

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2022

OR

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

For the transition period from _____ to _____

Commission File Number: 0-23081

FARO TECHNOLOGIES, INC.

(Exact Name of Registrant as Specified in Its Charter)

Florida

(State or other Jurisdiction of Incorporation or Organization)

59-3157093

(I.R.S. Employer Identification No.)

**250 Technology Park,
(Address of Principal Executive Offices)**

Lake Mary, Florida

**32746
(Zip Code)**

(407) 333-9911

(Registrant's Telephone Number, including Area Code)

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

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

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

| | | | |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/> |
| Emerging growth company | <input type="checkbox"/> | | |

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

There were 18,779,816 shares of the registrant's common stock outstanding as of October 31, 2022.

FARO TECHNOLOGIES, INC.

Quarterly Report on Form 10-Q
Quarter Ended September 30, 2022

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PART I. FINANCIAL INFORMATION**Item 1. Financial Statements****FARO TECHNOLOGIES, INC. AND SUBSIDIARIES**
CONDENSED CONSOLIDATED BALANCE SHEETS

| <i>(in thousands, except share and per share data)</i> | September 30, 2022 (unaudited) | December 31, 2021 |
|--|-----------------------------------|-------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 48,534 | \$ 121,989 |
| Accounts receivable, net | 75,347 | 78,523 |
| Inventories, net | 50,956 | 53,145 |
| Prepaid expenses and other current assets | 33,801 | 19,793 |
| Total current assets | 208,638 | 273,450 |
| Non-current assets: | | |
| Property, plant and equipment, net | 20,424 | 22,194 |
| Operating lease right-of-use assets | 18,404 | 22,543 |
| Goodwill | 101,279 | 82,096 |
| Intangible assets, net | 48,094 | 25,616 |
| Service and sales demonstration inventory, net | 28,249 | 30,554 |
| Deferred income tax assets, net | 18,092 | 21,277 |
| Other long-term assets | 2,047 | 2,010 |
| Total assets | \$ 445,227 | \$ 479,740 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 17,546 | \$ 14,199 |
| Accrued liabilities | 22,881 | 28,208 |
| Income taxes payable | 6,421 | 4,499 |
| Current portion of unearned service revenues | 36,440 | 40,838 |
| Customer deposits | 5,873 | 5,399 |
| Lease liabilities | 5,532 | 5,738 |
| Total current liabilities | 94,693 | 98,881 |
| Unearned service revenues - less current portion | 20,868 | 22,350 |
| Lease liabilities - less current portion | 14,344 | 18,648 |
| Deferred income tax liabilities | 5,708 | 1,058 |
| Income taxes payable - less current portion | 10,131 | 11,297 |
| Other long-term liabilities | 19 | 1,047 |
| Total liabilities | 145,763 | 153,281 |
| Commitments and contingencies - See Note 12 | | |
| Shareholders' equity: | | |
| Common stock - par value \$0.001, 50,000,000 shares authorized; 20,153,287 and 19,588,003 issued, respectively; 18,776,936 and 18,205,636 outstanding, respectively | 20 | 20 |
| Additional paid-in capital | 325,244 | 301,061 |
| Retained earnings | 49,022 | 73,544 |
| Accumulated other comprehensive loss | (44,165) | (17,374) |
| Common stock in treasury, at cost - 1,376,351 and 1,382,367 shares held, respectively | (30,657) | (30,792) |
| Total shareholders' equity | 299,464 | 326,459 |
| Total liabilities and shareholders' equity | \$ 445,227 | \$ 479,740 |

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

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

| | Three Months Ended | | Nine Months Ended | |
|---|--------------------|--------------------|--------------------|--------------------|
| | September 30, 2022 | September 30, 2021 | September 30, 2022 | September 30, 2021 |
| Sales | | | | |
| Product | \$ 65,581 | \$ 57,838 | \$ 182,015 | \$ 172,748 |
| Service | 19,751 | 21,331 | 59,891 | 64,862 |
| Total sales | <u>85,332</u> | <u>79,169</u> | <u>241,906</u> | <u>237,610</u> |
| Cost of sales | | | | |
| Product | 30,375 | 25,650 | 82,879 | 75,909 |
| Service | 11,692 | 11,188 | 34,299 | 33,481 |
| Total cost of sales | <u>42,067</u> | <u>36,838</u> | <u>117,178</u> | <u>109,390</u> |
| Gross profit | <u>43,265</u> | <u>42,331</u> | <u>124,728</u> | <u>128,220</u> |
| Operating expenses | | | | |
| Selling, general and administrative | 37,226 | 33,433 | 108,734 | 100,375 |
| Research and development | 12,586 | 12,731 | 36,756 | 36,464 |
| Restructuring costs | 580 | 1,376 | 2,512 | 3,679 |
| Total operating expenses | <u>50,392</u> | <u>47,540</u> | <u>148,002</u> | <u>140,518</u> |
| Loss from operations | <u>(7,127)</u> | <u>(5,209)</u> | <u>(23,274)</u> | <u>(12,298)</u> |
| Other (income) expense | | | | |
| Interest (income) expense, net | (24) | 5 | (28) | 54 |
| Other (income) expense, net | (1,428) | 299 | (3,077) | (433) |
| Loss before income tax expense (benefit) | <u>(5,675)</u> | <u>(5,513)</u> | <u>(20,169)</u> | <u>(11,919)</u> |
| Income tax expense (benefit) | 586 | (1,658) | 4,352 | (3,667) |
| Net loss | <u>\$ (6,261)</u> | <u>\$ (3,855)</u> | <u>\$ (24,521)</u> | <u>\$ (8,252)</u> |
| Net loss per share - Basic | <u>\$ (0.34)</u> | <u>\$ (0.21)</u> | <u>\$ (1.34)</u> | <u>\$ (0.45)</u> |
| Net loss per share - Diluted | <u>\$ (0.34)</u> | <u>\$ (0.21)</u> | <u>\$ (1.34)</u> | <u>\$ (0.45)</u> |
| Weighted average shares - Basic | <u>18,436,615</u> | <u>18,194,960</u> | <u>18,336,537</u> | <u>18,166,930</u> |
| Weighted average shares - Diluted | <u>18,436,615</u> | <u>18,194,960</u> | <u>18,336,537</u> | <u>18,166,930</u> |

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

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

| (in thousands) | Three Months Ended | | Nine Months Ended | |
|---|--------------------|--------------------|--------------------|--------------------|
| | September 30, 2022 | September 30, 2021 | September 30, 2022 | September 30, 2021 |
| Net loss | \$ (6,261) | \$ (3,855) | \$ (24,521) | \$ (8,252) |
| Currency translation adjustments, net of income taxes | (11,796) | (328) | (26,791) | (5,635) |
| Comprehensive loss | \$ (18,057) | \$ (4,183) | \$ (51,312) | \$ (13,887) |

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

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

| (in thousands) | Nine Months Ended | |
|---|--------------------|--------------------|
| | September 30, 2022 | September 30, 2021 |
| Cash flows from: | | |
| Operating activities: | | |
| Net loss | \$ (24,521) | \$ (8,252) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization | 10,061 | 9,560 |
| Stock-based compensation | 10,024 | 8,657 |
| Provisions for bad debts, net of recoveries | 80 | 33 |
| Loss on disposal of assets | 356 | 130 |
| Provision for excess and obsolete inventory | 209 | 1,955 |
| Deferred income tax expense (benefit) | 568 | (3,667) |
| Change in operating assets and liabilities: | | |
| Decrease (Increase) in: | | |
| Accounts receivable | 867 | 4,311 |
| Inventories | 2,129 | (9,106) |
| Prepaid expenses and other current assets | (14,566) | (2,935) |
| (Decrease) Increase in: | | |
| Accounts payable and accrued liabilities | (2,249) | (14,153) |
| Income taxes payable | 1,008 | (1,847) |
| Customer deposits | 588 | 1,966 |
| Unearned service revenues | (2,710) | (2,223) |
| Net cash used in operating activities | <u>(18,156)</u> | <u>(15,571)</u> |
| Investing activities: | | |
| Purchases of property and equipment | (4,978) | (4,845) |
| Cash paid for technology development, patents and licenses | (9,154) | (1,933) |
| Acquisition of business, net of cash acquired | (29,068) | (33,908) |
| Net cash used in investing activities | <u>(43,200)</u> | <u>(40,686)</u> |
| Financing activities: | | |
| Payments on finance leases | (172) | (229) |
| Payments for taxes related to net share settlement of equity awards | (1,584) | (4,137) |
| Proceeds from issuance of stock related to stock option exercises | — | 5,835 |
| Net cash (used in) provided by financing activities | <u>(1,756)</u> | <u>1,469</u> |
| Effect of exchange rate changes on cash and cash equivalents | (10,343) | (5,031) |
| Decrease in cash and cash equivalents | (73,455) | (59,819) |
| Cash and cash equivalents, beginning of period | 121,989 | 185,633 |
| Cash and cash equivalents, end of period | <u>\$ 48,534</u> | <u>\$ 125,814</u> |

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

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

| (in thousands, except share data) | Common Stock | | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Common Stock in Treasury | Total |
|--|--------------|---------|----------------------------------|----------------------|---|--------------------------------|------------|
| | Shares | Amounts | | | | | |
| BALANCE JANUARY 1, 2022 | 18,205,636 | \$ 20 | \$ 301,061 | \$ 73,544 | \$ (17,374) | \$ (30,792) | \$ 326,459 |
| Net loss | — | — | — | (9,687) | — | — | (9,687) |
| Currency translation adjustment | — | — | — | — | (1,984) | — | (1,984) |
| Stock-based compensation | — | — | 2,867 | — | — | — | 2,867 |
| Common stock issued, net of shares withheld for employee taxes | 55,041 | — | (1,051) | — | — | 135 | (916) |
| BALANCE MARCH 31, 2022 | 18,260,677 | \$ 20 | \$ 302,877 | \$ 63,857 | \$ (19,358) | \$ (30,657) | \$ 316,739 |
| Net loss | — | — | — | (8,574) | — | — | (8,574) |
| Currency translation adjustment | — | — | — | — | (13,011) | — | (13,011) |
| Stock-based compensation | — | — | 3,491 | — | — | — | 3,491 |
| Common stock issued, net of shares withheld for employee taxes | 6,080 | — | (249) | — | — | — | (249) |
| BALANCE JUNE 30, 2022 | 18,266,757 | \$ 20 | \$ 306,119 | \$ 55,283 | \$ (32,369) | \$ (30,657) | \$ 298,396 |
| Net loss | — | — | — | (6,261) | — | — | (6,261) |
| Currency translation adjustment | — | — | — | — | (11,796) | — | (11,796) |
| Stock-based compensation | — | — | 3,666 | — | — | — | 3,666 |
| Common stock issued, net of shares withheld for employee taxes | 4,617 | — | (418) | — | — | — | (418) |
| Acquisition of business | 495,562 | — | 15,878 | — | — | — | 15,878 |
| BALANCE SEPTEMBER 30, 2022 | 18,766,936 | \$ 20 | \$ 325,244 | \$ 49,022 | \$ (44,165) | \$ (30,657) | \$ 299,464 |

| (in thousands, except share data) | Common Stock | | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Common Stock in Treasury | Total |
|--|--------------|---------|----------------------------------|----------------------|---|--------------------------------|------------|
| | Shares | Amounts | | | | | |
| BALANCE JANUARY 1, 2021 | 17,990,707 | \$ 19 | \$ 287,979 | \$ 113,508 | \$ (10,160) | \$ (31,043) | \$ 360,303 |
| Net loss | — | — | — | (3,221) | — | — | (3,221) |
| Currency translation adjustment | — | — | — | — | (10,174) | — | (10,174) |
| Stock-based compensation | — | — | 2,094 | — | — | — | 2,094 |
| Common stock issued, net of shares withheld for employee taxes | 163,457 | — | 1,530 | — | — | 251 | 1,781 |
| BALANCE MARCH 31, 2021 | 18,154,164 | \$ 19 | \$ 291,603 | \$ 110,287 | \$ (20,334) | \$ (30,792) | \$ 350,783 |
| Net loss | — | — | — | (1,176) | — | — | (1,176) |
| Currency translation adjustment | — | — | — | — | 4,867 | — | 4,867 |
| Stock-based compensation | — | — | 3,283 | — | — | — | 3,283 |
| Common stock issued, net of shares withheld for employee taxes | 20,709 | 1 | (396) | — | — | — | (395) |
| BALANCE JUNE 30, 2021 | 18,174,873 | \$ 20 | \$ 294,490 | \$ 109,111 | \$ (15,467) | \$ (30,792) | \$ 357,362 |
| Net loss | — | — | — | (3,855) | — | — | (3,855) |
| Currency translation adjustment | — | — | — | — | (328) | — | (328) |
| Stock-based compensation | — | — | 3,280 | — | — | — | 3,280 |
| Common stock issued, net of shares withheld for employee taxes | 27,543 | — | 312 | — | — | — | 312 |
| BALANCE SEPTEMBER 30, 2021 | 18,202,416 | \$ 20 | \$ 298,082 | \$ 105,256 | \$ (15,795) | \$ (30,792) | \$ 356,771 |

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

FARO TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

(in thousands, except share and per share data, or as otherwise noted)

NOTE 1 – DESCRIPTION OF BUSINESS

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

COVID-19 and Impact On Our Business

Our business is significantly vulnerable to the economic effects of pandemics and other public health crises, including the ongoing coronavirus (“COVID-19”) pandemic that has surfaced in virtually every country of our global operating footprint. During 2020, we experienced a significant decline in the demand for our products and services across all of our served markets as a result of the impact of the spread of COVID-19.

During 2022, we continue to mitigate the ongoing impact of COVID-19 on our business results and we remain committed to taking actions to mitigate both the impact on the health and safety of our employees, as well as negative business effects resulting from demand disruption, material availability and potential production and shipment challenges, including, but not limited to, the following:

- Operating our business with a focus on our employee health and safety, which includes minimizing travel, implementing remote work policies, maintaining employee distancing and enhancing the sanitation of all of our facilities;
- Recommending that our employees receive vaccinations and vaccine boosters to help protect our colleagues, families, and communities;
- Aggressively pursuing required raw materials to ensure continuity of supply and minimize material cost increases in collaboration with our third party manufacturer, Sanmina;
- Aggressively pursuing alternative logistics paths when intermittent government-ordered shutdowns affect current logistics paths;
- Monitoring our liquidity, disciplined inventory management, and scrutinizing our capital expenditures while executing our strategic plan; and
- Continuously reviewing our financial strategy to enhance financial flexibility in these volatile financial markets.

We continue to maintain a strong capital structure with a cash balance of \$48.5 million and no debt as of September 30, 2022. We believe that our liquidity position is adequate to meet our projected needs in the reasonably foreseeable future.

Future developments, such as the potential resurgence of COVID-19 in countries and new actions taken by governments in response to future resurgence, are highly uncertain. Therefore, the Company is not able to predict the extent to which the COVID-19 outbreak continues to impact the Company’s results of operations and financial conditions.

NOTE 2 – PRINCIPLES OF CONSOLIDATION

Our condensed consolidated financial statements include the accounts of FARO Technologies, Inc. and its subsidiaries, all of which are wholly owned. All intercompany transactions and balances have been eliminated. The financial statements of our foreign subsidiaries are translated into U.S. dollars using exchange rates in effect at period-end for assets and liabilities and average exchange rates during each reporting period for results of operations. Adjustments resulting from financial statement translations are reflected as a separate component of accumulated other comprehensive loss. Foreign currency transaction gains and losses are included in net loss.

NOTE 3 – BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements and notes thereto have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) for interim financial information and with the instructions of Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. These condensed consolidated financial statements include all normal recurring accruals and adjustments considered necessary by management for a fair presentation in conformity with U.S. GAAP. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates. The condensed consolidated results of operations for the nine months ended September 30, 2022 are not necessarily indicative of results that may be expected for the year ending December 31, 2022 or any future period.

The information included in this Quarterly Report on Form 10-Q, including the interim condensed consolidated financial statements and the accompanying notes, should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2021. The accompanying December 31, 2021 condensed consolidated balance sheet has been derived from those audited consolidated financial statements.

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

| | Three Months Ended | | Nine Months Ended | |
|-------------------------------------|--------------------|--------------------|--------------------|--------------------|
| | September 30, 2022 | September 30, 2021 | September 30, 2022 | September 30, 2021 |
| Cost of sales | | | | |
| Product | \$ 231 | \$ 147 | \$ 635 | \$ 435 |
| Service | 42 | 43 | 121 | 35 |
| Total cost of sales | \$ 273 | \$ 190 | \$ 756 | \$ 470 |
| Operating expenses | | | | |
| Selling, general and administrative | \$ 2,742 | \$ 2,581 | \$ 7,475 | \$ 6,789 |
| Research and development | 651 | 509 | 1,793 | 1,398 |
| Total operating expenses | \$ 3,393 | \$ 3,090 | \$ 9,268 | \$ 8,187 |

NOTE 4 – IMPACT OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Impact of Recently Adopted Accounting Standards

In December 2019, the FASB issued ASU No. 2019-12, Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes, which amends and aims to simplify accounting disclosure requirements regarding a number of topics, including intraperiod tax allocation, accounting for deferred taxes when there are changes in consolidation of certain investments, tax basis step up in an acquisition and the application of effective rate changes during interim periods, amongst other improvements. We adopted ASU 2019-12 effective as of January 1, 2021, and the adoption of the new guidance did not have a material impact on our condensed consolidated financial statements.

