in sales outstanding, respectively.

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The Company's increase in backlog at December 31, 2009 is primarily related to the increase in orders at the end of the fourth quarter of 2009. The Company believes that substantially all of the outstanding sales orders as of February 12, 2010 will be shipped during 2010.

Employees

At December 31, 2009, the Company had 734 full-time employees, consisting of 306 sales and marketing professionals, 114 production staff, 83 research and development staff, 96 administrative staff, and 135 customer service/application engineering specialists. The Company is not a party to any collective bargaining agreements and believes its employee relations are satisfactory. Management believes that its future growth and success will depend in part on its ability to retain and continue to attract highly skilled personnel. The Company anticipates that it will be able to obtain the additional personnel required to satisfy its staffing requirements over the foreseeable future.

Geographic Information

The Company has three reportable segments based upon geographic regions: Americas, Europe/Africa and Asia Pacific. The Company develops, manufactures, markets, supports and sells CAD-based quality assurance products integrated with CAD-based inspection and statistical process control software in each of these regions. These activities represent approximately 99% of consolidated sales. Information regarding the Company's net sales, operating income, and long-lived assets by geographic region is set forth in Note 17 to the Consolidated Financial Statements under Part II. Item 8 to this Annual Report on Form 10-K.

Available Information

The Company makes available, free of charge on its internet website, its Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission, or the SEC. You can find these reports on the Company's website at www.faro.com under the heading "Investor". The information on the Company's website is not a part of this Annual Report on Form 10-K.

These reports may also be obtained at the SEC's Public Reference Room at 100 F Street NE, Washington, D.C. 20549. Information on the operation of the Public Reference Room is available by calling the SEC at (800) SEC-0330. You may also access this information at the SEC's website (<http://www.sec.gov>). This site contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC.

ITEM 1A. RISK FACTORS.

The statements in this section describe the most significant risks to the Company's business and should be considered carefully in conjunction with the "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Notes to Consolidated Financial Statements" of this Annual Report on Form 10-K.

The following is a discussion of risks and uncertainties that the Company believes could, individually or in the aggregate, make its actual results differ materially from expected and past results. Predicting or identifying all such risks and uncertainties is not possible. As a result, the following factors should not be considered to be a complete discussion of risks and uncertainties. The Company undertakes no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise.

The global economic crisis may continue to adversely impact the Company's financial condition and results of operations.

The Company's results of operations have been materially affected by the conditions in the global economy generally and in the global capital markets in 2009. As widely reported, financial markets in the United States, Europe, and Asia experienced extreme disruptions in 2009, including extreme volatility in security prices, severely diminished liquidity and credit availability, and rating downgrades of certain investments. Although these conditions have not materially adversely impacted the Company's liquidity, these economic developments affect the Company in a number of other ways. Tightening of credit in financial markets adversely affects the ability of the Company's customers to obtain financing, which may result in a decrease in and cancellation of orders for the Company's products and may impact the ability of the Company's customers to make payments. Similarly, tightening of credit may adversely affect the Company's supplier base and may increase the potential for one or more of our suppliers to experience financial distress. In addition, as a result of decreases in business spending, combined with financial difficulties and uncertainties experienced by customers of the Company, the length of time for these customers to make purchase decisions may increase and the size of such customers' orders may decrease. The Company cannot predict the duration and severity of the current disruption in financial markets and adverse economic conditions in the United States, Europe, and Asia, and there can be no assurance that there will not be a further deterioration in financial markets and economic conditions. Should these economic conditions continue, they could have a material adverse effect on the Company's financial condition and results of operations.

Competitors may develop products that make the Company's products obsolete or less competitive.

The CAM2 market is characterized by rapid technological change. Competitors may develop new or improved products, processes or technologies that may make the Company's products obsolete or less competitive. The Company can provide no assurance that it will be able to adapt to evolving markets and technologies or maintain its technological advantage.

The Company's success depends, in part, on its ability to maintain its technological advantage by developing new products and applications and enhancing its existing products, which can be complex and time-consuming and require substantial investment by the Company. Significant delays in new product releases or difficulties in developing new products could adversely affect the Company's business, revenues and results of operations.

The Company's financial performance is dependent on the conditions of the automotive, aerospace, and heavy equipment industries, which have experienced significant disruptions in the current economic environment.

A significant portion of the Company's sales are to manufacturers in the automotive, aerospace and heavy equipment industries. A reduction in sales in any one of these industries could cause a significant decline in the Company's revenues. The Company is dependent upon the continued viability and financial stability of its customers in these industries, which are highly cyclical and dependent upon the general health of the economy and consumer spending. The cyclical nature of these industries may exert significant influence on the Company's revenues and results of operations. In addition, the volume of orders from customers may be adversely impacted by decreases in capital spending by customers. If one or more of its significant customers were to become insolvent or otherwise were unable to pay for the products provided by the Company, the Company's results of operations could be materially adversely affected.

The Company expects the challenging operating and financial environment currently faced by manufacturers in the automotive, aerospace, and heavy equipment industries to continue and cannot predict the duration or severity of this challenging operating and financial environment or whether it will further deteriorate.

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Customers' buying process for the Company's products is highly decentralized and typically requires significant time and expense for the Company to further penetrate the potential market of a specific customer, which may delay its ability to generate additional revenue.

The Company's success depends, in part, on its ability to further penetrate its customer base. During 2009, approximately 49% of the Company's revenue was attributable to sales to its existing customers. If the Company is not able to continue to further penetrate its existing customer base, its sales growth may decline. Most of its customers have a decentralized buying process for measurement devices. Thus, the Company must spend significant time and resources to increase revenues from a specific customer. For example, the Company may provide products to only one of its customer's manufacturing facilities or for a specific product line within a manufacturing facility. The Company cannot offer any assurance that it will be able to maintain or increase the amount of sales to its existing customers, which could adversely affect its growth.

The Company's inability to protect its patents and proprietary rights in the United States and foreign countries could adversely affect its revenues.

The Company's success depends, in large part, on its ability to obtain and maintain patents and other proprietary right protection for its processes and products in the United States and other countries. The Company also relies upon trade secrets, technical know-how and continuing inventions to maintain its competitive position. The Company seeks to protect its technology and trade secrets, in part, by confidentiality agreements with its employees and contractors. However, the Company's employees may breach these agreements or the Company's trade secrets may otherwise become known or be independently discovered by inventors. If the Company is unable to obtain or maintain protection of its patents, trade secrets and other proprietary rights, it may not be able to prevent third parties from using its proprietary rights, which could have a material adverse effect on the Company's results of operations.

The Company's patent protection involves complex legal and technical questions. Its patents may be challenged, narrowed, invalidated or circumvented. Further, the Company may be able to protect its proprietary rights from infringement by third parties only to the extent that its proprietary processes and products are covered by valid and enforceable patents or are effectively maintained as trade secrets. Furthermore, others may independently develop similar or alternative technologies or design around the Company's patented technologies. Litigation or other proceedings to defend or enforce its intellectual property rights could require the Company to spend significant time and money, which could have an adverse impact on the Company's financial condition.

Claims from others that the Company infringes their intellectual property rights may adversely affect its financial condition.

From time to time, the Company receives notices from others claiming it infringes their intellectual property rights. Responding to these claims may require the Company to enter into royalty or licensing agreements on unfavorable terms, require it to stop selling or to redesign affected products, or require it to pay damages. In addition, from time to time, the Company is involved in intellectual property lawsuits. On July 11, 2008, Metris USA, Inc. filed a complaint for patent infringement against the Company concerning two U.S. patents. The Company believes that it does not infringe the asserted patents and that the patents are invalid. Although it is not possible to predict with certainty the outcome of every claim and lawsuit, the Company believes that the complaint by Metris USA, Inc. and other such claims and lawsuits against it will not individually or in the aggregate have a material impact on the Company's results. However, the Company could in the future incur judgments or enter into settlements of lawsuits and claims that could have a material adverse effect on the Company's financial condition. Any litigation or interference proceedings, regardless of their outcome, may be costly and may require significant time and attention of the Company's management and technical personnel.

Product failures or product availability and performance issues could result in increased warranty costs, delays in new product introductions and enhancements and adversely affect the Company's business.

The Company regularly introduces new products and enhances existing products. Product failures in new or existing products of the Company could result in increased warranty costs and delays in new product

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introductions, which could lead to a loss of sales and customers and have an adverse effect on the Company's business and financial condition.

The Company may not be able to achieve financial results within its target goals, and its operating results may fluctuate due to a number of factors, many of which are beyond its control.

The Company's ability to achieve financial results that are within its goals is subject to a number of factors many of which may be beyond its control. Moreover, the Company's annual and quarterly operating results have varied significantly in the past and likely will vary significantly in the future. Factors that cause the Company's financial results to fluctuate include the following:

- adverse changes in the manufacturing industry and general economic conditions,
- the effectiveness of sales promotions and sales of demonstration equipment;
- geographic expansion in the Asia/Pacific region and other regions;
- training and ramp-up time for new sales people;
- investments in potential acquisitions or strategic sales, product or other initiatives;
- investments in technologies and new products;
- quality issues with the Company's products;
- shrinkage or other inventory losses due to product obsolescence, scrap or material price changes;
- the efficiencies achieved in managing inventories and fixed assets;
- expansion of the Company's manufacturing capability and other inflationary pressures;
- the size and timing of customer orders, many of which are received towards the end of the quarter;
- the amount of time that it takes to fulfill orders and ship the Company's products;
- the length of the Company's sales cycle to new customers and the time and expense incurred in further penetrating its existing customer base;
- increases in operating expenses for product development and new product marketing;
- costs associated with new product introductions, such as assembly line start-up costs and low introductory period production volumes;
- the timing and market acceptance of new products and product enhancements;
- customer order deferrals in anticipation of new products and product enhancements;
- the Company's success in expanding its sales and marketing programs;
- start-up costs and ramp-up time associated with opening new sales offices outside of the United States;
- potential decreases in revenue without proportionate adjustments in fixed costs;
- changes in gross margins due to lower average selling prices, changing product mix of products sold and the different gross margins on different products;
- variations in the effective income tax rate and the difficulty in predicting the tax rate on a quarterly and annual basis;
- compliance with government regulations including health, safety, and environmental matters; and
- litigation and regulatory action brought against the Company.

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Any one or a combination of these factors could adversely affect the Company's annual and quarterly operating results in the future and could cause it to fail to achieve its target financial results.

The Company's growth depends on the ability of the Company's products to attain broad market acceptance.

The market for traditional fixed-base CMMs, check fixtures, handheld measurement tools, and surveying equipment is mature. Part of the Company's strategy is to continue to displace these traditional measurement devices. Displacing traditional measurement devices and achieving broad market acceptance of the Company's products requires significant effort to convince manufacturers to reevaluate their historical measurement procedures and methodologies.

The CAM2 market is emerging. The potential size and growth rate of this market is uncertain and difficult to quantify. If the CAM2 market does not continue to expand or does not expand as quickly as the Company anticipates, it may not be able to grow its sales, which may affect its results of operations.

The Company markets five closely interdependent products (FaroArm, FARO Laser ScanArm, FARO Laser Scanner Photon, FARO Laser Tracker and FARO Gage) and related software for use in measurement, inspection, and high density surveying applications. Substantially all of the Company's revenues are currently derived from sales of these products and software, and it plans to continue its business strategy of focusing on the portable software-driven, 3-D measurement and inspection market. Consequently, the Company's financial performance will depend in large part on portable, computer-based measurement, inspection, and high density surveying products achieving broad market acceptance. If its products cannot attain broad market acceptance, the Company will not grow as anticipated and may be required to make increased expenditures on research and development for new applications or new products.

The Company competes with manufacturers of portable measurement systems and traditional measurement devices, many of which have more resources than the Company and may develop new products and technologies.

The broad market for measurement devices is highly competitive. In the FARO Gage product line, the Company competes with manufacturers of handheld measurement tools and fixed-base CMMs, including some large, well-established companies. In the FaroArm, FARO Laser ScanArm, FARO Laser Tracker, and FARO Laser Scanner Photon product lines, the Company competes primarily with Hexagon Metrology, a division of Hexagon. The Company also competes in these product lines with a number of other smaller competitors. The Company competes on the basis of product performance, quality, and price with respect to all of its products.

The Company will be required to make continued investments in technology and product development to maintain the technological advantage that it believes it currently has over its competition. Some of its competitors, including some manufacturers of fixed based CMMs and Hexagon, possess substantially greater financial, technical, and marketing resources than it possesses. Moreover, the Company cannot be certain that its technology or its product development efforts will allow it to successfully compete as the industry evolves. As the market for its portable measurement systems expands, additional competition may emerge and the Company's existing and future competitors may commit more resources to the markets in which the Company participates. The Company's results of operations could be adversely affected by pricing strategies pursued by competitors or technological or product developments by competitors.

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The Company derives a substantial part of its revenues from its international operations, which are subject to greater volatility and often require more management time and expense to achieve profitability than its domestic operations.

The Company derives more than half of its revenues from international operations. The Company's international operations are subject to various risks, including:

- difficulties in staffing and managing foreign operations;
- political and economic instability;
- unexpected changes in regulatory requirements and laws;
- longer customer payment cycles and difficulty collecting accounts receivable;
- compliance with export and import regulations and trade restrictions;
- governmental restrictions on the transfer of funds to the Company from its operations outside the United States;
- burdens of complying with a wide variety of foreign laws and labor practices.

Several of the countries where the Company operates have emerging or developing economies, which may be subject to greater currency volatility, negative growth, high inflation, limited availability of foreign exchange and other risks. These factors may harm the Company's results of operations and any measures that it may implement to reduce the effect of volatile currencies and other risks of its international operations may not be effective.

Because a significant portion of the Company's revenues and expenses are denominated in foreign currencies, the Company faces significant exposure to foreign exchange rate risk.

Approximately 63% of the Company's sales are denominated in currencies other than the U.S. dollar. As a result, the Company's results of operations are affected by fluctuations in exchange rates, which could cause significant fluctuations in the Company's quarterly and annual results of operations. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material adverse effect on the business, results of operations and financial condition, and could specifically result in foreign exchange gains and losses. To the extent that the percentage of its non-U.S. dollar revenues derived from international sales increases in the future, the Company's exposure to risks associated with fluctuations in foreign exchange rates may increase.

Any failure to comply with the Company's settlement of the Foreign Corrupt Practices Act Matter could subject the Company to fines and penalties.

The Company has entered into settlement agreements and documents with the SEC and the DOJ concerning the FCPA Matter involving the Company's China subsidiary, pursuant to which the Company has, among other things, continuing obligations with the SEC and the DOJ with respect to compliance with the FCPA and other laws, full cooperation with the government, and the adoption of a compliance code containing specific provisions intended to prevent violations of the FCPA. Any failure to comply with any such continuing obligations could result in the SEC and the DOJ seeking to impose penalties against the Company in the future.

The Company may not be able to identify, consummate or achieve expected benefits from acquisitions, which could harm its growth.

The Company's growth strategy partly depends on its ability to obtain additional technologies, complementary product lines and sales channels through selective acquisitions and strategic investments. The Company may not be able to identify and successfully negotiate suitable acquisitions, obtain financing for future acquisitions, if necessary, on satisfactory terms or otherwise complete acquisitions in the future. In the past, the Company has used its stock as consideration for acquisitions. The Company's common stock may not remain at a price at which it can be used as consideration for acquisitions without diluting the Company's existing shareholders, and potential acquisition candidates may not view the Company's stock attractively.

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In addition, realization of the benefits of acquisitions often requires integration of some or all of the sales and marketing, distribution, manufacturing, engineering, finance and administrative organizations of the acquired companies. The integration of acquisitions demands substantial attention from senior management and the management of the acquired companies. Any acquisition may be subject to a variety of risks and uncertainties including:

- the inability to assimilate effectively the operations, products, technologies and personnel of the acquired companies (some of which may be located in diverse geographic regions);
- the inability to maintain uniform standards, controls, procedures and policies;
- the need or obligation to divest portions of the acquired companies; and
- the potential impairment of relationships with customers.

The Company cannot offer any assurance that it will be able to identify or complete suitable acquisitions, integrate successfully any acquisitions, that any acquired companies will operate profitably, or that it will realize the expected benefits from any acquisition.

The Company may face difficulties managing growth.

If its business grows rapidly in the future, the Company expects it to result in:

- increased complexity;
- increased responsibility for existing and new management personnel; and
- incremental strain on its operations and financial and management systems.

If the Company is not able to manage future growth, its business, financial condition and operating results may be harmed.

The Company's dependence on suppliers for materials could impair its ability to manufacture its products.

Outside vendors provide key components used by the Company in the manufacture of its products. Although the Company believes that alternative sources for these components are available, any supply interruption in a limited source component would harm its ability to manufacture its products until a new source of supply is identified. In addition, an uncorrected defect or supplier's variation in a component, either known or unknown to the Company, or incompatible with its manufacturing processes, could harm its ability to manufacture its products. The Company may not be able to find a sufficient alternative supplier in a reasonable period, or on commercially reasonable terms, if at all. If the Company fails to obtain a supplier for the manufacture of components of its potential products, it may experience delays or interruptions in its operations, which would adversely affect its results of business, operations and financial condition.

The Company's failure to attract and retain qualified personnel could lead to a loss of sales or decreased profitability or growth.

The Company may not be able to attract and retain sufficient qualified personnel to support its growth. In addition, the loss of the Company's Chief Executive Officer, or other key personnel, could adversely affect its sales, profitability, or growth. Moreover, the Company continues to rely in part on equity awards to attract and retain qualified personnel, which may result in an increase in compensation expense.

The Company is subject to risks of natural disasters.

The occurrence of one or more natural disasters, such as tornadoes, hurricanes, earthquakes, and other forms of severe weather in any region where the Company has a facility could result in physical damage to, and complete or partial closure of, one or more of the Company's manufacturing facilities, which could adversely affect the Company's business, operations and financial performance.

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The Company may experience volatility in its stock price.

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

- fluctuations in demand for, and sales of, the Company's products or prolonged downturns in the industries that the Company serves;
- actual or anticipated variations in quarterly or annual operating results;
- general economic uncertainties;
- speculation in the press or investment community; and
- announcements of technological innovations or new products by the Company or its competitors.

The market price of the Company's common stock may also be affected by its 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 the Company's common stock to decline. Volatility in its stock price may result in the inability of the Company's shareholders to sell their shares at or above the price at which they purchased them.

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

Anti-takeover provisions in the Company's articles of incorporation, its bylaws and provisions of Florida law could delay or prevent a change of control that you may favor.

The Company's articles of incorporation, its bylaws and provisions of Florida law could make it more difficult for a third party to acquire the Company. Although the Company believes such provisions are appropriate to protect long-term value for its shareholders, these provisions could discourage potential takeover attempts and could adversely affect the market price of the Company's shares. Because of these provisions, you might not be able to receive a premium on your investment. These provisions include:

- a limitation on shareholders' ability to call a special meeting of the Company's shareholders;
- advance notice requirements to nominate directors for election to the Company's board of directors or to propose matters that can be acted on by shareholders at shareholder meetings;
- the Company's classified board of directors, which means that approximately one-third of its directors are elected each year; and
- the authority of the board of directors to issue, without shareholder approval, preferred stock with such terms as the board of directors may determine.

The provisions described above could delay or make more difficult transactions involving a change in control of the Company, or its management.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

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ITEM 2. PROPERTIES.

The Americas

The Company's headquarters are located in a leased building in Lake Mary, Florida containing approximately 46,000 square feet. This facility houses the Company's sales, marketing, customer service/application operations and administrative staff. The Company's U.S. production, research and development and manufacturing are located in a leased building in Lake Mary, Florida consisting of approximately 35,000 square feet. The Company also has a leased facility consisting of two buildings totaling approximately 37,000 square feet located in Kennett Square, Pennsylvania containing research and development, manufacturing and service operations of the laser tracker product lines.

Europe/Africa

The Company's European headquarters are located in a leased building in Stuttgart, Germany containing approximately 62,000 square feet. This facility houses the manufacturing, administration, sales, marketing and service management personnel for the Company's European operations. Additionally, the Company has a leased facility consisting of approximately 16,000 square feet located in Schaffhausen, Switzerland containing manufacturing operations for the Company's products shipped to customers in Europe and Africa.

Asia/Pacific

The Company's Asian headquarters are located in a leased building in Singapore containing approximately 22,000 square feet. This facility houses the administration, sales, marketing, production and service management personnel for the Company's Asian operations. The Company's Japan headquarters are located in a leased building in Nagoya, Japan containing approximately 17,000 square feet. This facility houses the Company's Japan sales, marketing and service operations. The Company's China headquarters are located in a leased building in Shanghai, China containing approximately 11,000 square feet for sales, marketing and service operations.

The Company believes that its current facilities will be adequate for its foreseeable needs and that it will be able to locate suitable space for additional regional offices or enhanced production needs as necessary.

The information required by the remainder of this Item is incorporated herein by reference to Exhibit 99.1 to this Annual Report on Form 10-K.

ITEM 3. LEGAL PROCEEDINGS.

Securities Litigation—On December 6, 2005, the first of four essentially identical class action securities fraud lawsuits were filed against the Company and certain officers of the Company (the "Securities Litigation") in the U.S. District Court for the Middle District of Florida. On April 19, 2006, the four lawsuits were consolidated, and Kornitzer Capital Management, Inc. (the "Lead Plaintiff") was appointed as the lead plaintiff. The Lead Plaintiff sought to include in the class all persons who purchased or otherwise acquired the Company's common stock between April 15, 2004 and March 15, 2006 (the "Class"), and sought an unspecified amount of damages, premised on allegations that each defendant made misrepresentations and omissions of material fact during the class period in violation of the Securities Exchange Act of 1934.

On February 26, 2008, the parties to the Securities Litigation entered into a Memorandum of Understanding stating the principal terms of their agreement to settle the Securities Litigation. On April 9, 2008, the parties filed a detailed Stipulation of Settlement with the court seeking the court's preliminary and final approval of the terms of the proposed settlement. Pursuant to those terms, the issuer of the Company's Executive Liability and Entity Securities Liability insurance policy applicable to the Securities Litigation paid \$6.875 million into a settlement fund for the Securities Litigation. That sum was within the coverage limit of the policy and accordingly had no

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effect on the Company's financial results. On October 3, 2008, the court entered a Final Judgment and Order of Dismissal With Prejudice, whereby the court certified the Class for purposes of the settlement, approved the settlement, and dismissed the Securities Litigation, with prejudice, as against each defendant.

Derivative Action—On January 10, 2008, a Verified Shareholder Derivative Complaint was filed by an alleged shareholder of the Company in the U.S. District Court for the Middle District of Florida against six of the Company's current and former directors, as defendants, and against the Company, as a nominal defendant (the "Derivative Action"). The derivative complaint alleges breach of fiduciary duty and other claims against the individual defendants principally in connection with the alleged acts and omissions asserted in the Securities Litigation. In February 2008 and April 2008, the Company received two demands by other alleged shareholders that the Company assert substantially the same claims as set forth in the derivative complaint against seven of the Company's current and former directors. Both of those demands subsequently were withdrawn.

On November 12, 2008, the parties to the Derivative Action executed a Memorandum of Understanding of the material terms of a proposed settlement of the Derivative Action. On January 21, 2009, the parties filed with the court a Stipulation of Settlement seeking the court's preliminary and final approval of the terms of the proposed settlement. On February 13, 2009, the court granted preliminary approval of the settlement. On April 23, 2009, the court granted final approval of the settlement and entered an Order and Final Judgment directing the consummation of the settlement and dismissing the Derivative Action, with prejudice, as against each defendant. Pursuant to the terms of the settlement, the Company has adopted certain corporate governance policies for a period of three years, and the issuer of the Company's Executive Liability and Entity Securities Liability insurance policy applicable to the Derivative Action has paid \$0.4 million to the plaintiff's counsel for their fees and expenses. That sum is within the coverage limit of the policy and accordingly has no effect on the Company's financial results.

Patent Matters—On July 11, 2008, a complaint for patent infringement was filed against the Company in the U.S. District Court for the District of Massachusetts by Metris USA, Inc. and certain of its affiliates, which the Company refers to collectively as "Metris", concerning U.S. Patent Nos. 6,611,617 and 7,313,264. The Company responded with counterclaims alleging that the asserted patents, which are generally directed to laser scanning devices, are invalid, non-infringed, and unenforceable due to fraud during prosecution of the patents in the U.S. Patent and Trademark Office. On August 31, 2009, the Court granted the Company's motion to add counterclaims and defenses for violation of federal and state antitrust and unfair competition laws based on the alleged knowing assertion of invalid and fraudulent patents. On October 22, 2009, the Court issued an Order for the purpose of construing certain claim language of the asserted patents. Pursuant to the October 22, 2009 Order, the parties submitted a stipulation further construing claim language on November 9, 2009. Discovery in the case is ongoing and no trial date has been set. The Company believes that it does not infringe the asserted patents and/or that the patents are invalid. The Company does not anticipate this lawsuit will have a material impact on the Company's business, financial condition or results of operations. However, the outcome is difficult to predict and an adverse determination could have a material impact on the Company's business, financial condition or results of operations.

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

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.****Market Information and Holders**

The Company's common stock is listed and traded on the NASDAQ Global Market under the symbol "FARO".

The following table sets forth, for the periods indicated, the high and low sales prices of the Company's common stock as reported by the NASDAQ Global Market:

	2009		2008	
	High	Low	High	Low
First Quarter	17.67	10.85	34.74	19.00
Second Quarter	18.24	13.00	36.18	25.37
Third Quarter	18.63	13.63	27.34	20.51
Fourth Quarter	22.13	14.68	20.96	10.63

As of February 23, 2010, the last sale price of the Company's common stock was \$19.90, and the Company had 71 holders of record of common stock.

Dividends

The Company has not paid any cash dividends on its common stock to date. The Company expects to retain future earnings for use in operating and expanding its business and does not anticipate paying any cash dividends in the reasonably foreseeable future.

Recent Sales of Unregistered Securities

During the year ended December 31, 2009, no equity securities of the Company were sold by the Company that were not registered under the Securities Act of 1933, as amended.

Purchases of Equity Securities

On November 24, 2008, the Company's Board of Directors approved a \$30 million share repurchase program. Acquisitions for the share repurchase program will be made from time to time at prevailing prices as permitted by securities laws and other legal requirements, and subject to market conditions and other factors. The share repurchase program may be discontinued at any time. There is no restriction date or other restriction governing the period over which the Company can repurchase shares under the program. Set forth below is information regarding the Company's stock repurchases made during the year ended December 31, 2009 under this program.

