

RUDOLPH TECHNOLOGIES INC  
Form 10-Q  
October 31, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

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

For the quarterly period ended: September 30, 2008

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 No. 000-27965

**RUDOLPH TECHNOLOGIES, INC.**

(Exact name of registrant as specified in its charter)

DELAWARE 22-3531208 (State or Other Jurisdiction of (I.R.S. Employer Incorporation or Organization) Identification Number)

**One Rudolph Road, PO Box 1000**

**Flanders, New Jersey 07836**

(Address of principal executive offices, including zip code)

**(973) 691-1300**

(Registrant's telephone number, including area code)

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. (See definition of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Securities Exchange Act of 1934). Large accelerated filer  Accelerated filer  Non-accelerated filer  (do not check if smaller reporting company) Smaller reporting company

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

The number of outstanding shares of the Registrant's Common Stock on October 20, 2008 was 30,660,557.

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## PART I FINANCIAL INFORMATION

### Item 1.

Financial Statements (unaudited)

Condensed Consolidated Balance Sheets at September 30, 2008 and December 31, 2007

Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2008 and 2007

Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2008 and 2007

Notes to Condensed Consolidated Financial Statements

### Item 2.

Management's Discussion and Analysis of Financial Condition and Results of Operations

### Item 3.

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Item 1A.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

RUDOLPH TECHNOLOGIES, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(In thousands)

**September 30,  
2008  
(unaudited)**

**December 31,  
2007**

<b>ASSETS</b>	Current assets:	Cash and cash equivalents	\$ 70,110	\$ 57,420	Marketable securities	4,121	16,505	Accounts receivable, net	39,438	50,015	Inventories	72,092	70,987	Prepaid expenses and other current assets	16,125	8,700	Total current assets	201,886	203,627	Property, plant and equipment, net	18,065	16,062	Goodwill	190,391	188,832	Identifiable intangible assets, net	44,734	48,125	Other assets	2,616	3,570	Total assets	\$ 457,692	\$ 460,216
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**LIABILITIES AND STOCKHOLDERS' EQUITY**

Current liabilities:	Accounts payable and accrued liabilities	\$ 13,600	\$ 15,030	Other current liabilities	11,933	12,299	Total current liabilities	25,533	27,329
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Non-current liabilities

10,963 8,409

Total liabilities

36,496	35,738	Commitments and contingencies	Stockholders' equity:	Common stock	30	30	Additional paid-in capital	382,574	379,886	Accumulated other comprehensive loss	(2,105)	(214)	Retained earnings	40,697	44,776	Total stockholders' equity	421,196	424,478	Total liabilities and stockholders' equity	\$ 457,692	\$ 460,216
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The accompanying notes are an integral part of these financial statements.

RUDOLPH TECHNOLOGIES, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (In thousands, except per share data)  
 (Unaudited)

	Three Months Ended September 30,				Nine Months Ended September 30,						
	2008				2007						
	2008				2007						
Revenues	\$ 38,986	\$ 31,461	\$ 114,612	\$ 127,547	Cost of revenues	22,180	15,921	64,970	60,907	Gross profit	
	16,806	15,540	49,642	66,640	Operating expenses:						
					Research and development	8,342	6,505	24,582	23,319		
					Selling, general and administrative	7,903	7,791	27,534	25,330	Amortization	1,734
										1,119	5,128
					Total operating expenses	17,979	15,415	57,244	52,017	Operating income (loss)	(1,173)
										125	(7,602)
											14,623
					Interest income and other, net	295	1,078	847	3,034	Income (loss) before income taxes	(878)
										1,203	(6,755)
											17,657
					Provision (benefit) for income taxes	(430)	(185)	(2,676)	5,254	Net income (loss)	\$ (448)
											\$ 1,388
											\$ (4,079)
											\$ 12,403
Earnings (loss) per share:					Basic	\$ (0.01)	\$ 0.05	\$ (0.13)	\$ 0.43	Diluted	\$ (0.01)
											\$ 0.05
					(0.13)	\$ 0.42	Weighted average shares outstanding:			Basic	30,781
											29,152
											30,591
											29,099
											Diluted
											30,781
											29,250
											30,591
											29,265

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

RUDOLPH TECHNOLOGIES, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (In thousands)

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(Unaudited)