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

NOTE 5 – REVENUES

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

| | For the Three Months Ended September 30, | | For the Nine Months Ended September 30, | |
|---|--|-----------|---|------------|
| | 2022 | 2021 | 2022 | 2021 |
| Product sales | | | | |
| Product transferred to customers at a point in time | \$ 60,090 | \$ 53,536 | \$ 165,750 | \$ 161,080 |
| Product transferred to customers over time | 5,491 | 4,302 | 16,265 | 11,668 |
| Total product sales | \$ 65,581 | \$ 57,838 | \$ 182,015 | \$ 172,748 |

| | For the Three Months Ended September 30, | | For the Nine Months Ended September 30, | |
|---|--|-----------|---|-----------|
| | 2022 | 2021 | 2022 | 2021 |
| Service sales | | | | |
| Service transferred to customers at a point in time | \$ 8,651 | \$ 9,332 | \$ 25,973 | \$ 28,931 |
| Service transferred to customers over time | 11,100 | 11,999 | 33,918 | 35,931 |
| Total service sales | \$ 19,751 | \$ 21,331 | \$ 59,891 | \$ 64,862 |

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

| | For the Three Months Ended September 30, | | For the Nine Months Ended September 30, | |
|--|--|-----------|---|------------|
| | 2022 | 2021 | 2022 | 2021 |
| Total sales to external customers | | | | |
| Americas ⁽¹⁾ | \$ 38,732 | \$ 33,944 | \$ 110,077 | \$ 100,195 |
| EMEA ⁽¹⁾ | 22,802 | 23,387 | 66,494 | 75,315 |
| APAC ⁽¹⁾ | 23,798 | 21,838 | 65,335 | 62,100 |
| | \$ 85,332 | \$ 79,169 | \$ 241,906 | \$ 237,610 |

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

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

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

We capitalize commission expenses related to deliverables transferred to a customer over time and amortize such costs ratably over the term of the contract. As of September 30, 2022, the deferred cost asset related to deferred commissions was approximately \$3.1 million. For classification purposes, \$2.1 million and \$1.0 million are comprised within the Prepaid expenses and other current assets and Other long-term assets, respectively, on our condensed consolidated balance sheet as of September 30, 2022. As of December 31, 2021, the deferred cost asset related to deferred commissions was approximately \$3.5 million. For classification purposes, \$2.3 million and \$1.2 million were comprised within the Prepaid expenses and other current assets and Other long-term assets, respectively, on our condensed consolidated balance sheet as of December 31, 2021.

The unearned service revenue liabilities reported on our condensed consolidated balance sheets reflect the contract liabilities to satisfy the remaining performance obligations for extended warranties, subscription-based software and software maintenance. The current portion of unearned service revenues on our condensed consolidated balance sheets is what we expect to recognize as revenue within twelve months after the applicable balance sheet date relating to extended warranties, subscription-based software and software maintenance contract liabilities. The unearned service revenues less the current portion on our condensed consolidated balance sheets is what we expect to recognize as revenue extending beyond twelve months after the applicable balance sheet date relating to extended warranties, subscription-based software and software maintenance contract liabilities. Customer deposits on our condensed consolidated balance sheets represent customer prepayments on contracts for performance obligations that we must satisfy in the future to recognize the related contract revenue. These amounts are generally related to performance obligations which are delivered in less than 12 months. During the three and nine months ended September 30, 2022, we recognized \$8.7 million and \$29.1 million of revenue that was deferred on our condensed consolidated balance sheet as of December 31, 2021. During the three and nine months ended September 30, 2021, we recognized \$7.6 million and \$29.2 million of revenue that was deferred on our condensed consolidated balance sheet as of December 31, 2020.

The nature of certain of our contracts gives rise to variable consideration, primarily related to an allowance for sales returns. We are required to estimate the contract asset related to sales returns and record a corresponding adjustment to Cost of Sales. Our allowance for sales returns for September 30, 2022 and September 30, 2021 was approximately \$0.2 million, and \$0.1 million, respectively.

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

NOTE 6 – ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

| | As of September 30, 2022 | As of December 31, 2021 |
|-----------------------------|--------------------------|-------------------------|
| Accounts receivable | \$ 77,591 | \$ 80,754 |
| Allowance for credit losses | (2,244) | (2,231) |
| Total | <u>\$ 75,347</u> | <u>\$ 78,523</u> |

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

| | Nine Months Ended September 30, 2022 |
|--|---|
| Beginning balance of the allowance for credit losses | \$ (2,231) |
| Current period provision for expected credit losses, net of recoveries | (80) |
| Charge-offs of amounts previously expensed | 67 |
| Ending balance of the allowance for credit losses | <u>\$ (2,244)</u> |

NOTE 7 – INVENTORIES

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

Inventories consist of the following:

| | As of September 30, 2022 | As of December 31, 2021 |
|--|--------------------------|-------------------------|
| Raw materials | \$ 30,440 | \$ 34,617 |
| Finished goods | 20,516 | 18,528 |
| Inventories, net | <u>\$ 50,956</u> | <u>\$ 53,145</u> |
| | | |
| Service and sales demonstration inventory, net | <u>\$ 28,249</u> | <u>\$ 30,554</u> |

NOTE 8 – NET LOSS PER SHARE

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

For the three and nine months ended September 30, 2022, there were approximately 578,121 shares issuable upon the exercise of options, the vesting of time-based restricted stock and the contingent vesting of market-based restricted stock units that were excluded from the dilutive calculations, as they were anti-dilutive. For the three months and nine months ended September 30, 2021, there were approximately 393,995 issuable upon the exercise of options that were excluded from the dilutive calculations, as they were anti-dilutive.

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

| | Three Months Ended | | | |
|-------------------------------|--------------------|------------------|--------------------|------------------|
| | September 30, 2022 | | September 30, 2021 | |
| | Shares | Per-Share Amount | Shares | Per-Share Amount |
| Basic net loss per share | 18,436,615 | \$ (0.34) | 18,194,960 | \$ (0.21) |
| Effect of dilutive securities | — | — | — | — |
| Diluted net loss per share | 18,436,615 | \$ (0.34) | 18,194,960 | \$ (0.21) |

| | Nine Months Ended | | | |
|-------------------------------|--------------------|------------------|--------------------|------------------|
| | September 30, 2022 | | September 30, 2021 | |
| | Shares | Per-Share Amount | Shares | Per-Share Amount |
| Basic net loss per share | 18,336,537 | \$ (1.34) | 18,166,930 | \$ (0.45) |
| Effect of dilutive securities | — | — | — | — |
| Diluted net loss per share | 18,336,537 | \$ (1.34) | 18,166,930 | \$ (0.45) |

NOTE 9 – ACCRUED LIABILITIES

Accrued liabilities consist of the following:

| | As of September 30, 2022 | As of December 31, 2021 |
|-----------------------------------|--------------------------|-------------------------|
| Accrued compensation and benefits | \$ 15,310 | \$ 15,723 |
| Accrued restructuring costs | 520 | 3,919 |
| Accrued warranties | 2,192 | 1,880 |
| Professional and legal fees | 1,386 | 2,053 |
| Taxes other than income | 194 | 3,674 |
| Other accrued liabilities | 3,279 | 959 |
| Total accrued liabilities | \$ 22,881 | \$ 28,208 |

Activity related to accrued warranties was as follows:

| | Nine Months Ended | |
|-------------------------------------|--------------------|--------------------|
| | September 30, 2022 | September 30, 2021 |
| Balance, beginning of period | \$ 1,880 | \$ 1,683 |
| Provision for warranty expense | 2,548 | 1,941 |
| Fulfillment of warranty obligations | (2,236) | (1,951) |
| Balance, end of period | \$ 2,192 | \$ 1,673 |

NOTE 10 – FAIR VALUE MEASUREMENTS

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

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

| | As of September 30, 2022 | | |
|---|--------------------------|-------------|-----------------|
| | Level 1 | Level 2 | Level 3 |
| Liabilities: | | | |
| Contingent consideration ⁽¹⁾ | \$ — | \$ — | \$ 881 |
| Total | \$ — | \$ — | \$ 881 |
| | As of December 31, 2021 | | |
| | Level 1 | Level 2 | Level 3 |
| Liabilities: | | | |
| Contingent consideration ⁽¹⁾ | \$ — | \$ — | \$ 1,028 |
| Total | \$ — | \$ — | \$ 1,028 |

(1) Contingent consideration liability represents arrangements to pay the former owners of certain companies we acquired based on the attainment of future product release milestones and is reported in Other long-term liabilities. We use a probability-weighted discounted cash flow model to estimate the fair value of contingent consideration liabilities. These probability weightings are developed internally and assessed on a quarterly basis. The remaining undiscounted maximum payment under these arrangements was \$1.0 million as of September 30, 2022. We expect to make payments earned by former owners under these arrangements on August 31, 2023.

NOTE 11 – RESTRUCTURING

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

On July 15, 2021, we entered into a manufacturing services agreement (the “Agreement”) with Sanmina Corporation (Nasdaq: SANM) (“Sanmina”), in connection with the Restructuring Plan. Under the Agreement, Sanmina will provide manufacturing services for the Company’s measurement device products previously manufactured by the Company at the Company’s Lake Mary, Florida, Exton, Pennsylvania, and Stuttgart, Germany manufacturing sites. This phased transition to a Sanmina production facility was completed at the beginning of the third quarter of 2022 as part of our cost reduction initiative. We are currently evaluating these manufacturing sites with the intention to reduce our leased floor space. However, all of these facilities are mixed-use spaces shared with our service, research and development, or sales teams who continue to use these spaces. The Company, in collaboration with third party lessors and architectural resources, intends to conduct studies over the feasibility of abandoning or demising leased floor space against our current needs. Our current needs continue to include access to existing spaces previously constructed to closely monitor temperature and vibration for our service and research and development teams. The conclusion of this evaluation and any subsequent approval to abandon or reduce these leased spaces would be considered as a change in the manner of the use of these corresponding assets, and thereby will be evaluated for impairment. We expect to complete this evaluation before the first half of fiscal year 2023. As of September 30, 2022, the remaining value of leasehold improvements for these facilities is approximately \$3 million and a portion of this may be impaired, if the Company decides to reduce or abandon the leased space. Separately, we may also incur additional charges for the modification of leases for these facilities.

In connection with the Restructuring Plan, we paid \$5.9 million during the nine months ended September 30, 2022, primarily consisting of severance and related benefits. Since the approval of the Restructuring Plan, we have paid \$24.8 million, primarily consisting of severance and related benefits. Activity related to the accrued restructuring charge and cash payments during the nine months ended September 30, 2022 and September 30, 2021 was as follows:

| | Severance and other benefits | Professional fees and other related charges | Total |
|-------------------------------|------------------------------|--|-----------------|
| Balance at December 31, 2021 | \$ 3,442 | \$ 477 | \$ 3,919 |
| Additions charged to expense | 1,439 | 1,072 | 2,511 |
| Cash payments | (4,619) | (1,291) | (5,910) |
| Balance at September 30, 2022 | <u>\$ 262</u> | <u>\$ 258</u> | <u>\$ 520</u> |
| Balance at December 31, 2020 | \$ 1,481 | \$ 867 | \$ 2,348 |
| Additions charged to expense | 2,515 | 1,164 | 3,679 |
| Cash payments | (2,784) | (1,750) | (4,534) |
| Balance at September 30, 2021 | <u>\$ 1,212</u> | <u>\$ 281</u> | <u>\$ 1,493</u> |

Substantially all of our planned activities under the Restructuring Plan are complete and as part of our final steps, we expect to potentially incur remaining pre-tax charges in the range of \$1.5 million to \$3.5 million through the first half of fiscal year 2023. We have reduced our total headcount by approximately 390 employees. The Company expects to make concluding cash payments of approximately \$1.5 million in the remainder of fiscal year 2022, primarily consisting of remaining severance and related benefits.

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Purchase Commitments — We enter into purchase commitments for products and services in the ordinary course of business. These purchases generally cover production requirements for 60 to 120 days as well as materials necessary to service customer units through the product lifecycle and for warranty commitments. As of September 30, 2022, we had approximately \$46.2 million in purchase commitments that are expected to be delivered within the next 12 months. To ensure adequate component availability, as of September 30, 2022, we also had \$6.6 million in long-term commitments for purchases to be delivered after 12 months.

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

U.S. Government Contracting Matter — We have sold our products and related services to the U.S. Government (the “Government”) under General Services Administration (“GSA”) Federal Supply Schedule contracts (the “GSA Contracts”) since 2002 and are currently selling our products and related services to the Government under two such GSA Contracts. Each GSA Contract is subject to extensive legal and regulatory requirements and includes, among other provisions, a price reduction clause (the “Price Reduction Clause”), which generally requires us to reduce the prices billed to the Government under the GSA Contracts to correspond to the lowest prices billed to certain benchmark customers.

Late in the fourth quarter of 2018, during an internal review we preliminarily determined that certain of our pricing practices may have resulted in the Government being overcharged under the Price Reduction Clauses of the GSA Contracts (the “GSA Matter”). As a result, we performed remediation efforts, including but not limited to, the identification of additional controls and procedures to ensure future compliance with the pricing and other requirements of the GSA Contracts. We also retained outside legal counsel and forensic accountants to assist with these efforts and to conduct a comprehensive review of our pricing and other practices under the GSA Contracts (the “Review”). On February 14, 2019, we reported the GSA Matter to the GSA and its Office of Inspector General.

Effective as of February 25, 2021, as a result of the review, we entered into a settlement agreement with the GSA. Pursuant to the settlement agreement, we agreed to, among other things, pay to the GSA \$12.3 million in full and final satisfaction of any and all claims, causes of actions, appeals and the like, including damages, costs, attorney’s fees and interest arising under or related to the GSA Matter. As of September 30, 2022, we no longer have any outstanding liability related to this matter.

NOTE 13 – LEASES

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

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

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

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

The components of lease expense were as follows:

| | Three Months Ended September 30, 2022 | Three Months Ended September 30, 2021 | Nine Months Ended September 30, 2022 | Nine Months Ended September 30, 2021 |
|-------------------------------|--|--|---|---|
| Operating lease cost | \$ 1,805 | \$ 2,010 | \$ 5,453 | \$ 5,901 |
| Finance lease cost: | | | | |
| Amortization of ROU assets | 18 | 60 | \$ 96 | \$ 221 |
| Interest on lease liabilities | 4 | 5 | \$ 15 | \$ 14 |
| Total finance lease cost | \$ 22 | \$ 65 | \$ 111 | \$ 235 |

We recognize lease payments made for short-term leases where terms are 12 months or less as the payments are incurred. Our short-term lease costs for the three months ended September 30, 2022 and September 30, 2021 were both less than \$0.1 million. Our short-term lease costs for the nine months ended September 30, 2022 and September 30, 2021 were both \$0.1 million.