	Stock Purchase Program			
	Total Number of Shares	Average Price Paid Per Share	Total Number of Shares Purchased as part of Publicly Announced Plans or Programs	Approximate Dollar Value that may yet be Purchased Under the Plans or Program
January 1, 2009—January 31, 2009	342,407	\$ 14.00	342,407	\$ 25,135,285
February 1, 2009—February 28, 2009	282,020	\$ 14.32	282,020	\$ 21,094,621
March 1, 2009—December 31, 2009	—	—	—	\$ 21,094,621
Total	624,427	\$ 14.15	624,427	

The Company did not purchase any shares in the fourth quarter of 2009 under the repurchase program.

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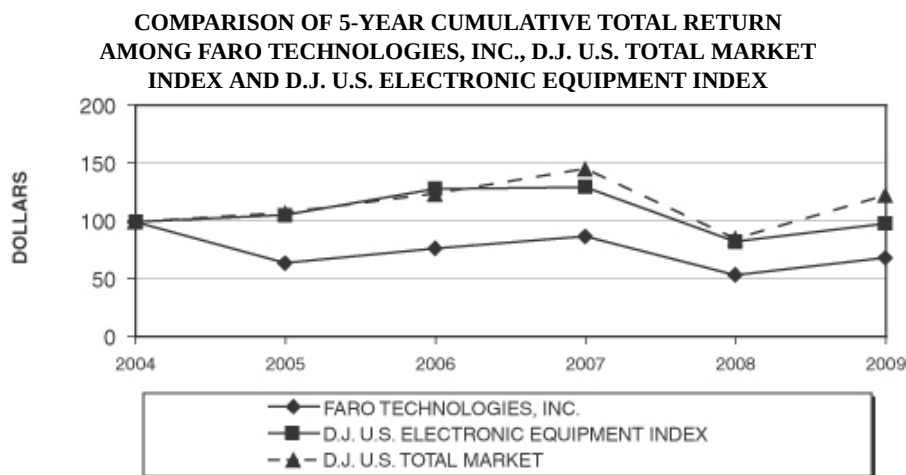
Performance Graph

The following performance graph and related information shall not be deemed “soliciting material” or to be “filed” with the SEC, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or the Exchange Act, except to the extent that the Company specifically incorporates it by reference into such filing.

The following line graph compares the cumulative five-year returns on the Company’s common stock with (1) the cumulative returns of the Dow Jones U.S. Total Market Index and (2) the Dow Jones U.S. Electronic Equipment Index.

For purposes of preparing the graph, we assumed that an investment of \$100 was made on January 1, 2005, with reinvestment of any dividends at the time they were paid. The Company did not pay any dividends during the period indicated.

The comparison in the graph below is based on historical data and is not necessarily indicative of future performance of the Company’s common stock.



ASSUMES \$100 INVESTED ON JAN. 01, 2005
ASSUMES DIVIDEND REINVESTED
FISCAL YEAR ENDING DEC. 31, 2009

<u>Date</u>	<u>FARO</u>	<u>Dow</u>	<u>Dow Elec Eqmt</u>
31-Dec-04	\$100.00	\$100.00	\$ 100.00
31-Dec-05	\$ 64.14	\$107.66	\$ 105.71
31-Dec-06	\$ 77.10	\$124.18	\$ 128.57
31-Dec-07	\$ 87.17	\$145.71	\$ 130.00
31-Dec-08	\$ 54.07	\$ 85.54	\$ 82.79
31-Dec-09	\$ 68.76	\$123.00	\$ 98.50

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Equity Compensation Plan Information

The following table provides information as of December 31, 2009 regarding equity compensation plans under which the Company's common stock is authorized for issuance.

<u>Plan Category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)(2)</u>	<u>Weighted-average exercise price of outstanding options, warrants and rights (b)</u>	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))(c)</u>
Equity compensation plans approved by security holders(1)	1,094,073	\$ 20.58(3)	1,965,957(4)
Equity compensation plans not approved by security holders(5)	—	—	—
Total	1,094,073	\$ 20.58	1,965,957

- (1) Consists of the 1997 Employee Stock Option Plans, the 1997 Non-employee Director Plan, the 2004 Equity Incentive Plan, and the 2009 Equity Incentive Plan.
- (2) The Company had 1,030,578 options outstanding as of December 31, 2009. The Company also had an aggregate of 50,628 shares of restricted stock and 12,867 restricted stock units outstanding as of December 31, 2009.
- (3) Calculation of weighted average exercise price of outstanding awards includes stock options but does not include restricted stock or restricted stock units that convert to shares of common stock for no consideration. Weighted average remaining life is 5.3 years.
- (4) The Company is also authorized under the 2009 Plan to grant any shares underlying awards outstanding under the 2004 Plan as of the effective date of the 2009 Plan that thereafter terminate or expire unexercised, or are cancelled, forfeited or lapse for any reason.
- (5) The Company does not maintain any equity compensation plans that have not been approved by the Company's shareholders.

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in thousands, except share and per-share data	Historical—Year ended December 31,				
	2009	2008	2007	2006	2005
Consolidated Statement of Income Data:					
Sales	\$ 147,703	\$ 209,249	\$ 191,617	\$ 152,405	\$ 125,590
Gross profit	80,708	125,226	115,043	89,458	72,932
(Loss) income from operations	(10,989)	18,937	19,111	8,259	10,226
(Loss) income before income tax expense	(10,158)	18,360	23,036	9,776	9,898
Net (loss) income	(10,582)	13,952	18,093	8,196	8,179
Net (loss) income per common share:					
Basic	\$ (0.66)	\$ 0.84	\$ 1.17	\$ 0.57	\$ 0.58
Diluted	\$ (0.66)	\$ 0.83	\$ 1.15	\$ 0.56	\$ 0.57
Weighted average shares outstanding:					
Basic	16,125,449	16,632,608	15,443,259	14,397,050	14,169,140
Diluted	16,125,449	16,734,403	15,722,215	14,560,331	14,442,248
Consolidated Balance Sheet Data:					
Working capital	\$ 148,213	\$ 163,230	\$ 154,946	\$ 73,692	\$ 86,624
Total assets	235,710	259,314	243,539	144,276	122,648
Total debt	273	368	240	205	340
Total shareholders' equity	196,598	212,308	194,499	111,055	98,860

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following information should be read in conjunction with the Consolidated Financial Statements of the Company, including the notes thereto, included in Part II, Item 8 of this Annual Report on Form 10-K.

Overview

The Company designs, develops, manufactures, markets and supports portable, software driven, 3-D measurement and imaging systems used in a broad range of manufacturing, industrial, building construction and forensic applications. The Company's FaroArm, FARO Laser ScanArm and FARO Gage articulated measuring devices, the FARO Laser Scanner Photon, the FARO Laser Tracker, and their companion CAM2 software systems, provide for CAD-based inspection, and high-density surveying. Together, these products integrate the measurement, quality inspection, and reverse engineering functions with CAD software to improve productivity, enhance product quality and decrease rework and scrap in the manufacturing process.

The Company derives revenues primarily from the sale of its FaroArm, FARO Laser ScanArm, FARO Gage, FARO Laser Tracker and FARO Laser Scanner Photon 3-D measurement equipment, and their related multi-faceted CAM2 software programs. Revenue related to these products is generally recognized upon shipment. In addition, the Company sells one and three-year extended warranties and training and technology consulting services relating to its products. The Company recognizes the revenue from extended warranties on a straight-line basis. The Company also receives royalties from licensing agreements for its historical medical technology and recognizes the revenue from these royalties as licensees use the technology.

The Company operates in international markets throughout the world and maintains sales offices in France, Germany, Great Britain, Japan, Spain, Italy, Turkey, China, India, Poland, the Netherlands, Malaysia, Thailand,

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Singapore and Vietnam. The Company manages and reports its global sales in three regions: the Americas, Europe/Africa and Asia/Pacific.

The Company manufactures its FaroArm, FARO Gage, and FARO Laser Tracker products in its manufacturing facility located in Switzerland for customer orders from the Europe/Africa region and in its manufacturing facility located in Singapore for customer orders from the Asia/Pacific region. The Company manufactures its FaroArm, FARO Gage, and FARO Laser Tracker products in the Company's manufacturing facilities located in Florida and Pennsylvania for customer orders from the Americas. The Company manufactures its FARO Laser Scanner Photon product in its facility located in Stuttgart, Germany. The Company expects all its existing plants to have the production capacity necessary to support its volume requirements through 2010.

The Company accounts for wholly owned foreign subsidiaries in the currency of the respective foreign jurisdiction, and therefore, fluctuations in exchange rates may have an impact on inter-company accounts reflected in the Company's consolidated financial statements. The Company is aware of the availability of off-balance sheet financial instruments to hedge exposure to foreign currency exchange rates, including cross-currency swaps, forward contracts and foreign currency options. However, it does not regularly use such instruments, and none were utilized in 2009, 2008 or 2007.

The Company implemented three reductions-in-force during the year ended December 31, 2009 to lower costs in view of the effects of deteriorating global economic conditions. The first reduction-in-force was announced on February 20, 2009, and affected approximately 7% of the Company's workforce. As a result of this first reduction-in-force, the Company expected to save approximately \$4.5 million in compensation costs on an annualized basis. Severance costs related to the first reduction-in-force equaled \$0.7 million. The second reduction-in-force, effective April 3, 2009, was announced on April 6, 2009, and affected approximately 14% of the Company's workforce. As a result of this second reduction-in-force, the Company expected to save \$7.4 million in compensation costs on an annualized basis. Severance costs for the second reduction-in-force were \$1.0 million. The third reduction-in-force was effective August 24, 2009, and affected approximately 8% of the Company's workforce. As a result of this third reduction-in-force, the Company expected to save approximately \$4.1 million in compensation costs on an annualized basis. Severance costs for the third reduction-in-force were \$0.6 million.

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

On December 22, 2009, the Company filed a Registration Statement on Form S-3 with the SEC registering up to \$145 million of shares of common stock, preferred stock, and warrants to purchase common and preferred stock, either individually or in units. The proceeds from any offerings with respect to this registration statement, if any, would be used for either repayment or refinancing of debt, acquisition of additional businesses or technologies or for working capital and general corporate purposes.

FCPA Update

As previously reported by the Company, the Company conducted an internal investigation in 2006 into certain payments made by its China subsidiary that may have violated the FCPA and other applicable laws, which the Company refers to as the FCPA Matter, and entered into settlement agreements and documents with

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the SEC and the U.S. Department of Justice, or DOJ, in 2008 related to the FCPA Matter. The Company incurred expenses of \$3.8 million in 2006, \$3.1 million in 2007, and \$0.3 million in 2008 relating to the FCPA Matter and paid \$2.95 million in fines, penalties, and interest to the DOJ and SEC in 2008 related to the FCPA Matter. The Company has a two-year monitoring obligation and other continuing obligations with the SEC and the DOJ with respect to compliance with the FCPA and other laws, including full cooperation with the government and the adoption of a compliance code containing specific provisions intended to prevent violations of the FCPA. The selection process of the monitor, which the Company has been pursuing in conjunction with the SEC and DOJ, is not yet complete. Failure to comply with any such continuing obligations could result in the SEC and the DOJ seeking to impose penalties against the Company in the future.

Results of Operations

The following table sets forth, for the periods presented, the percentage of sales represented by certain items in the Company's consolidated statements of operations:

	Years ended December 31,		
	2009	2008	2007
Statement of Operations Data:			
Sales	100.0%	100.0%	100.0%
Cost of sales	45.4%	40.2%	40.0%
Gross margin	54.6%	59.8%	60.0%
Operating expenses:			
Selling	32.9%	30.1%	29.3%
General and administrative	16.9%	12.5%	13.3%
Depreciation and amortization	3.7%	2.2%	2.1%
Research and development	8.5%	6.0%	5.4%
Total operating expenses	62.0%	50.8%	50.1%
(Loss) income from operations	(7.4%)	9.0%	9.9%
Interest (income)	(0.2%)	(1.0%)	(1.1%)
Other (income) expense, net	(0.4%)	1.0%	(1.0%)
Interest expense	0.1%	0.2%	0.0%
(Loss) income before income tax expense	(6.9%)	8.8%	12.0%
Income tax expense	0.3%	2.1%	2.6%
Net (loss) income	<u>(7.2%)</u>	<u>6.7%</u>	<u>9.4%</u>

2009 Compared to 2008

Sales. Total sales decreased by \$61.5 million, or 29.4%, to \$147.7 million in the year ended December 31, 2009 from \$209.2 million for the year ended December 31, 2008. This decrease resulted primarily from a decrease in unit sales in all regions related to the weakness in the global economy. Product sales decreased by \$61.5 million, or 34.3%, to \$117.7 million for the year ended December 31, 2009 from \$179.2 million in the year ended December 31, 2008. Service revenue remained flat at \$30.0 million in 2009 and 2008.

Sales in the Americas region decreased \$23.3 million, or 29.8%, to \$55.0 million for the year ended December 31, 2009 from \$78.3 million in the prior year period. Product sales in the Americas region decreased by \$23.9 million, or 36.1%, to \$42.3 million for the year ended December 31, 2009 from \$66.2 million in the prior year. Service revenue in the Americas region increased by \$0.7 million, or 5.8%, to \$12.8 million for the year ended December 31, 2009 from \$12.1 million for the prior year.

Sales in the Europe/Africa region decreased \$30.6 million, or 32.7%, to \$63.0 million for the year ended December 31, 2009 from \$93.6 million in the year ended December 31, 2008. Product sales in the Europe/Africa

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region decreased by \$29.4 million, or 36.7%, to \$50.8 million for the year ended December 31, 2009 from \$80.2 million in the prior year. Service revenue in the Europe/Africa region decreased by \$1.3 million, or 9.7%, to \$12.1 million for the year ended December 31, 2009 from \$13.4 million in the prior year, primarily due to a decrease in customer service and training revenue.

Sales in the Asia/Pacific region decreased \$7.6 million, or 20.4%, to \$29.7 million for the year ended December 31, 2009 from \$37.3 million in the year ended December 31, 2008. Product sales in the Asia/Pacific region decreased by \$8.2 million, or 25.2%, to \$24.6 million for the year ended December 31, 2009 from \$32.8 million in the prior year. Service revenue in the Asia/Pacific region increased by \$0.6 million, or 13.3%, to \$5.1 million for the year ended December 31, 2009 from \$4.5 million in the same period during the prior year, primarily due to an increase in warranty revenue.

Gross profit decreased by \$44.5 million, or 35.6%, to \$80.7 million for the year ended December 31, 2009 from \$125.2 million for the year ended December 31, 2008. Gross margin decreased to 54.6% for the year ended December 31, 2009 from 59.8% for the year ended December 31, 2008, primarily due to a change in the sales mix between product sales and service revenue resulting from a decrease in product sales. Gross margin from product sales decreased to 60.7% in the year ended December 31, 2009 from 66.1% for the prior year, primarily due to a change in the product sales mix resulting in a decrease in average unit selling prices. Gross margin from service revenues increased to 31.0% in the year ended December 31, 2009 from 22.5% for the prior year, primarily due to a decrease in customer service costs. The Company expects the trend of changes in the sales mix to result in gross margins in the range of approximately 55% to 60% in 2010, but the continued economic downturn could negatively impact this range.

Selling Expenses. Selling expenses decreased by \$14.4 million, or 22.9%, to \$48.6 million for the year ended December 31, 2009 from \$63.0 million for the year ended December 31, 2008. This decrease was primarily due to a decrease in compensation expense of \$8.9 million, a decrease in travel-related expenses of \$2.5 million, a decrease in marketing and advertising costs of \$2.0 million, and a decrease in recruiting and training expenses of \$1.0 million. As a result of the reductions-in-force implemented by the Company in 2009, the Company incurred \$1.0 million in severance costs and expects to save \$6.2 million in compensation costs on an annualized basis.

Worldwide sales and marketing headcount decreased by 90, or 22.7%, to 306 at December 31, 2009 from 396 at December 31, 2008. Regionally, the Company's sales and marketing headcount decreased by 46, or 33.8%, to 90 at December 31, 2009 from 136 at December 31, 2008 for the Americas; decreased by 27, or 19.4%, to 112 at December 31, 2009 from 139 at December 31, 2008 in Europe/Africa; and decreased by 17, or 14.0%, in Asia/Pacific to 104 at December 31, 2009 from 121 at December 31, 2008.

As a percentage of sales, selling expenses increased to 32.9% of sales in the year ended December 31, 2009 from 30.1% in the year ended December 31, 2008. Regionally, selling expenses were 30.7% of sales in the Americas for the year ended December 31, 2009, compared to 29.6% of sales in the year ended December 31, 2008; 34.2% of sales for Europe/Africa for the year ended December 31, 2009 compared to 30.5% of sales in the prior year; and 34.3% of sales for Asia/Pacific for the year ended December 31, 2009 compared to 30.2% of sales in the prior year.

General and administrative expenses. General and administrative expenses decreased by \$1.2 million, or 4.5%, to \$24.9 million for the year ended December 31, 2009, from \$26.1 million for the year ended December 31, 2008. General and administrative expenses decreased primarily due to a decrease in compensation expense of \$1.8 million, a decrease in travel related costs of \$0.9 million, and a reduction in recruiting and training costs of \$0.7 million, offset by an increase in the allowance for doubtful accounts of \$0.5 million and an increase of \$2.0 million in legal and professional fees primarily related to patent litigation and the settlement of an IRS audit. General and administrative expenses as a percentage of sales increased to 16.9% for the year ended December 31, 2009 from 12.5% for the year ended December 31, 2008. As a result of the reductions-in-force

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implemented by the Company in 2009, the Company incurred \$0.7 million in severance costs and expects to save \$3.4 million in compensation costs on an annualized basis.

Depreciation and amortization expenses. Depreciation and amortization expenses increased by \$1.0 million to \$5.5 million for the year ended December 31, 2009 from \$4.5 million for the year ended December 31, 2008 as a result of an increase in property, equipment and intangible assets.

Research and development expenses. Research and development expenses remained flat at \$12.6 million for years ended December 31, 2009 and 2008. Research and development expenses as a percentage of sales increased to 8.5% for the year ended December 31, 2009, from 6.0% for the year ended December 31, 2008. As a result of the reductions-in-force implemented by the Company in 2009, the Company incurred \$0.1 million in severance costs and expects to save \$1.8 million in compensation costs on an annualized basis.

Interest income / expense. Interest income, net, decreased by \$1.5 million to \$0.2 million for the year ended December 31, 2009 from \$1.7 million for the year ended December 31, 2008, due to a decrease in interest rates related to cash and short term investments.

Other (income) expense, net. Other (income) expense, net increased by \$2.9 million to \$0.6 million of income for the year ended December 31, 2009, from an expense of \$2.3 million for the year ended December 31, 2008, due to foreign currency transaction gains.

Income tax expense. Income tax expense decreased by \$4.0 million to \$0.4 million for the year ended December 31, 2009 from \$4.4 million for the year ended December 31, 2008, primarily due to a decrease in pretax income. Income tax expense in the year ended December 31, 2009 included \$2.6 million, or \$0.16 per share, related to a settlement with the Internal Revenue Service in the fourth quarter of 2009 of an audit of the Company's federal corporate income tax returns for the period 2005 to 2007 related to the valuation of certain intangible assets contributed to a foreign subsidiary of the Company under a R&D Cost Sharing Arrangement entered into in 2001. Excluding the effects of the \$2.6 million tax settlement, the Company's effective tax benefit rate would have been 21.7% for 2009. The Company believes that calculating its effective tax rate without the impact of the IRS settlement is useful to management and investors to provide greater clarity and to facilitate internal and external comparisons to the Company's historical tax rate. The Company's effective tax rate was 4.2% for the year ended December 31, 2009, compared to 24.0% for the year ended December 31, 2008. Total deferred tax assets for the Company's foreign subsidiaries relating to net operating loss carryforwards were \$12.2 million and \$10.2 million at December 31, 2009 and 2008, respectively. The related valuation allowance was \$10.6 million and \$8.7 million at December 31, 2009 and 2008, respectively. The Company's tax rate continues to be lower than the statutory tax rate in the United States primarily as a result of favorable tax rates in foreign jurisdictions. However, the Company's tax rate could be impacted positively or negatively by geographic changes in the manufacturing or sales of its products and the resulting effect on taxable income in each jurisdiction.

Net income. Net income decreased by \$24.6 million to a net loss of \$10.6 million for the year ended December 31, 2009 from net income of \$14.0 million for the year ended December 31, 2008 as a result of the factors described above.

2008 Compared to 2007

Sales. Sales increased by \$17.6 million, or 9.2%, to \$209.2 million in the year ended December 31, 2008, from \$191.6 million for the year ended December 31, 2007. This increase resulted primarily from an increase in unit sales and an increase in average selling prices. Product sales increased by \$9.1 million, or 5.3%, to \$179.2 million for the year ended December 31, 2008 from \$170.1 million in the year ended December 31, 2007. Service revenue increased by \$8.5 million, or 39.5%, to \$30.0 million in the year ended December 31, 2008 from \$21.5 million in the year ended December 31, 2007.

Sales in the Americas region decreased \$1.7 million, or 2.1%, to \$78.3 million for the year ended December 31, 2008 from \$80.0 million in the prior year period. Product sales in the Americas region decreased

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by \$4.0 million, or 5.7%, to \$66.2 million for the year ended December 31, 2008 from \$70.2 million in the prior year. Service revenue in the Americas region increased by \$2.4 million, or 24.5%, to \$12.1 million for the year ended December 31, 2008 from \$9.8 million for the prior year.

Sales in the Europe/Africa region increased \$15.3 million, or 19.5%, to \$93.6 million for the year ended December 31, 2008 from \$78.3 million in the year ended December 31, 2007. Product sales in the Europe/Africa region increased by \$11.0 million, or 15.9%, to \$80.2 million for the year ended December 31, 2008 from \$69.2 million in the prior year. Service revenue in the Europe/Africa region increased by \$4.4 million, or 48.4%, to \$13.4 million for the year ended December 31, 2008 from \$9.1 million in the prior year, primarily due to an increase in customer service and training revenue.

Sales in the Asia/Pacific region increased \$4.0 million, or 12.0%, to \$37.3 million for the year ended December 31, 2008 from \$33.3 million in the year ended December 31, 2007. Product sales in the Asia/Pacific region increased by \$2.1 million, or 6.8%, to \$32.8 million for the year ended December 31, 2008 from \$30.7 million in the prior year. Service revenue in the Asia/Pacific region increased by \$1.9 million, or 73.1%, to \$4.5 million for the year ended December 31, 2008 from \$2.6 million in the same period during the prior year, primarily due to an increase in warranty revenue.

Gross Profit. Gross profit increased by \$10.2 million, or 8.9%, to \$125.2 million for year ended December 31, 2008 from \$115.0 million for the year ended December 31, 2007. Gross margin decreased to 59.8% for the year ended December 31, 2008, from 60.0% for the year ended December 31, 2007. The decrease in gross margin is primarily due to an increase in service costs as a percentage of sales.

Selling Expenses. Selling expenses increased by \$6.9 million, or 12.3%, to \$63.0 million for the year ended December 31, 2008 from \$56.1 million for the year ended December 31, 2007. This increase was primarily due to an increase in compensation expense of \$3.7 million, an increase in marketing and advertizing costs of \$0.5 million, and an increase in travel-related expenses of \$2.1 million. As a percentage of sales, selling expenses increased to 30.1% of sales in the year ended December 31, 2008 from 29.3% in the year ended December 31, 2007.

General and administrative expenses. General and administrative expenses increased by \$0.6 million, or 2.5%, to \$26.1 million for the year ended December 31, 2008, from \$25.5 million for the year ended December 31, 2007. General and administrative expenses increased primarily due to an increase in compensation expense of \$2.1 million, increased costs of \$1.4 million related to additional leased space to expand the Company's corporate offices, an increase in the allowance for doubtful accounts of \$0.7 million, and higher travel-related costs of \$0.3 million, offset by a reduction of \$3.7 million for estimated fines, penalties and professional fees related to the settlement of the FCPA Matter included in the year ended December 31, 2007. General and administrative expenses as a percentage of sales decreased to 12.5% for the year ended December 31, 2008 from 13.3% for the year ended December 31, 2007.

Depreciation and amortization expenses. Depreciation and amortization expenses increased by \$0.5 million to \$4.5 million for the year ended December 31, 2008 from \$4.0 million for the year ended December 31, 2007 as a result of an increase in property, equipment and intangible assets.

Research and development expenses. Research and development expenses increased by \$2.3 million to \$12.6 million for year ended December 31, 2008 from \$10.3 million for the year ended December 31, 2007, primarily as a result of an increase in compensation expense. Research and development expenses as a percentage of sales increased to 6.0% for the year ended December 31, 2008 from 5.4% for the year ended December 31, 2007.

Interest income / expense. Interest income, net decreased by \$0.3 million to \$1.7 million for the year ended December 31, 2008 from \$2.0 million for the year ended December 31, 2007, due to interest expense related to the payment of fines and penalties for the FCPA Matter.

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Other (income) expense, net. Other (income) expense, net decreased by \$4.2 million to \$2.3 million of expense for the year ended December 31, 2008 from income of \$1.9 million for the year ended December 31, 2007, due to foreign currency transaction losses.

Income tax expense. Income tax expense decreased by \$0.5 million to \$4.4 million for the year ended December 31, 2008 from \$4.9 million for the year ended December 31, 2007, primarily due to a decrease in pretax income. The Company's effective tax rate increased to 24.0% for the year ended December 31, 2008 from 21.5% for the year ended December 31, 2007, due to an increase in income in higher tax jurisdictions. Total deferred taxes for the Company's foreign subsidiaries relating to net operating loss carryforwards were \$10.2 million and \$7.7 million at December 31, 2008 and 2007, respectively. The related valuation allowance was \$8.7 million and \$6.3 million at December 31, 2008 and 2007, respectively.

Net income. Net income decreased by \$4.1 million to \$14.0 million for the year ended December 31, 2008 from \$18.1 million for the year ended December 31, 2007 as a result of the factors described above.

Liquidity and Capital Resources

The Company has financed its operations primarily from cash provided by operating activities, proceeds of its 1997 initial public offering of common stock of approximately \$31.5 million, a 2003 private placement of common stock totaling approximately \$24.9 million, and its 2007 registered direct offering on Form S-3 with proceeds of approximately \$53.0 million.

On December 22, 2009, the Company filed a Registration Statement on Form S-3 with the SEC registering shares of common stock, preferred stock, and warrants to purchase common and preferred stock, either individually or in units, with a value of up to \$145 million. The proceeds from any offerings with respect to this registration statement, if any, would be used for either repayment or refinancing of debt, acquisition of additional businesses or technologies or for working capital and general corporate purposes.