		Nine Months Ended			
		September 30,			
		2008		2007	
Cash flows from operating activities:	Net income (loss)	\$ (4,079)	\$ 12,403	Adjustments to reconcile net income (loss) to net cash and cash equivalents	
provided by operating activities:	Amortization	6,311	4,406	Depreciation	3,046 3,497
exchange (gain) loss	(1,637) 48	Net loss on sales of marketable securities	84 -	Share-based compensation	2,550
2,286	Provision for doubtful accounts and inventory valuation	2,427	287	Change in operating assets and liabilities excluding effects of business combinations:	
	Accounts receivable	13,484	14,054	Inventories	(3,276) (7,550)
expenses and other assets	(6,392) (713)	Accounts payable and accrued liabilities	(1,576) (8,030)	Prepaid	
liabilities	257 (6,823)	Non-current liabilities	60 558	Other current	
activities	11,259 14,423	Net cash and cash equivalents provided by operating activities		11,259	14,423
Proceeds from sales of marketable securities	20,494 74,396	Cash flows from investing activities:		Purchases of marketable securities	(8,248) (62,783)
Capitalized software	(30) (596)	Purchases of property, plant and equipment		(2,458)	(725)
investing activities	1,284 10,292	Cash flows from financing activities:		Proceeds from sales of shares through share-based compensation plans	138 1,235
compensation plans	138 1,235	Excess tax benefit for sale of shares through share-based compensation plans		-	150
Net cash and cash equivalents provided by financing activities	138 1,385	Effect of exchange rate changes on cash and cash equivalents		9	201
cash equivalents	9 201	Net increase in cash and cash equivalents		12,690	26,301
	57,420 72,479	Cash and cash equivalents at beginning of period			
		Cash and cash equivalents at end of period		\$ 70,110	\$ 98,780

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

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RUDOLPH TECHNOLOGIES, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share data)  
(Unaudited)

NOTE 1. Basis of Presentation

The accompanying interim unaudited condensed consolidated financial statements have been prepared by Rudolph Technologies, Inc. (the "Company" or "Rudolph") and in the opinion of management reflect all adjustments, consisting only of normal recurring accruals, necessary for their fair presentation in accordance with accounting principles generally accepted in the United States of America. Preparing financial statements requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual amounts could differ materially from those amounts. The interim results for the three and nine month periods ended September 30, 2008 are not necessarily indicative of results to be expected for the entire year. This interim financial information should be read in conjunction with the financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

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### NOTE 2. Business Combinations

#### PCTA

On December 18, 2007, Rudolph and a wholly-owned subsidiary of the Company entered into, and consummated the transactions contemplated by, an Asset Purchase Agreement with Applied Precision Holdings, LLC and Applied Precision, LLC (collectively, Applied ), pursuant to which the Company purchased substantially all of the assets and assumed certain liabilities of the semiconductor division of Applied to be known as the Rudolph Technologies Probe Card Test and Analysis division ( PCTA ). The PCTA is engaged in the business of designing, developing, manufacturing, marketing, selling and supporting advanced probe card metrology and wafer probe process monitoring equipment and is complementary to the Company's existing business.

The closing under the Asset Purchase Agreement occurred on December 18, 2007 and the Company paid \$59,134 in cash and acquisition costs and issued 1,307 shares of common stock for a total purchase price of \$73,168. The measurement date was determined to be the date the acquisition was consummated since the number of shares to be distributed was not determinable until that date. The market price used to value the Rudolph shares issued as consideration for PCTA was \$10.73, which represents the average closing market price of Rudolph's common stock for the three day period ended December 18, 2007. The purchase price has been preliminarily allocated based on estimates of the fair values of assets acquired and liabilities assumed. With the exception of future tax adjustments related to the acquisition, the final valuation of net assets is expected to be completed during 2008. The results of operations of the PCTA have been included in our consolidated financial statements since the date of the acquisition.

The Company has agreed to assume the following liabilities of the PCTA: accounts payable, assigned contracts, licenses and leases, warranty claims and employee liabilities, all as more fully described in the Asset Purchase Agreement. In addition, the Company has agreed to assume the defense of and all obligations relating to certain litigation currently pending against Applied.

The transaction was accounted for using the purchase method of accounting for business combinations and, accordingly, the results of operations of the PCTA have been included in the Company's consolidated financial statements since the date of acquisition. The following table summarizes the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition:

Accounts receivable	\$ 5,761	Inventories	11,962	Prepaid expenses and other current assets	157	Property, plant and equipment	1,122
Goodwill	43,693	Identifiable assets	16,200	Accounts payable and accrued liabilities	(5,569)	Deferred revenue	(158)
							\$ 73,168

The fair value of inventories included a step-up of \$3,200, of which \$1,407 was recognized in cost of revenues for the nine months ended September 30, 2008. At the acquisition date, the Company formulated a plan to exit or restructure certain activities. The Company recorded \$254 for these activities, of which \$78 was utilized for the nine months ended September 30, 2008.