Supplemental balance sheet information related to leases was as follows:

| | As of September 30, 2022 | As of December 31, 2021 |
|--|-----------------------------|----------------------------|
| Operating leases: | | |
| Operating lease right-of-use assets | \$ 18,404 | \$ 22,543 |
| Current operating lease liabilities | \$ 5,363 | \$ 5,601 |
| Operating lease liabilities - less current portion | 14,225 | 18,538 |
| Total operating lease liabilities | \$ 19,588 | \$ 24,139 |
| Finance leases: | | |
| Property and equipment, at cost | \$ 1,415 | \$ 1,380 |
| Accumulated depreciation | (1,312) | (1,222) |
| Property and equipment, net | \$ 103 | \$ 158 |
| Current finance lease liabilities | \$ 169 | \$ 137 |
| Finance lease liabilities - less current portion | 119 | 110 |
| Total finance lease liabilities | \$ 288 | \$ 247 |
| Weighted Average Remaining Lease Term (in years): | | |
| Operating leases | 5.01 | 5.69 |
| Finance leases | 1.97 | 2.12 |
| Weighted Average Discount Rate: | | |
| Operating leases | 5.67 % | 5.67 % |
| Finance leases | 5.35 % | 5.02 % |

Supplemental cash flow information related to leases was as follows:

| | Nine Months Ended September 30, 2022 | Nine Months Ended September 30, 2021 |
|--|---|---|
| Cash paid for amounts included in the measurement of lease liabilities: | | |
| Operating cash flows from operating leases | \$ 5,686 | \$ 5,874 |
| Operating cash flows from finance leases | \$ 15 | \$ 14 |
| Financing cash flows from finance leases | \$ 172 | \$ 229 |
| ROU assets obtained in exchange for lease obligations: | | |
| Operating leases | \$ 808 | \$ 1,209 |

Maturities of lease liabilities are as follows:

| Year Ending December 31, | Operating leases | Finance leases |
|-------------------------------------|------------------|----------------|
| 2022 (excluding the first 6 months) | \$ 1,673 | \$ 49 |
| 2023 | 6,105 | 170 |
| 2024 | 4,826 | 61 |
| 2025 | 3,074 | 12 |
| 2026 | 2,075 | 8 |
| Thereafter | 4,984 | 2 |
| Total lease payments | \$ 22,737 | \$ 302 |
| Less imputed interest | (3,149) | (14) |
| Total | \$ 19,588 | \$ 288 |

NOTE 14 – INCOME TAXES

For the three months ended September 30, 2022, we recorded an income tax expense of \$0.6 million compared with an income tax benefit of \$1.7 million for the three months ended September 30, 2021. Our effective tax rate was 10.3% for the three months ended September 30, 2022 compared with 30.1% in the prior year period. The tax rate for 2022 reflects a tax expense on a pre-tax loss and the tax rate for 2021 reflects a tax benefit on a pre-tax loss. The change in our income tax expense and our effective tax rate were primarily due to the impact of the capitalization of research and development (“R&D”) expenditures for income tax purposes. The Tax Cuts and Jobs Act (the “Act”) requires the capitalization and amortization of R&D costs incurred after December 31, 2021. We have considered the effects of the Act on the forecasted domestic cash tax payments for the year ending December 31, 2022. Our entity in the United States remains in a full valuation allowance position, hence we were not able to recognize the tax benefits associated with the capitalization of these R&D expenditures.

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

NOTE 15 - BUSINESS COMBINATIONS

On September 1, 2022, we completed the acquisition of UK-based GeoSLAM, a leading provider of mobile scanning solutions with proprietary high-productivity simultaneous localization and mapping (SLAM) software. We believe this acquisition enables the Company to provide mobile scanning solutions using SLAM software to create 3D models for use in Digital Twin applications. We believe these newly acquired capture technologies integrate into our 4D digital reality-based SaaS offering that will allow customers to access multiple 4D data sources for visualization and analysis through a single user experience. We acquired all voting equity interests of GeoSLAM held by the previous owners. The results of GeoSLAM’s operations as of and after the date of acquisition have been included in our condensed consolidated financial statements as of and for the period ended September 30, 2022. The total purchase price included \$29 million of cash paid, net of cash acquired and a non-cash payment of 495,562 shares of FARO stock valued at \$15.9 million that is subject to customary lock-up provisions for a total purchase price of \$44.9 million.

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

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

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

The goodwill arising from the acquisition consists largely of the expected synergies from combining operations as well as the value of the workforce. This goodwill is not tax deductible. Acquisition and integration costs are not included as components of consideration transferred, but are recorded as expense in the period in which such costs are incurred. As of September 30, 2022, we have incurred \$2.4 million of acquisition or integration costs for the GeoSLAM acquisition. Accounts receivable acquired represent a gross contractual amount of \$2.6 million of which we expect to collect \$2.5 million. We believe that the fair value of these receivables approximates the net book value given their short term nature. Pro forma financial results for GeoSLAM have not been presented because the effects of these transactions, individually and in the aggregate, were not material to our condensed consolidated financial results.

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

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

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

The following information should be read in conjunction with the condensed consolidated financial statements, including the notes thereto, included elsewhere in this Quarterly Report on Form 10-Q and Management’s Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2021.

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

FARO Technologies, Inc. (“FARO,” the “Company,” “us,” “we” or “our”) has made “forward-looking statements” in this report within the meaning of the Private Securities Litigation Reform Act of 1995. Statements that are not historical facts or that describe our plans, beliefs, goals, intentions, objectives, projections, expectations, assumptions, strategies, or future events are forward-looking statements. In addition, words such as “may,” “might,” “would,” “will,” “will be,” “future,” “strategy,” “believe,” “plan,” “should,” “could,” “seek,” “expect,” “anticipate,” “intend,” “estimate,” “goal,” “objective,” “project,” “forecast,” “target” and similar words identify forward-looking statements.

Forward-looking statements are not guarantees of future performance and are subject to a number of known and unknown risks, uncertainties, assumptions, and other factors that could cause actual results to differ materially from those expressed or implied by such forward-looking statements. Consequently, undue reliance should not be placed on these forward-looking statements. These forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q. We do not intend to update any forward-looking statements, whether as a result of new information, future events, or otherwise, unless otherwise required by law. Important factors that could cause actual results to differ materially from those contemplated in such forward-looking statements include, among others, the following:

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

- risks associated with expanding international operations, such as difficulties in staffing and managing foreign operations, increased political and economic instability, compliance with potentially evolving import and export regulations, and the burdens and potential exposure of complying with a wide variety of U.S. and foreign laws and labor practices;
- changes in trade regulation, which result in rising prices of imported steel, steel byproducts, aluminum and aluminum byproducts and various other raw materials that we use in the production of measurement devices, and our ability to pass those costs on to our customers or require our suppliers to absorb such costs;
- changes in foreign regulation which may result in rising prices of our measurement devices sold as exports to our international customers, our customers' willingness to absorb incremental import tariffs, and the corresponding impact on our profitability;
- our inability to successfully identify and acquire target companies and achieve expected benefits from, and effectively integrate acquisitions that are consummated;
- our inability to realize the intended benefits of the technology, products, operations, contracts, and personnel of our acquisitions;
- the cyclical nature of the industries of our customers and material adverse changes in our customers' access to liquidity and capital;
- changes in the potential for the computer-aided measurement market and the potential adoption rate for our products, which are difficult to quantify and predict;
- our inability to protect our patents and other proprietary rights in the United States and foreign countries;
- our inability to defend against a cyberattack, security or other data breach of our systems may compromise the confidentiality, integrity, or availability of our internal data and the availability of our products and websites designed to support our customers or their data;
- our inability to adequately maintain effective internal controls over financial reporting;
- fluctuations in our annual and quarterly operating results and the inability to achieve our financial operating targets as a result of a number of factors including, without limitation (i) litigation and regulatory action brought against us, (ii) quality issues with our products, (iii) excess or obsolete inventory, shrinkage or other inventory losses due to product obsolescence, change in demand for our products, scrap or material price changes, (iv) raw material price fluctuations and other inflationary pressures, (v) expansion of our manufacturing capability, (vi) the size and timing of customer orders, (vii) the amount of time that it takes to fulfill orders and ship our products, (viii) the length of our sales cycle to new customers and the time and expense incurred in further penetrating our existing customer base, (ix) manufacturing inefficiencies associated with new product introductions, (x) costs associated with new product introductions, such as product development, marketing, assembly line start-up costs and low introductory period production volumes, (xi) the timing and market acceptance of new products and product enhancements, (xii) customer order deferrals in anticipation of new products and product enhancements, (xiii) the inability of our sales and marketing programs to achieve their sales targets, (xiv) start-up costs associated with opening new sales offices outside of the United States, (xv) fluctuations in revenue without proportionate adjustments in fixed costs, (xvi) inefficiencies in the management of our inventories and fixed assets, (xvii) compliance with government regulations including health, safety, and environmental matters, and (xviii) costs associated with the training and ramp-up time for new sales people;
- changes in gross margins due to a changing mix of products sold and the different gross margins on different products and sales channels;
- changes in applicable laws, rules or regulations, or their interpretation or enforcement, or the enactment of new laws, rules or regulations that apply to our business operations or require us to incur significant expenses for compliance;
- our inability to successfully comply with the requirements of the Restriction of Hazardous Substances Directive and the Waste Electrical and Electronic Equipment Directive in the European Union;
- the inability of our products to displace traditional measurement devices and attain broad market acceptance;
- the impact of competitive products and pricing on our current offerings;
- the loss of any of our executive officers or other key personnel which may include an inability to competitively address inflationary pressures on employee compensation and flexibility in employee work arrangements;
- difficulties in recruiting research and development engineers, application engineers, or other key personnel;

- the failure to effectively manage the effects of any future growth;
- the impact of reductions or projected reductions in government spending, or uncertainty regarding future levels of government expenditures, particularly in the defense sector;
- variations in our effective income tax rate, which makes it difficult to predict our effective income tax rate on a quarterly and annual basis, and the impact of the U.S. Tax Cuts and Jobs Act of 2017 on the global intangible low-taxed income of foreign subsidiaries;
- the loss of key suppliers and the inability to find sufficient alternative suppliers in a reasonable period of time or on commercially reasonable terms;
- the impact of fluctuations in exchange rates on non-U.S. dollar-denominated revenues and expenses which could materially effect our reported financial results;
- the effect of estimates and assumptions with respect to critical accounting policies and the impact of the adoption of recently issued accounting pronouncements;
- the effect of changes in political conditions in the U.S. and other countries in which we operate, including the effect of changes in U.S. trade policies or the United Kingdom's withdrawal from the European Union, on general market conditions, global trade policies and currency exchange rates;
- the magnitude of increased warranty costs from new product introductions and enhancements to existing products;
- the sufficiency of our plants and third-party resources to meet manufacturing requirements;
- the continuation of our share repurchase program;
- the sufficiency of our working capital and cash flow from operations to fund our short- and long-term liquidity requirements;
- the impact of geographic changes in the manufacturing or sales of our products on our effective income tax rate;
- our ability to comply with the requirements for favorable tax rates in foreign jurisdictions
- our ability to effectively integrate the operations from Holobuilder, Inc. and UK-based GeoSLAM, including the intellectual property acquired; and
- other risks and uncertainties discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2021, elsewhere in this Quarterly Report on Form 10-Q, and in other SEC filings.

Moreover, new risks and uncertainties emerge from time to time, and we undertake no obligation to update publicly or review the risks and uncertainties included in this Quarterly Report on Form 10-Q, unless otherwise required by law.

Overview

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

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

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

Prior to the end of the second quarter of 2022, we manufactured our FARO Quantum Max Arm products in our manufacturing facility located in Florida for customer orders from North America and South America (the “Americas”) and Europe, the Middle East and Africa (“EMEA”), and in our manufacturing facility located in Singapore for customer orders from the Asia-Pacific region (“APAC”). We manufactured our FARO Focus laser scanner in our manufacturing facilities located in Germany for customer orders from EMEA and APAC, and in our manufacturing facility located in Pennsylvania for customer orders from the Americas. We manufactured our FARO Laser Tracker and our FARO Laser Projector products in our manufacturing facility located in Pennsylvania.

Under the manufacturing services agreement dated July 15, 2021 and in connection with the Restructuring Plan described below, Sanmina now provides manufacturing services for our measurement device products previously manufactured by us at the aforementioned manufacturing facilities. The phased transition to a Sanmina production facility was completed at the beginning of the third quarter of 2022 as part of our cost reduction initiative. The facilities which previously housed our manufacturing function are currently under evaluation for a reduction in occupancy. All of these facilities are mixed-use spaces with our service, research and development, or sales teams, and are in use for those functions. We expect our third party manufacturing facilities to have the production capacity necessary to support our volume requirements for the remainder of 2022.

We account for wholly-owned foreign subsidiaries in the currency of the respective foreign jurisdiction; therefore, fluctuations in exchange rates may have an impact on the value of the intercompany account balances denominated in different currencies and reflected in our consolidated financial statements. We are aware of the availability of off-balance sheet financial instruments to hedge exposure to foreign currency exchange rates, including cross-currency swaps, forward contracts and foreign currency options. No such instruments were utilized by the Company in 2021 or the nine months ended September 30, 2022. We have not used hedging instruments in the past as fluctuations in exchange rate on our revenue were mostly offset by those same fluctuations in exchange rate on our expenses, providing a natural hedge in foreign jurisdictions. Our exchange rate exposure may change as a result of our current or future operational strategies and we will continue assessing the appropriateness of hedging for our business.

Restructuring Plan

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

On July 15, 2021, we entered into a manufacturing services agreement (the “Agreement”) with Sanmina Corporation (Nasdaq: SANM) (“Sanmina”), in connection with the Restructuring Plan. Under the Agreement, Sanmina will provide manufacturing services for the Company’s measurement device products previously manufactured by the Company at the Company’s Lake Mary, Florida, Exton, Pennsylvania, and Stuttgart, Germany manufacturing sites. This phased transition to a Sanmina production facility was completed at the beginning of the third quarter of 2022 as part of our cost reduction initiative. We are currently evaluating these manufacturing sites with the intention to reduce our leased floor space. However, all of these facilities are mixed-use spaces shared with our service, research and development, or sales teams who continue to use these spaces. The Company, in collaboration with third party lessors and architectural resources, intends to conduct studies over the feasibility of abandoning or demising leased floor space against our current needs. Our current needs continue to include access to existing spaces previously constructed to closely monitor temperature and vibration for our service and research and development teams. The conclusion of this evaluation and any subsequent approval to abandon or reduce these leased spaces would be considered as a change in the manner of the use of these corresponding assets, and thereby will be evaluated for impairment. We expect to complete this evaluation before the first half of fiscal year 2023. As of September 30, 2022, the remaining value of leasehold improvements for these facilities is approximately \$3 million and a portion of this may be impaired, if the Company decides to reduce or abandon the leased space. Separately, we may also incur additional charges for the modification of leases for these facilities.

Substantially all of our planned activities under the Restructuring Plan are complete and as part of our final steps, we expect to potentially incur remaining pre-tax charges in the range of \$1.5 million to \$3.5 million through the first half of fiscal year 2023. We have reduced our total headcount by approximately 390 employees. The Company expects to make concluding cash payments of approximately \$1.5 million in the remainder of fiscal year 2022, primarily consisting of remaining severance and related benefits.

FARO Sphere and the Unified Software Environment

FARO Sphere is our new cloud-based platform that is the foundation to our new software and solution strategy. Our objective is to provide differentiated value by offering workflow enhancements which include data uploads from any location, access to our existing suite of 3D software applications, cloud-based data analysis and global user access as well as ultimately, the ability for our customers to purchase, renew or manage all of their FARO software and hardware assets. FARO Sphere represents the first step in the expansion of our cloud-based software offerings that we believe will deliver greater value to our customers and to our shareholders. The FARO Sphere platform can be adopted globally across a wide range of markets, including construction management, facilities, operations and maintenance, robotic simulation and incident preplanning. If FARO Sphere is adopted widely, we would expect this to lead to an increase in the number of users and thus enable revenue growth of our software and a shift toward increased levels of recurring revenue over time. We launched FARO Sphere to the market on April 12, 2022.

Revenue from our current software products was \$10.6 million and \$11.0 million for the three months ended September 30, 2022 and September 30, 2021, respectively, and \$31.4 million and \$31.4 million for the nine months ended September 30, 2022 and September 30, 2021, respectively. Our recurring revenue which is comprised of hardware service contracts, software maintenance contracts, and subscription-based software applications was \$16.6 million and \$16.3 million for the three months ended September 30, 2022 and September 30, 2021, respectively, and \$50.2 million and \$47.6 million for the nine months ended September 30, 2022 and September 30, 2021, respectively.

Research and development costs incurred relating to the development of internal-use software and website development, including software used to upgrade and enhance our websites and applications to be sold as a service are capitalized in the period incurred and amortized over 1 year to 5 years. These costs include external direct costs of materials and services and internal costs such as payroll and benefits of those employees directly associated with the development of new functionality in internal use software to be sold as a service. The amount of costs capitalized relating to internally developed computer software to be sold as a service was \$1.3 million and \$1.1 million for the three months ended September 30, 2022 and September 30, 2021, respectively, and \$4.5 million and \$2.1 million for the nine months ended September 30, 2022 and September 30, 2021, respectively. Cash paid relating to these development costs are included as an investing activity within the Cash paid for technology development, patents and licenses line of our condensed consolidated statement of cash flows.

Acquisitions

On June 4, 2021, we acquired all of the outstanding shares of Holobuilder, Inc. (“Holobuilder”), a company focused on 3D photogrammetry-based technology for a purchase price of \$33.8 million, net of cash acquired. This acquisition enables us to provide reality-capture photo documentation and added remote access capability for industries such as construction management further expanding our Digital Twin solution portfolio. The results of Holobuilder’s operations as of and after the date of acquisition have been included in our condensed consolidated financial statements as of and for the period ended September 30, 2022.