Cash and cash equivalents increased by \$11.6 million to \$35.1 million at December 31, 2009 from \$23.5 million at December 31, 2008. The increase was primarily attributable to net proceeds of \$17.0 million from the sale of \$82.0 million of the Company's variable rate demand bonds, net of purchases of \$65.0 million of U.S. Treasury Bills, an increase in working capital of \$7.7 million, and \$1.2 million from the net loss and non-cash expenses, offset by purchases of \$8.8 million of the Company's common stock as part of the Company's share repurchase program, \$4.1 million in purchases of equipment and intangible assets, and the negative effect of exchange rate changes on cash of \$1.5 million.

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

The Company believes that its anticipated cash flow from operations, cash and cash equivalents, short term investments and credit facility will be sufficient to finance presently anticipated working capital and capital expenditure requirements for the foreseeable future.

Off Balance Sheet Items

None.

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Contractual Obligations and Commercial Commitments

The Company is party to capital leases on equipment with an initial term of 36 to 60 months and other non-cancelable operating leases. These obligations are presented below as of December 31, 2009:

	Payments Due by Period				
	Total	< 1 Year	1-3 Years	3-5 Years	> 5 Years
Contractual Obligations					
Capital lease obligations	\$ 274	\$ 80	\$ 153	\$ 41	\$ —
Operating lease obligations	24,381	5,461	8,394	6,341	4,185
Purchase obligations	12,459	12,459	—	—	—
Total	<u>\$37,114</u>	<u>\$18,000</u>	<u>\$8,547</u>	<u>\$6,382</u>	<u>\$ 4,185</u>

The Company enters into purchase commitments for products and services in the ordinary course of business. These purchases generally cover production requirements for 60 to 90 days. As of December 31, 2009, the Company does not have any long-term commitments for purchases.

The Company has a \$0.6 million liability for unrecognized tax benefits that is excluded from the contractual obligations table due to the uncertainty of the period of settlement, if any, with the respective taxing authorities.

Inflation

The Company believes that inflation has not had a material impact on its results of operations in recent years and does not expect inflation to have a material impact on its operations in 2010.

Critical Accounting Policies

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

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

Revenue Recognition

Revenue related to the Company's measurement equipment and related software is generally recognized upon shipment, as the Company considers the earnings process substantially complete as of the shipping date. Revenue from sales of software only is recognized when no further significant production, modification or

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customization of the software is required and where persuasive evidence of a sales agreement exists, delivery has occurred, and the sales price is fixed or determinable and deemed collectible. Revenues resulting from sales of comprehensive support, training and technology consulting services are recognized as such services are performed. Extended maintenance plan revenues are recognized on a straight-line basis over the life of the plan. The Company warrants its products against defects in design, materials and workmanship for one year. A provision for estimated future costs relating to warranty expense is recorded when products are shipped. Costs relating to extended maintenance plans are recognized as incurred. Revenue from the licensing agreements for the use of the Company's historical technology for medical applications is recognized when the technology is sold by the licensees.

Reserve for Excess and Obsolete Inventory

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

Income Taxes

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

The Company operates in a number of different countries around the world and considers the statutory rates within each jurisdiction to determine the overall effective tax rate. In 2003, the Company began to manufacture products in Switzerland, where it received a favorable income tax rate commitment from the Swiss government as an incentive to establish a manufacturing plant there. The aggregate dollar effect of this favorable tax rate was approximately \$1.2 million, or \$0.07 per share, for the year ended December 31, 2009, \$2.1 million, or \$0.13 per share, for the year ended December 31, 2008 and \$2.0 million, or \$0.13 per share, for the year ended December 31, 2007.

In 2005, the Company opened a regional headquarters and began to manufacture products in Singapore. In the third quarter of 2006, the Company received confirmation of a tax holiday for its operations from the Singapore Economic Development Board for a period of four years commencing January 1, 2006 and an additional six year extension at a favorable tax rate subject to certain terms and conditions including employment, spending, and capital investment. The aggregate dollar effect of this favorable tax rate was approximately \$1.1 million, or \$0.07 per share, for the year ended December 31, 2009, \$1.6 million, or \$0.10 per share, for the year ended December 31, 2008 and \$2.0 million, or \$0.13 per share, for the year ended December 31, 2007.

The Company is subject to certain terms and conditions, including employment, spending, and capital investment, in each of these countries in order to receive these favorable tax rates or be subject to the statutory

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

Reserve for Warranties

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

Goodwill Impairment

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

The goodwill impairment test is applied using a two-step approach. In performing the first step, the company calculates the fair values of the reporting units using discounted cash flows ("DCF") of each reporting unit. If the carrying amount of the reporting unit exceeds the fair market value, the second step is performed to measure the amount of the impairment loss, if any. In the second step, the implied fair value of the goodwill is estimated as the fair value of the reporting unit as calculated in the first step less the fair values of the net tangible and intangible assets of the reporting unit other than goodwill. If the carrying amount of goodwill exceeds its implied fair market value, an impairment loss is recognized in an amount equal to that excess, not to exceed the carrying amount of the goodwill. Management has concluded there was no goodwill impairment in the years ended December 31, 2009, 2008 and 2007.

Impact of Recently Issued Accounting Standards

As of January 1, 2008, the Company adopted the Financial Accounting Standards Board, or the FASB, Accounting Standards Codification, or ASC, 820-10 (formerly Statement of Financial Accounting Standards, or SFAS, No. 157), "Fair Value Measurements and Disclosures". This statement defines fair value, establishes a

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framework for measuring fair value in accordance with U.S. GAAP and expands disclosures about fair value measurements. This statement does not require any new fair value measurements; rather, it applies to other accounting pronouncements that require or permit fair value measurements. The Company previously adopted the provisions of this pronouncement for its financial assets and liabilities as of January 1, 2008. Effective January 1, 2009, the Company adopted ASC 820-10 for all non-financial assets and liabilities measured at fair value on a non-recurring basis. The adoption of ASC 820-10 did not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

As of January 1, 2009, the Company adopted FASB ASC 805-20 (formerly SFAS 141 and 141 Revised), "Business Combinations—Identifiable Assets and Liabilities, and Any Noncontrolling Interest," or ASC 805-20. ASC 805-20 requires an acquirer to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date. The statement also requires the acquirer in a business combination consummated in stages to recognize the identifiable assets and liabilities, as well as the noncontrolling interest in the acquiree, at the full amounts of their fair values. The provisions of ASC 805-20 are effective prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The adoption of ASC 805-20 had no material impact on the Company's financial position or results of operations.

As of January 1, 2009, the Company adopted FASB ASC 810-10 (formerly SFAS No. 160), "Consolidation," or ASC 810-10. ASC 810-10 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. ASC 810-10 is effective prospectively, except for certain retrospective disclosure requirements, for fiscal years beginning after December 15, 2008. The adoption of ASC 810-10 had no material impact on the Company's financial position or results of operations.

As of January 1, 2009, the Company adopted FASB ASC 815-10 (formerly SFAS No. 161), "Derivatives and Hedging," or ASC 815-10. This statement requires enhanced disclosures about an entity's derivative and hedging activities. ASC 815-10 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The adoption of ASC 815-10 had no material impact on the Company's consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, now codified in ASC 855-10, "Subsequent Events", which addresses the types and timing of events that should be reported in the financial statements for events occurring between the balance sheet date and the date the financial statements are issued or available to be issued. ASC 855-10 was effective for the Company on July 4, 2009. The adoption of ASC 855-10 had no material impact on the Company's consolidated financial statements.

In June 2009, the FASB issued SFAS No. 168, codified in ASC 105-10, "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles". ASC 105-10 establishes the FASB Accounting Standards Codification as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. GAAP. ASC 105-10 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The adoption of ASC 105-10 supersedes all references to pre-codification standards and had no material impact on the Company's consolidated financial statements.

In October 2009, the FASB issued Accounting Standards Update, or ASU, 2009-13, which amends ASC Topic 605, "Revenue Recognition". The guidance relates to the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting and modifies the manner in which the transaction consideration is allocated across the individual deliverables. Also, the guidance expands the disclosure requirements for revenue arrangements with multiple deliverables. ASU 2009-13 will be effective beginning on January 1, 2011, and may be applied retrospectively for all periods

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presented or prospectively to arrangements entered into or materially modified after the adoption date. The Company does not expect ASU 2009-13 to have a material impact on the Company's consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Foreign Exchange Exposure

The Company conducts a significant portion of its business outside the United States. At present, 62.7% of its revenues are invoiced, and a significant portion of its operating expenses paid, in foreign currencies. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material adverse effect on the business, results of operations and financial condition, and could specifically result in foreign exchange gains and losses. The impact of future exchange rate fluctuations on the results of the Company's operations cannot be accurately predicted. To the extent that the percentage of its non-U.S. dollar revenues derived from international sales increases in the future, the Company's exposure to risks associated with fluctuations in foreign exchange rates may increase.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
FARO Technologies, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of FARO Technologies, Inc. (a Florida corporation) and subsidiaries as of December 31, 2009 and 2008, and the related statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2009. Our audits of the basic consolidated financial statements included the financial statement schedule listed in the index appearing under Item 15(a)(2). These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of FARO Technologies, Inc. and subsidiaries as of December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2009 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), FARO Technologies, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated February 26, 2010 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Orlando, Florida
February 26, 2010

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

<u>(in thousands, except share data)</u>	<u>December 31,</u> <u>2009</u>	<u>December 31,</u> <u>2008</u>
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 35,078	\$ 23,494
Short-term investments	64,986	81,965
Accounts receivable, net	42,944	49,713
Inventories	26,582	33,444
Deferred income taxes, net	4,473	5,581
Prepaid expenses and other current assets	6,016	7,879
Total current assets	<u>180,079</u>	<u>202,076</u>
Property and Equipment:		
Machinery and equipment	19,867	16,748
Furniture and fixtures	5,225	4,099
Leasehold improvements	9,434	9,893
Property and equipment at cost	<u>34,526</u>	<u>30,740</u>
Less: accumulated depreciation and amortization	<u>(20,788)</u>	<u>(16,604)</u>
Property and equipment, net	<u>13,738</u>	<u>14,136</u>
Goodwill	19,934	18,951
Intangible assets, net	7,985	8,580
Service inventory	12,079	12,843
Deferred income taxes, net	1,895	2,728
Total Assets	<u>\$ 235,710</u>	<u>\$ 259,314</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 8,985	\$ 10,813
Accrued liabilities	8,173	14,032
Income taxes payable	229	1,988
Current portion of unearned service revenues	12,226	11,501
Customer deposits	2,173	425
Current portion of obligations under capital leases	80	87
Total current liabilities	<u>31,866</u>	<u>38,846</u>
Unearned service revenues - less current portion	5,910	6,772
Deferred tax liability, net	1,143	1,107
Obligations under capital leases - less current portion	193	281
Total Liabilities	<u>39,112</u>	<u>47,006</u>
Commitments and contingencies - See Note 13		
Shareholders' Equity:		
Common stock - par value \$.001, 50,000,000 shares authorized; 16,795,289 and 16,741,488 issued; 16,115,054 and 16,658,552 outstanding, respectively	17	17
Additional paid-in-capital	152,380	149,298
Retained earnings	46,915	57,497
Accumulated other comprehensive income	6,361	5,742
Common stock in treasury, at cost - 680,235 and 55,808 shares, respectively	<u>(9,075)</u>	<u>(246)</u>
Total Shareholders' Equity	<u>196,598</u>	<u>212,308</u>
Total Liabilities and Shareholders' Equity	<u>\$ 235,710</u>	<u>\$ 259,314</u>

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

<u>(in thousands, except share and per share data)</u>	<u>Years ended December 31,</u>		
	<u>2009</u>	<u>2008</u>	<u>2007</u>
SALES			
Product	\$ 117,714	\$ 179,209	\$ 170,236
Service	29,989	30,040	21,381
Total Sales	<u>147,703</u>	<u>209,249</u>	<u>191,617</u>
COST OF SALES			
Product	46,293	60,736	59,930
Service	20,702	23,287	16,644
Total Cost of Sales (exclusive of depreciation and amortization, shown separately below)	<u>66,995</u>	<u>84,023</u>	<u>76,574</u>
GROSS PROFIT	<u>80,708</u>	<u>125,226</u>	<u>115,043</u>
OPERATING EXPENSES:			
Selling	48,598	63,015	56,134
General and administrative	24,956	26,144	25,508
Depreciation and amortization	5,530	4,505	4,034
Research and development	12,613	12,625	10,256
Total operating expenses	<u>91,697</u>	<u>106,289</u>	<u>95,932</u>
(LOSS) INCOME FROM OPERATIONS	<u>(10,989)</u>	<u>18,937</u>	<u>19,111</u>
OTHER (INCOME) EXPENSE			
Interest income	(253)	(2,170)	(2,036)
Other (income) expense, net	(592)	2,295	(1,898)
Interest expense	14	452	9
(LOSS) INCOME BEFORE INCOME TAX EXPENSE	<u>(10,158)</u>	<u>18,360</u>	<u>23,036</u>
INCOME TAX EXPENSE	424	4,408	4,943
NET (LOSS) INCOME	<u>\$ (10,582)</u>	<u>\$ 13,952</u>	<u>\$ 18,093</u>
NET (LOSS) INCOME PER SHARE—BASIC	<u>\$ (0.66)</u>	<u>\$ 0.84</u>	<u>\$ 1.17</u>
NET (LOSS) INCOME PER SHARE—DILUTED	<u>\$ (0.66)</u>	<u>\$ 0.83</u>	<u>\$ 1.15</u>
Weighted average shares—Basic	<u>16,125,449</u>	<u>16,632,608</u>	<u>15,443,259</u>
Weighted average shares—Diluted	<u>16,125,449</u>	<u>16,734,403</u>	<u>15,722,215</u>

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2009, 2008, AND 2007

<u>(in thousands, except share data)</u>	Common Stock		Additional Paid-in Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income	Common Stock in Treasury	Total
	Shares	Amounts					
BALANCE DECEMBER 31, 2006	<u>14,504,715</u>	<u>\$ 14</u>	<u>\$ 85,160</u>	<u>\$ 25,452</u>	<u>580</u>	<u>\$ (151)</u>	<u>\$ 111,055</u>
Net income				18,093			18,093
Currency translation adjustment					4,019		4,019
Comprehensive income							<u>22,112</u>
Stock Option Expense			1,041				1,041
Issuance of restricted stock	23,553		176				176
Stock issued for iQvolution milestone earn-outs	24,773		730				730
Stock options exercised	441,011	1	5,381				5,382
Tax benefit from employee stock option exercises			963				963
Issuance of stock	1,650,000	2	53,038				53,040
BALANCE DECEMBER 31, 2007	<u>16,644,052</u>	<u>\$ 17</u>	<u>\$ 146,489</u>	<u>\$ 43,545</u>	<u>\$ 4,599</u>	<u>\$ (151)</u>	<u>\$ 194,499</u>
Net income				13,952			13,952
Currency translation adjustment					1,143		1,143
Comprehensive income							<u>15,095</u>
Stock Option Expense			1,793				1,793
Issuance of restricted stock	29,724		343				343
Stock issued for iQvolution milestone earn-outs	17,219		433				433
Stock options exercised	14,362		195				195
Tax benefit from employee stock option exercises			45				45
Stock Buy Back	(6,805)					(95)	(95)
BALANCE DECEMBER 31, 2008	<u>16,698,552</u>	<u>\$ 17</u>	<u>\$ 149,298</u>	<u>\$ 57,497</u>	<u>\$ 5,742</u>	<u>\$ (246)</u>	<u>\$ 212,308</u>
Net loss				(10,582)			(10,582)
Currency translation adjustment					619		619
Comprehensive loss							<u>(9,963)</u>
Stock Option Expense			1,679				1,679
Issuance of restricted stock	42,487		770				770
Stock issued for iQvolution milestone earn-outs	30,692		546				546
Stock options exercised	7,750		83				83
Tax benefit from employee stock option exercises			4				4
Stock Buy Back	(624,427)					(8,829)	(8,829)
BALANCE DECEMBER 31, 2009	<u>16,155,054</u>	<u>\$ 17</u>	<u>\$ 152,380</u>	<u>\$ 46,915</u>	<u>\$ 6,361</u>	<u>\$ (9,075)</u>	<u>\$ 196,598</u>

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)	Years Ended December 31,		
	2009	2008	2007
CASH FLOWS FROM:			
OPERATING ACTIVITIES:			
Net (loss) income	\$(10,582)	\$ 13,952	\$ 18,093
Adjustments to reconcile net (loss) income to net cash provided by operating activities:			
Depreciation and amortization	5,530	4,505	4,034
Compensation for stock options and restricted stock units	2,449	2,237	1,216
Provision for bad debts	1,852	1,092	373
Deferred income tax expense (benefit)	1,986	(1,972)	(464)
Change in operating assets and liabilities:			
Decrease (increase) in:			
Accounts receivable	5,769	2,993	(9,121)
Inventories, net	8,301	(6,429)	(7,265)
Prepaid expenses and other current assets	1,964	(1,187)	(3,208)
Income tax benefit from exercise of stock options	(4)	(45)	(963)
Increase (decrease) in:			
Accounts payable and accrued liabilities	(7,891)	(5,317)	9,884
Income taxes payable	(1,749)	(355)	1,278
Customer deposits	1,736	82	(269)
Unearned service revenues	(396)	3,710	8,007
Net cash provided by operating activities	<u>8,965</u>	<u>13,266</u>	<u>21,595</u>
INVESTING ACTIVITIES:			
Purchases of property and equipment	(3,387)	(9,705)	(2,930)
Payments for intangible assets	(670)	(3,766)	(359)
Purchases of short-term investments	(64,986)	(81,965)	(77,375)
Proceeds from sales of short-term investments	81,965	77,375	15,790
Net cash provided by (used in) investing activities	<u>12,922</u>	<u>(18,061)</u>	<u>(64,874)</u>
FINANCING ACTIVITIES:			
Payments on capital leases	(88)	(11)	(92)
Income tax benefit from exercise of stock options	4	45	963
Purchases of treasury stock	(8,829)	(95)	—
Proceeds from issuance of stock, net	83	92	58,421
Net cash (used in) provided by financing activities	<u>(8,830)</u>	<u>31</u>	<u>59,292</u>
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	<u>(1,473)</u>	<u>2,460</u>	<u>(5,904)</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<u>11,584</u>	<u>(2,304)</u>	<u>10,109</u>
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	<u>23,494</u>	<u>25,798</u>	<u>15,689</u>
CASH AND CASH EQUIVALENTS, END OF PERIOD	<u>\$ 35,078</u>	<u>\$ 23,494</u>	<u>\$ 25,798</u>

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2009, 2008 and 2007
(in thousands, except share and per share data or as otherwise noted)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business—FARO Technologies, Inc. and its subsidiaries (collectively the “Company” or “FARO”) design, develop, manufacture, market and support software-based three-dimensional measurement and imaging systems for manufacturing, industrial, building construction and forensic applications. The Company’s principal products include the FaroArm, FARO Laser ScanArm and FARO Gage, all articulated electromechanical measuring devices, and the FARO Laser Tracker and the FARO Laser Scanner Photon, both laser-based measuring devices. Markets for the Company’s products include automobile, aerospace, heavy equipment, and law enforcement agencies. The Company sells the vast majority of its products through a direct sales force located in many of the world’s largest industrialized countries.

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

Revenue Recognition, Product Warranty and Extended Maintenance Contracts—Revenue related to the Company’s measurement systems (integrated combinations of a measurement device, a computer and software loaded on the computer and the measurement device) is generally recognized upon shipment, as the Company considers the earnings process substantially complete as of the shipping date. The Company warrants its products against defects in design, materials and workmanship for one year. A provision for estimated future costs relating to warranty expense is recorded when products are shipped. The Company separately sells one and three year extended warranties. Extended warranty revenues are recognized on a straight-line basis over the term of the warranty. Costs relating to extended maintenance plans are recognized as incurred. Revenue from sales of software only is recognized when no further significant production, modification or customization of the software is required and when the following criteria are met: persuasive evidence of a sales agreement exists, delivery has occurred, and the sales price is fixed or determinable and deemed collectible. Revenues resulting from sales of comprehensive support, training and technology consulting services are recognized as such services are performed and are deferred when billed in advance of the performance of services. Revenue from the licensing agreements for the use of the Company’s technology for medical applications is generally recognized as licensees use the technology. Amounts representing royalties for the current year and not received as of year-end are estimated as due based on historical data and recognized in the current year.

Cash and Cash Equivalents—The Company considers cash on hand and amounts on deposit with financial institutions with maturities of three months or less when purchased to be cash and cash equivalents. The Company had deposits with foreign banks totaling \$23,181 and \$17,907 as of December 31, 2009 and 2008, respectively.

Accounts Receivable and Related Allowance for Doubtful Accounts—Credit is extended to customers based on an evaluation of a customer’s financial condition and, generally, collateral is not required. Accounts receivable are generally due within 30-90 days and are stated at amounts due from customers net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due. The Company makes judgments as to the collectability of accounts receivable based on historical trends and future expectations. Management estimates an allowance for doubtful accounts, which adjusts gross trade accounts receivable to its net realizable value. The allowance for doubtful accounts is based on an analysis of all

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receivables for possible impairment issues and historical write-off percentages. The Company writes off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts. The Company does not generally charge interest on past due receivables.

Inventories—Inventories are stated at the lower of cost or net realizable value using the first-in first-out method. Shipping and handling costs are classified as a component of cost of sales in the consolidated statements of operations. Sales demonstration inventory is comprised of measuring devices utilized by sales representatives to present the Company’s products to customers. These products remain in sales demonstration inventory for approximately six to twelve months and are subsequently sold at prices that produce slightly reduced gross margins. Service inventory is comprised of inventory that is not expected to be sold within twelve months, such as training and loaned equipment.

Property and Equipment—Property and equipment purchases exceeding a thousand dollars are capitalized and recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the various classes of assets as follows:

Machinery and equipment	2 to 5 years
Furniture and fixtures	3 to 10 years

Leasehold improvements are amortized on the straight-line basis over the lesser of the life of the asset or the term of the lease, not to exceed 7 years.

Depreciation expense was \$4,143, \$3,485 and \$3,319 in 2009, 2008 and 2007, respectively. Accelerated methods of depreciation are used for income tax purposes in contrast to book purposes, and as a result, appropriate provisions are made for the related deferred income taxes.

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

The goodwill impairment test is applied using a two-step approach. In performing the first step, the company calculates the fair values of the reporting units using discounted cash flows (“DCF”) of each reporting unit. If the carrying amount of the reporting unit exceeds the fair market value, the second step is performed to measure the amount of the impairment loss, if any. In the second step, the implied fair value of the goodwill is estimated as the fair value of the reporting unit as calculated in the first step less the fair values of the net tangible and intangible assets of the reporting unit other than goodwill. If the carrying amount of goodwill exceeds its implied fair market value, an impairment loss is recognized in an amount equal to that excess, not to exceed the carrying amount of the goodwill. Management has concluded there was no goodwill impairment in the years ended December 31, 2009, 2008 and 2007.

Other acquired intangibles principally include patents, existing product technology and customer relationships that arose in connection with the acquisition of iQvolution AG and Dimensional Photonics International. Other acquired intangibles are recorded at fair value at the date of acquisition and are amortized over their estimated useful lives of 3 to 15 years.

Patents are recorded at cost. Amortization is computed using the straight-line method over the lives of the patents.

Long-Lived Assets—Long-lived assets, other than goodwill, are evaluated for impairment when events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. Management concluded that there was no impairment of these assets for the years ended December 31, 2009, 2008 and 2007.

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Research and Development—Research and development costs incurred in the discovery of new knowledge and the resulting translation of this new knowledge into plans and designs for new products, prior to the attainment of the related products’ technological feasibility, are recorded as expenses in the period incurred.

Reserve for Warranties—The Company establishes a liability for included twelve-month warranties by the creation of a warranty reserve, which is an estimate of the repair expenses likely to be incurred for the remaining period of the warranty measured in installation-months in each major product group. Warranty reserve is reflected in accrued liabilities in the accompanying consolidated balance sheets. The warranty expense is estimated by determining the total repair expenses for each product group in the period and determining a rate of repair expense per installation month. This repair rate is multiplied by the number of installation-months of warranty for each product group sold during the period to determine the provision for warranty expenses for the period. The Company evaluates its exposure to warranty costs at the end of each period using the estimated expense per installation month for each major product group, the number of units remaining under warranty, and the remaining number of months each unit will be under warranty. While such expenses have historically been within its expectations, the Company cannot guarantee this will continue in the future.

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

The Company recognizes tax benefits related to uncertain tax positions only if it is more likely than not the tax position will be sustained upon examination by taxing authorities. For those positions where there is less than a 50% likelihood that a tax benefit will be sustained, no tax benefit has been recognized in the financial statements. In the ordinary course of business, the Company and its subsidiaries are examined by various federal, state, and foreign tax authorities. The Company regularly assesses the potential outcomes of these examinations and any future examinations for the current or prior years in determining the adequacy of our provision for income taxes.

Fair Value of Financial Instruments—The Company’s financial instruments include cash and cash equivalents, short-term investments, accounts receivable and accounts payable and accruals. Due to their short-term nature, the carrying amounts of such financial instruments approximate their fair value.

Earnings Per Share—Basic earnings per share (“EPS”) is computed by dividing earnings available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS includes the effect of all dilutive stock options and equity instruments. A reconciliation of the number of common shares used in calculation of basic and diluted EPS is presented in Note 15 Earnings Per Share.

Concentration of Credit Risk—Financial instruments that expose the Company to concentrations of credit risk consist principally of short-term investments and operating demand deposit accounts. The Company’s policy is to place its operating demand deposit accounts with high credit quality financial institutions.

Estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Impact of Recently Issued Accounting Standards

In December 2007, the Financial Accounting Standards Board (“FASB”) issued Statements of Financial Accounting Standards (“SFAS”) No. 141 (R), *Business Combinations*, codified as Accounting Standards Codification (“ASC”) 805, *Business Combinations*. ASC 805 requires an acquirer to measure the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquired entity at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. This impacted acquisitions closed on or after January 1, 2009. The adoption did not have a material effect on the Company’s financial position or results of operations.