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Factors that contributed to a purchase price that resulted in recognition of goodwill include:

the combination of PCTA and Rudolph products should allow the combined company to offer its customers a more comprehensive suite of tools and a better integrated set of tools, thus enhancing the Company's ability to compete more effectively;

the ability of the assembled workforce to continue to deliver value-added solutions and develop new products and industry leading production technologies that solve customer problems;

consolidation of territorial sales activities and common marketing programs;

redeployment or elimination of duplicative functional and facilities costs;

reduction of customer service costs as a result of the consolidation of the companies' global customer service and regional support networks; and

the combined experience, financial resources, development expertise, size and breadth of product offerings of the combined company may allow it to respond more quickly and effectively to technological change, increased consolidation and industry demands

Of the \$16,200 of acquired identifiable assets, the following table reflects the allocation of the acquired identifiable assets and related preliminary estimates of useful lives:

Developed technology
\$ 11,600 8 years estimated useful life
Customer and distributor relationships

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2,900 7.2 years weighted average estimated useful life

Trade names

700 3 years estimated useful life

In-process research and development

1,000

\$ 16,200

Approximately \$1.0 million of the acquired identifiable intangible assets represents the estimated fair value of in-process research and development ( IPRD ) projects that had not yet reached technological feasibility and had no alternative future use. Accordingly, this amount was immediately expensed in the Consolidated Statement of Operations at the merger date. The purchased in-process technology project was a probe card test project, related to the next generation of the company s ProbeWoRx systems with enhanced capabilities, and was approximately 20% complete as of the date of acquisition. The costs to complete this project consist primarily of internal engineering labor costs and will be completed in the first half of 2009. If we are not successful in completing the inspection project on a timely basis, the future sales of the Company s inspection products may be adversely affected resulting in erosion of the Company s market share.

*Pro Forma Combined Results of Operations*

The following unaudited pro forma consolidated financial information presents the combined results of operations of the Company and PCTA as if the respective merger and acquisition occurred at the beginning of the period presented, after giving effect to certain adjustments, including interest income and amortization expense. Due to the non-recurring nature of the IPRD and inventory step-up charges, these amounts have not been included in the unaudited pro forma consolidated financial information. The unaudited pro forma consolidated financial information does not necessarily reflect the results of operations that would have occurred had the merger and acquisition been completed as of the date indicated or of the results that may be obtained in the future.

**Three Months Ended  
September 30, 2007    Nine Months Ended  
September 30, 2007**

(unaudited)

(unaudited)

Revenues

\$ 41,739    \$ 157,581

Net income

\$ 2,604    \$ 14,801



## Earnings per share:

	Basic	
\$	0.09	\$ 0.49
	Diluted	
\$	0.09	\$ 0.48

*RVSI Inspection*

On January 22, 2008, the Company announced that it had acquired all intellectual property and selected assets from privately-held RVSI Inspection, LLC, headquartered in Hauppauge, New York. The acquired business is currently known as the Rudolph Technologies Wafer Scanner Product Group. The transaction was accounted for using the purchase method of accounting for business combinations. The impact of the acquisition was not material to the Company's consolidated financial position or results of operations.

**NOTE 3. Fair Value Measurements**

In September 2006, the FASB issued SFAS No. 157, which is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. This statement defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. This statement applies under other accounting pronouncements that require or permit fair value measurements. The statement indicates, among other things, that a fair value measurement assumes that the transaction to sell an asset or transfer a liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. SFAS No. 157 defines fair value based upon an exit price model.

The Company adopted SFAS No. 157 on January 1, 2008, with the exception of the application of the statement to non-recurring nonfinancial assets and nonfinancial liabilities. Non-recurring nonfinancial assets and nonfinancial liabilities for which the Company has not applied the provisions of SFAS No. 157 include those measured at fair value in goodwill impairment testing and those initially measured at fair value in a business combination.