On September 1, 2022, we completed the acquisition of UK-based GeoSLAM, a leading provider of mobile scanning solutions with proprietary high-productivity simultaneous localization and mapping (SLAM) software for a purchase price of \$29 million cash paid, net of cash acquired and a non-cash payment of 495,562 shares of FARO stock valued at \$15.9 million that is subject to customary lock-up provisions for a total purchase price of \$44.9 million. We believe this acquisition enables the Company to provide mobile scanning solutions using SLAM software to create 3D models for use in Digital Twin applications. We believe these newly acquired capture technologies integrate into our 4D digital reality-based SaaS offering that will allow customers to access multiple 4D data sources for visualization and analysis through a single user experience. The results of GeoSLAM’s operations as of and after the date of acquisition have been included in our condensed consolidated financial statements as of and for the period ended September 30, 2022.

Results of Operations

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

| (dollars in thousands) | Three months ended September 30, | | | | Nine months ended September 30, | | | |
|-------------------------------------|----------------------------------|------------|------------|------------|---------------------------------|------------|------------|------------|
| | 2022 | % of Sales | 2021 | % of Sales | 2022 | % of Sales | 2021 | % of Sales |
| Sales | | | | | | | | |
| Product | \$ 65,581 | 76.9 % | \$ 57,838 | 73.1 % | \$ 182,015 | 75.2 % | \$ 172,748 | 72.7 % |
| Service | 19,751 | 23.1 % | 21,331 | 26.9 % | 59,891 | 24.8 % | 64,862 | 27.3 % |
| Total sales | 85,332 | 100.0 % | 79,169 | 100.0 % | 241,906 | 100.0 % | 237,610 | 100.0 % |
| Cost of sales | | | | | | | | |
| Product | 30,375 | 35.6 % | 25,650 | 32.4 % | 82,879 | 34.3 % | 75,909 | 31.9 % |
| Service | 11,692 | 13.7 % | 11,188 | 14.1 % | 34,299 | 14.2 % | 33,481 | 14.1 % |
| Total cost of sales | 42,067 | 49.3 % | 36,838 | 46.5 % | 117,178 | 48.4 % | 109,390 | 46.0 % |
| Gross profit | 43,265 | 50.7 % | 42,331 | 53.5 % | 124,728 | 51.6 % | 128,220 | 54.0 % |
| Operating expenses | | | | | | | | |
| Selling, general and administrative | 37,226 | 43.6 % | 33,433 | 42.2 % | 108,734 | 44.9 % | 100,375 | 42.2 % |
| Research and development | 12,586 | 14.7 % | 12,731 | 16.1 % | 36,756 | 15.2 % | 36,464 | 15.3 % |
| Restructuring costs | 580 | 0.7 % | 1,376 | 1.7 % | 2,512 | 1.0 % | 3,679 | 1.5 % |
| Total operating expenses | 50,392 | 59.1 % | 47,540 | 60.0 % | 148,002 | 61.2 % | 140,518 | 59.1 % |
| Loss from operations | (7,127) | (8.4)% | (5,209) | (6.6)% | (23,274) | (9.6)% | (12,298) | (5.2)% |
| Other (income) expense | | | | | | | | |
| Interest (income) expense, net | (24) | — % | 5 | — % | (28) | — % | 54 | — % |
| Other (income) expense, net | (1,428) | (1.7)% | 299 | 0.4 % | (3,077) | (1.3)% | (433) | (0.2)% |
| Loss before income tax benefit | (5,675) | (6.7)% | (5,513) | (7.0)% | (20,169) | (8.3)% | (11,919) | (5.0)% |
| Income tax expense (benefit) | 586 | 0.7 % | (1,658) | (2.1)% | 4,352 | 1.8 % | (3,667) | (1.5)% |
| Net loss | \$ (6,261) | (7.3)% | \$ (3,855) | (4.9)% | \$ (24,521) | (10.1)% | \$ (8,252) | (3.5)% |

Consolidated Results

Three Months Ended September 30, 2022 Compared to the Three Months Ended September 30, 2021

Sales. Total sales increased by \$6.1 million, or 7.8%, to \$85.3 million for the three months ended September 30, 2022 from \$79.2 million for the three months ended September 30, 2021, after the impact of foreign exchange rates. Foreign exchange rates had a negative impact on total sales of \$6.9 million, or 8.4%, primarily due to the weakening of the Euro and the Japanese Yen relative to the U.S. dollar in the current period as compared to the foreign exchange rates applicable in the prior period. Total product sales increased by \$7.8 million, or 13.4%, to \$65.6 million for the three months ended September 30, 2022 from \$57.8 million for the three months ended September 30, 2021. Total product sales increased due to an increased global demand of our new Quantum Max Arm, new Focus Laser Scanner, and Vantage Laser Tracker products which were partially offset by the negative impact on sales related to the weakening of the Euro and the Japanese Yen relative to the U.S. dollar during the three months ended September 30, 2022. Service sales decreased by \$1.5 million, or 7.4%, to \$19.8 million for the three months ended September 30, 2022 from \$21.3 million for the three months ended September 30, 2021.

Gross profit. Gross profit increased by \$1.0 million, or 2.2%, to \$43.3 million for the three months ended September 30, 2022 from \$42.3 million for the three months ended September 30, 2021, and gross margin decreased by 2.8 percentage points to 50.7% for the three months ended September 30, 2022 from 53.5% for the three months ended September 30, 2021. Gross margin from product revenue decreased by 2.0 percentage points to 53.7% for the three months ended September 30, 2022 from 55.7% for the prior year period primarily due to changes in product mix and unfavorable price variances due to global supply shortages. We expect continued unfavorable price variances until global supply and cost conditions normalize. Gross margin from service revenue decreased by 6.8 percentage points to 40.8% for the three months ended September 30, 2022 from 47.6% for the prior year period, primarily due to the aforementioned decrease in service sales with relatively consistent fixed costs.

Selling, general and administrative expenses. Selling, general and administrative expenses increased by \$3.8 million, or 11.3%, to \$37.2 million for the three months ended September 30, 2022 from \$33.4 million for the three months ended September 30, 2021. This increase was primarily driven by higher personnel costs resulting from additional headcount obtained primarily from both of our recent acquisitions, base compensation increases and transaction costs for the GeoSLAM acquisition. Selling, general and administrative expenses as a percentage of sales increased by 1.4 percentage points to 43.6% for the three months ended September 30, 2022 from 42.2% for the three months ended September 30, 2021. Our worldwide period-ending selling, general and administrative headcount increased by 42, or 5.6%, to 795 at September 30, 2022, from 753 at September 30, 2021.

Research and development expenses. Research and development expenses decreased by \$0.1 million, or 0.8%, to \$12.6 million for the three months ended September 30, 2022 from \$12.7 million for the three months ended September 30, 2021. Research and development expenses as a percentage of sales decreased to 14.7% for the three months ended September 30, 2022 from 16.1% for the three months ended September 30, 2021.

Restructuring costs. In February 2020, we initiated the Restructuring Plan to improve business effectiveness, streamline operations and achieve a stated target cost level for the Company as a whole. Restructuring costs included in operating expenses decreased by \$0.8 million to \$0.6 million for the three months ended September 30, 2022 from \$1.4 million for the three months ended September 30, 2021 primarily consisting of reduced severance and related benefits charges and professional fees as we conclude the Restructuring Plan and completed our transition to our third party contract manufacturer, Sanmina.

Interest (income) expense, net. We recorded net interest income of less than \$0.1 million for the three months ended September 30, 2022 and net interest expense of less than \$0.1 million for the three months ended September 30, 2021.

Other (income) expense, net. For the three months ended September 30, 2022, other income was \$1.4 million compared with other expense of \$0.3 million for the three months ended September 30, 2021. This change was primarily driven by the effect of foreign exchange rates on our non-U.S. dollar-denominated balance sheet.

Income tax expense (benefit). For the three months ended September 30, 2022 we recorded an income tax expense of \$0.6 million compared with an income tax benefit of \$1.7 million for the three months ended September 30, 2021. Our effective tax rate was 10.3% for the three months ended September 30, 2022 compared with 30.1% in the prior year period. The tax rate for 2022 reflects a tax expense on a pre-tax loss and the tax rate for 2021 reflects a tax benefit on a pre-tax loss. The change in our income tax expense and our effective tax rate were primarily due to the impact of the capitalization of research and development (“R&D”) expenditures for income tax purposes. The Tax Cuts and Jobs Act (the “Act”) requires the capitalization and amortization of R&D costs incurred after December 31, 2021. We have considered the effects of the Act on the forecasted domestic cash tax payments for the year ending December 31, 2022. Our entity in the United States remains in a full valuation allowance position, hence we were not able to recognize the tax benefits associated with the capitalization of these R&D expenditures.

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

Net loss. Our net loss was \$6.3 million for the three months ended September 30, 2022 compared with net loss of \$3.9 million for the prior year period, reflecting the impact of the factors described above.

Nine Months Ended September 30, 2022 Compared to the Nine Months Ended September 30, 2021

Sales. Total sales increased by \$4.3 million, or 1.8%, to \$241.9 million for the nine months ended September 30, 2022 from \$237.6 million for the nine months ended September 30, 2021, after the impact of foreign exchange rates. Foreign exchange rates had a negative impact on total sales of \$13.8 million, or 8.7%, primarily due to the weakening of the Euro and the Japanese Yen relative to the U.S. dollar in the current period as compared to the foreign exchange rates applicable in the prior period. Total product sales increased by \$9.3 million, or 5.4%, to \$182.0 million for the nine months ended September 30, 2022 from \$172.7 million for the nine months ended September 30, 2021 due to global demand of our new Quantum Max Arm products. Service sales decreased by \$5.0 million, or 7.7%, to \$59.9 million for the nine months ended September 30, 2022 from \$64.9 million for the nine months ended September 30, 2021.

Gross profit. Gross profit decreased by \$3.5 million, or 2.7%, to \$124.7 million for the nine months ended September 30, 2022 from \$128.2 million for the nine months ended September 30, 2021 and gross margin decreased by 2.4 percentage points to 51.6% for the nine months ended September 30, 2022 from 54.0% for the nine months ended September 30, 2021. Gross margin from product revenue decreased by 1.6 percentage points to 54.5% for the nine months ended September 30, 2022 from 56.1% for the prior year period, primarily due to unfavorable cost variances as a result of global supply shortages. We expect continued unfavorable price variances until global supply and cost conditions normalize. Gross margin from service revenue decreased by 5.7 percentage points to 42.7% for the nine months ended September 30, 2022 from 48.4% for the prior year period, primarily due to the aforementioned decrease in service sales with relatively consistent fixed costs.

Selling, general and administrative expenses. Selling, general and administrative expenses increased by \$8.3 million, or 8.3%, to \$108.7 million for the nine months ended September 30, 2022 from \$100.4 million for the nine months ended September 30, 2021. This increase was primarily driven by higher personnel costs resulting from additional headcount obtained primarily from both of our recent acquisitions, base compensation increases and transaction costs for the GeoSLAM acquisition. Selling, general and administrative expenses as a percentage of sales increased by 2.7 percentage points to 44.9% for the nine months ended September 30, 2022, compared with 42.2% of sales for the nine months ended September 30, 2021. Our worldwide period-ending selling headcount increased by 42, or 5.6%, to 795 at September 30, 2022, from 753 at September 30, 2021.

Research and development expenses. Research and development expenses increased by \$0.3 million, or 0.8%, to \$36.8 million for the nine months ended September 30, 2022 from \$36.5 million for the nine months ended September 30, 2021. This increase was primarily driven by higher compensation expense resulting from increased engineering headcount and costs to accelerate new product development and from our acquisition of Holobuilder. Research and development expenses as a percentage of sales decreased to 15.2% for the nine months ended September 30, 2022 from 15.3% for the nine months ended September 30, 2021.

Restructuring costs. In February 2020, we initiated the Restructuring Plan to improve business effectiveness, streamline operations and achieve a stated target cost level for the Company as a whole. Restructuring costs included in operating expenses decreased by \$1.2 million to \$2.5 million for the nine months ended September 30, 2022 from \$3.7 million for the nine months ended September 30, 2021 primarily consisting of reduced severance and related benefits charges and professional fees as we conclude the Restructuring Plan and completed our transition to our third party contract manufacturer, Sanmina.

Interest (income) expense, net. For the nine months ended September 30, 2022, we recorded interest income of less than \$0.1 million compared with interest expense of less than \$0.1 million for the nine months ended September 30, 2021.

Other (income) expense, net. For the nine months ended September 30, 2022, other income was \$3.1 million compared to other income of \$0.4 million for the nine months ended September 30, 2021. This change was primarily driven by the effect of foreign exchange rates on our non-U.S. dollar-denominated balance sheet.

Income tax expense (benefit). For the nine months ended September 30, 2022, we recorded an income tax expense of \$4.4 million compared with income tax benefit of \$3.7 million for the nine months ended September 30, 2021. Our effective tax rate was 21.6% for the nine months ended September 30, 2022 compared with 30.8% in the prior year period. The tax rate for 2022 reflects a tax expense on a pre-tax loss and the tax rate for 2021 reflects a tax benefit on a pre-tax loss. The change in our income tax expense and our effective tax rate were primarily due to the impact of the capitalization of research and development ("R&D") expenditures for income tax purposes. The Tax Cuts and Jobs Act (the "Act") requires the capitalization and amortization of R&D costs incurred after December 31, 2021. We have considered the effects of the Act on the forecasted domestic cash tax payments for the year ending December 31, 2022. Our entity in the United States remains in a full valuation allowance position, hence we were not able to recognize the tax benefits associated with the capitalization of these R&D expenditures.

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

Net loss. Our net loss was \$24.5 million for the nine months ended September 30, 2022 compared to \$8.3 million for the prior year period, reflecting the impact of the factors described above.

Liquidity and Capital Resources

Cash and cash equivalents decreased by \$73.5 million to \$48.5 million at September 30, 2022 from \$122.0 million at December 31, 2021. The decrease was primarily driven by net cash used in investing activities.

Cash used in operating activities was \$18.2 million during the nine months ended September 30, 2022, compared to \$15.6 million of cash used in operating activities during the nine months ended September 30, 2021. The increase was due to a larger current year net loss and changes in working capital accounts, primarily consisting of an increase in other current assets originating from our relationship with our third party contract manufacturer, Sanmina.

Cash used in investing activities during the nine months ended September 30, 2022 was \$43.2 million compared to cash used in investing activities of \$40.7 million during the nine months ended September 30, 2021. The increase was primarily due to the acquisition of GeoSLAM and higher cash paid for technology development, patents, and licenses during the nine months ended September 30, 2022, compared to the acquisition of Holobuilder and lower cash paid for technology development, patents, and licenses during the nine months ended September 30, 2021.

Cash used in financing activities was \$1.8 million during the nine months ended September 30, 2022 compared to cash provided by financing activities of \$1.5 million for the nine months ended September 30, 2021. The decrease was primarily due to lower proceeds from the issuance of stock related to stock option exercises during the nine months ended September 30, 2022, compared to during the nine months ended September 30, 2021.

Of our cash and cash equivalents, \$41.3 million was held by foreign subsidiaries as of September 30, 2022. On December 22, 2017, the United States enacted the U.S. Tax Cuts and Jobs Act, resulting in significant modifications to existing tax law, which included a transition tax on the mandatory deemed repatriation of foreign earnings. As a result of the U.S. Tax Cuts and Jobs Act, the Company can repatriate foreign earnings and profits to the U.S. with minimal U.S. income tax consequences, other than the transition tax and global intangible low-taxed income (“GILTI”) tax. We have reinvested a large portion of our undistributed foreign earnings and profits in acquisitions and other investments and intends to bring back a portion of foreign cash in certain jurisdictions where we will not be subject to local withholding taxes and which were subject already to transition tax and GILTI tax.

On November 24, 2008, our Board of Directors approved a \$30.0 million share repurchase program. Acquisitions for the share repurchase program may be made from time to time at prevailing prices, as permitted by securities laws and other legal requirements, and subject to market conditions and other factors. The share repurchase program may be discontinued at any time. There is no expiration date or other restriction governing the period over which we can repurchase shares under the program. In October 2015, our Board of Directors authorized an increase to the existing share repurchase program from \$30.0 million to \$50.0 million. We made no stock repurchases during the nine-month period ended September 30, 2022 under this program. As of September 30, 2022, we had authorization to repurchase \$18.3 million remaining under the repurchase program.

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

We have no off-balance sheet arrangements.

Contractual Obligations and Commercial Commitments

We enter into purchase commitments for products and services in the ordinary course of business. These purchases generally cover production requirements for 60 to 120 days as well as materials necessary to service customer units through the product lifecycle and for warranty commitments. As of September 30, 2022, we had \$46.2 million in purchase commitments that are expected to be delivered within the next 12 months. We also had \$6.6 million in long-term commitments for purchases to be delivered after 12 months. Other than as described in the preceding sentences, there have been no material changes to the contractual obligations and commercial commitments table included in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2021.