In March 2008, the FASB issued guidance now codified within ASC 815 which expands the disclosure requirements for derivative instruments and hedging activities requiring enhanced disclosure of how derivative instruments impact a company’s financial statements, why companies engage in such transactions and a tabular disclosure of the effects of such instruments and related hedged items on a company’s financial position, results of operations and cash flows. The Company adopted these amendments on January 1, 2009 on a prospective basis. The adoption did not have a material effect on the Company’s financial position or results of operations.

In April 2008, the FASB issued guidance now codified within ASC 350 which outlines the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of recognized intangible assets. The intent of this guidance is to improve the consistency between the useful life of a recognized intangible asset and the period of expected cash flows used to measure the fair value of the asset in accordance with ASC 350 and other U.S. GAAP authoritative literature. These amendments must be applied prospectively to all intangible assets acquired after its effective date. The Company adopted these amendments effective January 1, 2009. The adoption did not have a material effect on the Company’s financial position or results of operations.

In June 2009, the FASB issued guidance now codified within ASC Topic 105, *Generally Accepted Accounting Principles* (“ASC 105”). ASC 105 establishes the FASB Accounting Standards Codification (the “Codification”) as the single source of authoritative non-governmental U.S. GAAP. ASC 105 does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all authoritative literature related to a particular topic in one place. Rules and interpretative releases of the Securities and Exchange Commission (“SEC”) under authority of federal securities laws are also sources of authoritative U.S. GAAP for SEC registrants. All guidance contained in the Codification carries an equal level of authority. The Codification superseded all existing non-SEC accounting and reporting standards, and all other non-grandfathered, non-SEC accounting literature not included in the Codification became non-authoritative. The provisions of ASC 105 are effective for interim and annual reporting periods ending after September 15, 2009. The Company adopted ASC 105 in its interim reporting for the period ended September 30, 2009. The adoption of ASC 105 is for disclosure purposes only and did not have a material effect on the Company’s financial position or results of operations.

In June 2009, the FASB issued guidance now codified within ASC Topic 810, *Consolidation* (“ASC 810”). ASC 810 requires entities to perform an analysis to determine whether the enterprise’s variable interest or interests give it a controlling financial interest in a variable interest entity. This analysis identifies the primary beneficiary of a variable interest entity as one with the power to direct the activities of a variable interest entity that most significantly impact the entity’s economic performance and obligation to absorb losses of the entity that could potentially be significant to the variable interest. The guidance is effective as of the beginning of the annual reporting period commencing after November 15, 2009, with early adoption prohibited. The Company does not expect the adoption of ASC 810 to have a material effect on its financial position or results of operations.

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In October 2009, the FASB issued Accounting Standards Update (“ASU”) No. 2009-13, *Multiple-Delivery Revenue Arrangements* (“ASU 2009-13”). ASU 2009-13 establishes the accounting and reporting guidance for arrangements, including multiple revenue-generating activities, and provides amendments to the criteria for separating deliverables and measuring and allocating arrangement consideration to one or more units of accounting. The amendments of ASU 2009-13 also establish a selling price hierarchy for determining the selling price of a deliverable. Significantly enhanced disclosures are also required to provide information about a vendor’s multiple-deliverable revenue arrangements, including information about the nature and terms, significant deliverables, and its performance within arrangements. The amendments also require providing information about the significant judgments made and changes to those judgments and about how the application of the relative selling-price method affects the timing or amount of revenue recognition. The amendments in ASU 2009-13 are effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with early application permitted. The Company does not expect the adoption of ASU 2009-13 to have a material impact on its consolidated financial statements.

In January 2010, the FASB issued ASU 2010-6, *Improving Disclosures About Fair Value Measurements*, (“ASU 2010-6”) which requires reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information on purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair-value measurements. ASU 2010-6 is effective for annual reporting periods beginning after December 15, 2009, except for Level 3 reconciliation disclosures which are effective for annual periods beginning after December 15, 2010. The Company does not expect the adoption of ASU 2010-6 to have a material impact on its consolidated financial statements.

Reclassification—Certain 2008 and 2007 amounts have been reclassified to conform with the 2009 presentation.

2. SUPPLEMENTAL CASH FLOW INFORMATION

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

	Years ended December 31,		
	2009	2008	2007
Cash paid for interest	\$ 7	\$ 452	\$ 9
Cash paid for income taxes	2,431	6,846	4,302
Non-cash investing and financing activities:			
Value of shares issued for acquisition of iQvolution	546	433	730

3. ALLOWANCE FOR DOUBTFUL ACCOUNTS

The allowance for doubtful accounts is as follows:

	Years ended December 31,		
	2009	2008	2007
Balance, beginning of year	\$ 1,727	\$ 739	\$ 458
Provision	1,852	1,092	373
Amounts written off, net of recoveries	(420)	(104)	(92)
Balance, end of year	<u>\$ 3,159</u>	<u>\$ 1,727</u>	<u>\$ 739</u>

4. SHORT-TERM INVESTMENTS

Short-term investments of \$82.0 million at December 31, 2008 were variable rate, long-term, tax-exempt municipal bonds. These bonds were sold in 2009. Short term investments of \$65.0 million at December 31, 2009 are comprised of U.S. Treasury Bills that mature through June 17, 2010. The interest rate on the U.S. Treasury Bills is less than one percent. The investments are classified as held-to-maturity and recorded at cost. The fair value of the U.S. Treasury Bills at December 31, 2009, approximated cost.

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5. INVENTORIES

Inventories consist of the following:

	As of <u>December 31, 2009</u>	As of <u>December 31, 2008</u>
Raw materials	\$ 9,382	\$ 11,997
Finished goods	3,561	6,597
Sales demonstration inventory	16,111	16,321
Reserve for excess and obsolete	(2,472)	(1,471)
Inventory	<u>\$ 26,582</u>	<u>\$ 33,444</u>
Service inventory	<u>\$ 12,079</u>	<u>\$ 12,843</u>

6. GOODWILL

The Company's goodwill at December 31, 2009 and 2008 is related to its acquisition of three previous businesses. The Company evaluates each reporting unit's fair value versus its carrying value on December 31 of each year or more frequently if events or changes in circumstances indicate that the carrying value may exceed the fair value. Recoverability of goodwill is measured using a discounted cash flow model incorporating discount rates commensurate with the risks involved for each reporting unit. The key assumptions used in the discounted cash flow model include discount rates, growth rates, cash flow projections and terminal value rates. These rates are susceptible to change and require significant management judgment. Impairments to goodwill are charged against earnings in the period the impairment is identified. The Company has three reporting units for which goodwill was tested on December 31, 2009: the Americas Region, the Europe/Asia Region, and the Asia Pacific Region, as shown in the table below. As of December 31, 2009 and 2008, the Company did not have any goodwill that was identified as impaired. The increase in goodwill of \$1.0 million in 2009 and the decrease of \$0.2 million in 2008 relates to adjustments to the purchase of an acquisition made in 2005.

<u>December 31, 2009</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Foreign Currency Translation</u>	<u>Ending Balance</u>
Americas Region	\$ 6,994	\$ —	\$ —	\$ 6,994
Europe/Africa region	11,957	546	437	12,940
Asia Pacific Region	—	—	—	—
Total	<u>\$ 18,951</u>	<u>\$ 546</u>	<u>\$ 437</u>	<u>\$ 19,934</u>
<u>December 31, 2008</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Foreign Currency Translation</u>	<u>Ending Balance</u>
Americas Region	\$ 6,994	\$ —	\$ —	\$ 6,994
Europe/Africa region	12,123	433	(599)	11,957
Asia Pacific Region	—	—	—	—
Total	<u>\$ 19,117</u>	<u>\$ 433</u>	<u>\$ (599)</u>	<u>\$ 18,951</u>

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Intangible assets consist of the following:

	December 31,	
	2009	2008
Amortizable intangible assets:		
Product technology	\$ 11,617	\$ 11,076
Patents	5,641	5,308
Other	7,937	7,452
Total	25,195	23,836
Accumulated amortization	(17,210)	(15,256)
Intangible assets—net	<u>\$ 7,985</u>	<u>\$ 8,580</u>

Amortization expense was \$1,387, \$1,021 and \$715 in 2009, 2008 and 2007, respectively. The estimated amortization expense for each of the years 2010 through 2014 and thereafter is as follows:

Years ending December 31,	Amount
2010	\$1,250
2011	1,188
2012	976
2013	803
2014	747
Thereafter	2,771
	<u>\$7,735</u>

8. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	As of December 31,	
	2009	2008
Accrued compensation and benefits	\$3,605	\$ 7,533
Accrued warranties	1,253	2,381
Professional and legal fees	894	742
Other accrued liabilities	2,421	3,376
	<u>\$8,173</u>	<u>\$14,032</u>

Activity related to accrued warranties was as follows:

	Years ended December 31,		
	2009	2008	2007
Beginning Balance	\$ 2,381	\$ 1,980	\$ 1,369
Provision for warranty expense	1,731	3,212	1,984
Warranty expired	(2,859)	(2,811)	(1,373)
Ending Balance	<u>\$ 1,253</u>	<u>\$ 2,381</u>	<u>\$ 1,980</u>

9. LINE OF CREDIT

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

10. CAPITAL LEASES

Assets under capital leases were \$366 and \$417 at December 31, 2009 and 2008, respectively. Accumulated depreciation on assets under capital leases was \$134 and \$85 at December 31, 2009 and 2008, respectively.

11. OTHER (INCOME) EXPENSE, NET

Other (income) expense, net consists of the following:

	Years ended December 31,		
	2009	2008	2007
Foreign exchange transaction (gains) losses	<u>\$(571)</u>	<u>\$2,345</u>	<u>\$(1,559)</u>
Other	<u>(21)</u>	<u>(50)</u>	<u>(339)</u>
Total other (income) expense, net	<u>\$(592)</u>	<u>\$2,295</u>	<u>\$(1,898)</u>

12. INCOME TAXES

During fiscal 2009, the Company increased its unrecognized tax benefit by \$0.3 million. The increase was due to tax developments primarily related to U.S. operations, which impacted the Company's valuation of uncertain tax positions. As of December 31, 2009, the Company's gross unrecognized tax benefits totaled \$0.6 million, which includes approximately \$0.03 million of interest and penalties. The Company estimates that the unrecognized tax benefits will not change significantly within the next year.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	2009	2008	2007
Balance at January 1,	<u>\$349</u>	<u>\$ 510</u>	<u>\$468</u>
Additions based on tax positions related to the current year	31	48	19
Additions for tax positions of prior years	265	—	23
Reductions for tax positions of prior years	—	(209)	—
Settlements	—	—	—
Balance at December 31,	<u>\$644</u>	<u>\$ 349</u>	<u>\$510</u>

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The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The table below summarizes the open tax years and ongoing tax examinations in major jurisdictions as of December 31, 2009:

<u>Jurisdiction</u>	<u>Open Years</u>	<u>Examination in Process</u>
United States—Federal Income Tax	2005 - 2009	2005-2007
United States—various states	2005 - 2009	N/A
Germany	2004 - 2009	N/A
Switzerland	2004 - 2009	N/A
Singapore	2005 - 2009	N/A
United Kingdom	2008 - 2009	N/A

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in tax expense. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is \$0.6 million. FARO does not currently anticipate that the total amount of unrecognized tax benefits will result in material changes to its financial position. The Company is subject to income taxes at the federal, state and foreign country level. The Company's tax returns are subject to examination at the U.S. federal level from 2005 forward and at the state level subject to a three to five year statute of limitations.

The United States Internal Revenue Service ("IRS") commenced an examination of the Company's 2005 to 2007 income tax returns in late 2007. This examination resulted in an assessment of approximately \$2.6 million related to the valuation of certain intangible assets contributed to a foreign subsidiary of the Company under a R&D Cost Sharing Arrangement entered into in 2001. This assessment was paid in January 2010 and included in income tax expense for the year ended December 31, 2009. The Company does not expect this assessment will have a prospective impact on its global effective tax rate. The Company believes that it has provided appropriately for any uncertain tax positions that may arise. The Company is not currently under examination in any other tax jurisdiction.

The effective income tax rate for 2009, 2008, and 2007 includes a reduction in the statutory corporate tax rates for the Company's operations in Switzerland. The favorable tax rate ruling requires the Company to maintain a certain level of manufacturing operations in Switzerland. The aggregate dollar effect of this favorable tax rate was approximately \$1.2 million, or \$0.07 per share, in the year ended December 31, 2009, \$2.1 million, or \$0.13 per share, in the year ended December 31, 2008, and \$2.0 million, or \$0.13 per share, in the year ended December 31, 2007.

In 2005, the Company opened a regional headquarters and began to manufacture its products in Singapore. In the third quarter of 2006, the Company received confirmation of a tax holiday for its operations from the Singapore Economic Development Board for a period of four years commencing January 1, 2006 and an additional six year extension at a favorable tax rate subject to certain terms and conditions including employment, spending, and capital investment. The aggregate dollar effect of this favorable tax rate was approximately \$1.1 million, or \$0.07 per share, during the year ended December 31, 2009, \$1.6 million, or \$0.10 per share, in the year ended December 31, 2008 and \$2.0 million, or \$.13 per share, during the year ended December 31, 2007.

At December 31, 2009 and 2008, the Company's domestic entities had deferred income tax assets in the amount of \$4,789 and \$6,775, respectively.

At December 31, 2009 and 2008, the Company's foreign subsidiaries had deferred income tax assets relating to net operating loss carry forwards, which do not expire, of \$12,181 and \$10,224, respectively. For financial reporting purposes, a valuation allowance of \$10,603 and \$8,690, respectively, has been recognized to offset the deferred tax assets relating to net operating losses. The Company maintains a valuation allowance on net operating losses in jurisdictions for which it does not have a history of earnings over the last three years and

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where the Company believes that the deferred tax assets are not more-likely-than-not to be realized based upon two-year projections of taxable income. The Company released a valuation allowance of approximately \$0.8 million in Germany in 2008, which was based on the demonstrated history of earnings over the past three years, and with management's assessment that it will be more-likely-than-not to utilize their deferred tax assets. Management calculated the amount to release from the valuation allowance using projections of future taxable earnings over the next two years. The Company had refundable income taxes related to domestic net operating losses of approximately \$5.9 million as of December 31, 2009 which will be carried back to 2005 and 2006 which are recorded in prepaid expenses and other current assets in the accompanying consolidated balance sheets.

The Company has not recognized any U.S. tax expense on undistributed international earnings, as it intends to reinvest the earnings outside the U.S. for the foreseeable future. The Company's net undistributed international earnings were approximately \$39.0 million and \$34.1 million at December 31, 2009 and 2008, respectively.

Significant judgment is required in determining the Company's worldwide provision for income taxes. In the ordinary course of a global business, there are many transactions for which the ultimate tax outcome is uncertain. The Company reviews its tax contingencies on a regular basis and makes appropriate accruals as necessary.

Income (loss) before income taxes consists of the following:

	Years ended December 31,		
	2009	2008	2007
Domestic	\$ (7,239)	\$10,708	\$ 7,081
Foreign	\$ (2,919)	7,652	15,955
(Loss) Income before income taxes	<u>\$ (10,158)</u>	<u>\$18,360</u>	<u>\$23,036</u>

The components of the income tax (benefit) expense are as follows:

	Years ended December 31,		
	2009	2008	2007
Current:			
Federal	\$ (1,369)	\$ 4,052	\$3,925
State	(133)	393	381
Foreign	(61)	1,818	1,235
	<u>(1,562)</u>	<u>6,263</u>	<u>5,541</u>
Deferred:			
Federal	1,199	(695)	(721)
State	116	(67)	(70)
Foreign	671	(1,093)	193
	<u>1,986</u>	<u>(1,855)</u>	<u>(598)</u>
	<u>\$ 424</u>	<u>\$ 4,408</u>	<u>\$4,943</u>

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Income tax expense (benefit) for the years ended December 31, 2009, 2008, and 2007 differs from the amount computed by applying the federal statutory corporate rate to (loss) income before income taxes. The differences are reconciled as follows:

	Years ended December 31,		
	2009	2008	2007
Tax (benefit) expense at statutory rate of 35%	\$(3,555)	\$ 6,426	\$ 8,063
State income taxes, net of federal benefit	(239)	353	234
Foreign tax rate difference	(1,977)	(4,600)	(6,042)
Research and development credit	(123)	(191)	(77)
Change in valuation allowance	2,486	2,540	1,887
Change in foreign tax rate	—	—	164
IRS settlement	2,628	—	—
Penalties	—	—	988
Equity based compensation	828	717	480
Tax expense related to uncertain tax positions	265	—	—
Tax exempt interest income	(39)	(707)	(549)
Other	150	(130)	(205)
Total income tax expense	\$ 424	\$ 4,408	\$ 4,943

The components of the Company's net deferred income tax asset are as follows:

	December 31,	
	2009	2008
Net deferred income tax asset—Current		
Intercompany profit in inventory	\$ 2,160	\$ 2,831
Warranty costs	166	380
Bad debt reserve	110	153
Inventory reserve	603	406
Unearned service revenue	1,677	1,539
Other	(243)	272
Deferred income tax asset—Current	4,473	5,581
Valuation Allowance	—	—
Net deferred income tax asset—Current	\$ 4,473	\$ 5,581
Net deferred income tax asset—Non-current		
Depreciation	\$ 721	\$ 1,380
Goodwill amortization	(1,175)	(1,009)
Product design costs	(150)	(22)
Employee stock options	42	(2)
Unearned service revenue	879	847
Loss carryforwards	12,181	10,224
Deferred income tax asset—Non-current	12,498	11,418
Valuation Allowance	(10,603)	(8,690)
Net deferred income tax asset—Non-current	\$ 1,895	\$ 2,728
Net deferred income tax liability—Non-current Intangible assets	\$ (1,143)	\$ (1,107)

13. COMMITMENTS AND CONTINGENCIES

Leases—The Company leases buildings and equipment under operating leases. The following is a schedule of future minimum lease payments required under non-cancelable operating leases with initial terms in excess of one year, in effect at December 31, 2009:

<u>Years ending December 31,</u>	<u>Amount</u>
2010	\$ 5,461
2011	4,543
2012	3,851
2013	3,386
2014	2,955
Thereafter	4,185
Total future minimum lease payments	<u>\$ 24,381</u>

Rent expense for 2009, 2008 and 2007 was approximately \$4,680, \$4,644 and \$3,662, respectively.

Securities Litigation—On December 6, 2005, the first of four essentially identical class action securities fraud lawsuits were filed against the Company and certain officers of the Company (the “Securities Litigation”) in the U.S. District Court for the Middle District of Florida. On April 19, 2006, the four lawsuits were consolidated, and Kornitzer Capital Management, Inc. (the “Lead Plaintiff”) was appointed as the lead plaintiff. The Lead Plaintiff sought to include in the class all persons who purchased or otherwise acquired the Company’s common stock between April 15, 2004 and March 15, 2006 (the “Class”), and sought an unspecified amount of damages, premised on allegations that each defendant made misrepresentations and omissions of material fact during the class period in violation of the Securities Exchange Act of 1934.

On February 26, 2008, the parties to the Securities Litigation entered into a Memorandum of Understanding stating the principal terms of their agreement to settle the Securities Litigation. On April 9, 2008, the parties filed a detailed Stipulation of Settlement with the court seeking the court’s preliminary and final approval of the terms of the proposed settlement. Pursuant to those terms, the issuer of the Company’s Executive Liability and Entity Securities Liability insurance policy applicable to the Securities Litigation paid \$6.875 million into a settlement fund for the Securities Litigation. That sum was within the coverage limit of the policy and accordingly had no effect on the Company’s financial results. On October 3, 2008, the court entered a Final Judgment and Order of Dismissal With Prejudice, whereby the court certified the Class for purposes of the settlement, approved the settlement, and dismissed the Securities Litigation, with prejudice, as against each defendant.

Derivative Action—On January 10, 2008, a verified shareholder derivative complaint was filed by an alleged shareholder of the Company in the U.S. District Court for the Middle District of Florida against six of the Company’s current and former directors, as defendants, and against the Company, as a nominal defendant (the “Derivative Action”). The derivative complaint alleges breach of fiduciary duty and other claims against the individual defendants principally in connection with the alleged acts and omissions asserted in the Securities Litigation. In February 2008 and April 2008, the Company received two demands by other alleged shareholders that the Company assert substantially the same claims as set forth in the derivative complaint against seven of the Company’s current and former directors. Both of those demands subsequently were withdrawn.

On November 12, 2008, the parties to the Derivative Action executed a Memorandum of Understanding of the material terms of a proposed settlement of the Derivative Action. On January 21, 2009, the parties filed with the court a Stipulation of Settlement seeking the court’s preliminary and final approval of the terms of the proposed settlement. On February 13, 2009, the court granted preliminary approval of the settlement. On April 23, 2009, the court granted final approval of the settlement and entered an Order and Final Judgment directing the consummation of the settlement and dismissing the Derivative Action, with prejudice, as against each defendant. Pursuant to the terms of the settlement, the Company has adopted certain corporate governance

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policies for a period of three years, and the issuer of the Company's Executive Liability and Entity Securities Liability insurance policy applicable to the Derivative Action has paid \$0.4 million to the plaintiff's counsel for their fees and expenses. That sum is within the coverage limit of the policy and accordingly had no effect on the Company's financial results.

Patent Matters—On July 11, 2008, a complaint for patent infringement was filed against the Company in the U.S. District Court for the District of Massachusetts by Metris USA, Inc. and certain of its affiliates, which the Company refers to collectively as "Metris", concerning U.S. Patent Nos. 6,611,617 and 7,313,264. The Company responded with counterclaims alleging that the asserted patents, which are generally directed to laser scanning devices, are invalid, non-infringed, and unenforceable due to fraud during prosecution of the patents in the U.S. Patent and Trademark Office. On August 31, 2009, the Court granted the Company's motion to add counterclaims and defenses for violation of federal and state antitrust and unfair competition laws based on the alleged knowing assertion of invalid and fraudulent patents. On October 22, 2009, the Court issued an Order for the purpose of construing certain claim language of the asserted patents. Pursuant to the October 22, 2009 Order, the parties submitted a stipulation further construing claim language on November 9, 2009. Discovery in the case is ongoing and no trial date has been set. The Company believes that it does not infringe the asserted patents and/or that the patents are invalid. The Company does not anticipate this lawsuit will have a material impact on the Company's business, financial condition or results of operations. However, the outcome is difficult to predict and an adverse determination could have a material impact on the Company's business, financial condition or results of operations.

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

14. STOCK COMPENSATION PLANS

The Company has four stock option plans that provide for the granting of stock options to key employees and non-employee members of the Board of Directors. The 1997 Employee Stock Option Plan ("1997 Plan") provides for granting incentive stock options and nonqualified stock options to officers and key employees of the Company. The 1997 Non-employee Director Plan provides for granting nonqualified stock options and formula options to non-employee directors. The 2004 Equity Incentive Plan ("2004 Plan") and the 2009 Equity Incentive Plan ("2009 Plan") provide for granting options, restricted stock, restricted stock units or stock appreciation rights to employees and non-employee directors.

The Company was authorized to grant awards for up to 1,400,000 shares of common stock under the 1997 Plan, of which 74,782 options are currently outstanding at exercise prices between \$1.50 and \$27.40. These options have a 10 year term and vest over a 3-year period. The Company was also authorized to grant awards for up to 250,000 shares of common stock under the 1997 Non-employee Director Plan of which 60,000 options are currently outstanding at exercise prices between \$1.61 and \$21.56. The Company was also authorized to grant awards for up to 1,750,000 shares of common stock under the 2004 Plan, of which 895,796 options are currently outstanding at exercise prices between \$12.50 and \$31.45, and 12,867 restricted stock units are outstanding at a stock price of \$13.04 to \$31.06. These options and restricted stock units have a 10 year term (7 years on new grants) and vest over a 3-year period. The Company will not make any further grants under the 1997 Plan, the 1997 Non-employee Director or the 2004 Plan. The Company is authorized to grant awards for up to 1,781,546 shares of common stock under the 2009 Plan as well as any shares underlying awards outstanding under the 2004 Plan as of the effective date of the 2009 Plan that thereafter terminate or expire unexercised, or are canceled, forfeited or lapse for any reason. There are no grants currently outstanding under the 2009 Plan. Prior to 2009, upon election to the Board, each non-employee director was granted 3,400 restricted shares of common stock that vested ratably over three years. On the day following the Annual Meeting of Shareholders, each non-employee director, other than a non-employee director who received the initial equity grant in that same year, was granted 2,200 restricted shares of common stock that vested ratably over three years. Beginning in 2009, each

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non-employee director is granted restricted shares of common stock with a value equal to \$70,000, calculated as of the closing share price on the day following the Annual Meeting of Shareholders. The shares of restricted stock will vest on the first anniversary of the grant date, subject to a director's continued membership on the Board. The Company records compensation cost associated with its restricted stock unit grants on a straight-line basis over the vesting term.

In addition to the four stock incentive plans, the Company has the 1997 Non-Employee Directors Fee Plan (1997 Fee Plan) under which the Company is authorized to issue up to 250,000 shares of common stock and permits non-employee directors to elect to receive directors' fees in the form of common stock rather than cash. Common stock issued in lieu of cash directors' fees is issued at the end of the quarter in which the fees are earned, with the number of shares based on the fair market value of the common stock for the five trading days immediately preceding the last business day of the quarter. The 1997 Fee Plan also permits non-employee directors to irrevocably elect to defer receipt of all or any portion of the shares of common stock which would otherwise be payable.

Compensation costs charged to operations associated with the Company's stock incentive plans were \$2,449, \$2,098, and \$1,217 in 2009, 2008, and 2007, respectively. The changes in stock option associated compensation cost were due to the vesting of options and the accrual of expenses relating to the issuance of restricted stock.

The Company used the Black-Scholes option-pricing model to determine the fair value of grants made using the following assumptions:

	For the Years Ended		
	December 31, 2009	December 31, 2008	December 31, 2007
Risk-free interest rate	1.38% and 1.44%	1.44 - 3.04%	3.26 - 4.5%
Expected dividend yield	0%	0%	0%
Expected option life	4 years	4 years	4 years
Expected volatility	48.3%	54.7% - 58%	58.0% - 62.8%
Weighted-average expected volatility	48.3%	57.9%	62.6%

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

A summary of stock option activity and weighted average exercise prices follows:

	Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value as of December 31, 2009
Outstanding at beginning of period	949,572	\$ 22.48		
Granted	258,607	13.06		
Forfeited	(169,851)	20.20		
Exercised	(7,750)	10.76		
Outstanding at December 31, 2009	1,030,578	\$ 20.58	5.3	\$ 3,560
Options exercisable at December 31, 2009	684,568	\$ 20.72	4.9	\$ 1,992

The weighted-average grant-date fair value of the stock options granted during the years ended December 31, 2009, 2008 and 2007 was \$5.08, \$13.99 and \$12.80, respectively. The aggregate intrinsic value of

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stock options exercised during the years ended December 31, 2009, 2008 and 2007 was \$0.05 million, \$0.2 million and \$8.0 million, respectively. The total fair value of stock options vested during the years ended December 31, 2009, 2008 and 2007 was \$1.7 million, \$0.81 million and \$0.05 million, respectively.