SFAS No. 157 establishes a valuation hierarchy for disclosure of the inputs to valuation used to measure fair value. This hierarchy prioritizes the inputs into three broad levels as follows. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument. Level 3 inputs are unobservable inputs based on the management's assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The following table provides the assets carried at fair value measured on a recurring basis as of September 30, 2008:

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Fair value measurements at September 30, 2008		Total carrying	Quoted prices in Significant other			Significant	value at	active markets
observable inputs	unobservable inputs	September 30, 2008	(Level 1)	(Level 2)	(Level 3)	U.S. Treasury notes	\$ 212	\$ 212
			\$	-	\$	-	-	All other marketable securities 3,909 -
								3,909 - Foreign currency forward contracts (3,391) (3,391)
								- -
Total								
			\$ 730	\$ (3,179)				
							\$ 3,909	\$ -

The Company's investments classified as Level 1 are based on quoted prices that are available in active markets. The forward foreign currency exchange contracts are primarily measured based on the foreign currency spot and forward rates quoted by the banks or foreign currency dealers. The U.S. Treasury Notes are measured based on quoted market prices.

Level 2 investments are valued using observable inputs to quoted market prices, benchmark yields, reported trades, broker/dealer quotes or alternative pricing sources with reasonable levels of price transparency. These investments, which are held by a custodian, include: corporate debt securities, auction rate securities, government-sponsored enterprise and asset-backed securities. Investment prices are obtained from third party pricing providers, which models prices utilizing the above observable inputs, for each asset class.

The Company did not hold financial assets and liabilities which were recorded at fair value in the Level 3 category as of September 30, 2008.

The carrying value of other financial instruments, including cash, accounts receivable, accounts payable, and accrued liabilities approximate fair value due to their short maturities.

The Company has adopted SFAS No. 159 effective January 1, 2008 and did not elect the fair value option for its financial instruments.

NOTE 4. Marketable Securities

The Company has evaluated its investment policies consistent with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," and determined that all of its investment securities are to be classified as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses reported in Stockholders' Equity under the caption "Accumulated other comprehensive loss". Realized gains and losses, interest and dividends on available-for-sale securities are included in "Interest income and other, net". Net realized gains on available-for-sale securities were \$2 for the three months ended September 30, 2008. Net realized losses on available-for-sale securities were \$84 for the nine months ended September 30, 2008. Net realized gains on available-for-sale securities were \$4 and \$0 for the three and nine months ended September 30, 2007, respectively. Gross unrealized gains on available-for-sale securities were \$2 and \$29 as of September 30, 2008 and December 31, 2007, respectively. Gross unrealized losses on available-for-sale securities were \$25 and \$152 as of September 30,

2008 and December 31, 2007, respectively.

As of September 30, 2008, the Company held \$0.7 million of auction-rate securities. The underlying assets of the Company's auction-rate securities consisted of municipal bonds with an auction reset feature. Due to auction rate securities markets being disrupted in 2008, the Company's securities experienced auction failures. An auction failure means that the parties wishing to sell their securities could not be matched with an adequate volume of buyers. The securities for which auctions have failed will continue to accrue interest at the contractual rate and be auctioned every seven, 28 or 35 days until the auction succeeds, the issuer calls the securities, or they mature. The Company held two auction rate securities at September 30, 2008, of which both had experienced failed auctions. The Company does not believe these securities are impaired currently and also believes it will sell them within the next twelve months. In addition, while all of the Company's auction rate securities are currently rated A or above, if the issuers are unable to successfully close future auctions and their credit ratings deteriorate, the Company may in the future be required to record an impairment charge on these investments.

NOTE 5. Derivative Instruments and Hedging Activities

The Company, when it considers it to be appropriate, enters into forward contracts to hedge the economic exposures arising from foreign currency denominated transactions. At September 30, 2008 and December 31, 2007, these contracts included the sale of Japanese Yen to purchase U.S. dollars. The foreign currency forward contracts were entered into by our Japanese subsidiary to economically hedge a portion of certain intercompany obligations. The forward contracts are not designated as hedges for accounting purposes and therefore, the change in fair value is recorded in selling, general and administrative expenses in the Consolidated Statements of Operations.