Critical Accounting Policies

The preparation of our condensed consolidated financial statements requires our management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, as well as disclosure of contingent assets and liabilities. We base our estimates on historical experience, along with various other factors believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Some of these judgments can be subjective and complex and, consequently, actual results may differ from these estimates under different assumptions or conditions. A discussion of our critical accounting policies is included in Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our Annual Report on Form 10-K for the year ended December 31, 2021, as filed with the Securities and Exchange Commission on February 16, 2022. As of September 30, 2022, our critical accounting policies have not changed from those described in our Annual Report on Form 10-K for the year ended December 31, 2021.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Foreign Exchange Exposure

We conduct a significant portion of our business outside the United States. As of and for the nine months ended September 30, 2022, 59% of our revenue was invoiced, and a significant portion of our operating expenses and manufacturing costs were paid, in foreign currencies, and 30% of our assets were denominated in foreign currencies. Fluctuations in exchange rates between the U.S. dollar and such foreign currencies may have a material effect on our results of operations and financial condition and could specifically result in foreign exchange gains and losses. The impact of future exchange rate fluctuations on the results of our operations cannot be accurately predicted due to our constantly changing exposure to various currencies, and the fact that all foreign currencies do not react in the same manner in relation to the U.S. dollar. Our most significant exposures are to the Euro, Japanese Yen, Swiss Franc, Chinese Yuan and Brazilian Real. To the extent that the percentage of our non-U.S. dollar revenues derived from international sales increases in the future, our exposure to risks associated with fluctuations in foreign exchange rates may increase.

Global Inflation Exposure

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

Item 4. Controls and Procedures

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

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

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of September 30, 2022. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2022 to provide reasonable assurance that information required to be disclosed in this Quarterly Report on Form 10-Q was recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and was accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

During the quarter ended September 30, 2022, there was no change in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

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

Item 1A. Risk Factors

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed under “Risk Factors” in this Item 1A and in our Annual Report on Form 10-K for the year ended December 31, 2021 as filed with the SEC, before deciding to invest in, or retain, shares of our common stock. These risks and uncertainties could materially and adversely affect our business, financial condition, and results of operations. The risks described in our Annual Report on Form 10-K for the year ended December 31, 2021 and in subsequent periodic reports filed with the SEC are not the only risks we face. Our operations could also be affected by additional factors that are not presently known by us or by factors that we currently consider to be immaterial to our business. There have been no material changes in our risk factors from those set forth in our Annual Report on Form 10-K for the year ended December 31, 2021, other than as set forth below.

The risk factors entitled “*Because a significant portion of our revenues and expenses are denominated in foreign currencies, we face significant exposure to foreign exchange rate risk*” and “*Increases in the cost and constraints in the availability of raw materials or components used in our products could negatively impact our business and profitability*” have been updated to read as follows:

Because a significant portion of our revenues, expenses, and assets are denominated in foreign currencies, we face significant exposure to foreign exchange rate risk.

We conduct a significant portion of our business outside the United States and consequently much of our revenues, expenses and assets are denominated in foreign currencies, most notably the Euro, Japanese Yen, Swiss Franc, Chinese Yuan and Brazilian Real. Our results of operations are affected by fluctuations in exchange rates, which have caused, and may in the future cause, significant fluctuations in our quarterly and annual results of operations. Fluctuations in exchange rates may have a material adverse effect on our results of operations and financial condition and could result in potentially significant foreign exchange gains and losses. The impact of future exchange rate fluctuations on the results of our operations cannot be accurately predicted due to our constantly changing exposure to various currencies, and the fact that all foreign currencies do not react in the same manner in relation to the U.S. dollar. Additionally, currency fluctuations could require us to increase prices to foreign customers, which could result in lower net sales by us to those customers. If we do not adjust the prices for our products in response to unfavorable currency fluctuations, we could be forced to sell our products at a lower margin or at a net loss. To the extent that the percentage of our non-U.S. dollar revenues derived from international sales increases in the future, our exposure to risks associated with fluctuations in foreign exchange rates will increase. We are aware of the availability of off-balance sheet financial instruments to hedge exposure to foreign currency exchange rates, including cross-currency swaps, forward contracts and foreign currency options; however, we have not used such instruments in the past as fluctuations in exchange rate on our revenue were mostly offset by those same fluctuations in exchange rate on our expenses, providing a natural hedge in foreign jurisdictions. Our exchange rate exposure may change as a result of our current or future operational strategies and we will continue assessing the appropriateness of hedging for our business.

Increases in the cost and constraints in the availability of raw materials or components used in our products could negatively impact our business and profitability.

Our products contain various raw materials, including steel, steel byproducts, aluminum, aluminum byproducts, resin products and various electronic components. We use raw materials directly in manufacturing and in components that we purchase from our suppliers. These raw materials are subject to extensive laws, governmental regulations, policies, including tariffs and other import restrictions, inflationary pressures, exchange rate fluctuations and supply shortages. Some of the raw materials are obtained from suppliers outside the United States, and to the extent that the quantity or proportion of materials derived from such foreign suppliers increases in the future, our exposure to tariffs and other import restrictions, supply chain disruptions and exchange rate fluctuations may increase. The occurrence and impact of future changes in laws, governmental regulations, policies, inflationary pressures, exchange rate fluctuations and supply shortages cannot be accurately predicted. Changes to the laws, governmental regulations and policies governing these raw materials, including tariffs and other import restrictions, have increased and could continue to increase the cost of such raw materials and, correspondingly, the cost of manufacturing our products. Further, interruptions in global supply chains, inflationary pressures and exchange rate fluctuations have increased and could continue to increase the cost of such raw materials, and have constrained and could continue to constrain the availability of such raw materials. If the costs of our raw materials further increase, whether due to changes in laws, governmental regulations, policies, supply shortages or for other reasons, we may not be able to pass on these costs to our customers, which could have a material adverse effect on our business, results of operations and financial condition. Even in the event that increased costs can be substantially passed through to our customers, our gross margin percentages would decline.

The following risk factor has been added:

Inflation in the global economy could negatively impact our business and results of operations.

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

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

Recent Sales of Unregistered Securities

Rajani Ramanathan was automatically granted restricted stock units equal to an aggregate total of 3,189 shares of the Company's common stock in connection with her appointment to our Board of Directors on July 25, 2022 pursuant to our 2022 Equity Incentive Plan, which was approved at our 2022 annual meeting of shareholders and our Company's Non-Employee Director Compensation Policy (the "Initial Director Grant"). The Initial Director Grant shall vest on July 25, 2025, subject to the director's continued service on our Board of Directors as of such date.

During the quarter ended June 30, 2022, we also issued restricted stock units equal to an aggregate total of 1,986 shares of the Company's common stock to certain employees (the "Employee Grants"). The Employee Grants shall vest in three equal annual installments on the anniversary dates of each respective grant.

The restricted stock units were granted in accordance with Section 4(a)(2) of the Securities Act of 1933, as amended. The shares underlying these restricted stock units were registered on a Form S-8 registration statement subsequent to the granting of such awards.

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

On November 24, 2008, our Board of Directors approved a \$30.0 million share repurchase program. Acquisitions for the share repurchase program may be made from time to time at prevailing prices, as permitted by securities laws and other legal requirements, and subject to market conditions and other factors. The share repurchase program may be discontinued at any time. There is no expiration date or other restriction governing the period over which we can repurchase shares under the program. In October 2015, our Board of Directors authorized an increase to the existing share repurchase program from \$30.0 million to \$50.0 million. We made no stock repurchases during the nine month period ended September 30, 2022 under this program. As of September 30, 2022, we had authorization to repurchase \$18.3 million remaining under the repurchase program.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

None.

Item 6. Exhibits

EXHIBIT INDEX

| Exhibit Number | Exhibit Description | Incorporated by Reference | | | | Provided Herewith |
|------------------------|---|---------------------------|-----------|---------|--------------------|-------------------|
| | | Form | File No. | Exhibit | Filing Date | |
| 3.1 | Amended and Restated Articles of Incorporation, as amended | S-1/A | 333-32983 | 3.1 | September 10, 1997 | |
| 3.2 | Amended and Restated Bylaws | 10-K | 0-23081 | 3.2 | February 16, 2022 | |
| 4.1 | Specimen Stock Certificate | S-1/A | 333-32983 | 4.1 | September 10, 1997 | |
| 10.1* | Key Executive Change in Control and Severance Plan | | | | | X |
| 31.1 | Certification of the President and Chief Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | | | | | X |
| 31.2 | Certification of the Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | | | | | X |
| 32.1** | Certification of the President and Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | | | | | X |
| 32.2** | Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | | | | | X |
| 101.SCH | Inline XBRL Taxonomy Extension Schema Document | | | | | |
| 101.CAL | Inline XBRL Taxonomy Extension Calculation Linkbase Document | | | | | |
| 101.LAB | Inline XBRL Taxonomy Extension Label Linkbase Document | | | | | |
| 101.PRE | Inline XBRL Taxonomy Presentation Linkbase Document | | | | | |
| 101.DEF | Inline XBRL Taxonomy Extension Definition Linkbase Document | | | | | |
| 104 | Cover Page Interactive Data File (formatted as inline XBRL with applicable taxonomy extension information contained in Exhibits 101.*) | | | | | |

* - Indicates management contracts or compensatory plans or arrangements.

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

SIGNATURE

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

FARO Technologies, Inc.

(Registrant)

Date: November 2, 2022

By: /s/ Allen Muhich

Name: Allen Muhich

Title: Chief Financial Officer

(Duly Authorized Officer and Principal Financial Officer)

FARO TECHNOLOGIES, INC.
KEY EXECUTIVE CHANGE IN CONTROL AND SEVERANCE PLAN

1. **Introduction.** This Key Executive Change in Control and Severance Plan (the “**Plan**”) has been adopted by FARO Technologies, Inc. (the “**Company**”), effective as of October 25, 2022 (the “**Effective Date**”), in order to secure the continued services of certain key executives of the Company and its Subsidiaries and to ensure their continued dedication to their duties, notwithstanding the possibility or occurrence of an involuntary termination including without limitation in connection with a Change in Control. The Plan is established in order to provide certain severance benefits to eligible employees of the Company Group who both incur a Qualifying Termination and otherwise meet the terms and conditions of the Plan, as set forth below.

2. **Definitions.** As used in this Plan, the following terms shall have the respective meanings set forth below:

2.1. “**Administrator**” means the “administrator” of the Plan, as defined in Section 3(16)(A) of ERISA. As of the Effective Date, the Administrator is the Company, acting through the Board or its authorized delegate, or any person to whom the Administrator has delegated any authority or responsibility with respect to the Plan pursuant to Section 10, but only to the extent of such delegation.

2.2. “**Base Salary**” means the Participant’s annual rate of base salary.

2.3. “**Board**” means the Board of Directors of the Company.

2.4. “**Cause**” means (a) the failure of the Participant to perform substantially the Participant’s duties with the Company Group (excluding any such failure resulting from the Participant’s Disability) after a written demand for substantial performance is delivered to the Participant by or on behalf of the Administrator which identifies the manner in which the Administrator believes that the Participant has not substantially performed the Participant’s duties and providing the Participant a minimum of thirty (30) days to cure the identified deficiencies; (b) the Participant engaging in illegal conduct or gross misconduct that is materially injurious to any member of the Company Group (or the Company Group as a whole), (c) the Participant engaging in conduct or misconduct that materially harms the reputation or financial position of any member of the Company Group (or the Company Group as a whole), (d) the Participant obstructing, impeding or failing to materially cooperate with an investigation authorized by the Board (provided that the Participant shall be given written notice and a reasonable opportunity to cure any alleged breach of this clause (d)), (e) the Participant being convicted of, or pleading *nolo contendere* to, a felony or of a crime involving fraud, dishonesty, violence or moral turpitude, (f) the Participant being found liable in any SEC or other civil or criminal securities law action, (g) the Participant committing an act of fraud or embezzlement against any member of the Company Group, or (h) the Participant accepting a bribe or kickback.

2.5. “**Change in Control**” means the occurrence of any one of the following events:

(a) the sale of all or substantially all of the assets of the Company on a consolidated basis to an unrelated person or entity,

(b) a merger, reorganization or consolidation pursuant to which the holders of the Company’s outstanding voting power and outstanding stock immediately prior to such transaction do not own a majority of the outstanding voting power and outstanding stock or other equity interests of the resulting or successor entity (or its ultimate parent, if applicable) immediately upon completion of such transaction,

(c) the sale of all of the Stock of the Company to an unrelated person, entity or group thereof acting in concert,

(d) any other transaction in which the owners of the Company's outstanding voting power immediately prior to such transaction do not own at least a majority of the outstanding voting power of the Company or any successor entity immediately upon completion of the transaction other than as a result of the acquisition of securities directly from the Company; or

(e) individuals who, as of the Effective Date, constitute the Board (the "**Incumbent Directors**") cease for any reason to constitute at least a majority of the Board or other governing body or entity of the Company, its successor or survivor, provided that any person becoming a director subsequent to the Effective Date but prior to any Sale Event, whose election or nomination for election was approved or recommended by a vote of a majority of the Incumbent Directors then on the Board (either by a specific vote or by approval of the proxy statement of the Company in which such person is named as a nominee for director, without written objection to such nomination), shall be an Incumbent Director; provided, however, that no individual initially elected or nominated as a director of the Company as a result of an actual or threatened election contest with respect to directors or as a result of any other actual or threatened solicitation of proxies or consents by or on behalf of any person other than the Board shall be deemed to be an Incumbent Director.

Notwithstanding the foregoing, a Change in Control shall not be deemed to occur solely because any person acquires beneficial ownership of a majority of the Company Voting Securities as a result of the acquisition of Company Voting Securities by the Company or its affiliates which reduces the number of Company Voting Securities outstanding; provided, that if after the consummation of such acquisition by the Company such person becomes the beneficial owner of additional Company Voting Securities that increases the percentage of outstanding Company Voting Securities beneficially owned by such person, a Change in Control of the Company shall then occur.

Notwithstanding the foregoing, for purposes of this Change in Control definition, a transaction will not be deemed a Change in Control unless the transaction qualifies as a change in control event within the meaning of Section 409A. Further and for the avoidance of doubt, a transaction will not constitute a Change in Control if: (x) its sole purpose is to change the jurisdiction of the Company's incorporation, or (y) its sole purpose is to create a holding company that will be owned in substantially the same proportions by the persons who held the Company's securities immediately before such transaction.

2.6. "**Change in Control Period**" means, unless defined otherwise in a Participant's Participation Agreement, the period beginning on (and inclusive of) the day that is ninety (90) days prior to a Change in Control and ending on (and inclusive of) the day that is twelve (12) months following such Change in Control.

2.7. "**Code**" means the U.S. Internal Revenue Code of 1986, as amended. Reference to a specific section of the Code or regulation under the Code will include such section or regulation, and any valid regulation or other formal guidance of general or direct applicability promulgated under such section, and any comparable provision of any future legislation amending, supplementing or superseding such section or regulation.

2.8. "**Company**" means FARO Technologies, Inc., a Florida corporation, and any successor, survivor, or other entity that succeeds to the interests of FARO Technologies, Inc.

2.9. "**Company Group**" means the Company and any of its Subsidiaries.

2.10. "**Deferred Payment**" means any Severance Benefits to be paid or provided to a Participant pursuant to this Plan and any other severance payments or separation benefits to be

paid or provided to such Participant, that in each case, when considered together, are considered deferred compensation under Section 409A.

2.11. **"Disability"** has the same meaning ascribed to that term in Section 409A(a)(2)(C) of the Code. The Administrator will determine whether a Participant has incurred a Disability based on such evidence as the Administrator deems necessary or advisable. The Administrator's determination as to a Participant's Disability will be final and binding.

2.12. **"Eligible Employee"** means an employee who is a member of a "select group of management or highly compensated employees" (within the meaning of Sections 201(2), 301(a)(3) and 401(a)(1) of ERISA) of the Company Group and who both has (a) been designated by the Administrator, in its sole discretion from time to time, as eligible to participate in the Plan, and (b) been provided a Participation Agreement under the Plan by the Administrator. For purposes of clarity, an Eligible Employee becomes a Participant only by satisfying the additional requirements for participation set forth in the Plan (including without limitation executing and timely returning the applicable Participation Agreement to the Administrator as described in Section 2.17).

2.13. **"Employer"** means, with respect to an individual employed by the Company Group, the member of the Company Group that directly employs such individual.

2.14. **"ERISA"** means the U.S. Employee Retirement Income Security Act of 1974, as amended. Reference to a specific section of ERISA will include such section, and any valid regulation or other formal guidance of general or direct applicability promulgated under such section, and any comparable provision of any future legislation amending, supplementing or superseding such section or regulation.

2.15. **"Exchange Act"** means the U.S. Securities Exchange Act of 1934, as amended.