The following table summarizes the restricted stock activity and weighted average grant-date fair values for the year ended December 31, 2009:

	Shares	Weighted-Average Grant Date Fair Value
Non-vested at beginning of period	52,660	\$ 26.69
Granted	57,955	14.45
Forfeited	(24,121)	18.83
Vested	(22,999)	26.12
Non-vested at December 31, 2009	<u>63,495</u>	<u>\$ 18.61</u>

As of December 31, 2009, there was \$2.3 million in total unrecognized stock-based compensation expense related to non-vested stock-based compensation arrangements. The expense is expected to be recognized over a weighted average period of 1.5 years.

15. EARNINGS PER SHARE

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

	Years Ended					
	December 31, 2009		December 31, 2008		December 31, 2007	
	Shares	Per-Share Amount	Shares	Per-Share Amount	Shares	Per-Share Amount
Basic EPS	16,125,449	\$ (0.66)	16,632,608	\$ 0.84	15,443,259	\$ 1.17
Effect of dilutive securities	—	—	101,795	(0.01)	278,956	(0.02)
Diluted EPS	<u>16,125,449</u>	<u>\$ (0.66)</u>	<u>16,734,403</u>	<u>\$ 0.83</u>	<u>15,722,215</u>	<u>\$ 1.15</u>

The effect of 1,030,578; 509,290; and 10,000 potentially dilutive securities were not included for 2009, 2008 and 2007 respectively, as they were antidilutive.

16. EMPLOYEE RETIREMENT BENEFIT PLAN

The Company maintains a 401(k) defined contribution retirement plan for its eligible U.S. employees. The Company terminated matching contributions on April 18, 2009. Costs charged to operations in connection with the 401(k) plan during 2009, 2008, and 2007 aggregated \$291, \$909 and \$569, respectively.

17. SEGMENT REPORTING

The Company has three reportable segments based upon geographic regions: Americas, Europe/Africa and Asia Pacific. The Company includes costs related to Corporate in its Americas region. The Company does not incur R&D expenses in its Asia region. The Company develops, manufactures, markets, supports and sells CAD-based quality assurance products integrated with CAD-based inspection and statistical process control software in each of these regions. These activities represent approximately 99% of consolidated sales. The Company evaluates performance and allocates resources based upon profitable growth and assets deployed.

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

	2009	2008	2007
Americas Region			
Net sales to external customers	\$ 55,062	\$ 78,321	\$ 79,984
Operating loss	(13,353)	(4,385)	(1,554)
Long-lived assets	21,579	21,366	12,594
Capital expenditures	2,898	7,155	1,879
Total assets	131,477	155,342	144,865
Europe/Africa Region			
Net sales to external customers	\$ 62,968	\$ 93,585	\$ 78,299
Operating (loss) income	(371)	15,009	11,716
Long-lived assets	18,245	18,253	18,423
Capital expenditures	515	2,152	1,079
Total assets	74,126	76,996	75,279
Asia Pacific Region			
Net sales to external customers	\$ 29,673	\$ 37,343	\$ 33,334
Operating income	2,735	8,313	8,949
Long-lived assets	1,833	2,048	1,597
Capital expenditures	536	939	439
Total assets	30,107	26,976	23,395
Totals			
Net sales to external customers	\$ 147,703	\$ 209,249	\$ 191,617
Operating (loss) income	(10,989)	18,937	19,111
Long-lived assets	41,657	41,667	32,614
Capital expenditures	3,949	10,246	3,397
Total assets	235,710	259,314	243,539

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

18. QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

<u>Quarter ended</u>	<u>April 4, 2009</u>	<u>July 4, 2009</u>	<u>October 3, 2009</u>	<u>December 31, 2009</u>
Sales	\$ 31,449	\$ 34,516	\$ 35,713	\$ 46,025
Gross profit	16,260	19,364	19,602	25,482
Net (loss)	(6,585)	(2,104)	(1,273)	(620)
Net (loss) per share:				
Basic	\$ (0.41)	\$ (0.13)	\$ (0.08)	\$ (0.04)
Diluted	\$ (0.41)	\$ (0.13)	\$ (0.08)	\$ (0.04)
<u>Quarter ended</u>	<u>March 29, 2008</u>	<u>June 28, 2008</u>	<u>September 27, 2008</u>	<u>December 31, 2008</u>
Sales	\$ 46,090	\$ 57,749	\$ 49,095	\$ 56,315
Gross profit	27,707	36,239	29,009	32,272
Net income	3,378	6,365	2,011	2,199
Net income per share:				
Basic	\$ 0.20	\$ 0.38	\$ 0.12	\$ 0.13
Diluted	\$ 0.20	\$ 0.38	\$ 0.12	\$ 0.13

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 9A. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

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

As of the end of the period covered by this report, the Company's management carried out an evaluation, under the supervision and with the participation of its Chief Executive Officer and its Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures, as defined by Rule 13a-15(e) under the Exchange Act, were effective as of December 31, 2009.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the fourth quarter ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Management's Report on Internal Control Over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is the process designed under the Chief Executive Officer's and the Chief Financial Officer's supervision, and effected by the Company's Board of Directors, management and other personnel, 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 in the United States.

Under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, the Company conducted an evaluation of the effectiveness of the Company's internal control over financial reporting as of December 31, 2009 as required by the Securities and Exchange Act of 1934 Rule 13a-1(c). In making this assessment, the Company used the criteria set forth in the framework in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on the Company's evaluation under the framework in *Internal Control—Integrated Framework*, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2009.

There are inherent limitations in the effectiveness of internal control over financial reporting, including the possibility that misstatements may not be prevented or detected. Accordingly, an effective control system, no matter how well designed and operated, can provide only reasonable assurance of achieving the designed control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company

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have been detected. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Grant Thornton LLP, the independent registered public accounting firm that audited the Company's consolidated financial statements, has issued an attestation report on the Company's internal control over financial reporting as of December 31, 2009, which appears below.

FARO Technologies, Inc.
Lake Mary, Florida
February 26, 2010

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
FARO Technologies, Inc. and Subsidiaries

We have audited FARO Technologies, Inc. (a Florida Corporation) and subsidiaries' internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). FARO Technologies, Inc. and subsidiaries' management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on FARO Technologies, Inc. and subsidiaries' internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, FARO Technologies, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control—Integrated Framework* issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of FARO Technologies, Inc. and subsidiaries as of December 31, 2009 and 2008, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2009 and our report dated February 26, 2010 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Orlando, Florida
February 26, 2010

ITEM 9B. OTHER INFORMATION.

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE.

The information required by this Item with respect to directors and executive officers is incorporated herein by reference from the information under the captions “Election of Directors” and “Executive Officers” contained in the Company’s definitive proxy statement for its 2010 Annual Meeting of Shareholders, which the Company refers to as the Proxy Statement.

The information required by this Item regarding compliance with Section 16(a) of the Exchange Act appears under the heading “Other Matters-Section 16(a) Beneficial Ownership Reporting Compliance” in the Proxy Statement and is incorporated by reference into this Annual Report on Form 10-K.

The information required by this Item with respect to corporate governance and the Company’s Code of Conduct is incorporated herein by reference from the information contained in the Proxy Statement under the heading “Corporate Governance and Board Matters”.

ITEM 11. EXECUTIVE COMPENSATION.

The information required by this Item regarding executive compensation is incorporated herein by reference from the information contained in the Proxy Statement under the captions “Executive Compensation” and “Director Compensation”.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

The information required by this Item regarding security ownership of certain beneficial owners and management is incorporated herein by reference from the information contained in the Proxy Statement under the captions “Security Ownership of Beneficial Owners and Management” and “Equity Compensation Plan Information”.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE.

The information required by this Item about certain relationships and related transactions appears under the heading “Certain Relationships and Related Transactions” in the Proxy Statement and is incorporated herein by reference.

The information required by this Item regarding director independence is incorporated herein by reference from the information contained in the Proxy Statement under the heading “Corporate Governance and Board Matters”.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

The information required by this Item about principal accountant fees and services as well as related pre-approval policies appears under the heading “Independent Public Accountants” in the Proxy Statement and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) Documents Filed as Part of this Report. The following documents are filed as part of this Annual Report on Form 10-K:

(1) Consolidated Financial Statements. Included in Part II, Item 8 are the consolidated financial statements, the notes thereto and the report of the Independent Registered Public Accounting Firm.

(2) Financial Statement Schedules. Schedule II—Valuation and Qualifying Accounts is filed as a part hereof along with the related report of the Independent Registered Public Accounting Firm on the Company's financial statement schedule. All other schedules have been omitted because the information required to be set forth therein is not applicable or is included in the consolidated financial statements or notes thereto.

(3) Exhibits. The exhibits listed in the accompanying Exhibit Index are filed or incorporated by reference as part of this Annual Report on Form 10-K.

SCHEDULE II—VALUATION AND QUALIFYING ACCOUNTS

Valuation and Qualifying Accounts were as follows for the three years ended December 31, 2009:

Description	Balance at beginning of period	Additions charged to costs and expenses or revenues	Deductions for purposes for which accounts were set up	Balance at end of period
Year ended December 31, 2009				
Deducted from assets which apply				
Uncollectible accounts	\$ 1,727	\$ 1,852	\$ 420	\$ 3,159
Reserve for inventory obsolescence	1,471	1,486	485	2,472
Total	\$ 3,198	\$ 3,338	\$ 905	\$ 5,631
Year ended December 31, 2008				
Deducted from assets which apply				
Uncollectible accounts	\$ 739	\$ 1,092	\$ 104	\$ 1,727
Reserve for inventory obsolescence	1,865	1,161	1,555	1,471
Total	\$ 2,604	\$ 2,253	\$ 1,659	\$ 3,198
Year ended December 31, 2007				
Deducted from assets which apply				
Uncollectible accounts	\$ 458	\$ 373	\$ 92	\$ 739
Reserve for inventory obsolescence	404	1,841	380	1,865
Total	\$ 862	\$ 2,214	\$ 472	\$ 2,604

EXHIBIT INDEX

Exhibit No.	Description
3.1	Articles of Incorporation, as amended (Filed as Exhibit 3.1 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference)
3.2	Amended and Restated Bylaws (Filed as Exhibit 3.1 to current Report on Form 8-K, dated January 28, 2010 and incorporated herein by reference)
4.1	Specimen Stock Certificate (Filed as Exhibit 4.1 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference)
10.1	1993 Stock Option Plan, as amended (Filed as Exhibit 10.1 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference)*
10.2	1997 Amended and Restated Employee Stock Option Plan (Filed as Exhibit 4. 2 to Registrant's Registration Statement on Form S-8, No. 333-125021, and incorporated herein by reference)*
10.3	Amended and Restated 2004 Equity Incentive Plan (Filed as Exhibit 10.1 to Registrant's Form 8-K dated November 20, 2008, and incorporated herein by reference)*
10.4	Amendment to Amended and Restated 2004 Equity Incentive Plan (Filed as Exhibit 10.3 to Registrant's Form 8-K, dated April 8, 2009, and incorporated herein by reference)*
10.5	1997 Non-Employee Director Stock Option Plan (Filed as Exhibit 10.3 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference)*
10.6	1997 Non-Employee Directors Fee Plan (Filed as Exhibit 10.4 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference)*
10.7	2009 Equity Incentive Plan (Filed as Appendix A to Registrant's Definitive Proxy Statement on Schedule 14A dated April 13, 2009, and incorporated herein by reference)*
10.8	Summary of Director Compensation Program (Filed as Exhibit 10.19 to Registrant's Quarterly Report on Form 10-Q for the quarter ended April 4, 2009 and incorporated herein by reference)*
10.9	Form of Patent and Confidentiality Agreement between the Company and each of its employees (Filed as Exhibit 10.10 to Registrant's Registration Statement on Form S-1, No. 333-32983, and incorporated herein by reference)
10.10	Form of Restricted Stock Grant Agreement under the 2004 Equity Incentive Plan (Filed as Exhibit 10.7 to Registrant's Annual Report on Form 10-K for the year ended December 31, 2006)*
10.11	Form of Restricted Stock Unit Grant Agreement under the 2004 Equity Incentive Plan (Filed as Exhibit 10.8 to Registrant's Annual Report on Form 10-K for the year ended December 31, 2006)*
10.12	Form of Stock Option Grant Agreement under the 2004 Equity Incentive Plan (Filed as Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 29, 2008 and incorporated herein by reference)*
10.13	Amended and Restated Loan Agreement, dated as of July 11, 2006, between the Company and SunTrust Bank. (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K dated July 11, 2006 and incorporated herein by reference)
10.14	First Amendment to Amended and Restated Loan Agreement, dated November 21, 2008, between FARO Technologies, Inc. and SunTrust Bank (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K dated November 21, 2008, and incorporated herein by reference)
10.15	Second Amendment to Amended and Restated Loan Agreement, dated April 22, 2009, between FARO Technologies, Inc. and SunTrust Bank (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K, dated April 24, 2009, and incorporated herein by reference)

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<u>Exhibit No.</u>	<u>Description</u>
10.16	Third Amendment to Amended and Restated Loan Agreement, dated June 18, 2009, between FARO Technologies, Inc. and SunTrust Bank (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K, dated June 22, 2009, and incorporated herein by reference)
10.17	Amended and Restated Employment Agreement, dated November 7, 2008, by and between the Company and Jay Freeland (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K dated November 7, 2008, and incorporated herein by reference)*
10.18	Amended and Restated Employment Agreement, dated November 7, 2008, by and between the Company and Keith Bair (Filed as Exhibit 10.2 to Registrant's Current Report on Form 8-K dated November 7, 2008 and incorporated herein by reference)*
10.19	Amendment to Amended and Restated Employment Agreement, dated April 2, 2008, by and between the Company and Jay Freeland (Filed as Exhibit 10.1 to Registrant's Current Report on Form 8-K, dated April 8, 2009, and incorporated herein by reference)*
10.20	Amendment to Amended and Restated Employment Agreement, dated April 2, 2008, by and between the Company and Keith S. Bair (Filed as Exhibit 10.2 to Registrant's Current Report on Form 8-K, dated April 8, 2009, and incorporated herein by reference)*
10.21	FARO Technologies, Inc. Change in Control Severance Policy (Filed as Exhibit 10.3 to Registrant's Current Report on Form 8-K, dated November 7, 2008, and incorporated herein by reference)*
10.22	Lease Agreement dated July 8, 2008, by and between the Company and James W. Hickman Revocable Trust (Filed as Exhibit 10.16 to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 27, 2008 and incorporated herein by reference)
10.23	Lease Agreement dated September 15, 2008, by and between the Company and NB MS NEBC LLC (Filed as Exhibit 10.17 to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 27, 2008 and incorporated herein by reference)
10.24	Sublease Agreement dated September 30, 2007 between the Company and Priority HealthCare Corporation (Filed as Exhibit 10.14 to Registrant's Annual Report on Form 10-K for the year ended December 31, 2007 and incorporated herein by reference)
10.25	Lease Agreement dated September 26, 2007, by and between the Company and Sun Life Assurance Company of Canada (Filed as Exhibit 10.15 to Registrant's Annual Report on Form 10-K for the year ended December 31, 2007 and incorporated herein by reference)
10.26	Amended and Restated Lease Agreement, dated October 1, 2009, by and between the Company and Emma Investments, LLC
10.27	First Amendment to Lease Agreement, dated October 1, 2009, by and between the Company and Sun Life Assurance Company of Canada
21.1	List of Subsidiaries
23.1	Consent of Grant Thornton LLP
24.1	Power of Attorney relating to subsequent amendments (included on the signature page(s) of this report).
31-A	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31-B	Certification of the Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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<u>Exhibit No.</u>	<u>Description</u>
32-A	Certification of the Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32-B	Certification of the Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99.1	Properties

* Indicates management contracts and compensatory plans and arrangements

AMENDED AND RESTATED LEASE AGREEMENT

THIS AMENDED AND RESTATED LEASE AGREEMENT, hereinafter referred to as the "Lease", is hereby made by and between **EMMA INVESTMENTS, LLC**, a Florida limited liability company, hereinafter referred to as the "Lessor", whose address is Post Office Box 941618, Maitland, Florida 32794, and **FARO TECHNOLOGIES, INC.**, a Florida corporation, hereinafter referred to as the "Lessee" whose address is 250 Technology Park, Lake Mary, Florida 32746.

WITNESSETH:

That Lessor, for and in consideration of the covenants and agreements hereinafter set forth and the rent hereinafter specifically reserved, does hereby lease unto Lessee the premises identified herein, in accordance with the following terms and conditions:

1. Premises:

1.01 Lessor hereby leases to Lessee and Lessee hereby leases from Lessor, for the term and subject to the covenants and conditions set forth in this Lease the premises located at 125 Technology Park, Lake Mary, Seminole County, Florida 32746, more specifically depicted on Exhibit "A" attached hereto and incorporated herein, hereinafter referred to as the "Premises".

1.02 This Lease is subject to the following:

- (a) conditions, restrictions, and limitations, if any, that are of record;
- (b) present and future building restrictions or zoning ordinances of any municipality, Seminole County, the State of Florida, and any other governmental agency or body now existing, or which may hereinafter exist during the term of this lease by reason of any legal authority;
- (c) the conditions and state of repair of the Premises;
- (d) rights, if any, of any utility companies relating to the furnishing of water, gas, electric and other utility lines, wires, pipes and poles, and the maintenance thereof.

2. Use Of The Premises And Compliance With Laws:

2.01 Lessee shall use and occupy the Premises for general office and light industrial uses only, subject to the terms of this Lease. Lessee shall not do or permit anything to be done on or about the Premises or the building that will unreasonably interfere with the rights of other tenants in neighboring buildings or allow the Premises to be used for any unlawful purpose. Lessee shall not do, permit or suffer in, on or about the Premises the sale of any alcoholic liquor without the written consent of Lessor first obtained.

2.02 Lessee shall not use and/or occupy the Premises for any use or uses other than as described in Section 2.01 above without the express prior written approval of the Lessor. Lessee will neither use, nor permit the use of the Premises, in any manner that is in conflict with any "Laws", as hereinafter defined. In connection with Lessee's use of the Premises, it, its invitees, licensees, guests and employees shall, at all times, comply with all Laws of any nature whatsoever which govern its use of the Premises including, but not limited to, all zoning regulations, all Environmental Laws and all rules and regulations of any board of fire underwriters having jurisdiction thereof. Lessee, at its sole cost and expense, shall be responsible for obtaining any and all governmental permits and approvals that may be necessary in connection with Lessee's use and

occupation of the Premises. Further, Lessee agrees to indemnify and hold Lessor harmless against any and all claims and/or damages to which Lessor may be exposed as a result of Lessee's failure to obtain any necessary permits and/or approvals. As used herein "Laws" shall mean all federal, state, county and local laws, statutes, codes, ordinances, rules, regulations, decrees, orders and other such requirements now or hereafter imposed, including, but not limited to, any and all Environmental Laws (as hereinafter defined).

2.03 Lessee shall not place or park any vehicle on the Premises, nor allow any of its employees, agents, customers, guests or invitees to place or park any vehicle on the Premises, in such a manner that impedes the flow of traffic or blocks access to or from the Premises or surrounding property.

2.04 Lessee, at its sole cost and expense, shall be responsible for complying with all applicable provisions, during the Term of the Lease, of the ADA as may be amended from time to time, relating to: (a) the physical condition of the Premises; (b) Lessee's policies and the operation of its business from the Premises; and, (c) Lessee's employment-related practices. As used herein, "ADA" means The Americans With Disabilities Act of 1990 (42 U.S.C. §1201 et seq.) and the regulations and guidelines promulgated or published thereunder as any of the foregoing may be amended. Lessor shall have no responsibility whatsoever for compliance with the ADA with regard to the Premises during the Term of this Lease and Lessee shall indemnify, defend and hold Lessor harmless from and against any and all claims, actions, damages, liabilities, costs and expenses, including reasonable attorneys' fees, in connection with, or resulting from, compliance or non-compliance with the ADA during the Term of the Lease.

3. Term:

3.01 The term of this Lease shall be for a period beginning October 1, 2009 and ending September 30, 2014. The beginning date of this period, October 1, 2009, shall hereinafter be referred to as the Commencement Date. This term shall hereinafter be referred to as the "Primary Term". For the purposes of this Lease, the Primary Term and the Option Term discussed in section 3.02 are sometimes herein collectively referred to as the "Term".

3.02 Upon the expiration of the Primary Term of this Lease, and provided Lessee is not then in default hereunder, Lessee shall have the option to extend the Term of this Lease for one additional five (5) year period, hereinafter referred to as the "Option Term". In order to exercise the option for the Option Term, Lessee must give Lessor notice, in writing, of its intent to exercise the option at least one hundred eighty (180) days prior to the expiration of the Primary Term. Failure by the Lessee to give the required written notice of its election to exercise the option for the Option Term shall result in the waiver and cancellation of Lessee's right to elect such option. The Option Term, if Lessee properly exercises the option, shall be governed by the terms and conditions of this Lease. The base rent for the Option Term shall be calculated in accordance with the provisions of 4.02 and 4.03 below.

3.03 The parties recognize that the Premises are currently leased by Lessee under that certain Lease Agreement dated August 8, 2006 (the "Prior Lease"), which Prior Lease was assigned to Lessor upon its purchase of the Premises. The parties confirm and ratify the validity and effectiveness of the Prior Lease up to the Commencement Date of this Lease. Upon the Commencement Date, the Prior Lease shall be deemed amended, totally restated and superseded by this Lease. As a result, the conduct and relationship of the parties thereafter as to the Premises shall be solely governed by the terms and conditions of this Lease and the Prior Lease shall be of no further force and effect.

4. Rent:

4.01 Beginning on the Commencement Date and continuing during the Term of this Lease, Lessee shall pay to Lessor, as rent for the use and occupancy of the Premises: (a) the base rent provided for in this section; (b) the Operating Expense Charge as described below; and (c) applicable sales tax. The foregoing shall hereinafter sometimes be collectively referred to as the "Rent". The Rent shall be paid by Lessee to Lessor, monthly in advance, on the first day of each and every month during the Term. With regard to the first payment of Rent, the same shall be paid by Lessee to Lessor upon the Commencement Date.

4.02 The base rent during the Primary Term shall be as follows:

(a) The base rent for the first year of the Term shall be \$309,408.48. The base rent for the first year of the Term shall be paid by Lessee to Lessor in twelve equal monthly installments of \$25,784.04.

(b) On October 1, 2010, and again on October 1 of each succeeding year occurring during the Primary Term, the base rent shall be increased by three percent (3%). The Lessee agrees to pay the adjusted base rent, together with the rest of the Rent due, in equal monthly installments on the first day of each and every month for the next ensuing twelve month period. Accordingly, the scheduled base rent increases for the Primary Term shall be as follows:

10/1/2010 – 9/30/2011 – Annual Base Rent: \$318,690.72 (\$26,557.56/mo.)

10/1/2011 – 9/30/2012 – Annual Base Rent: \$328,251.48 (\$27,354.29/mo.)

10/1/2012 – 9/30/2013 – Annual Base Rent: \$338,099.04 (\$28,174.92/mo.)

10/1/2013 – 9/30/2014 – Annual Base Rent: \$348,241.92 (\$29,020.16/mo.)

(c) If properly and timely elected, the base rent of the first year of the Option Term shall be determined as set forth in Section 4.03. On October 1 of each succeeding year following the beginning of the Option Term through the remainder of the Option Term, the base rent shall be increased by three percent (3%). The Lessee agrees to pay the adjusted base rent, together with the rest of the Rent due, on the first day of each and every month for the next ensuing twelve month period.

4.03 Within fifteen (15) days of Lessee's timely election of the Option Term described in section 3.02, Lessor shall deliver written notice to Lessee as to Lessor's estimation as to the fair market base rent rate and thereafter should negotiate in good faith with Lessee in an attempt to agree upon a fair market base rent rate for the first year of the Option Term. The term "fair market base rent rate" shall mean the annual rental rate, projected to the date of the commencement of the Option Term, which Lessee would expect to pay and Lessor would expect to receive under leases for space of comparable size and quality to the Premises in the same sub-market area, upon terms and conditions comparable to this Lease. The base rent for the first year of the Option Term shall be ninety-five percent (95%) of the fair market base rent rate, as agreed upon not later than sixty (60) days following Lessee's timely election of the Option Term. In the event the Lessor and Lessee are unable to agree as to the fair market base rent rate within such sixty (60) day period, then within ten (10) days of such date, each party shall employ a qualified real estate professional, with at least five (5) years experience immediately prior to the date in question, to appraise and establish the fair market base rent rate for similar leases. The two real estate professionals thus appointed shall meet promptly and attempt to agree upon and establish said rate or, upon failing to do so, shall then jointly designate a third real estate professional within fifteen (15) days of their appointment. Within fifteen (15) days after selection of the third real estate professional, such professional shall select the fair market base rent rate proposed by either Lessee's or Lessor's real estate professional as the amount more reflective of the fair market base rent rate. Such determination shall be finally determinative of such fair market base rent rate. Each of the parties shall pay the cost of its own real estate professional and bear one-half (1/2) of the cost of the third real professional.

4.04 Lessee shall pay to Lessor, monthly in advance, commencing on the Commencement Date and continuing thereafter on the first day of each month during the Lease Term, charges associated with operating costs for the Premises. This payment, hereinafter referred to as the "Operating Expense Charge", shall begin at the base rate of \$6,217.62 per month. The Operating Expense Charge shall include, without limitation: (a) real property taxes; (b) building structure and liability insurance on the building; and (c) property owners association dues. Within sixty (60) days of the Lease anniversary, Lessor shall furnish Lessee with a written statement of the total estimated installments paid by Lessee for the immediately previous year of the Term and the actual operating costs for the Premises (the "Reconciliation Notice"). Lessee shall pay any deficiency as shown on such statement to Lessor within fifteen (15) days after delivery of such statement. Any excess payment by Lessee shown on such statement shall be credited against payments next due from Lessee or, if no such payments are next due, such excess payment shall be refunded to Lessee. Lessor will notify Lessee, within sixty (60) days of the Lease anniversary, of the estimated amount to be due for the Operating Expense Charge for the next Lease year of the Term and the corresponding monthly amount to be due.