The dollar equivalent of the US dollar forward contracts and related fair values were as follows:

September 30,  
2008

December 31,  
2007

Notional amount \$ 3,535 \$ 5,706 Fair value of liability \$ 144 \$ 127

NOTE 6. Identifiable Intangible Assets

Identifiable intangible assets as of September 30, 2008 are as follows:

	Gross Carrying Amount		Accumulated Amortization		Net
Developed technology	\$ 51,329	\$ 15,277	\$ 36,052	Customer and distributor relationships	7,300 1,668 5,632
Trade names	4,100	1,050	3,050	Total identifiable intangible assets	
				\$ 62,729	\$ 17,995 \$ 44,734

Identifiable intangible assets as of December 31, 2007 are as follows:

Gross Carrying  
Amount

Accumulated  
Amortization

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Net

Developed technology	\$ 49,591	\$ 11,324	\$ 38,267	Customer and distributor relationships	7,300	917	6,383	Trade names	4,100	625	
			3,475	Total identifiable intangible assets							
					\$ 60,991	\$ 12,866	\$ 48,125				

Intangible asset amortization expense for the three and nine months ended September 30, 2008 was \$1,734 and \$5,128, respectively. For the three and nine months ended September 30, 2007, intangible asset amortization expense was \$1,120 and \$3,358, respectively. Estimated amortization expense for the remainder of 2008 amounts to \$1,696 and in each of the next five years amounts to \$6,546 for 2009, \$6,329 for 2010, \$6,096 for 2011, \$6,096 for 2012, and \$6,096 for 2013.

NOTE 7. Accounts Receivable

Accounts receivable are net of the allowance for doubtful accounts of \$418 and \$214 as of September 30, 2008 and December 31, 2007, respectively.

NOTE 8. Inventories

September 30,

December 31,

**2008**

**2007**

Materials	\$ 38,277	\$ 34,556	Work-in-process	15,582	20,820	Finished goods	18,233	15,611	Total inventories	\$ 72,092	\$ 70,987
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The Company has established reserves of \$4,498 and \$3,394 as of September 30, 2008 and December 31, 2007, respectively, for slow moving and obsolete inventory.

NOTE 9. Property, Plant and Equipment

September 30,

December 31,

**2008**

**2007**

Land and building	\$ 5,184	\$ 5,185	Machinery and equipment	14,641	11,829	Furniture and fixtures	2,720	2,668			
Computer equipment	7,085	6,407	Leasehold improvements	7,003	5,791	36,633	31,880	Accumulated depreciation	(18,568)	(15,818)	Net property, plant and equipment

\$ 18,065 \$ 16,062

NOTE 10. Commitments and Contingencies

*Warranty Reserves*

Changes in the Company's warranty reserves are as follows:

	Nine Months Ended September 30,	
	<b>2008</b>	
	<b>2007</b>	
Balance, beginning of the period		\$ 2,365
		\$ 2,171
Accruals 1,591 2,140 Warranty liability assumed in merger 215 - Settlements (1,928)		(2,230)
Balance, end of the period		
	\$ 2,243	
		\$ 2,081

Warranty reserves are reported in the Condensed Consolidated Balance Sheets under the caption "Accounts payable and other accrued liabilities".

NOTE 11. Share-Based Compensation

*Restricted Stock Unit Activity*

A summary of the Company's nonvested restricted stock unit activity with respect to the nine month period ended September 30, 2008 follows:

	Number of Shares	
		<b>Weighted Average Grant Date Fair Value</b>
Nonvested at December 31, 2007 680 \$ 16.08	Granted 431 \$ 8.74	Vested (153) \$ 16.31
	Forfeited (95) \$ 14.35	Nonvested at September 30, 2008 863 \$ 12.56

As of September 30, 2008 and December 31, 2007, there was \$8,480 and \$7,852 of total unrecognized compensation cost related to restricted stock units granted under the plans, respectively. That cost is expected to be recognized over a weighted average period of 3.2 years and 3.7 years for the respective periods.

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### NOTE 12. Interest Income and Other, Net

		Three Months Ended			
		September 30, Nine Months Ended			
September 30, 2008	2007	2008	2007		
Interest income	\$ 293	\$ 1,074	\$ 931	\$ 3,034	Realized gains (losses) on sales of marketable securities, net
24	(84)	-	-	Total interest income and other, net	\$ 295 \$ 1,078 \$ 847 \$ 3,034

### NOTE 13. Income Taxes

The Company adopted the provisions of FIN 48, as amended by FSP 48-1, effective January 1, 2007. As a result of the implementation of FIN 48, as amended, the Company recognized increases in the liability for unrecognized tax benefits of \$2,173, non-current deferred tax assets of \$1,948 and goodwill of \$245. The adoption of FIN 48, as amended, resulted in a cumulative effect adjustment to retained earnings of \$20 as of January 1, 2007. There are no known tax positions which are reasonably possible to change over the next twelve months necessitating a significant change in the Company's unrecognized tax benefits.

The Company is continuing its practice of recognizing interest and penalties related to income tax matters in income tax expense. As of September 30, 2008, the Company had accrued interest and penalties expense related to unrecognized tax benefits of \$148.