2.16. **"Good Reason"** means, without the Participant's express written consent, the occurrence of any of the following events after a Change in Control:

(a) an ongoing material diminution in the duties or responsibilities of the Participant that is inconsistent in any material and adverse respect with the Participant's position(s), duties, or responsibilities with the Company Group immediately prior to such Change in Control; provided, however, that Good Reason shall not be deemed to occur upon a change in duties or responsibilities that is solely and directly a result of the Company no longer being a publicly traded entity and does not involve any other event set forth in this Section 2.18;

(b) a material reduction in the Participant's annual base salary as in effect immediately prior to such Change in Control;

(c) a material reduction in the Participant's cash bonus opportunities in the aggregate under the Company Group's applicable incentive plan, as in effect from immediately prior to such Change in Control;

(d) the Company Group requiring the Participant to be based at any office or location more than fifty (50) miles from the office where the Participant is located at the time of the Change in Control and, as a result, causing the Participant's commute from the Participant's residence at the time of the Change in Control to the new location to increase by more than fifty (50) miles; or

(e) the failure of the Company to obtain the assumption of the Company's obligations hereunder from any successor as contemplated in Section 14;

provided, however, that the occurrence of any of the foregoing events in this Section 2.18 shall constitute Good Reason only if the Company Group fails to cure such event within thirty (30) days after receipt from the Participant of written notice of such occurrence and the Participant's resignation from employment with the Company Group as a result of such event(s) occurs no later than ninety (90) days following the expiration of such cure period; provided, further, that Good Reason shall cease to exist after ninety (90) days following its occurrence, unless the Participant has given the Company written notice thereof prior to such date. The Participant's right to terminate employment for Good Reason shall not be affected by the Participant's incapacities due to mental or physical illness and the Participant's continued employment shall not constitute consent to, or a waiver of rights with respect to, any event or condition constituting Good Reason.

2.17. "**Participant**" means each Eligible Employee who has executed and timely returned a the Participant's Participation Agreement to the Administrator, as specified therein.

2.18. "**Participation Agreement**" means the individual agreement delivered by the Administrator to an employee of the Company Group who, upon such delivery, otherwise qualifies as an Eligible Employee under the Plan. A form of Participation Agreement is attached hereto as Appendix A. For purposes of clarity, in the event that a Participant has entered into more than one Participation Agreement, only the Participation Agreement most recently entered into and timely returned to the Administrator will be deemed the applicable Participation Agreement for such Participant. Further, for the avoidance of doubt, any description in the Participation Agreement of the payments and benefits that may become payable to such Participant under the Plan, including, but not limited to, the amount of such payments and benefits, at all times is subject to the terms and conditions of the Plan. In the event of any conflict, the Plan terms will govern.

2.19. "**Person**" means any individual, firm, partnership, corporation, or other entity, including any successor (by merger or otherwise) of such entity, or a group of any of the foregoing acting in concert.

2.20. "**Qualifying Termination**" means a termination of the Participant's employment with the Company Group as described in Sections 4.1 and 4.2 that qualifies the Participant for eligibility to receive Severance Benefits under the Plan.

2.21. "**SEC**" means the U.S. Securities and Exchange Commission.

2.22. "**Section 409A**" means Code Section 409A and the Treasury Regulations and guidance thereunder, and any applicable state law equivalent, as each may be promulgated, amended or modified from time to time.

2.23. "**Separation from Service**" means the date a Participant separates from service from the Company Group within the meaning of, and applying the default rules of, the regulations promulgated under Section 409A.

2.24. "**Severance Benefits**" means the separation-related compensation and other benefits that a Participant will be provided in Section 4.1 or Section 4.2 (and Section 5.2, as applicable) and such Participant's Participation Agreement.

2.25. "**Subsidiary**" means any corporation or other entity in which the Company has a direct or indirect ownership interest of 50% or more of the total combined voting power of the then-outstanding securities or interests of such corporation or other entity entitled to vote generally in the election of directors (or members of any similar governing body) or in which the Company has the right to receive 50% or more of the distribution of profits or 50% of the assets or liquidation or dissolution.

2.26. **"Target Bonus Amount"** means a Participant's annual (or annualized, as applicable) target cash bonus opportunity for the year in which the Participant's Qualifying Termination occurs, or if greater, the Participant's annual (or annualized, as applicable) target cash bonus opportunity in effect as of immediately prior to the completion of the Change in Control.

3. **Eligibility for Severance Benefits.** A Participant is eligible for Severance Benefits under the Plan, as described in Section 4, only if such Participant is an Eligible Employee on the date the Participant experiences a Qualifying Termination and otherwise satisfies the requirements of the Plan.

4. **Severance Benefits Upon Qualifying Termination.**

4.1. **Qualifying Termination Outside of Change in Control Period.** If, other than during the Change in Control Period, the Participant's employment with the Company Group is terminated by the Company Group other than for Cause and not due to the Participant's death or Disability, then, solely to the extent specifically provided in the Participant's Participation Agreement, the Participant will receive the following Severance Benefits, subject to Sections 5 through 7 and 18 through 20:

4.1.1. **Cash Severance Benefit.** A single lump sum cash payment for the amount set forth in the Participant's Participation Agreement; and

4.1.2. **COBRA Benefit.** If the Participant and any spouse and/or other dependents of the Participant ("**Family Members**") have coverage under the group health plan(s) sponsored by a member of the Company Group on the day immediately before the date of the Participant's Qualifying Termination (such coverage, "**Qualifying Health Coverage**"), either reimbursement for the payments the Participant makes, or direct payments by the Company (or Employer, as applicable) to the applicable provider, at the Company's election, of the premiums for medical, vision and dental coverage for the Participant and the Participant's eligible dependents under Title X of the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended or comparable applicable state law ("**COBRA**") (such reimbursements or direct payments, the "**COBRA Severance**"), for the period set forth in the Participant's Participation Agreement or until Participant has secured other employment that provides group health insurance coverage, whichever occurs first, subject to Participant timely electing COBRA coverage, remaining eligible for COBRA continuation coverage and, with respect to reimbursements, timely paying for COBRA coverage. Any COBRA reimbursements under this Plan will be made by the Company to Participant consistent with the Company's normal expense reimbursement policy, provided further that Participant timely submits documentation to the Company substantiating the Participant's payments for COBRA coverage.

4.1. **Qualifying Termination During Change in Control Period.** If, during the Change in Control Period, the Participant's employment with the Company Group is terminated either (x) by the Company Group other than for Cause and not due to the Participant's death or Disability, or (y) by the Participant for Good Reason, then, solely to the extent specifically provided in the Participant's Participation Agreement, the Participant will receive the following Severance Benefits, subject to Sections 5 through 7 and 18 through 20:

4.2.1. **Cash Severance Benefit.** A single lump sum cash payment for the amount set forth in the Participant's Participation Agreement; and

4.2.2. **COBRA Benefit.** If the Participant and any Family Members have Qualifying Health Coverage, COBRA Severance for the period set forth in the Participant's Participation Agreement or until Participant has secured other employment that provides group health insurance coverage, whichever occurs first, and subject to Participant timely electing COBRA coverage, remaining eligible for COBRA continuation coverage and, with respect to reimbursements, timely paying for COBRA coverage. Any COBRA reimbursements under this Plan will be made by the

Company to Participant consistent with the Company's normal expense reimbursement policy, provided further that Participant submits documentation to the Company substantiating his or her payments for COBRA coverage.

5. **Conditions to Receipt of Severance Benefits.**

5.1. **Release Requirement.** Notwithstanding any contrary Plan provision, as a condition to receiving any Severance Benefits, a Participant will be required to sign and not revoke a separation agreement and release of claims in a form reasonably satisfactory to the Company (the "**Release**"). In all cases, the Release must become effective and irrevocable no later than the sixtieth (60th) day following the Participant's Qualifying Termination (the "**Release Deadline Date**"). If the Release does not become effective and irrevocable by the Release Deadline Date, the Participant will forfeit any right to receive any and all Severance Benefits. In no event will any Severance Benefits be paid or provided until the Release becomes effective and irrevocable. A Participant's receipt of Severance Benefits under the Plan will be subject to the Participant continuing to comply with the provisions of the Participant's Release, including that Participant will agree to refrain from any disparagement, defamation, libel or slander of the Company Group or any of its current and former employees, directors, officers, affiliates, or successors, and will agree to refrain from any tortious interference with the contracts and relationships of such parties. Any Severance Benefits will terminate immediately for a Participant if the Participant at any time, violates the Participant's Release, and Participant will be obligated to repay all Severance Benefits paid or provided to the Participant.

5.2. **COBRA Severance Limitations.** If the Company determines in its sole discretion that it cannot provide COBRA Severance to a Participant without potentially violating, or being subject to an excise tax under, applicable law (including, without limitation, Section 2716 of the Public Health Service Act), then in lieu of such COBRA Severance, subject to any delay required by Section 19 below, the Company will provide to such Participant a taxable monthly payment payable on the last day of a given month (except as provided by the last sentence in this Section 5.2), in an amount equal to two (2) times the monthly COBRA premium that would be required to continue coverage under the Company's group health, dental and vision care plans for the Participant and the Participant's eligible dependents, as applicable, as in effect on the date of the Qualifying Termination, in each case, which amount will be based on the premium rates applicable for the first month of COBRA Severance for the Participant and any eligible dependents of the Participant (each, a "**COBRA Replacement Payment**"), and which COBRA Replacement Payments will be made regardless of whether the Participant elects COBRA continuation coverage and will end on the earlier of (a) the date upon which the Participant obtains other employment, or (b) the date the Company has paid an amount totaling the number of COBRA Replacement Payments equal to the number of months in the applicable COBRA Severance period set forth in the Participant's Participation Agreement with respect to such COBRA Severance to be provided pursuant to Section 4.1.2 or Section 4.2.2, as applicable. For the avoidance of doubt, the COBRA Replacement Payments may be used for any purpose, including, but not limited to continuation coverage under COBRA, and will be subject to any applicable withholdings. Notwithstanding anything to the contrary under the Plan, if the Company determines in its sole discretion at any time that it cannot provide the COBRA Replacement Payments without violating applicable law (including, without limitation, Section 2716 of the Public Health Service Act), the Participant will not receive the COBRA Replacement Payments or any further COBRA Severance.

6. **Payment Timing.** Provided that a Participant's Release becomes effective and irrevocable by the Release Deadline Date and subject to Section 19 and the terms of the Participant's Participation Agreement, (a) any Severance Benefits payable in a lump sum will be paid, or in the case of installments, will commence, on the sixtieth (60th) day following the Participant's Qualifying Termination (the "**Payment Date**"), and (b) any Severance Benefits otherwise payable to the Participant during the period immediately following the Participant's Qualifying Termination through the Payment Date will be paid in a lump sum to the Participant on the Payment Date, with any

remaining payments to be made as provided in the Plan or the Participant's Participation Agreement, as applicable.

7. Nonduplication; Mitigation; Certain Other Limitations.

7.1. Nonduplication of Severance Benefits Within the Plan. For purposes of clarity, in the event of a Qualifying Termination that occurs during the Change in Control Period but prior to the Change in Control, any Severance Benefits (including any COBRA Replacement Payments, as applicable) to be provided to a Participant under Section 4.2 will be reduced by any amounts that already were provided to the Participant under Section 4.1 and no further amounts will be provided to the Participant under Section 4.1.

7.2. Prior Benefits. Except as otherwise specifically set forth in a Participant's Participation Agreement or Section 7.4, (a) the payments and benefits, if any, provided under this Plan (i) will be the exclusive benefits for such Participant related to a termination of such Participant's employment with the Company Group (or any member thereof) and (ii) will supersede and replace any severance and/or change in control payments and benefits set forth in any offer letter, employment or severance agreement, and/or other agreement between the Participant and the Company or Employer (including without limitation any Participation Agreement previously entered into between the Participant and the Company), as applicable, in effect as of the date the Participant enters into a Participation Agreement, and (b) upon becoming a Participant, the Participant's participation in the Plan will supersede and replace eligibility to participate in any other severance and/or change in control plan, program, policy or arrangement, of the Company, Employer or other member of the Company Group.

7.3. Other Benefits. Except as set forth in Section 7.4, if a Participant is entitled to any cash severance, continued health coverage benefits, or other severance or separation benefits similar to those provided under the Plan, by operation of applicable law or under a plan, program, policy, contract, or arrangement sponsored by any member of the Company Group or to which any member of the Company Group is a party other than this Plan ("**Other Benefits**"), then the corresponding severance payments and benefits under Plan will be reduced by the amount of Other Benefits paid or provided to the Participant.

7.4. Equity Awards. Notwithstanding Sections 7.2 and 7.3 or any other provision of the Plan to the contrary, any vesting, payments, or acceleration of vesting or payments, under any awards granted to a Participant under the Company's 2014 Equity Incentive Plan, 2022 Equity Incentive Plan, or similar or successor equity compensation plan ("**Equity Awards**"), will not be subject to reduction under the Plan and each such Equity Award will remain subject to the terms of the plan and award agreement under which the Equity Award was granted and any other applicable written agreement between the Company and the Participant governing the terms of the such Equity Award.

7.5. Indebtedness. If a Participant is indebted to the Company Group on the date of the Qualifying Termination, the Company Group reserves the right to offset the payment of any Severance Benefits otherwise payable under the Plan by the amount of such indebtedness. However, such offset will be made only to the extent permitted under applicable laws (as determined by the Administrator in its discretion).

7.6. No Duty to Mitigate. Except with respect to any reductions specifically set forth in the Plan, Participants will not be required to mitigate the amount of any Severance Benefits contemplated by the Plan, nor will any payment be reduced by any earnings that a Participant may receive from any other source.

8. No Enlargement of Employment Rights. Neither the establishment or maintenance or amendment of the Plan, nor the making of any benefit payment hereunder, will be construed to confer upon any individual any right to continue to be an employee of the Company Group or any

affiliates thereof. The Company and the applicable Employers expressly reserve the right to discharge any of their employees at any time and for any reason, with or without cause or notice, as permitted by applicable law. However, as described in the Plan, a Participant may be entitled to payments and benefits under the Plan depending upon the circumstances of the termination of the Participant's employment.

9. Notice.

9.1. **Addresses.** For purposes of this Plan, all notices and other communications required or permitted hereunder (other than with respect to notices or communications under Section 21 which shall be provided in accordance with the terms of such Section) shall be in writing and shall be deemed to have been duly given (a) upon actual delivery to the party to be notified, (b) upon transmission by email, (c) 24 hours after confirmed facsimile transmission, (d) one (1) business day after deposit with a recognized overnight courier, (e) three (3) business days after deposit with the United States postal service by first class certified or registered mail, return-receipt requested, postage prepaid, addressed as follows:

If to the Participant: the address listed as the Participant's address in the Company's personnel files.

If to the Company:

FARO Technologies, Inc.
Attention: Administrator of FARO Technologies, Inc. Key Executive Change in Control and Severance Plan
250 Technology Park
Lake Mary, FL 32746

or to such other address as either party may have furnished to the other in writing in accordance herewith, except that notices of change of address shall be effective only upon receipt.

9.2. **Notice for Termination of Employment.** A written notice of the date of termination of Participant's employment with the Company Group by the Company or the Participant, as the case may be, to the other, shall (a) indicate the specific termination provision in this Plan relied upon, (b) to the extent applicable, set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of the Participant's employment under the provision so indicated and (c) specify the date of termination, which date shall be not less than fifteen (15) nor more than sixty (60) days after the giving of such notice (except as provided otherwise in Section 2.18). The failure by the Participant or the Company to set forth in such notice any fact or circumstance which contributes to a showing of Good Reason or Cause shall not waive any right of the Participant or the Company hereunder or preclude the Participant or the Company from asserting such fact or circumstance in enforcing the Participant's or the Company's rights hereunder.

10. **Interpretation and Administration.** The Plan will be administered, interpreted and operated by the Administrator, in its sole discretion. The Administrator will have the exclusive right and full discretion to (a) interpret the Plan, (b) designate the management or highly compensated employees of the Company Group who are eligible to participate in the Plan and to provide Participation Agreements to any such Eligible Employees, (c) decide any and all matters arising under the Plan or any Participation Agreement (including the right to remedy possible ambiguities, inconsistencies, or omissions), (d) make, amend and rescind such rules as it deems necessary or appropriate for the proper administration of the Plan, and (e) make all other determinations and resolve all questions of fact necessary or advisable for the administration of the Plan, including eligibility for any benefit or payment under the Plan. Any decision made or other action taken by the Administrator (or its authorized delegates) with respect to the Plan, and any interpretation by the Administrator (or its authorized delegates) of any term or condition of the Plan (including but not limited with respect to whether a Qualifying Termination or a Change in Control has occurred), or

any related document, will be final, conclusive and binding on all persons and be given the maximum possible deference allowed by law. In accordance with Section 2.1, the Administrator (x) in its sole discretion and on such terms and conditions as it may provide, may delegate in writing to one or more officers of the Company all or any portion of its authority or responsibility with respect to the Plan, and (y) has the authority to act for the Company as to any matter pertaining to the Plan. To the extent that the Administrator has delegated administrative authority or responsibility to one or more officers of the Company in accordance with Section 2.1 and this Section 10, each such officer will not be excluded from participating in the Plan if otherwise eligible, but such officer is not entitled to act upon or make determinations regarding any matters pertaining specifically to such officer's own benefit or eligibility under the Plan. The Administrator will act upon and make determinations regarding any matters pertaining specifically to the benefit or eligibility of each such officer under the Plan. The Administrator is the appropriate named fiduciary of the Plan solely for purposes of the Plan's claims and appeal procedures set forth in Section 21.