4.05 The total monthly payment due for Rent hereunder shall be paid by Lessee to Lessor in lawful money of the United States, without notice or demand, and without abatement, reduction, setoff, counterclaim, defense or deduction, except as specifically provided for herein.

4.06 Lessee shall promptly pay all Rent and other charges at Lessor's address: Post Office Box 941618, Maitland, Florida 32794, or to such other person or corporation and at such other address, as shall be designated by Lessor in writing at least ten (10) days prior to the next ensuing Rent payment date.

5. Tenant Improvements:

5.01 Lessor agrees to expend certain funds toward the construction of approved tenant improvements made to the Premises in accordance with the conditions of this section. Lessor agrees to pay, as a one time expense to Lessor, anytime during the Term hereof, the sum of Twenty Thousand and No/100 Dollars (\$20,000.00) to be applied to new paint and carpet and other repairs and replacements in the Premises as determined by Lessee. These funds shall be used to pay expenses for such improvements which will stay with the Premises and benefit the property following the termination/expiration of this Lease. The tenant improvement funds described herein shall be paid directly to the improvement vendors following (a) completion of all approved tenant improvements (b) three (3) days following presentation of all necessary paperwork to clear the property of any potential or actual liens arising from such improvements and (c) following Lessor's inspection of same to ensure completion, which inspection shall occur within ten (10) days following notice from the Lessee to Lessor that the improvements are complete. All approved tenant improvements must be made within the constraints of section 14.01. Any and all costs associated with the approved tenant improvements in excess of the \$20,000.00 allowance shall be made at the sole cost and expense of Lessee. With the exception of Lessor's agreement to provide tenant improvement funds as described in this section, Lessee agrees to and does accept the Premises in its "as-is" condition as of the execution of this Lease. Lessee's occupancy of the Premises shall be conclusive evidence of Lessee's agreement and acceptance in this regard.

6. Property Taxes:

6.01 As part of the monthly Operating Expense Charge, Lessee shall pay, during the Term of this Lease, all real estate taxes attributable to the Premises. The phrase "real estate taxes attributable to the Premises" as used in this paragraph shall mean, an amount equal to the real estate taxes, any assessments and any governmental charges levied upon or with respect to the Premises and the building located upon the Premises. Lessee shall be liable for all taxes levied upon the personal property and trade fixtures placed by

Lessee in or about the Premises. If any taxes attributable to the personal property and trade fixtures placed by Lessee in or about the Premises shall be levied against Lessor or Lessor's property, and if Lessor pays the same, or if the assessed value of Lessor's land is increased by the inclusion thereof, and if Lessor pays the taxes based upon such increased assessment, Lessee upon demand shall repay to Lessor the taxes so paid by Lessor. Lessee will have the right to contest the amount or validity, in whole or in part, of any tax on Lessee's personal property and trade fixtures by appropriate proceedings diligently conducted in good faith by Lessee, only after paying such tax or posting security that Lessor reasonably requires in order to protect the Premises against loss or forfeiture. Upon termination of any proceedings, Lessee will pay the amount of the tax or part of the tax as finally determined, the payment of which may have been deferred during the prosecution of the proceedings, together with any costs, fees, interest, penalties or other related liabilities. Lessor will not be required to join in any contest or proceedings unless the provisions of any law or regulations then in effect require that the Lessor participate in such proceedings. In the event Lessor does join in the proceedings, Lessor shall not be subjected to any liability for the payment of any costs or expenses in connection with any such contest or proceeding. Further, Lessee shall indemnify Lessor against and save Lessor harmless from any and all such costs and expenses.

7. Building Structure Insurance:

7.01 Lessor will at all times during the Term hereof maintain in effect the following policy or policies of insurance: (a) property insurance on the "Special Form" or equivalent form on a replacement cost basis against loss or damage to the building structure on the Premises in the amount of the full replacement cost of the building, (b) loss of rental income for not less than 12 months, and (c) commercial general liability insurance in amounts typically carried by lessors of similar buildings. Lessee shall have the responsibility to pay for all premiums for such insurance within the monthly Operating Expense Charge.

8. Additional Rent:

8.01 All taxes, charges, costs and expenses that Lessee assumes or agrees to pay hereunder, together with all interest and penalties that may accrue thereon in the event of the failure of the Lessee to comply with the terms and conditions of this Lease, other than base rent shall be deemed to be "additional rent" and, in the event of non-payment, Lessor shall have all the rights and remedies as herein provided for failure to pay rent. With regard to additional rent which is estimated in monthly payments, notwithstanding any particular increase or reconciliation notice times set forth elsewhere herein, Lessor's failure to timely notify Lessee of a change in the estimated monthly amounts or timely reconcile the estimated payments with actual expenses shall not alter or diminish Lessee's responsibilities therefor.

9. Interest On Past Due Rent And Additional Rent:

9.01 If Lessee shall fail to pay, within seven (7) days after the same is due, any Rent or additional rent, or any other amount or charges due from Lessee under this Lease, such unpaid amounts shall bear interest from the due date thereof to the date of payment by Lessee at eighteen (18%) percent per annum.

10. Late Charges:

10.01 At Lessor's sole and absolute discretion, Lessee agrees to pay Lessor a late charge of five (5%) percent of each payment of Rent or additional rent required to be paid by Lessee hereunder not received by Lessor within seven (7) days of the due date thereof. It is agreed by the parties hereto that said late charge shall be for reimbursement to Lessor for collection charges incurred as a result of the overdue Rent and/or additional rent. Such late charge shall be in addition to any interest payable by the Lessee as set forth in Section 9.01 above, resulting from Lessee's failure to pay any Rent or additional rent due hereunder. In the event any check,

bank draft, order for payment or negotiable instrument given to Lessor for any payment attributable to Lessee is not immediately collectable, Lessor shall be entitled to make an administrative charge to Lessee of Seventy-Five Dollars (\$75.00), or any amount provided by law whichever is greater. In addition, Lessor shall be reimbursed by Lessee for any costs incurred by Lessor as a result of said payment being dishonored.

11. Security Deposit:

11.01 Intentionally Deleted.

12. Public Utilities - Utility Charges:

12.01 Lessee shall pay all utility and other charges and expenses for any services provided to the Premises, including, without limitation, gas, pest control, water (building and lawn sprinkler), sewer, waste removal, electricity, telephone, high-speed internet, janitorial, security monitoring and any other utility services used on the Premises during the Term of this Lease. All accounts for such utility services shall be opened and maintained in the name of the Lessee. If any such charges are not paid when due, Lessor may pay the same, and any amounts so paid by Lessor shall thereupon become due to Lessor from Lessee as additional rent. Lessor shall not be liable in damages, or otherwise, for any failure or interruption of any utility service being furnished to the Premises.

13. Waste, Damage Maintenance And Repair:

13.01 Lessee, at its sole expense, shall keep the interior of the Premises in good working order, condition and repair and maintain the same and every part thereof, including, but not limited to, all of the plumbing, electrical and lighting facilities, fire sprinklers (inspection, repairs, monitoring and phone line charges), security equipment, HVAC systems and air conditioning units, including monthly filter changes, floors, interior walls, interior doors, windows and ceilings. Additionally, Lessee, at its sole expense, shall keep the exterior of the Premises in good working order, condition and repair and maintain the same and every part thereof, including, but not limited to, the driveway and parking areas, exterior lighting and landscape maintenance (mowing, trimming, sprinkler repair, fertilization, etc). All maintenance, repairs, replacements and renewals made by Lessee shall be of equal or better quality of materials and workmanship to that originally in existence, and shall be made only by a licensed and bonded contractor acceptable to Lessor. To ensure compliance with the obligations under this section, Lessor may at its option enter upon the Premises, following reasonable notice to Lessee (except in the event of an emergency in which case no notice of entry shall be required), and put the same in good order, condition and repair and the cost thereof shall become due and payable as additional rent by Lessee to Lessor upon demand.

13.02 Lessee shall keep the Premises free from Lessee's waste and debris. Further, Lessee shall not cause or permit any waste, damage or injury to the Premises. All waste, damage or injury to the Premises, or any part thereof, or to its fixtures, equipment or appurtenances caused by Lessee, its employees, agents, customers, guests or invitees, shall be repaired to Lessor's satisfaction by Lessee, at Lessee's sole cost and expense. Lessee shall also repair, at its sole cost and expense, all damage to the Premises caused by the installation or moving of Lessee's fixtures, furniture and/or equipment. All such repairs shall be of equal or better quality of materials and workmanship to that originally in existence, and shall be made only by a licensed and bonded contractor acceptable to Lessor. To ensure compliance with the obligations under this section, Lessor may at its option enter upon the Premises, following reasonable notice to Lessee (except in the event of an emergency in which case no notice of entry shall be required), and put the same in good order, condition and repair and the cost thereof shall become due and payable as additional rent by Lessee to Lessor upon demand.

13.03 Lessor shall keep the building structure, roof, sub-floor, exterior walls, exterior doors, gutters and down spouts in good repair. Lessor shall be obligated for costs of replacing HVAC systems, in the event a replacement is deemed necessary within the reasonable discretion of the Lessor. Lessor shall have no responsibility for any repairs to the Premises except as set forth in this sub-section. Lessor shall make repairs for which it is responsible in such a manner so as to minimize interference with the operation of Lessee's business and within a reasonable time after receiving notice from Lessee. If Lessor fails to undertake and complete repairs for which it is responsible, the failure of which materially and adversely affects the operation of Lessee's business, then thirty (30) days following Lessee's request for same (or such longer period as may be required to complete the repair if the same cannot be reasonably completed within the thirty (30) day time frame), Lessee may undertake to repair the same at Lessor's cost and expense. In conducting such work, Lessee shall (i) proceed in accordance with all Laws as well as the provisions of this Lease regarding Lessee made improvements and repairs, (ii) complete such repairs in a reasonable time and (iii) indemnify and hold Lessee and its lender(s), if any, harmless from any and all liability, damage and expense arising from injury to person or property arising out of or resulting from Lessee's exercise of such right. Lessor shall have thirty (30) days from receipt of Lessee's invoice(s) for such costs to make payment in full. In the event Lessor fails to so pay, Lessee may thereafter begin to offset such costs against up to 10% of each monthly installment of Rent due hereunder until the entire cost has been recovered.

14. Improvements, Additions And Alterations:

14.01 Lessee shall not begin any alterations, additions or improvements to the Premises or any part thereof, without the prior written consent of Lessor, which consent shall not be unreasonably withheld so long as the requested alterations do not affect the structure or main systems of the building located on the Premises. All alterations, additions or improvements made by Lessee to the premises shall become part of the Premises and shall become the sole property of Lessor without compensation to Lessee. All alterations, additions or improvements to the Premises made by Lessee during the Lease Term shall be in keeping with the quality and type of structures presently located on the Premises. Any alterations, additions or improvements shall be done in a good and workmanlike manner and performed only by a licensed and bonded contractor, to the reasonable satisfaction of Lessor, and in compliance with all Laws including, without limitation, all applicable building and zoning laws, ordinances, orders and requirements of all sovereign authorities and the appropriate departments, commissions, boards and officers thereof. The costs of any such alterations, additions or improvements to the Premises shall be paid by Lessee (except to the extent of the tenant improvement allowance of Section 5.01) in cash or its equivalent so that Lessor's fee simple title to the Premises shall at all times be free of liens for labor and materials supplied or claimed to have been supplied. Lessor reserves the right before approving any such alterations, additions or improvements to require Lessee to furnish reasonably satisfactory evidence of available funds with which to pay for the completion of such alterations, additions or improvements. Lessee hereby agrees to indemnify, defend and hold Lessor harmless from and against any and all costs and liabilities incurred by Lessor with respect to any alterations, additions or improvements to the Premises made by or on behalf of Lessee and against any and all construction, materialmen's, laborer's, or other statutory or common law liens arising out of or from such work by or on behalf of Lessee, or the cost thereof, which may be asserted, claimed or charged against all or any part of the Premises, or against the Lessor. Such indemnity obligation shall survive the Term, or any earlier termination, of this Lease. Lessee shall permit Lessor or his agents to enter upon the Premises with reasonable and appropriate advance notice during the period that alterations, additions, or improvements are being made on or to the Premises to inspect such alterations, additions or improvements and to determine whether the Lessee is complying with the provisions of this section. Notwithstanding the foregoing, Lessee shall have the right to make Minor Alterations (as hereinafter defined) to the Premises without obtaining Lessor's prior written consent. "Minor Alterations" shall mean minor alterations in the building located upon the Premises which (1) are not structural in nature, (2) do not affect the main building systems, and (3) are not visible from outside the building (provided, however, that any painting, wall covering installation, carpeting installation and removal of cabling and

lighting fixtures will not be deemed visible from outside the building for purposes of this paragraph and may be made without Lessor's consent.

15. Construction Liens:

15.01 Lessor's interest in the Premises shall not be subject to construction liens arising from Lessee's work or alterations and any repairs made by Lessee to the Premises. Lessee will not knowingly permit or suffer any lien attributable to Lessee or its agents or employees to attach to the Premises and nothing contained herein shall be deemed to imply any agreement of Lessor to subject Lessor's interest or estate to any construction lien or any other lien. If any construction lien is filed against the Premises as a result of alterations, installations, improvements or repairs made or claimed to have been made by Lessee or anyone holding any part of the Premises through or under Lessee, or any other work or act of any of the foregoing, Lessee shall discharge the same within twenty (20) days from Lessee's receipt of notice of the filing thereof. If Lessee fails to so discharge by payment, bond or court order any such construction lien, Lessor, at its option, in addition to all other rights or remedies herein provided, may pay or bond said lien or claim for the account of Lessee without inquiring into the validity thereof, and all sums so advanced by Lessor shall be paid by Lessee to Lessor as additional rent on demand, together with interest on all such amounts, at the rate of eighteen (18%) per annum. Pursuant to Florida Statutes, Section 713.10, notice is hereby given that Lessor shall not be liable for any labor or materials furnished or to be furnished to Lessee, and that no construction or other lien for any such labor or materials shall attach to or affect the reversionary or other estate or real or personal property interest of Lessor in and to the Premises. Lessee agrees, if requested by Lessor, to join with Lessor in the execution of a short form lease or memorandum of lease to be recorded in the Public Records of Seminole County, Florida, for the purposes of giving notice of this provision of this Lease.

16. Insurance:

16.01 Throughout the Term of this Lease, Lessee, at its sole cost and expense, shall obtain and maintain in full force and effect a commercial general public liability insurance policy with respect to the Premises, which insurance, shall be written with a carrier acceptable to the Lessor and with coverage limits of not less than One Million and No/100 Dollars (\$1,000,000.00) in respect of bodily injury or death to any one person, Two Million and No/100 Dollars (\$2,000,000.00) in respect to any one accident or occurrence, and One Million and No/100 Dollars (\$1,000,000.00) for property damage, and such protection shall continue at not less than the said limits until reasonably required to be changed by Lessor in writing by reason of changed economic conditions making such protection inadequate. The insurance policy shall name the Lessor as an additional insured and shall provide that the policy may not be canceled or modified by the carrier without thirty (30) days' prior written notice to the Lessor. To the extent obtainable, the insurance policy shall contain a clause or an endorsement to the effect that no act or negligence of Lessee, or anyone acting for Lessee, or any sublessee, or occupant of the Premises, which might otherwise result in a forfeiture of such insurance or any part thereof, shall in anyway affect the validity or enforceability of such insurance insofar as Lessor. Lessee shall provide the Lessor with a certificate of insurance evidencing its compliance with this paragraph on or before the date of the execution of this Lease. Renewals of the policy or policies referred to in this paragraph shall be delivered to Lessor at least twenty (20) days prior to the expiration of any such policy, accompanied by evidence reasonably satisfactory to Lessor of payment of the premiums therefore.

16.02 Throughout the Term of this Lease, Lessee shall also maintain such other insurance in such amounts as may from time to time be reasonably required by Lessor against other insurable hazards which at the time are commonly insured against in the case of demolition, construction and alterations of buildings and/or in the case of property similarly situated, due regard being or to be given to the height or type of building, its location, construction, use and occupancy.

16.03 Lessee shall maintain worker's compensation insurance to comply with the laws of the State of Florida.

16.04 If Lessee shall fail to procure and maintain the insurance required hereunder, Lessor may, at its option, pay the same, and the amount or amounts of money so paid, together with interest on all such amounts at the rate of eighteen percent (18%) percent per annum, shall be repaid by Lessee to Lessor, upon the demand of Lessor, and the payment thereof may be collected or enforced by Lessor in the same manner as though said amount were an installment of rent specifically required by the terms of this Lease to be paid by Lessee unto Lessor, upon the day when the Lessor demands reimbursement therefore from the Lessee; but the election of Lessor to pay such premiums shall not waive the default thus committed by Lessee.

16.05 Lessee will not do or permit anything to be done on the Premises, or bring or keep anything therein which shall in any way increase the rate of fire or other insurance on the Premises, or on the property kept therein, or conflict with the fire or other insurance on the Premises, or on the property kept therein, or conflict with any fire laws or regulations, or with any insurance policy upon said Premises, or any part thereof, or with any statutes, rules or regulations enacted or established by any appropriate governmental authority.

16.06 Lessee has the duty and responsibility to purchase casualty insurance covering Lessee's property and any losses by reason of fire, wind, storm, water, theft or other casualty and to have the Lessor named as an additional insured in connection therewith. LESSOR SHALL NOT BE LIABLE FOR LOSS OR DAMAGE TO THE CONTENTS OF THE PREMISES FROM ANY CAUSE WHATSOEVER. LESSOR DOES NOT CARRY INSURANCE TO COVER ANY LOSS OR DAMAGE TO THE CONTENTS OF THE PREMISES FROM ANY CAUSE WHATSOEVER.

16.07 Lessee hereby waives its rights of recovery against Lessor and Lessor's officers, directors, shareholders, partners, joint venturers, employees, agents, customers, invitees, or business visitors of either party, for any loss arising from any cause covered or that could be covered by fire, extended coverage, all risks or other insurance. Lessee will cause from time to time its insurers to issue appropriate waivers of subrogation rights endorsements to all insurance policies carried in connection with the building, the Premises, the contents of either and Lessee's use of same.

17. Casualty Damage:

17.01 If the Premises shall be partially destroyed by fire or other casualty, the damages may, at the sole option of Lessor, be repaired by and at the expense of Lessor or an appropriate insurer and the rent until such repair is made shall be apportioned according to the part of the Premises which is useable by Lessee for its particular use. No penalty shall accrue for reasonable delay which may arise by reason of adjustments of insurance on the part of Lessor or for reasonable delay on account of "labor troubles" or any other cause beyond Lessor's control. If Lessor shall decide not to restore or not to rebuild the Premises, or if the Premises are totally damaged or are rendered wholly untenable by fire or other casualty, or if the Premises shall be so damaged that Lessor shall decide to demolish it or to rebuild it, then Lessor may, within ninety (90) days after such fire or other casualty, give Lessee a notice in writing of such decision and thereupon the terms of this Lease shall expire and terminate effective as of the date of the casualty and Lessee shall immediately vacate the Premises and surrender the same to Lessor, and except as may otherwise be provided herein, the obligations of the parties hereto shall cease and terminate. Additionally, if the Premises are totally damaged or are rendered wholly untenable by fire or other casualty, then Lessee may, within ninety (90) days after such fire or other casualty, give Lessor a fifteen (15) day notice in writing of Lessee's decision to terminate the Lease and thereupon the terms of this Lease shall expire and terminate effective fifteen (15) days from the date of such notice and Lessee shall vacate the Premises by such date and surrender the same to Lessor, and except as may otherwise be provided herein, the obligations of the parties hereto shall cease and terminate.

18. Condemnation:

18.01 The parties hereto agree that if the Premises, or any such portion thereof as will make the Premises unusable for the purpose herein leased as determined by Lessor, are taken or condemned by competent authority for public or quasi-public use, then this Lease shall terminate from the date of taking, and except as may otherwise be provided herein, the obligations of the parties hereto shall cease and terminate. If the Lease continues after a partial taking, the rent shall abate proportionately as to the part taken. All compensation awarded for such taking of the Premises, the improvements located thereon, the fee, and the leasehold shall belong to and be the property of Lessor. Lessee shall not be entitled to any damages for the unexpired portion of the Term of this Lease, or injury to its leasehold interest, except that Lessee may seek the award of business damages, so long as such effort of Lessee does not diminish the compensation paid to Lessor.

19. Indemnification:

19.01 Lessee hereby indemnifies Lessor and saves it harmless from and against any and all claims, actions, damages, liability and expense in connection with loss of life, personal injury and/or damage to property arising from or out of any occurrence in, upon or at the Premises, or the occupancy or use by Lessee of the Premises or any part thereof, or occasioned wholly or in part by any negligent or intentional, act or omission of Lessee, its agents, contractors, employees, servants, sub-lessee or concessionaires (including, without limitation, any failure by Lessee to keep, perform and observe each and every one of the covenants, conditions and agreements contained in this Lease to be kept, performed and observed by Lessee), unless caused by the willful act or gross negligence of Lessor, its agents and employees. This indemnity and hold harmless agreement shall include indemnity against all costs, expenses and liabilities, including attorney's fees, incurred by Lessor in connection with any such claim or action or any trial, appellate or bankruptcy proceeding relative thereto. In case Lessor shall, without fault on its part, be made a party to any such action or proceeding, then Lessee shall protect and hold Lessor harmless and shall pay all costs, expenses, and reasonable attorney's fees incurred or paid by Lessor in connection with such litigation and Lessee, upon written notice from Lessor, shall defend such action or proceeding by counsel approved in writing by Lessor, which approval shall not be unreasonably withheld or delayed. The provisions of this section shall survive the Term and any earlier termination of this Lease.

20. Exemption Of Lessor For Damage:

20.01 Lessor shall not be liable for injury or damage which may be sustained by the employees, invitees or customers of Lessee or any other person in or about the Premises or for injury or damage to any goods, wares, merchandise or property of Lessee, its employees, invitees or customers or any other person in or about the Premises, whether or not caused or resulting from fire, steam, electricity, gas, water or rain, which may leak or flow from or into any part of the Premises, or from the breakage, leakage, obstruction or other defects in the pipes, sprinklers, wires, appliances, plumbing, air conditioning or lighting fixtures of the same, whether the said damage or injury results from conditions arising upon the Premises, or from other sources, except to the extent the same are caused directly by the willful act or gross negligence of Lessor, its agents or employees.

21. Surrender Of Possession:

21.01 Lessee shall peaceably and quietly surrender the Premises upon the last day of the Term of this Lease, or upon the date of termination if prior to that, and shall surrender the Premises in as good a condition as the Premises was at the beginning of the Lease, except for reasonable wear and tear and except as expressly

provided herein. Any property belonging to the Lessee not removed upon the termination of this Lease, if Lessor shall so elect, shall be deemed abandoned and become the property of Lessor without any payment or offset therefor. Lessor may remove such property belonging to Lessee from the Premises and store them at the risk and expense of Lessee if Lessor shall so elect. Lessee shall repair and restore all damage to the Premises caused by the removal of any property belonging to Lessee and any other equipment, trade fixtures, and personal property belonging to Lessee. Without limitation of other damages, Lessee shall be liable to Lessor for any cost, damage or expense incurred by Lessor as a result of Lessee's failure to vacate the Premises under these terms and conditions.

22. Holding Over:

22.01 Lessee agrees that if Lessee does not surrender the Premises to Lessor at the end of the Term (as extended if the Option Term is properly elected), or upon any cancellation of the Term of this Lease, without prior written consent of Lessor, such holdover tenancy shall be a tenancy at will, and during any holdover period, Lessee shall pay to Lessor base rent equal to one hundred fifty percent (150%) of the base rent specified in this Lease for the immediately preceding lease year, without necessity of additional demand therefor. The acceptance of such rent shall not be deemed to be a consent to such continued occupancy nor shall it be deemed a waiver of any right of the Lessor as set forth herein, at law or in equity. Should a tenancy at will be created under the provisions of this paragraph, the tenancy may subsequently be terminated by either party hereto giving fifteen (15) days' written notice of the intention to terminate the tenancy to the other party to this Lease. In addition, if such failure to surrender the Premises at the end of the Lease Term, or following any termination of the Term, interferes with Lessor's ability to deliver the Premises to a succeeding tenant pursuant to a new lease agreement executed by and between Lessor and such tenant, so long as Lessor has delivered Lessee written notice of the new lease and the date by which the Premises must be surrendered to Lessor in order to comply with the terms of such new lease (the "Absolute Surrender Date"), which notice must be received by Lessee thirty (30) days prior to the Absolute Surrender Date, Lessee shall defend, indemnify and hold Lessor harmless from and against all losses or damages resulting from such failure accruing from and after the Absolute Surrender Date including, without limitation, any losses suffered by Lessor such as lost rents as well as any damages asserted against Lessor by any succeeding tenant founded upon such failure to timely surrender the Premises. This provision does not give Lessee any right to hold-over at the expiration of the Term of this Lease, and all other terms and conditions of this Lease shall remain in force during any tenancy at will created by the holding over by Lessee.

23. Covenants Of Lessee:

23.01 To induce Lessor to execute this Lease, and in consideration thereof, Lessee covenants and agrees as follows:

- (a) Lessee agrees to give to Lessor prompt written notice of any accident, fire or damage occurring in, on or to the Premises.
- (b) Lessee agrees that all loading and unloading of goods shall be done only in the areas and through such entrances as may be designated for such purposes by Lessor.
- (c) Lessee agrees to keep the outside areas immediately adjoining the Premises clear and not to burn, place or permit any rubbish, obstruction or merchandise in such areas.
- (d) Lessee shall install, maintain and keep current, at its expense, all fire extinguishers and other safety equipment as shall be required by applicable law, ordinance, regulation, or fire and extended coverage insurance underwriting compliance.

(e) Lessee shall not use or operate any machinery that, in Lessor's opinion, is harmful to the Premises or disturbing to others; nor shall Lessee use any loud speakers, televisions, radios, or other devices in a manner so as to disturb persons outside of the Premises; nor display merchandise on the exterior of the Premises either for sale or for promotional purposes, without obtaining the prior written consent of Lessor.

(f) Lessee shall not conduct any auction, fire, bankruptcy, selling-out, or going-out-of-business sale on or about the Premises.

(g) Lessee shall notify Lessor of the death of any surety or guarantor, if any, of this Lease on or before the date of the first publication of the Notice of Administration of the estate of the deceased surety or guarantor.

(h) Lessee shall not commit or suffer to be committed any waste upon the Premises or any nuisance or other act or thing which may disturb the quiet enjoyment of any person outside the boundaries of the Premises.

(i) Lessee agrees all mechanical apparatus shall be kept free from vibrations and noise which may be transmitted beyond the Premises.

(j) Lessee shall not do or suffer to be done any act, manner or thing objectionable to the fire insurance companies whereby the fire insurance or any other insurance now in force or hereafter to be placed on the Premises or any part thereof, shall become void or suspended. Upon the breach of this covenant, in addition to all other remedies of Lessor and not as a limitation thereof, Lessee agrees to pay to Lessor as additional rent any and all increase or increases of premiums on insurance carried by Lessor on the Premises.

(k) Lessee acknowledges that the Premises is subject to certain covenants, conditions and restrictions recorded at O.R. Book 1986, Page 1410, Public Records of Seminole County, Florida, as supplemented and amended ("Restrictive Covenants"). Lessee agrees to abide by such Restrictive Covenants, as supplemented and amended. Lessor represents and warrants to Lessee that Lessor has no knowledge of any violations of or non-compliance with the Restrictive Covenants occurring from and after the date of that certain Estoppel Certificate executed by Technology Park Owners' Association, Inc. dated March 29, 2007, a copy of which has been provided to Lessee.

24. Event Of Default And Remedies:

24.01 Each of the following events shall constitute an event of default or breach ("Event of Default") of this Lease by Lessee:

(a) The filing of a voluntary petition by Lessee, or any sureties or guarantors of this Lease, for adjudication as a bankrupt or insolvent, or for its reorganization or for the appointment of a receiver or trustee of its property; or an assignment by Lessee or any sureties or guarantors of this Lease for the benefit of creditors; or

(b) The filing of an involuntary petition against Lessee, or any sureties or guarantors of this Lease, seeking any reorganization, liquidation, dissolution or similar relief under any present or future federal, state or other law or regulation relating to bankruptcy, insolvency or other relief of debtors, or the appointment of any trustee, receiver or liquidator of Lessee, or any sureties or guarantors of this Lease, unless such petition or appointment shall be dismissed within thirty (30) days after such filing, but in any event prior to the entry of an order, judgment or decree approving such petition; or

(c) If Lessee shall fail to pay Lessor any Rent, additional rent or other sums due hereunder when said amount shall become due and shall not make the payment within seven (7) days after the date Lessor has delivered written notice to Lessee that said Rent and/or additional rent or other sum shall be due; however, an Event of Default shall occur hereunder without any obligation of Lessor to give any notice if Lessee fails to pay Rent when due and, during the 12 month interval preceding such failure, Lessor has given Lessee written notice of failure to pay Rent on one or more occasions; or

(d) If Lessee shall fail to perform or defaults in the performance of any of the conditions of this Lease other than the nonpayment of Rent or any other monetary obligation and if the nonperformance or default shall continue for a period of thirty (30) days after written notice thereof by Lessor to Lessee or, if the nature of Lessee's cure requires more than thirty (30) days, Lessee shall be permitted to commence the cure within such thirty (30) days and diligently prosecute such cure to completion; or

(e) If Lessee shall vacate or abandon the premises (Lessee shall be deemed to have abandoned the Premises if Rent and/or any other monetary obligation due under this Lease is not currently paid and Lessee is absent from the Premises for a period of fifteen (15) consecutive days); or

(f) If this Lease or the estate of Lessee hereunder shall be transferred to or shall pass to or devolve on any other person or party, except in the manner herein permitted; or

(g) If Lessee is a corporation which is not validly existing and in good standing and good standing is not restored within ten (10) business days after receipt of written notice from Lessor; or

(h) If Lessee is a partnership which is dissolved or liquidated.

24.02 If an Event of Default shall occur, Lessor may without prejudice to its other rights hereunder, avail itself of any right available to Lessor under the law or this Lease, including, without limitation, do any one or more of the following:

(a) Terminate this Lease and re-enter and take possession of the Premises without prejudice to any financial liability of Lessee;

(b) Recover possession of the Premises (with or without terminating the Lease, at Lessor's option) in a manner prescribed by any statute relating to summary process, and any demand for rent, re-entry for condition broken, and any and all notices to quit, including, without limitation, the notice required by the provisions of Section 83.20, Florida Statutes, or any similar statutes, or other formalities of any nature, to which Lessee may be entitled, are hereby specifically waived;

(c) Bring suit for the breach which has occurred without affecting the obligations of the parties to perform the balance of the Lease;

(d) Declare the entire Rent for the balance of the Term of the Lease due and payable; and

(e) Re-let the Premises or any part thereof without thereby avoiding or terminating the Lease to any person, firm or corporation other than Lessee for such rent, for such time, and upon such terms as Lessor in Lessor's sole discretion shall determine. In any such case, Lessor may make repairs in or to the Premises, and redecorate the same to the extent deemed by Lessor necessary or desirable, and Lessee shall, upon demand, pay the cost thereof together with Lessor's expenses of re-letting including, without limitation, any brokerage commission. If the consideration collected by Lessor upon any such re-letting for Lessee's

account is not sufficient to pay the full amount of unpaid rent reserved in this Lease, together with the cost of repairs, alterations, additions, redecorating, and Lessor's expenses, Lessee shall pay to Lessor the amount of each deficiency each month upon demand.

24.03 No re-entry or taking possession of the Premises by Lessor shall be construed as an election on Lessor's part to terminate this Lease unless a written notice of such intention be given by Lessor to Lessee or unless the termination thereof be decreed by a court of competent jurisdiction.

24.04 The failure of Lessor to re-let the Premises or any part thereof after recovery of possession shall not release or affect Lessee's liability for damages. Lessor shall in no event be liable in any way whatsoever for failure to re-let the Premises, or in the event that the Premises are re-let, for failure to collect the rent under such re-letting.

24.05 All of the damages which are specified in this Lease are in addition to all other damages and costs to which Lessor may be entitled under the laws of the State of Florida.

24.06 After an Event of Default, the acceptance of rent (or any portion thereof) or failure to re-enter by Lessor shall not be held to be a waiver of its rights to terminate this Lease, and Lessor may re-enter and take possession of the Premises as if no rent had been accepted after such default.

24.07 No right or remedy hereunder shall be exclusive of any other right or remedy, but shall be cumulative and in addition to any other right or remedy hereunder or now or hereafter existing. Failure to insist upon the strict performance of any provision hereof or to exercise any option, right, power or remedy contained herein shall not constitute a waiver or relinquishment thereof for the future.

24.08 Lessor shall not be deemed to be in default in the performance of any obligation required to be performed by Lessor hereunder unless and until it has failed to perform such obligation within thirty (30) days after receipt of written notice thereof from Lessee; provided, however, that if the nature of Lessor's obligations is such that more than thirty (30) days are required for its performance, then Lessor shall not be deemed to be in default if it shall commence such performance within such thirty (30) day period and thereafter diligently prosecute the same to completion.

25. Assignment And Subletting:

25.01 Lessee covenants and agrees not to encumber or mortgage Lessee's leasehold interest hereunder nor assign this Lease or sublet all or any part of the Premises without the prior written consent of Lessor, which consent will not be unreasonably withheld. If Lessor consents to an assignment or subletting, the assignee or sublessee shall first be obligated to assume, in writing, all of the obligations of Lessee under this Lease and Lessee shall, for the full term of this Lease, continue to be jointly and severally liable with such assignee or sublessee for the payment of the Rent, additional rent, any other sums due by Lessee under this Lease and the performance of all obligations required by Lessee under this Lease. However, in the event the approved assignee is of greater financial standing than Lessee, as determined within the reasonable discretion of Lessor, Lessee may seek to be released from its continuing, joint obligation. Such request shall be made by Lessee in writing no earlier than one (1) year following the date of assignment and will only be permitted if no uncured defaults have occurred and are outstanding under the Lease from the date of the assignment to the date of Lessee's request. In no event shall Lessee assign or sublet the Premises for any terms, conditions and covenants other than those contained herein. In no event shall this Lease be assigned or be assignable by operation of law or by voluntary or involuntary bankruptcy proceedings or otherwise, and in no event shall this Lease, or any rights or privileges hereunder, be an asset of Lessee under bankruptcy, insolvency or reorganization proceedings. Should Lessor consent to any assignment or sublease, any economic benefit that is derived shall be for the account of the Lessor.

26. Access To Premises:

26.01 Lessor and Lessor's representatives shall have the right to enter upon the Premises following reasonable notice to Lessee (except in the event of an emergency in which case no notice of entry shall be required) for the purpose of inspecting the same or for making repairs, additions or alterations or for the purpose of exhibiting the same to prospective tenants, purchasers, mortgagors or others. Lessee shall not cause the Premises to be locked or otherwise secured in such a manner as to prevent Lessor or Lessor's representatives from inspecting the Premises. Prospective purchasers, tenants or mortgagees authorized by Lessor may inspect the Premises during reasonable hours at any time.

27. Subordination:

27.01 Lessee agrees to subordinate its interest in this Lease to any mortgage or deed of trust encumbering the Premises and held by an institutional mortgagee by the execution of a Subordination, Non-Disturbance and Attornment Agreement ("SNDA"). The SNDA must be tendered to Lessee in a commercially reasonable, generally accepted form. Lessee agrees to execute and deliver the SNDA within ten business (10) days of the request for same from Lessor. Such SNDA shall provide that the Lease will remain in effect and the mortgagee will recognize the Lessee as a tenant so long as the Lessee is not in default under the lease. If Lessee fails to execute the SNDA within the ten business (10) day time frame set forth herein, Lessee's interest shall be deemed subject and subordinate to the lien of such mortgage or deed of trust.

28. Signs:

28.01 Lessee shall not place or suffer to be placed or maintained on any exterior door, wall or window of the Premises, any sign, awning or canopy, or advertising matter or other thing of any kind, and will not place or maintain any decoration, lettering or advertising matter on the glass of any window, exterior door or wall of the Premises without first obtaining Lessor's written approval or consent. Lessee further agrees to maintain said sign, awning, canopy, decoration, lettering, advertising matter or other thing as may be approved in writing by Lessor in good condition and repair at all times.

29. Right Of Lessor To Display Signs:

29.01 Lessor reserves the right to display a "For Sale" sign at any time on the Premises. Additionally, Lessor reserves the right to display a "For Rent" sign at any time within six (6) months prior to the expiration of this Lease, or after default of Lessee, or following delivery of notice by either party of their intention to terminate this Lease. All of said signs may be placed upon such part of the Premises as Lessor shall require.

30. Removal And Restoration By Lessee:

30.01 All alterations, decorations, additions, and improvements on or in the Premises as of the date of this Lease, and that may be erected or installed during the Lease Term, shall become part of the Premises and shall become the sole property of Lessor, except that all moveable trade fixtures installed by Lessee shall be and remain the property of Lessee; provided that such trade fixtures can be removed without damaging the Premises. Any damage caused by Lessee as a result of removal of its trade fixtures shall be promptly repaired by Lessee at its expense.

31. Personal Property:

31.01 All personal property of the Lessee in the Premises shall be maintained at the sole risk of the Lessee. The Lessor shall not be liable for any accident to or damage to property of Lessee resulting from the use or operation of the heating, cooling, electrical or plumbing apparatus. Lessor shall not in any event, be liable for damages to property resulting from water, steam or other causes. Lessee hereby expressly releases and agrees to hold Lessor harmless from, any liability incurred or claimed by reason of damage to Lessee's property. Lessor shall not be liable for damages, nor shall this Lease be affected, for conditions arising or resulting, and which may affect the Premises, due to construction on contiguous properties.

32. No Waiver:

32.01 No delay or omission of the exercise of any right by either party hereto shall impair any such right or shall be construed as a waiver of any default or as an acquiescence thereto. One or more waivers of any violation or breach or failure to comply with any of the covenants, terms, provisions or conditions of this Lease by either party shall not be construed by the other party as a waiver of any subsequent violation, breach or failure to comply with the same or any other covenant, term, provision, or condition contained in this Lease. No requirements whatsoever of this Lease shall be deemed waived or varied because of either party's failure or delay in exercising its rights resulting from any default, and Lessor's acceptance of any payment from Lessee with knowledge of any default shall not constitute a waiver of Lessor's right with respect to such default, nor of any subsequent default. All remedies provided for herein shall be construed as cumulative and shall be in addition to every other remedy otherwise available to Lessor.

33. Exculpation:

33.01 Lessee agrees that Lessee shall look solely to Lessor's interest in the Premises and Lessor's personal property used in connection therewith for the satisfaction of any claim, judgment or decree requiring the payment of money by Lessor to Lessee based upon any default hereunder and no other property or assets of Lessor, its heirs, successors and assigns, shall be subject to levy, execution or other enforcement procedure for the satisfaction of any claim, judgment, injunction or decree of Lessee against Lessor.

34. Brokers:

34.01 Lessor and Lessee each warrant and represent to the other that neither has employed or dealt with any broker, agent or leasing consultant in connection with this Lease. Lessor and Lessee covenant and agree, each to the other, to indemnify and hold the other harmless from and against any and all liability, costs, claims, demands, damages, actions, causes of action, suits and expenses (including, but not limited to, attorney's fees and costs and disbursements of litigation) the other party may incur, arising out of or in any manner related to any claim or action by any other broker, agent or leasing consultant claiming to have dealt with the indemnifying party, or claiming to be due a commission or other compensation from the indemnifying party with respect to this Lease.

35. Transfer Of Lessor's Interest:

35.01 In the event of any transfer or transfers of Lessor's interest in the Premises, upon the transferee assuming liability therefore, Lessor shall be automatically relieved of any and all obligations and liabilities on the part of Lessor accruing from and after the date of such transfer.

36. Rules And Regulations:

36.01 Lessee shall conduct its business in the Premises during the regular customary days and hours for such type of business in the city and trade area in which the Premises is located, with due allowance for vacations, holiday, and deaths or illness of Lessee's officers, directors, and shareholders and their family members.

36.02 Lessor reserves the right from time to time to adopt, promulgate, amend or supplement rules and regulations applicable to the Premises. Notice of such rules and regulations, and any amendments and supplements, shall be given to Lessee, and Lessee agrees thereupon to comply with and observe all such rules and regulations, and amendments and supplements thereto. However, such newly adopted, promulgated, amended or supplemental rules and regulations shall not change the terms of this Lease nor substantially impede the continuing operation of Lessee's business.

37. Successor In Interest:

37.01 All provisions herein contained shall bind and inure to the benefit of the respective parties hereto, their heirs, personal representatives, successors and assigns. In the event Lessor or any successor-owner of the Property shall convey or otherwise dispose of the Premises, all liabilities and obligations of Lessor or any successor-owner as Lessor to Lessee under this Lease shall terminate upon such conveyance or disposal and the giving of written notice thereof to Lessee.

38. Notices:

38.01 Wherever in this Lease it shall be required or permitted that notice or demand be given or served by either party to this Lease to or on the other, such notice or demand shall not be deemed to have been duly given or served unless in writing and either personally delivered, delivered by Federal Express or other courier service, delivered by facsimile transmission with proof of transmittal or deposited in the United States Mail, postage prepaid, return receipt requested. If given by regular mail, the notice shall be deemed to have been given within a required time if received, evidenced by the return receipt, within the time limit. For the purpose of calculating time limits which run from the giving of a particular notice, the time shall be calculated from actual receipt of the notice. Notices shall be addressed as follows:

TO THE LESSOR AT: Emma Investments, LLC
 Post Office Box 941618
 Maitland, Florida 32794
 (407) 629-9192 (fax)

TO THE LESSEE AT: Faro Technologies, Inc.
 250 Technology Park
 Lake Mary, Florida 32746
 (407) 562-5287 (fax)

Such addresses may be changed from time to time by either party by serving notices as above provided, but Lessee shall at all times have a physical street address within the continental United States of America as one of the addresses to which notices may be delivered.

39. Entire Agreement:

39.01 This Lease contains the entire and only agreement between the parties concerning the Premises and no prior oral or written statement or representations, if any, of any party hereto or any representative of a party hereto, not contained in this instrument, shall have any force or effect. This Lease shall not be modified in any way except by a written document executed by Lessor and Lessee.

40. Authority To Execute:

40.01 If Lessee is a corporation (or partnership), each individual executing this Lease on behalf of said corporation (or partnership) represents and warrants that he/she is duly authorized to execute and deliver this Lease on behalf of said corporation (or partnership) in accordance with a duly adopted resolution of the Board of Directors of said corporation or in accordance with the bylaws of said corporation (or under the pertinent partnership agreements), that any required consents or approvals of third parties have been obtained, and that this Lease is binding upon said corporation (or partnership) in accordance with its terms. Lessor represents and warrants that all necessary approval action has been undertaken by the entity as necessary to approve its representative's execution hereof and that it is binding upon said entity in accordance with its terms.

41. Lease Not Recordable:

41.01 At the request of either party, Lessor and Lessee shall promptly execute, acknowledge and deliver a memorandum or short form of lease sufficient for recording. In no event shall this Lease be recorded and if Lessee records this Lease in violation of the terms hereof, in addition to any other remedy available to Lessor upon Lessee's default, Lessor shall have the option to terminate this Lease by recording a notice to such effect. If a memorandum or short form of lease is recorded, on the termination of this Lease, Lessee shall execute, acknowledge and deliver to Lessor an instrument in writing releasing and quit-claiming to Lessor all right, title and interest of Lessee in and to the premises by reason of this Lease or otherwise.

42. Radon Gas:

42.01 Radon gas is a naturally occurring radioactive gas that when it has accumulated in a building in sufficient quantities, may present health risks to persons who are exposed to it over time. Levels of radon testing may be obtained from your county public health unit.

43. Time Of Essence:

43.01 It is understood and agreed between the parties hereto that time is of the essence as to all of the terms, provisions, covenants and conditions of this Lease.

44. Attorneys' Fees:

44.01 The prevailing party in any litigation arising out of this Lease, including any appellate proceedings, insolvency proceedings and bankruptcy proceedings, shall be entitled to the award of its reasonable attorney's fees and costs.

45. Severability:

45.01 If any provision of this Lease or the application thereof to any person or circumstance shall to any extent be invalid or unenforceable, the remainder of this Lease, or the application of such provisions to persons or circumstances other than those as to which it is invalid or unenforceable, shall not be affected thereby and each provision of this Lease shall be valid and enforceable to the fullest extent permitted by law.

46. Applicable Law:

46.01 This Lease shall be construed under the laws of the State of Florida and the venue of any action to enforce rights hereunder shall be Seminole County, Florida.

47. Accord And Satisfaction:

47.01 Lessor is entitled to accept, receive and cash or deposit any payment made by Lessee for any reason or purpose, or in any amount whatsoever and apply the same at Lessor's option to any obligation of Lessee and the same shall not constitute payment of any amount owed except that to which Lessor has applied the same. No endorsement or statement on any check or letter of Lessee shall be deemed an accord and satisfaction or otherwise recognized for any purpose whatsoever. The acceptance of any such check or payment shall be without prejudice to Lessor's right to recover any and all amounts owed by Lessee hereunder and Lessor's right to pursue any other available remedy and shall not be deemed to constitute a waiver of any of Lessor's rights hereunder.

48. Lessor's Right To Satisfy Lessee's Obligations:

48.01 If Lessee fails to observe or perform any term or condition of this Lease within the grace period, if any, applicable thereto, then Lessor may immediately or at any time thereafter perform the same for the account of Lessee. If Lessor makes any expenditure or incurs any obligation for the payment of money in connection with such performance for Lessee's account (including reasonable attorneys' fees and costs in instituting, prosecuting and/or defending any action or proceeding through appeal), the sums paid or obligations incurred, together with interest at the highest rate allowable by law, shall be paid by Lessee to Lessor upon demand. In the event Lessee, in the performance or non-performance of any term or condition of this Lease, should cause an emergency situation to occur or arise upon the Premises, Lessor will have all rights set forth in this paragraph immediately without the necessity of providing Lessee any advance notice.

49. Estoppel Statement:

49.01 Upon the request of either party at anytime and from time to time, Lessor and Lessee agree to execute and deliver to the other within ten (10) days after receipt of such request, a written instrument, duly executed, addressed to either Lessor or Lessee, as may be applicable, and/or to any person designated by either Lessor or Lessee, at their sole cost and expense, (a) ratifying this Lease; (b) stating the commencement and termination dates of this Lease and (c) certifying (1) that this Lease is in full force and effect and has not been assigned, modified, supplemented or amended except by such writing as shall be stated, (2) that all conditions under this Lease to be performed by either the Lessor or Lessee have been satisfied (stating exceptions, if any), (3) no defenses or offsets against the enforcement of this Lease by Lessor or Lessee exist (or, if any, stating those claimed), (4) advance rent, if any, paid by Lessee, (5) the date to which rent has been paid, (6) the amount of security deposited with Lessor, and such other information as either party may reasonably require. Persons receiving such statements shall be entitled to rely upon them.

50. Captions And Headings:

50.01 The captions and headings of this Lease are inserted only as a matter of convenience and in no way define, limit, construe, or describe the scope or intent of such paragraphs of this Lease or in any way affect this Lease.

51. Hazardous Substances:

51.01 Lessee shall not, nor shall Lessee permit its agents, contractors, employees, licensees and invitees to discharge, release, dump, spill or store on the Premises any Hazardous Materials (as hereinafter defined) in violation of any of the Environmental Laws (as hereinafter defined).

51.02 As used herein "Environmental Laws" means, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, 42 U.S.C. §9601 et seq., the Solid Waste Disposal Act, as amended, 42 U.S.C. §6901 et seq., the Federal Water Pollution Control Act, as amended, 33 U.S.C. §1251 et seq., the Toxic Substances Control Act of 1976, 15 U.S.C. §2601 et seq., the Emergency Planning and Community Right-to-Know Act of 1986, 42 U.S.C. §11001 et seq., the Clean Air Act of 1966, as amended, 42 U.S.C. §7401 et seq., the National Environmental Policy Act of 1969, 42 U.S.C. §4321, the Rivers and Harbors Appropriations Act of 1899, 33 U.S.C. §401 et seq., the Endangered Species Act of 1973, as amended, 16 U.S.C. §1531 et seq., the Occupational Safety and Health Act of 1970, as amended, 29 U.S.C. §651 et seq., and the Safe Drinking Water Act of 1974, as amended, 42 U.S.C. §300f et seq., and the regulations and guidelines promulgated or published thereunder as any of the foregoing may be amended, and any other applicable present or future federal, state or local laws, statutes, codes, ordinances, rules, regulations, decrees, orders and other such requirements.

51.03 As used herein "Hazardous Materials" shall mean any hazardous or toxic substances, materials or wastes, including, but not limited to, those substances, materials and wastes listed in the United States Department of Transportation Hazardous Materials Table (49 C.F.R. §172.101 and any amendments thereto) or by the Environmental Protection Agency as hazardous substances (40 C.F.R. Part 302 and any amendments thereto), or such substances, materials, and wastes which are or become regulated under any applicable federal, state or local law including, without limitation, any material, waste or substance which is: (i) asbestos; (ii) polychlorinated biphenyls; or (iii) defined as a "hazardous waste," "extremely hazardous waste," "restricted hazardous waste," "hazardous substance," "hazardous material," "regulated substance," or other similar term under the Environmental Laws, but excluding Hazardous Materials contained in products used by Lessee in de minimis quantities for ordinary cleaning and office purposes.

51.04 Lessee, its agents, employees, contractors or invitees, shall not use the Premises in any manner that violates any applicable Environmental Laws, including, but not limited to, any such law, regulation or ordinance pertaining to air and water quality, the handling, transportation, storage, treatment, usage or disposal of Hazardous Materials, air emissions and other environmental matters. Lessee shall not cause or permit the Premises to be used for the generation, handling, storage, transportation, disposal or release of any Hazardous Materials, except as exempted or properly permitted under applicable Environmental Laws.

51.05 Lessee represents and warrants to Lessor that:

(a) Lessee is not in violation of or subject to any existing, pending or threatened investigation by any governmental authority under any applicable Environmental Laws, including, but not limited to, those pertaining to air and water quality, the handling, transportation, storage, treatment, usage or disposal of Hazardous Materials, air emissions and other environmental matters.

(b) The activities to be conducted upon the Premises by Lessee shall not pose any significant hazard to human health or the environment or violate any Environmental Laws.

(c) Lessee's intended use of the Premises will not result in the disposal, release or discharge of any Hazardous Materials on, under or to the Premises, except as permitted under any Environmental Laws.

(d) Lessee does not and will not use any Hazardous Materials on the Premises, except as permitted under any Environmental Laws.

51.06 Lessee agrees to indemnify Lessor and hold Lessor and its employees, partners, heirs, personal representatives, successors and assigns harmless from and against any and all claims, losses, damages (including all foreseeable and unforeseeable consequential damages), liabilities, fines, penalties, charges, interest, administrative or judicial proceedings and orders, judgments, remedial action requirements, enforcement actions of any kind, and all costs and expenses incurred in connection therewith (including without limitation attorney's fees and expenses), directly or indirectly resulting in whole or in part from Lessee's violation of any Environmental Laws applicable to the Premises or any activity conducted thereon, or from any present or future use, generation, handling, storage, transportation, disposal or release by Lessee of Hazardous Materials at or in connection with the Premises, or any decontamination, detoxification, closure, cleanup or other remedial measures required with respect to the Premises under any Environmental Laws resulting from Lessee's use or occupancy of the Premises (collectively, the "Lessee's Violations"). Lessor shall be reimbursed by Lessee immediately upon demand for any and all sums paid and costs incurred by Lessor with respect to the foregoing matters. Said sums paid and costs incurred shall bear interest at the highest rate permitted by law and same shall be paid to Lessor by Lessee immediately upon demand. The foregoing Lessee's environmental indemnity shall survive the expiration or termination of this Lease and/or any transfer of all or any portion of the Premises, or of any interest in this Lease.

51.07 Lessee shall immediately notify Lessor in writing of all spills or releases of any Hazardous Materials, all failures to comply with any Environmental Laws, all inspections of the Premises by any regulatory entity concerning the same, all notices, orders, fines or communications of any kind from any governmental entity or third party that relate to the existence of or potential for environmental pollution of any kind existing on or resulting from the use of the Premises or any activity conducted thereon, and all responses or interim cleanup action taken by or proposed to be taken by any government entity or private party on the Premises.

51.08 If Lessee is not in compliance with the provisions of this paragraph, Lessor, without waiving or releasing any right or remedy it may have with respect to such noncompliance, shall have the right to immediately enter upon the Premises to remedy any contamination caused by Lessee's failure to comply, notwithstanding any other provision of this Lease. Lessor shall use reasonable efforts to minimize interference with Lessee's business but shall not be liable for any interference caused thereby.