11. **Effective Date.** The Plan shall be effective as of the Effective Date set forth further above.

12. **Term.** The Plan will become effective upon the Effective Date and will terminate automatically upon the completion of all benefits (if any) under the terms of the Plan.

13. **Amendment or Termination.** The Company, by action of the Board (or its authorized delegate) or the Administrator, reserves the right to amend or terminate the Plan at any time (except as otherwise provided below) and without regard to the effect of the amendment or termination on any Participant or such other person or entity, provided that any such amendment or termination that reduces or alters to the detriment of the Participant the Severance Benefits or other payments and benefits under the Plan or causes the Participant to be no longer eligible for Severance Benefits (a) will not become effective, unless agreed to with the Participant in writing with respect to such Participant's Severance Benefits, to the extent such amendment or termination is adopted after the Participant satisfies the applicable requirements under the Plan and becomes entitled to receive Severance Benefits under the Plan; and (b) for any other Participants, will become effective no earlier than the date six (6) months following written notice of such amendment or termination to Participants. Any amendment or termination of the Plan must be in writing. In addition, notwithstanding the preceding, upon, in connection with or after a Change in Control, the Company, without a Participant's written consent, may neither amend or terminate the Plan in any way nor take any other action under the Plan, which (i) prevents that Participant from becoming eligible for Severance Benefits, or (ii) reduces or alters to the detriment of the Participant the Severance Benefits or other payments and benefits under the Plan, if any, payable, or potentially payable, to such Participant (including, without limitation, imposing additional conditions).

14. **Successors.** Any successor, survivor, or other entity that succeeds to the interests of FARO Technologies, Inc. ("**Company Successor**") will assume the obligations under the Plan and agree expressly to perform the obligations under the Plan in the same manner and to the same extent as the Company would be required to perform such obligations in the absence of a succession. For all purposes under the Plan, the term "Company" will include any Company Successor.

15. **Inalienability.** In no event may any current or former employee of any Employer sell, transfer, anticipate, assign or otherwise dispose of any right or interest under the Plan, except as provided in this Section. Any other attempted assignment, transfer, conveyance, or other disposition of a Participant's right to compensation or other benefits will be null and void. At no time will any of a Participant's rights or interests under the Plan be subject to the claims of creditors nor liable to attachment, execution or other legal process. If any payments or benefits are payable to a Participant who is unable to care for such Participant's affairs, payment may be made directly to the Participant's legal guardian or personal representative. Notwithstanding anything to the contrary in the Plan, if a Participant dies upon or after the Participant's Qualifying Termination and after the Participant (or the authorized representative of the Participant's estate) has timely executed and returned the Release to the Company (without having timely revoked it) but before receiving all of the payments and benefits otherwise payable under the Plan to the Participant, such remaining

payments and benefits instead will be paid to the executor of the Participant's estate, on behalf of the estate, at the time(s) and in the form(s) applicable to such payments and benefits, as applicable, under the Plan.

16. **Applicable Law; Severability.** The provisions of the Plan will be construed, administered and enforced in accordance with ERISA and, to the extent applicable, the internal substantive laws of the State of Florida (but not its conflict of laws provisions). If any provision of the Plan is held invalid or unenforceable, its invalidity or unenforceability will not affect any other provision of the Plan, and the Plan will be construed and enforced as if such provision had not been included.

17. **Type of Plan; Source of Payments.** This Plan is intended to be an unfunded deferred compensation plan as described in Section 2520.104-23 of the U.S. Department of Labor Regulations and will be construed, administered and enforced as such. The Plan will be maintained for Participants at all times in a manner to be considered "unfunded" for purposes of ERISA. Any Severance Benefits will be paid from the general funds of the Company; no separate fund will be established under the Plan, and the Plan will have no assets. No right of any person to receive any payment or benefit under the Plan will be any greater than the right of any other general unsecured creditor of the Company, Employer or any other member of the Company Group or affiliate of any of the foregoing.

18. **Certain Tax Matters.**

18.1. **Withholdings.** The Company and/or Employer (and/or other member of the Company Group or an affiliate of any of the foregoing, as applicable) will have the right and authority to deduct from any payments or benefits all applicable federal, state, local, and/or non-U.S. taxes or other required withholdings and payroll deductions ("**Withholdings**"). Prior to the payment of any amounts or provision of any benefits under this Plan, the Company and/or Employer (and/or other member of the Company Group or an affiliate of any of the foregoing, as applicable) is permitted to deduct or withhold, or require the Participant to remit to the Company Group, an amount sufficient to satisfy any applicable Withholdings with respect to such payments and benefits. Neither the Company, Employer nor any other member of the Company Group or affiliate of any of the foregoing, will have any responsibility, liability or obligation to pay the Participant's taxes arising from or relating to any payments or benefits under this Plan.

18.2. **No Guarantee of Tax Consequences.** Participants (or their beneficiaries) solely will be responsible for any and all taxes with respect to any payments or benefits provided under the Plan. None of the Administrator, the Board, the Company, Employer or any other member of the Company Group or affiliate of any of the foregoing makes any guarantees regarding the tax treatment to any person of any payments or benefits provided under the Plan.

19. **Section 409A.** Notwithstanding anything to the contrary in this Plan or any Participation Agreement, with respect to a Participant who is a U.S. taxpayer or may become a U.S. taxpayer:

19.1. **General.** No Deferred Payments, if any, will be paid or provided until the Participant has a Separation from Service. Similarly, no Severance Benefits payable to a Participant, if any, which otherwise would be exempt from Section 409A pursuant to Treasury Regulation Section 1.409A-1(b)(9), will be payable until the Participant has a Separation from Service.

19.2. **Required Delay.** If a Participant is a "specified employee" within the meaning of Section 409A at the time of the Participant's Separation from Service (other than due to the Participant's death), then the Deferred Payments, if any, that are payable within the first six (6) months following such Separation from Service, will become payable on the date that is six (6) months and one (1) day following the date of such Separation from Service. Any subsequent Deferred Payments under the Plan, if any, will be payable in accordance with the payment schedule applicable to such payment. Notwithstanding anything herein to the contrary, in the event of the Participant's death following the Participant's Separation from Service, but before the date six (6)

months following such Separation from Service, then any payments delayed in accordance with this Section 19.2 will be payable in a lump sum as soon as administratively practicable after the date of the Participant's death and any other Deferred Payment under the Plan will be payable in accordance with the payment schedule applicable to such payment. Each payment, installment and benefit payable under this Plan is intended to constitute a separate payment under Treasury Regulation Section 1.409A-2(b)(2).

19.3. Certain Exemptions. Any amount paid under this Plan that (x) satisfies the requirements of the "short-term deferral" rule set forth in Treasury Regulation Section 1.409A-1(b)(4) or (y) qualifies as a payment made as a result of an involuntary separation from service pursuant to Treasury Regulation Section 1.409A-1(b)(9)(iii) that does not exceed the limit set forth in Treasury Regulation Section 1.409A-1(b)(9)(iii)(A) will not constitute a Deferred Payment for purposes of Section 19.2.

19.4. Interpretation; Other Requirements. The foregoing provisions are intended to comply with or be exempt from the requirements of Section 409A so that none of the Severance Benefits or other payments or benefits to be provided under the Plan will be subject to the additional tax imposed under Section 409A, and any ambiguities and ambiguous terms herein will be interpreted to so comply or be exempt. For purposes of the Plan, to the extent required to be exempt from or comply with Section 409A, any references to Participant's Qualifying Termination or similar phrases relating to the termination of an Participant's employment will be references to the Participant's Separation from Service. Notwithstanding any contrary Plan provision, including but not limited to Section 13, the Company, by action of the Board (or its authorized delegate) or the Administrator, reserves the right to amend the Plan as it deems necessary or advisable, in its sole discretion and without the consent of any Participant or other person or entity, to comply with Section 409A or to avoid income recognition under Section 409A or to otherwise avoid the imposition of additional tax under Section 409A prior to the actual payment or provision of any Severance Benefits or any other payments and benefits hereunder. In no event will Participant have any discretion to choose Participant's taxable year in which any Severance Benefits or any other payments or benefits are provided under this Plan. In no event will any member of the Company Group, any Employer or any affiliate of the Company Group have any responsibility, liability or obligation to reimburse, indemnify or hold harmless Participant for any taxes, penalties or interest that may be imposed, or other costs that may be incurred, as a result of Section 409A.

19.5. Reimbursements. The Participant's rights to payment or reimbursement of expenses pursuant to Section 22 shall be for the duration of the Participant's lifetime. No right to reimbursement of such expenses shall be subject to liquidation or exchange for another benefit, and the amount of expenses eligible for reimbursement pursuant to Section 22 during a Participant's taxable year will not affect the expenses eligible for reimbursement in any other taxable year of the Participant. Any COBRA Severance provided as reimbursements will be paid no later than last day of the second taxable year of the Participant following the taxable year in which the Participant's Separation from Service occurs.

20. Limitation on Payments.

20.1. Reduction of Severance Benefits. If any payment or benefit that Participant would receive from the Company Group, an Employer or any other party whether in connection with the provisions in this Plan or otherwise (the "**Payments**") would (a) constitute a "parachute payment" within the meaning of Section 280G of the Code and (b) but for this sentence, be subject to the excise tax imposed by Section 4999 of the Code (the "**Excise Tax**"), then the Payments will be either delivered in full, or delivered as to such lesser extent that would result in no portion of the Payments being subject to the Excise Tax, whichever of the foregoing amounts, taking into account the applicable federal, state and local income taxes and the Excise Tax, results in Participant's receipt, on an after-tax basis, of the greatest amount of Payments, notwithstanding that all or some of the Payments may be subject to the Excise Tax. If a reduction in Payments is made in accordance with the immediately preceding sentence, the reduction will occur, with respect to the

Payments considered parachute payments within the meaning of Code Section 280G, in the following order: (i) reduction of cash payments in reverse chronological order (that is, the cash payment owed on the latest date following the occurrence of the event triggering the Excise Tax will be the first cash payment to be reduced); (ii) cancellation of equity awards that were granted "contingent on a change in ownership or control" within the meaning of Section 280G of the Code in the reverse order of date of grant of the equity awards (that is, the most recently granted equity awards will be cancelled first); (iii) reduction of the accelerated vesting of equity awards in the reverse order of date of grant of the equity awards (that is, the vesting of the most recently granted equity awards will be cancelled first); and (iv) reduction of employee benefits in reverse chronological order (that is, the benefit owed on the latest date following the occurrence of the event triggering the Excise Tax will be the first benefit to be reduced). In no event will Participant have any discretion with respect to the ordering of Payment reductions. Participant will be solely responsible for the payment of all personal tax liability that is incurred as a result of the payments and benefits received under this Plan, and neither the Company nor any Employer or other affiliate of the Company will have any responsibility, liability or obligation to reimburse, indemnify or hold harmless any Participant for any of those payments of personal tax liability.

20.2. Determination of Excise Tax Liability. Any determinations required under this Section 20 will be made in writing by a nationally recognized accounting or valuation firm (the "**Firm**") selected by the Company, whose determinations will be conclusive and binding upon Participant and the Company for all purposes. For purposes of making the calculations required by this Section 20, the Firm may make reasonable assumptions and approximations concerning applicable taxes and may rely on reasonable, good faith interpretations concerning the application of Sections 280G and 4999 of the Code. The Company and Participant will furnish to the Firm such information and documents as the Firm reasonably may request in order to make determinations under this Section 20. The Company will bear the costs and make all payments required to be made to the Firm for the Firm's services that are rendered in connection with any calculations contemplated by this Section 20. Neither the Company, Employer nor any other member of the Company or any affiliate of the foregoing will have any liability to Participant for the determinations of the Firm.

21. Claims and Review Procedures.

21.1. General. Any Participant who believes the Participant is entitled to but has not received a benefit or payment under the Plan or disagrees with the determination of the amount of any Plan benefit or payment or any other decision regarding the Participant's interest under the Plan (or the Participant's duly authorized legal representative) (the "**Claimant**") must submit such claim (the "**Claim**") in writing to the Administrator at the following address within ninety (90) days after the date the Claimant first knew or should have known of the facts on which the Claim is based, unless the Administrator consents otherwise in writing or ERISA provides otherwise: FARO Technologies, Inc., Attention: Administrator of the FARO Technologies, Inc. Key Executive Change in Control and Severance Plan, 250 Technology Park, Lake Mary, FL 32746. The Claim must set forth the nature of the benefit claimed, the amount of such benefit and the basis for claiming entitlement to such benefit.

21.2. Non-Disability Benefit Claims.

(a) **Claims Procedure.** If a Claimant submits a Non-Disability Benefit Claim (as defined below) to the Administrator in accordance with the requirements set forth in Section 21.1 and such Claim is denied (in full or in part), the Claimant will be provided a written notice of such denial within ninety (90) days after the Administrator's receipt of the Non-Disability Benefit Claim, unless special circumstances require an extension of time (up to ninety (90) more days), in which case written notice of the extension will be given to the Claimant within the initial ninety (90)-day review period. This notice of extension will indicate the special circumstances requiring the extension of time and the date by which the Administrator expects to render its decision on the Non-Disability Benefit Claim. The denial notice will include: (i) the specific reason(s) for the denial; (ii)

references to the specific Plan and/or Participation Agreement provision(s) on which the denial was based; (iii) a description of any additional material or information that is necessary to perfect such Claim and an explanation of why such material or information is necessary; (iv) a description of the Plan's procedures for appealing the denial and the time limits applicable to such procedures; (v) a statement regarding the Claimant's right to bring a civil action under Section 502(a) of ERISA following an adverse benefit determination on appeal pursuant to the Plan's procedures; and (vi) any other information required by ERISA. A "Non-Disability Benefit Claim" means a Claim that does not involve any determination of Disability by the Administrator.

(b) **Appeal Procedure.** If a Claimant's Non-Disability Benefit Claim has been denied by the Administrator under Section 21.2(a), the Claimant may appeal such denial by filing a written request for review of the denial with the Administrator at the address specified in Section 21.1. Such request must be made no later than sixty (60) days following the date the Claimant received the written notice of denial or such later deadline as may be prescribed by ERISA. The Claimant then has the right to review and obtain copies of all documents and other information relevant to the Non-Disability Benefit Claim, upon written request and at no charge, and to submit comments, documents and other information relating to such Claim in writing. If the Claimant files a timely appeal, as described above, the Administrator will provide written notice of its decision on review (whether or not adverse) within sixty (60) days after it received the timely request for review, unless special circumstances require a longer period of time, in which case a decision will be rendered as soon as possible, but not later than one hundred and twenty (120) days after receipt of the timely review request. The Claimant will be given written notice of any such extension before the end of the original sixty (60)-day review period, as well as the special circumstances requiring the extension of time and the date by which the Administrator expects to render its decision. If the Administrator denies the appealed Non-Disability Benefit Claim, the notice of denial will include: (i) the specific reason(s) for the denial; (ii) references to the specific provision(s) of the Plan and/or Participation Agreement on which the denial was based; (iii) a statement that the Claimant will be provided, upon request and free of charge, reasonable access to, and copies of, all documents and other information relevant to such Claim; (iv) a statement regarding the Claimant's right to bring a civil action under Section 502(a) of ERISA following the denial on review pursuant to the Plan's procedures; and (v) any other information required by ERISA.