51.09 In the event any investigation, site monitoring, containment, cleanup, removal, restoration or other remedial work ("Remedial Work") of any kind is necessary under any applicable Environmental Laws, or is required by any governmental entity or other third person because of or in connection with the presence or suspected presence of Hazardous Materials on or under the Premises resulting from Lessee's Violations, Lessee shall assume responsibility for all such Remedial Work and shall promptly commence and thereafter diligently prosecute to completion all such Remedial Work. Lessee shall pay for all costs and expenses of such Remedial Work, including, without limitation, Lessor's reasonable attorneys' fees and costs incurred in connection with monitoring or review of such Remedial Work. In the event Lessee shall fail to timely commence, or cause to be commenced, or fail to diligently prosecute to completion, such Remedial Work, Lessor may, but shall not be required to, cause such Remedial Work to be performed and all costs and expenses thereof, or incurred in connection therewith, shall become immediately due and payable, as additional rent to the Lessor from the Lessee.

51.10 Any default of Lessee under these provisions shall be an Event of Default hereunder, enabling Lessor to exercise any of the remedies set forth in this Lease.

51.11 The provisions of this Section 51 shall survive the termination or expiration of this Lease.

52. Independent Covenants:

52.01 The covenants to pay Rent, additional rent and other amounts hereunder are independent covenants, and Lessee shall not have the right to hold back, offset, or fail to pay any such amounts for default by Lessor or any other reason whatsoever.

53. Construction And Interpretation:

53.01 The fact that a party may be deemed to have drafted or structured any provision hereof shall not be considered in construing that particular provision either in favor of or against such party.

54. Quiet Enjoyment:

54.01 Upon payment by the Lessee of the rents herein provided, and upon the observance and performance of all covenants, terms and conditions of Lessee's part to be observed and performed, Lessee shall peacefully and quietly hold and enjoy the Premises for the term hereby demised without hindrance or interruption by Lessor, subject nevertheless, to the terms and conditions of this Lease.

55. Relationship Of Parties:

55.01 Notwithstanding anything contained herein to the contrary, it is agreed that the Lessor shall in no event be deemed to be a partner or engaged in a joint venture with, or an associate of, Lessee in the conduct of its business, nor shall Lessor be liable for any debts incurred by Lessee in the conduct of its business. Nothing in this Lease contained shall be deemed or construed to confer upon Lessor any interest in the business of the Lessee. The relationship of the parties during the Lease Term shall at all times be that of Lessor and Lessee.

IN WITNESS WHEREOF, intending to be legally bound, the parties hereto have set their hands and seals on the dates indicated below their respective signatures.

Witnesses:

/s/ Susan Luther
Print Name: Susan Luther

/s/ Paul M. Sills
Print Name: Paul M. Sills

/s/ Nancy Setteducati
Print Name: Nancy Setteducati

/s/ Lezlie Craig
Print Name: Lezlie Craig

LESSOR

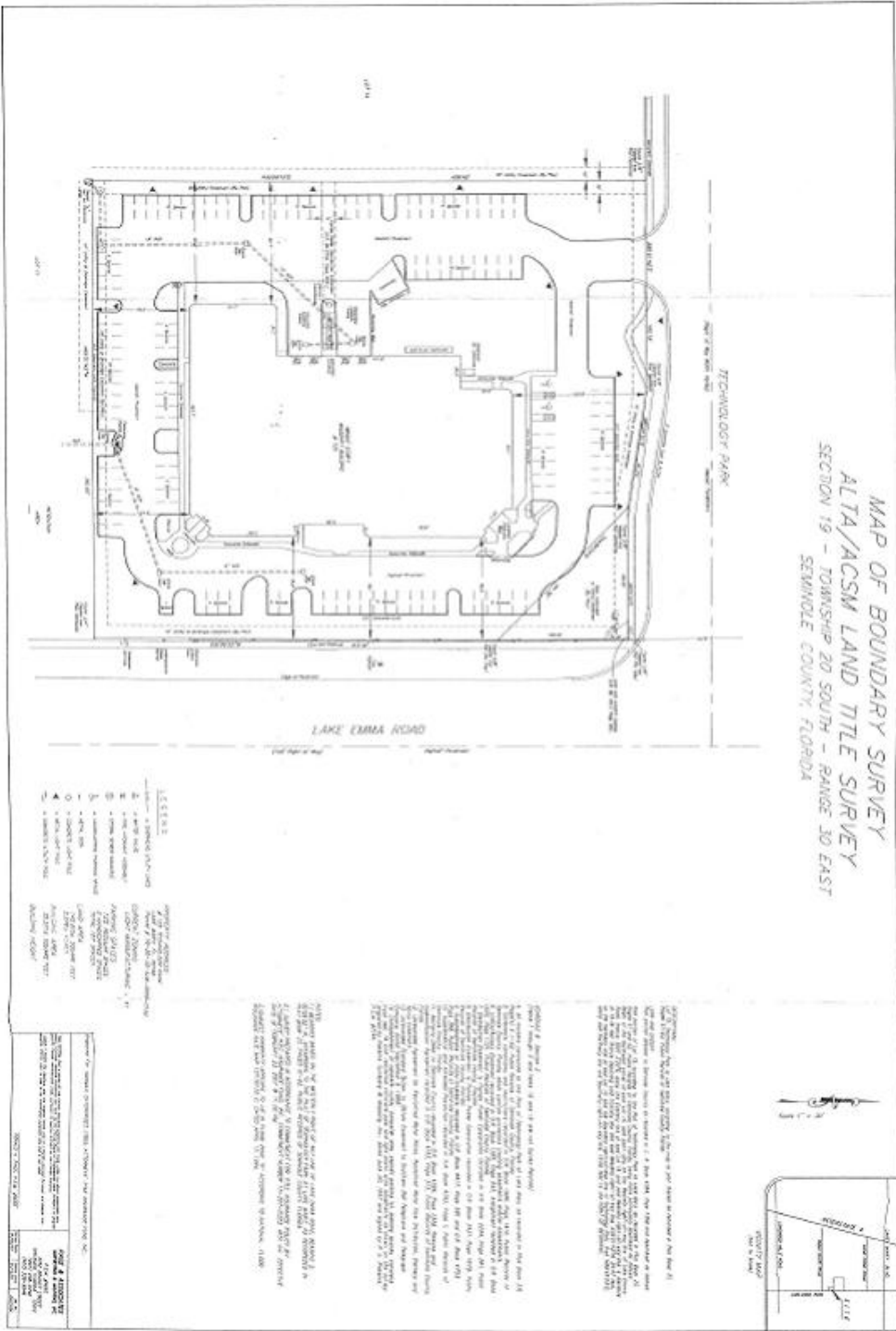
EMMA INVESTMENTS, LLC, a Florida limited liability company

/s/ Andre F. Hickman
ANDRE F. HICKMAN, Manager
Date: 10/12/2009

LESSEE

FARO TECHNOLOGIES, INC., a Florida corporation

By: /s/ David Morse
Name Printed: David Morse
Title: SVP Managing Director Americas
Date: 10/9/2009



Re: 250 Technology Parkway
Lake Mary, Florida

FIRST AMENDMENT TO LEASE

THE STATE OF FLORIDA §
 § KNOW ALL MEN BY THESE PRESENTS:
COUNTY OF SEMINOLE §

THIS FIRST AMENDMENT TO LEASE (this "Amendment") has been executed as of (but not necessarily on) October 1st, 2009, by SUN LIFE ASSURANCE COMPANY OF CANADA, a Canadian corporation ("Landlord"), and FARO TECHNOLOGIES, INC., a Florida corporation ("Tenant").

R E C I T A L S:

A. Landlord and Tenant entered into that certain Lease Agreement, last executed as of September 26, 2007, as amended by Notice of Lease Term Dates, dated as of October 1, 2007, confirming the commencement date as October 1, 2007 (collectively, the "Lease"), relating to certain premises containing approximately 46,481 square feet located in the building located at 250 Technology Parkway, in Lake Mary, Florida, as more particularly described in the Lease (the "Building"). Unless otherwise provided herein, capitalized and uncapitalized words and phrases defined in the Lease shall have the same meaning as those set forth in the Lease.

B. Landlord and Tenant desire to execute this Amendment in order to evidence their agreement to (i) extend the Term of the Lease and (ii) make certain other amendments to the Lease, all as more particularly set forth in this Amendment.

NOW THEREFORE, in consideration of the foregoing and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Landlord and Tenant agree as follows:

Article I

CERTAIN AMENDMENTS

SECTION 1.01. Lease Term. The Term of the Lease is hereby extended through and including September 30, 2019, subject to adjustment or earlier termination as set forth in the Lease. Except as set forth in Exhibit B attached hereto, all renewal rights or options under the Lease, if any, are hereby deleted.

SECTION 1.02. Base Rent. As of October 1, 2009, the Base Rent, on a triple net basis for the Premises during the Lease Term, as hereby extended, shall be as follows:

<u>Period:</u>	<u>Annual Rent per Rentable Square Foot*:</u>	<u>Monthly Rent*:</u>
10/01/2009-09/30/2010	\$ 8.50	\$32,924.04
10/01/2010-09/30/2011	\$ 9.00	\$34,860.75
10/01/2011-09/30/2012	\$ 9.50	\$36,797.46
10/01/2012-09/30/2013	\$ 10.00	\$38,734.17
10/01/2013-09/30/2014	\$ 10.50	\$40,670.88
10/01/2014-09/30/2015	\$ 11.00	\$42,607.58
10/01/2015-09/30/2016	\$ 11.50	\$44,544.29
10/01/2016-09/30/2017	\$ 12.00	\$46,481.00
10/01/2017-09/30/2018	\$ 12.50	\$48,417.71
10/01/2018-09/30/2019	\$ 13.00	\$50,354.42

* In addition, to the Base Rent set forth above, Tenant shall pay to Landlord, simultaneously with Tenant's payments of such Base Rent, all Florida sales or rental taxes due on such rents.

The Base Rent under the Lease shall be due and payable in equal monthly installments, each such monthly installment due and payable on the first day of each calendar month, in advance, without demand and without setoff or deduction whatsoever. Prior to October 1, 2009, the Base Rent shall remain as set forth in the Lease. In addition, Tenant shall be liable to pay all other amounts set forth in the Lease on a triple net basis.

SECTION 1.03. Commissions. Landlord and Tenant acknowledge that no brokers have been involved in this Amendment other than Crescent Resources, LLC and Sperry Van Ness/Paradigm Commercial Real Estate Group ("Sperry") and Landlord will pay such brokers any commission owed by separate agreement; provided, however, in no event shall the commission payable to Sperry exceed a flat fee of \$15,000. Landlord and Tenant hereby indemnify each other from the payment of any commissions owed to any other broker with respect to this Amendment resulting from the acts of such party, but not otherwise.

SECTION 1.04. Exhibits. Landlord and Tenant agree that the following exhibits have been attached hereto and will be deemed a part of this Amendment and the Lease for all purposes and will be in lieu of any similar rights or provisions currently set forth in the Lease:

Exhibit A - Floor Plan of Premises

Exhibit B - Renewal Option

SECTION 1.05 Release by Tenant. In order to induce Landlord enter into this Amendment, Tenant hereby covenants and agrees not to sue, threaten, or make claim against and does hereby release, acquit, and forever discharge Landlord and Broker and their respective employees, agents, officers, directors, managers, shareholders, parents, subsidiaries, affiliated companies, successors, attorneys, and assigns from any and all prior and existing claims, damages, defenses, demands, actions and causes of action of whatsoever nature, whether in contract or in tort, by statute or otherwise, known or unknown, suspected or unsuspected, related to the initial Construction Allowance and any work performed by Landlord under Exhibit D of the Original Lease; including without limitation, any and all claims relating to the construction management fees.

SECTION 1.06. Further Amendments. The Lease shall be and hereby is further amended wherever necessary, even though not specifically referred to herein, in order to give effect to the terms of this Amendment. The Lease is also amended as follows: (a) the parties acknowledge the contingency contained in the last paragraph of Part I of the Lease has been satisfied, (b) Landlord agrees to subordinate its statutory lien, as well as the security interest granted to it under Section 5.02 of the Lease, to liens in connection with purchase money financing loans from third party lenders for furniture, fixtures and equipment used in Tenant's business. In connection therewith, Tenant agrees to reimburse Landlord for its reasonable administrative costs and attorneys' fees, (c) the reference to "third" in Section 8.1(a) of the Lease is deleted and replaced with "second," (d) the last sentence of Section 10.1 of the Lease is deleted and replaced with the following: "Notwithstanding the foregoing, subject to Section 10.3 below, if any holder of a Senior Interest succeeds to the interest of Landlord under this Lease, then, at the option of such holder, this Lease shall continue in full force and effect and Tenant shall attorn to such holder and to recognize such holder as its Landlord," (e) attached hereto as Exhibit A is the floor plan of the Premises as it existed on the date of the Lease and the attached is retroactively made a part of the Lease effective as of the date of the Lease.

Article II

MISCELLANEOUS

SECTION 2.01. Ratification. The Lease, as amended hereby, is hereby ratified, confirmed and deemed in full force and effect in accordance with its terms. Tenant represents to Landlord that Tenant (a) is currently unaware of any default by Landlord under the Lease; (b) has full power and authority to execute and deliver this Amendment and this Amendment represents a valid and binding obligation of Tenant enforceable in accordance with its terms; (c) Landlord has completed all improvements to the Premises in compliance with all requirements in the Lease; and (d) all tenant finish costs or allowances payable by Landlord have been paid and no such costs or allowances are payable hereafter under the Lease.

SECTION 2.02. Governing Law. This Amendment shall be governed by and construed in accordance with the laws of the State of Florida.

SECTION 2.03. Counterparts. This Amendment may be executed in multiple counterparts each of which is deemed an original but together constitute one and the same instrument. This Amendment may be executed by facsimile and each party has the right to rely upon a facsimile counterpart of this Amendment signed by the other party to the same extent as if such party had received an original counterpart.

SECTION 2.04. Recitals. The recitals set forth above are true and correct.

SECTION 2.05. OFAC. To the actual knowledge of Landlord and Tenant, respectively, neither party nor any of their respective affiliates, is a person or entity with whom U.S. persons or entities are restricted from doing business under regulations of the Office of Foreign Asset Control ("OFAC") of the Department of the Treasury (including those named on OFAC's Specially Designated and Blocked Persons List) or under any statute, executive order (including the September 24, 2001, Executive Order Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit, or Support Terrorism), or other governmental action.

SECTION 2.06. Radon. Radon is a naturally occurring radioactive gas, that when it has accumulated in a building in sufficient quantities, may present a health risk to persons who are exposed to it over time. Levels of radon that exceed federal and state guidelines have been found in buildings in Florida. Additional information regarding radon and radon testing may be obtained from your county public health unit.

SECTION 2.07. No Offer. The submission of this Amendment to Tenant shall not be construed as an offer, nor shall Tenant have any rights under this Amendment unless Landlord executes a copy of this Amendment and delivers it to Tenant.

[SIGNATURES FOLLOW NEXT PAGE]

IN WITNESS WHEREOF, this Amendment has been executed as of the date and year first above written.

WITNESSES AS TO TENANT:

/s/ Nancy L. Setteducati
Nancy L. Setteducati
(Print name as signed above)

/s/ David Morse
David Morse
(Print name as signed above)

*Note: If Tenant is a corporation, an authorized corporate officer must execute this Agreement and have two subscribing witnesses.

(CORPORATE SEAL)

Following execution, four originals hereof shall be returned to Landlord.

WITNESSES AS TO LANDLORD:

/s/ Marlyss Whalen
Marlyss Whalen
(Print name as signed above)

/s/ Marlyss Whalen
Marlyss Whalen
(Print name as signed above)

TENANT:

FARO TECHNOLOGIES, INC.,
a Florida corporation

By: /s/ Jay W. Freeland
Name: Jay W. Freeland
Title: President & CEO

By: _____
Name: _____
Title: _____

LANDLORD:

SUN LIFE ASSURANCE COMPANY OF
CANADA, a Canadian corporation

By: /s/ Charles S. Andes
Name: Charles S. Andes
Title: Managing Director

By: /s/ Alena R. Tverskoy
Name: Alena R. Tverskoy
Title: Director

EXHIBIT A
FLOOR PLAN OF PREMISES

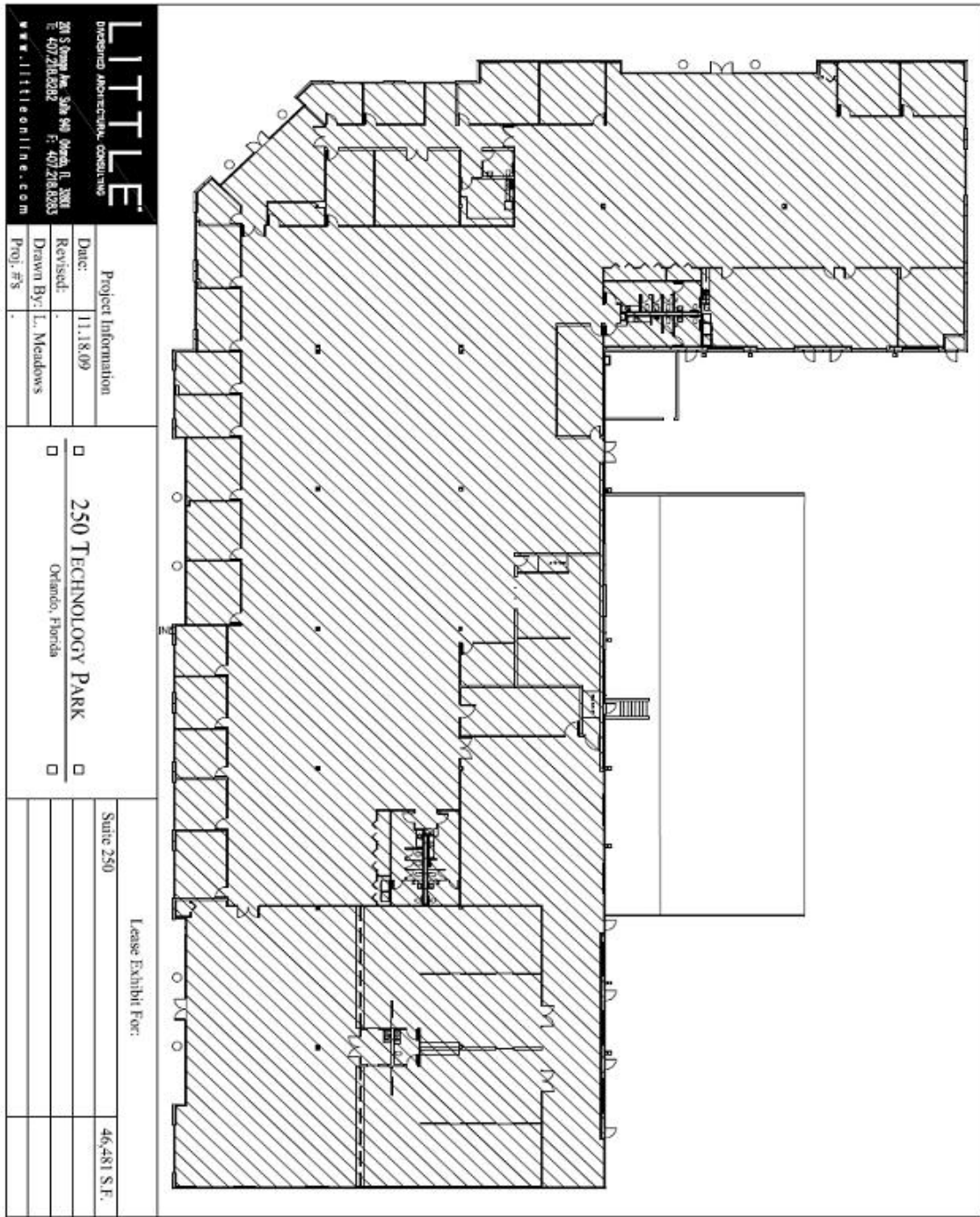


EXHIBIT B

RENEWAL OPTION

1. Provided no default exists at the time of such election and Tenant's financial condition is reasonably acceptable to Landlord, Tenant may renew this Lease for one (1) additional period of five (5) years on the same terms provided in this Lease (except as set forth below), by delivering binding written notice of ("**Tenant's Notice**") the exercise thereof to Landlord not later than nine (9) months prior to the end of the Term described in the Amendment. On or before the commencement date of the extended Term, Landlord and Tenant shall execute an amendment to this Lease extending the term on the same terms provided in this Lease, except as follows:

(a) The Base Rent payable for each month during each such extended term shall be as follows:

<u>Period:</u>	<u>Rent per s.f. per Annum:</u>	<u>Monthly:</u>
10/1/19 – 9/30/20	\$ 13.39	\$51,865.05
10/1/20 – 9/30/21	\$ 13.79	\$53,414.42
10/1/21 – 9/30/22	\$ 14.20	\$55,002.52
10/1/22 – 9/30/23	\$ 14.63	\$56,668.09
10/1/23 – 9/30/24	\$ 15.07	\$58,372.39

(b) Tenant shall have no further renewal options unless expressly granted by Landlord in writing; and

(c) Landlord shall lease to Tenant the Premises in their then-current condition, and Landlord shall not provide to Tenant any allowances (e.g., moving allowance, construction allowance, and the like) or other tenant inducements.

2. Tenant's failure to timely deliver Tenant's Renewal Notice shall be deemed rejection by Tenant of the Extension Option.

3. Tenant's rights under this Exhibit shall terminate if (i) this Lease or Tenant's right to possession of the Premises is terminated, (ii) Tenant assigns any of its interest in this Lease or sublets any portion of the Premises (other than a transfer to an Affiliate), or (iii) Tenant fails to timely exercise its option under this Exhibit, time being of the essence with respect to Tenant's exercise thereof.

FARO TECHNOLOGIES, INC. LIST OF SUBSIDIARIES

Antares LDA	Antares, Portugal
Cam2 SRL	Rivoli, Italy
FARO Benelux BV	Eindhoven, Netherlands
FARO Business Technologies India Pvt. Ltd.	New Delhi, India
FARO Cayman LP	Georgetown, Cayman Islands
FARO Cayman Ltd	Grand Cayman, Cayman Islands
FARO Delaware Inc	Wilmington, Delaware, USA
FARO Deutschland Holding GmbH	Korntal-Münchingen, Germany
FARO Europe KG	Korntal-Münchingen, Germany
FARO FHN Netherlands BV	Amsterdam, Netherlands
FARO Japan KK	Nagoya, Japan
FARO Scanning AG	Korntal-Münchingen, Germany
FARO Scanner Production GmbH	Korntal-Münchingen, Germany
FARO Shanghai Co, Ltd	Shanghai, China
FARO Singapore PTE Ltd	Singapore, Singapore
FARO Spain SL	Barcelona, Spain
FARO Swiss Holding GmbH	Beringen, Switzerland
FARO Swiss Manufacturing GmbH	Beringen, Switzerland
FAO Tech Polska	Poznan, Poland
FARO Verwaltungs GmbH	Korntal-Münchingen, Germany
FARO Technologies (Thailand) Ltd.	Bangkok, Thailand
Faro Laser Trackers	Kennett Square, PA USA
3D Measurement Technologies, S de RL de CV	Los Alpes Alvaro Obrégon Cd. De Mexico, Mexico
FARO France	Röthenbach/Allgäu, France
FARO UK	Coventry, United Kingdom
FARO Australia	Sydney, Australia

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have issued our reports dated February 26, 2010, with respect to the consolidated financial statements, schedule, and internal control over financial reporting included in the Annual Report of FARO Technologies, Inc. and subsidiaries on Form 10-K for the year ended December 31, 2009. We hereby consent to the incorporation by reference of said reports in the Registration Statements of FARO Technologies, Inc. and subsidiaries on Forms S-3 (File No. 333-163950, effective January 10, 2010) and on Forms S-8 (File No. 333-160660, effective July, 17, 2009, File No. 333-125021, effective May, 18, 2005, File No. 333-41115, effective November 26, 1997, File No. 333-41125, effective November 26, 1997, File No. 333-41131, effective November 26, 1997, and File No. 333-41135, effective November 26, 1997).

/s/ GRANT THORNTON LLP

Orlando, Florida
February 26, 2010

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

I, Jay W. Freeland, certify that:

1. I have reviewed this Annual Report on Form 10-K 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 officers 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 officers 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: February 26, 2010

/s/ JAY W. FREELAND

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

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

I, Keith S. Bair, certify that:

1. I have reviewed this Annual Report on Form 10-K 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 officers 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 officers 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: February 26, 2010

/s/ KEITH S. BAIR

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

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

Solely for the purposes of complying with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, the undersigned President and Chief Executive Officer and Director of FARO Technologies, Inc., (the Company) hereby certify, based on my knowledge, that the Annual Report on Form 10-K, for the year ended December 31, 2009 (the Report) fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ JAY W. FREELAND

Jay W. Freeland
February 26, 2010

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

Solely for the purposes of complying with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, the undersigned Senior Vice President and Chief Financial Officer of FARO Technologies, Inc., (the Company), and the principal financial officer and principal accounting officer of the Company for the period covered the Report, hereby certify, based on my knowledge, that the Annual Report on Form 10-K, for the year ended December 31, 2009 (the Report) fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ KEITH S. BAIR

Keith S. Bair
February 26, 2010

FARO TECHNOLOGIES INC. PROPERTIES

<u>No.</u>	<u>Location</u>	<u>Sq. Ft.</u>	<u>Owned/Leased</u>	<u>Purposes</u>
1	125 Technology Park, Lake Mary, Florida	35,000	Leased	Manufacturing, research and development, service
2	250 Technology Park, Lake Mary	46,000	Leased	Headquarters, sales, marketing, administration
3	222 Gale Lane, Kennett Square, Pennsylvania	36,800	Leased	Manufacturing, research and development, service
4	Ingersheimer Str.12, D-70499 Stuttgart-Weilimdorf, Germany	62,300	Leased	European headquarters, manufacturing, sales, research and development, service
5	Wiesengasse 20 CH-8222 Beringen Switzerland	15,930	Leased	Manufacturing
6	716 Kumada Nagakute-cho, Nagoya, Aichi 465-0015, Japan	17,200	Leased	Sales, service
7	798 Zhaojiabang Road, Shanghai, China	11,500	Leased	Sales, service
8	No. 3 Changi South St 2 #01-01 Xilin Districentre Building B, Singapore	22,000	Leased	Asia headquarters, manufacturing, sales, service