21.3. Disability Benefit Claims.

(c) **Claims Procedure.** If a Claimant submits a Disability Benefit Claim (as defined below) to the Administrator in accordance with the requirements set forth in Section 21.1 and such Claim is denied (in full or in part), the Claimant will be provided a written notice of such denial within forty-five (45) days after the Administrator's receipt of the Disability Benefit Claim. However, this forty-five (45)-day time period may be extended for up to thirty (30) more days for matters beyond the control of the Administrator, in which case the Claimant will be notified in writing of the extension of time before the end of the initial forty-five (45)-day review period. This notice of extension will indicate the circumstances requiring the extension of time and the date by which the Administrator expects to render its decision on the Disability Benefit Claim. If, before the end of the first thirty (30)-day extension period, the Administrator determines that, due to matters beyond its control, a decision cannot be rendered within that extension period, then the period for making the determination may be extended for up to thirty (30) more days, in which case the Claimant will be notified in writing of the additional extension of time before the end of the initial thirty (30)-day extension period. This notice of extension will indicate the circumstances requiring the additional extension of time and the date by which the Administrator expects to render its decision on the Disability Benefit Claim. Any notice of extension also will explain the standards on which entitlement to the applicable benefit is based, the unresolved issues that prevent a decision on the Disability Benefit Claim, the additional information needed to resolve those issues, and notice that the Claimant will be afforded at least forty-five (45) days within which to provide the specified information. The denial notice will include: (i) the specific reason(s) for the denial; (ii) references to the provision(s) of the Plan and/or Participation Agreement on which the denial was based; (iii) a description of any additional material or information that is necessary to perfect the Disability Benefit

Claim and an explanation of why such material or information is necessary; (iv) a statement that the Claimant will be provided, upon request and free of charge, reasonable access to and copies of, all documents and other information relevant to the Disability Benefit Claim; (v) a description of the Plan's procedures for appealing the denial and the time limits applicable to such procedures; (vi) a statement regarding the Claimant's right to bring a civil action under Section 502(a) of ERISA following an adverse benefit determination on appeal pursuant to the Plan's procedures, including a description of the contractual limitations period that applies to bringing such action, as well as the calendar date on which the contractual limitations period expires; (vii) a copy of any internal rule, guideline, protocol or other similar criteria relied on in denying the Disability Benefit Claim or a statement that such rule, guideline, protocol or other similar criteria do not exist; (viii) a discussion of the Administrator's decision, including an explanation of the Administrator's basis for disagreeing with, or not following, as applicable: (A) the views of the Claimant's treating health care professionals and/or vocational experts who evaluated the Claimant, if provided by the Claimant, (B) the views of medical and/or vocational experts whose advice was obtained on behalf of the Plan in connection with the denial, without regard to whether the Administrator relied upon such advice in making the benefit determination, and (C) the federal Social Security Administration's determination of disability, if provided by the Claimant; and (ix) any other information required by ERISA. A "**Disability Benefit Claim**" means a Claim that involves a determination of Disability by the Plan Administrator.

(a) **Appeal Procedure.** If a Claimant's Disability Benefit Claim has been denied by the Administrator under Section 21.3(a), the Claimant may appeal such denial by filing a written request for review of the denial with the Administrator at the address specified in 21.1. Such request must be made no later than one hundred eighty (180) days following the date the Claimant received the written notice of denial or such later deadline as may be prescribed by ERISA. The Claimant then has the right to review and obtain copies of all documents and other information relevant to the Disability Benefit Claim, upon written request and at no charge, and to submit comments, documents and other information relating to such Claim in writing. If the Claimant files a timely appeal, as described above, the Administrator will provide written notice of its decision on review (whether or not adverse) within forty-five (45) days after it received the timely request for review, unless special circumstances require a longer period of time, in which case a decision will be rendered as soon as possible, but not later than ninety (90) days after receipt of the timely review request. The Claimant will be given written notice of any such extension before the end of the original forty-five (45)-day review period, as well as the special circumstances requiring the extension of time and the date by which the Administrator expects to render its decision. Before any denial on review may be issued, however, the Administrator will provide the Claimant, free of charge, with any new or additional evidence considered, relied upon or generated in connection with the Disability Benefit Claim. Moreover, before any denial on review based on a new or additional rationale may be issued, the Administrator will provide the Claimant, free of charge, with such rationale. Any evidence or rationale will be provided as soon as possible and sufficiently in advance of the date when the Administrator must issue its decision on review to give the Claimant a reasonable opportunity to respond before that date. The review of the appealed Disability Benefit Claim will be conducted by the Administrator (who will not be the individual who decided the initial Disability Benefit Claim nor the subordinate of such individual). In deciding an appeal of any denied Disability Benefit Claim that is based in full or in part on a medical judgment, the Administrator will consult with a health care professional (who will neither be an individual who was consulted in connection with the initial Disability Benefit Claim nor the subordinate of such individual) who has appropriate training and experience in the field of medicine involved in the medical judgment. Any medical or vocational experts whose advice was obtained on behalf of the Administrator in connection with the Disability Benefit Claim will be identified, regardless of whether the advice was relied upon in denying such Claim. If the Administrator denies the appealed Disability Benefit Claim, the denial notice will include: (i) the specific reason(s) for the denial; (ii) references to the provision(s) of the Plan and/or Participation Agreement on which the denial was based; (iii) a statement that the Claimant will be provided, upon request and free of charge, reasonable access to, and copies of, all documents and other information relevant to the Disability Benefit Claim; (iv) a copy of any internal rule, guideline, protocol or other similar criteria relied on in denying the

Disability Benefit Claim or a statement that such rule, guideline, protocol or other similar criteria do not exist; (v) a discussion of the Administrator's decision, including an explanation of the Administrator's basis for disagreeing with, or not following, as applicable: (A) the views of the Claimant's treating health care professionals and/or vocational experts who evaluated the Claimant, if provided by the Claimant, (B) the views of medical and/or vocational experts whose advice was obtained on behalf of the Plan in connection with the denial, without regard to whether the Administrator relied upon such advice in making the benefit determination, and (C) the federal Social Security Administration's determination of disability, if provided by the Claimant; (vi) a statement regarding the Claimant's right to bring a civil action under Section 502(a) of ERISA following an adverse benefit determination on appeal pursuant to the Plan's procedures, including a description of the contractual limitations period that applies to bringing such action, as well as the calendar date on which the contractual limitations period expires; and (vii) any other information required by ERISA. If the Administrator does not strictly adhere to the Plan's claims and appeal procedures for Disability Benefit Claims, as set forth herein (the "**Disability Benefit Claims Procedures**"), the Claimant may be deemed to have exhausted the Plan's administrative remedies and may be able to seek judicial review of the Claimant's Disability Benefit Claim. Such deemed exhaustion does not apply, however, if the Administrator's failure to strictly adhere to the Disability Benefit Claims Procedures was a de minimis violation not likely to cause prejudice or harm to the Claimant and if the other applicable requirements under ERISA are met. The Claimant may request a written explanation of any such violation from the Administrator. Within 10 days of the Claimant's request, the Administrator will provide such explanation, including a specific description of the bases, if any, for asserting that the violation should not cause the Disability Benefit Claims Procedures to be deemed exhausted. A Disability Benefit Claim rejected by a court for immediate review based on deemed exhaustion will be considered refiled under the Plan upon the Administrator's receipt of the court's decision. Within a reasonable time after receipt of the court's decision, the Administrator will provide the Claimant with notice of the Disability Benefit Claim's resubmission.

21.4. Exhaustion of Plan's Claims and Appeal Procedure Required; Limitations on any Legal Actions; Venue.

Exhaustion of the Plan's applicable claims and appeal procedure set forth in this Section 21 is mandatory for resolving any Claim under the Plan before initiating any legal action relating to the Claim. Any legal action with respect to a Claim, if permitted, must be brought (a) no later than six (6) months after the Administrator's denial of such Claim on appeal, regardless of any state or federal statutes establishing provisions relating to limitations on actions, and (b) in the U.S. District Court for the Middle District of Florida. In any such action, all determinations made by the Administrator (and its authorized delegates) in connection with its review of the Claim will be afforded the maximum possible deference permitted by law.

22. Reimbursement of Expenses. With respect to any Severance Benefits payable under Section 4.2, if any contest or dispute shall arise under the Plan involving termination of a Participant's employment with the Company Group or involving the failure or refusal of the Company Group to perform fully in accordance with the terms hereof, subject to Section 19.5, the Company shall reimburse the Participant on a current basis (but in no event later than the end of the calendar year following the calendar year in which the expense was incurred) for all reasonable legal fees and related expenses, if any, incurred by the Participant in connection with such contest or dispute (regardless of the result thereof), together with interest in an amount equal to the prime rate as reported in *The Wall Street Journal*, but in no event higher than the maximum legal rate permissible under applicable law, such interest to accrue thirty (30) days from the date the Company receives the Participant's statement for such fees and expenses through the date of payment thereof, regardless of whether the Participant's claim is upheld by a court of competent jurisdiction or an arbitration panel; provided, however, that the Participant shall be required to repay immediately any such amounts to the Company to the extent that a court or an arbitration panel issues a final and non-appealable order setting forth the determination that the position taken by the Participant was frivolous or advanced by the Participant in bad faith.

23. **Headings.** Headings in the Plan are for purposes of reference only and will not limit or otherwise affect the meaning, construction or interpretation of the Plan's provisions.

24. **Indemnification.** The Company hereby agrees to indemnify and hold harmless the Administrator, the officers and employees of the Company Group, and the members of the Board, from all losses, claims, costs or other liabilities arising from their acts or omissions in connection with the administration, amendment or termination of the Plan, to the maximum extent permitted by applicable law. This indemnity will cover all such liabilities, including judgments, settlements and costs of defense. The Company will provide this indemnity from its own funds to the extent that insurance does not cover such liabilities. This indemnity is in addition to and not in lieu of any other indemnity provided to such person by the Company.

25. **Protected Activity.** Notwithstanding any contrary provision of the Plan or of the Release, nothing in the Plan or the Release shall prohibit or impede a Participant from engaging in any Protected Activity. For purposes of this Plan, "**Protected Activity**" shall mean (i) filing and/or pursuing a charge or complaint with, or otherwise communicating or cooperating with or participating in any investigation or proceeding that may be conducted by, any federal, state or local government agency or commission, including the Securities and Exchange Commission, the Equal Employment Opportunity Commission, the Occupational Safety and Health Administration, and the National Labor Relations Board ("**Government Agencies**"); (ii) discussing the terms, wages, and working conditions of their employment among employees, as protected by applicable law; (iii) disclosing information pertaining to sexual harassment or any unlawful or potentially unlawful conduct, as protected by applicable law. Notwithstanding the foregoing, the Participant agrees to take all reasonable precautions to prevent any unauthorized use or disclosure of any information that may constitute Company confidential information (as defined in the DocuSign Non-Competition and Non-Solicitation Addendum entered into between the Company and the Participant (the "**Proprietary Agreement**") or any other agreement between the Participant and the Company, the Employer or any member of the Company Group or affiliate of any of the foregoing relating to the protection of confidential information) in a manner not protected by applicable law (each, a "**Confidentiality Agreement**"). Protected Activity does not include disclosure of any Company attorney-client privileged communications or attorney work product. Any language in a Participant's Proprietary Agreement or any Confidentiality Agreement that conflicts with, or is contrary to, this paragraph is superseded by this Section 25 of the Plan. Pursuant to the Defend Trade Secrets Act of 2016, (A) an individual shall not be held criminally or civilly liable under any Federal or State trade secret law for the disclosure of a trade secret that is made (i) in confidence to a Federal, state, or local government official or to an attorney solely for the purpose of reporting or investigating a suspected violation of law, or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal, and (B) an individual who files a lawsuit for retaliation by an employer for reporting a suspected violation of law may disclose the trade secret to the attorney of the individual and use the trade secret information in the court proceeding, if the individual files any document containing the trade secret under seal, and does not disclose the trade secret, except pursuant to court order.

IN WITNESS WHEREOF, the Company has executed this Plan on October 25, 2022.

FARO TECHNOLOGIES, INC.
/s/ Michael Burger
Name: Michael Burger
Title: President and Chief Executive Officer

Appendix A
FORM OF
FARO TECHNOLOGIES, INC.
KEY EXECUTIVE CHANGE IN CONTROL AND SEVERANCE PLAN
PARTICIPATION AGREEMENT

FARO Technologies, Inc. (the “**Company**”) is pleased to inform you, **[NAME]**, that you have been selected to participate in the Company’s Key Executive Change in Control and Severance Plan (the “**Plan**”). A copy of the Plan has been delivered to you with this Participation Agreement. Your participation in the Plan is subject to all of the terms and conditions of the Plan, including this Participation Agreement.

In order to actually become a Participant in the Plan, as described in the Plan, you must complete and sign this Participation Agreement and return it to **[NAME]** by no later than **[DATE]**.

The Plan describes in detail certain circumstances under which you, if you are a Participant in the Plan, may become eligible for Severance Benefits [and certain other benefits specified in this Participation Agreement]. Any capitalized term used in this Participation Agreement that is not otherwise defined herein will have the meaning ascribed to such term in the Plan.

As described more fully in Section 4.1 and other sections of the Plan, if you are a Participant in the Plan, and if, other than during the Change in Control Period, your employment with the Company Group is terminated by the Company Group other than for Cause and not due to your death or Disability, then subject to the terms and conditions of the Plan (including the Release requirement), you will receive:

1. **Cash Severance Benefits.** The cash Severance Benefit described in Section 4.1.1 of the Plan in an amount equal to 100% of your Base Salary in effect as of the date of your Qualifying Termination; and
2. **COBRA Benefit.** If you and any of your Family Members have Qualifying Health Coverage, the COBRA Severance described in Section 4.1.2 of the Plan, with the period over which such COBRA Severance will be provided equal to twelve (12) months or until you have secured other employment that provides group health insurance coverage, whichever occurs first.

As described more fully in Section 4.2 and other sections of the Plan, if you are a Participant in the Plan and if, during the Change in Control Period, your employment with the Company Group is terminated either (x) by the Company Group other than for Cause and not due to your death or Disability, or (y) by you for Good Reason, then subject to the terms and conditions of the Plan (including the Release requirement), you will receive:

1. **Cash Severance Benefits.** The cash Severance Benefit described in Section 4.2.1 of the Plan in an amount equal to the sum of:
 - a. 100% of your Base Salary in effect as of the date of your Qualifying Termination, or if greater, your Base Salary in effect as of immediately prior to the completion of the Change in Control (in each case, disregarding any reduction thereto that triggers a Qualifying Termination under clause (b) of the Good Reason definition, as applicable); and
 - b. 100% of your Target Bonus Amount (as defined in Section 2.26 of the Plan) (disregarding any reduction thereto that triggers a Qualifying Termination under clause (c) of the Good Reason definition, as applicable).

2. **COBRA Benefit.** If you and any of your Family Members have Qualifying Health Coverage, the COBRA Severance described in Section 4.2.2 of the Plan, with the period over which such COBRA Severance will be provided equal to twelve (12) months or until you have secured other employment that provides group health insurance coverage, whichever occurs first.

Release Requirement. In order to receive any Severance Benefits for which you otherwise become eligible under the Plan, you must satisfy the other terms and conditions under the Plan, including that you must sign and deliver to the Administrator the Release, which must become effective and irrevocable within the requisite period set forth in the Release and is subject to the Release timing requirements specified in the Plan.

Golden Parachute Limitations. As explained in more detail in the Plan, your Severance Benefits, if any, may be subject to reduction to the extent that, as determined by the applicable accounting or valuation firm retained for purposes of determining any parachute payments, after taking into account certain taxes you may owe, the reduction would result, on an after-tax basis, in the payment of a greater amount to you than if no reduction occurs.

Withholdings. The Company Group has the right to withhold, from any Severance Benefits you may receive under the Plan, any applicable U.S. federal, state, local and non-U.S. taxes required to be withheld and any other payroll deductions.

Other Severance Payments and Benefits. Participation in the Plan does not affect any rights you may have to vesting, payment, or acceleration of vesting or payments under any Equity Awards granted to you by the Company. Such Equity Awards remain subject to the terms and conditions of the applicable plan and award agreement, and any other written agreement between you and the Company governing their terms, and any vesting, payments or acceleration thereof will not constitute Severance Benefits under the Plan.

By your signature below, you and the Company agree that your participation in the Plan is governed by this Participation Agreement and the provisions of the Plan. Your signature below confirms that (1) you have received a copy of the FARO Technologies, Inc. Key Executive Change in Control and Severance Plan; (2) you have carefully read this Participation Agreement and the Plan, including, but not limited to, the terms and conditions for participation in, and receipt of any Severance Benefits under the Plan; and (3) the decisions and determinations by the Administrator under the Plan will be final and binding on you and your successors, and will be given the maximum possible deference permitted by law.

FARO TECHNOLOGIES, INC. **[NAME OF ELIGIBLE EMPLOYEE]**

Signature Signature

Name Date

Title

Attachment: FARO Technologies, Inc. Key Executive Change in Control and Severance Plan

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

I, Michael Burger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of FARO Technologies, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 2, 2022

/s/ Michael Burger

Michael Burger
President and Chief Executive Officer
(Principal Executive Officer)

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

I, Allen Muhich, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of FARO Technologies, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 2, 2022

/s/ Allen Muhich

Allen Muhich
Chief Financial Officer
(Principal Financial Officer)

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

Solely for the purposes of complying with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, the undersigned President and Chief Executive Officer of FARO Technologies, Inc. (the Company), hereby certify that the Quarterly Report on Form 10-Q for the quarter ended September 30, 2022 (the Report) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 2, 2022

/s/ Michael Burger

Michael Burger
President and Chief Executive Officer
(Principal Executive Officer)

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

Solely for the purposes of complying with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, the undersigned Chief Financial Officer of FARO Technologies, Inc. (the Company), hereby certify that the Quarterly Report on Form 10-Q for the quarter ended September 30, 2022 (the Report) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 2, 2022

/s/ Allen Muhich

Allen Muhich
Chief Financial Officer
(Principal Financial Officer)