The Company is subject to U.S. federal income tax as well as income tax in multiple state and foreign jurisdictions. Presently, the Company is not under examination by the Internal Revenue Service for examination of income tax returns for open periods, December 31, 2004 through December 31, 2007. The Company is currently under examination by the State of New Jersey for tax years 2005 through 2007. The Company is not currently under examination by any other U.S. state, local or foreign tax authority for all open tax periods beginning after December 31, 2002.

### NOTE 14. Comprehensive Income (Loss)

The difference between net income (loss) and comprehensive income (loss) for the Company is due to currency translation adjustments and unrealized gains (losses) on investments.

The components of comprehensive income (loss) are as follows:

		Three Months Ended			
		September 30, Nine Months Ended			
September 30, 2008	2007	2008	2007		
Net income (loss)	\$ (448)	\$ 1,388	\$ (4,079)	\$ 12,403	Change in net unrealized gains (losses) on investments, net of tax
adjustments	(2,685)	450	(1,855)	636	Change in currency translation
				Total comprehensive income (loss)	\$ (3,182) \$ 1,988 \$ (5,970) \$ 13,191

### NOTE 15. Earnings (Loss) Per Share

Basic earnings (loss) per share is calculated using the weighted average number of shares of common stock outstanding during the period. Diluted earnings (loss) per share is computed in the same manner and also gives effect to all dilutive common equivalent shares outstanding during the period. Potentially dilutive common equivalent shares consist of stock options and restricted stock units for 2007. For the three and nine month periods ended September 30, 2008, all outstanding stock options and restricted stock units totaling 3,211, were excluded from the computation of diluted loss per share because the effect in the periods would be anti-dilutive. During the three and nine months ended September 30, 2007, there were stock options with exercise prices above the average fair market value of the Company's common stock which were excluded from the computation of diluted earnings per share due

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to the anti-dilutive nature of these options. During the three and nine months ended September 30, 2007, there were restricted stock units which were excluded from the computation of diluted earnings per share as their effect would be anti-dilutive. For the three and nine months ended September 30, 2007, the weighted average number of stock options and restricted stock units excluded from the computation of diluted earnings per share was 2,848 and 2,113.

The Company's basic and diluted earnings (loss) per share amounts are as follows:

<b>Three Months Ended</b>		<b>Nine Months Ended</b>		<b>September 30, 2008</b>		<b>September 30, 2007</b>		<b>2008</b>		<b>2007</b>		Numerator:	Net income (loss) \$	(448)
	\$	1,388	\$	(4,079)	\$	12,403	Denominator:	Basic earnings (loss) per share -				weighted average shares		
outstanding	30,781	29,152	30,591	29,099	Effect of potential dilutive securities:		Employee stock options and					restricted stock units - dilutive		
					shares -	98	-	166	Diluted earnings (loss) per share -			weighted average shares		
outstanding	30,781	29,250	30,591	29,265	Earnings (loss) per share:	Basic \$	(0.01)	\$	0.05	\$	(0.13)	\$		
					0.43	Diluted \$	(0.01)	\$	0.05	\$	(0.13)	\$	0.42	

NOTE 16. Segment Reporting and Geographic Information

Operating segments are business units that have separate financial information and are separately reviewed by the Company's chief decision maker. The Company's chief decision maker is the Chief Executive Officer. The Company and its subsidiaries currently operate in a single reportable segment: the design, development, manufacture, sale and service of process control metrology, defect inspection and data analysis systems used in semiconductor device manufacturing. The chief operating decision maker allocates resources and assesses performance of the business and other activities at the operating segment level.

The following table lists the different sources of revenue:

**Three Months Ended**

**Nine Months Ended**

September 30,

**September 30,**

**2008**

**2007**

**2008**

**2007**

**Revenue Type**

Systems:

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Metrology \$ 3,886 10%

\$ 6,754

22% \$ 19,944 17%

\$ 30,467

24% Inspection 23,569 60% 15,963 50% 64,659 56% 66,207 52% Parts 6,568 17% 3,282 10% 15,493 14% 9,537 7% Services  
3,824 10% 3,540 11% 10,529 9% 10,530 8% Software licensing 1,139 3% 1,922 7% 3,987 4% 10,806 9%

Total

\$ 38,986 100%

\$ 31,461

100% \$ 114,612 100%

\$ 127,547

100%

For geographical reporting, revenues are attributed to the geographic location in which the customer is located. Revenue by geographic region is as follows:

Three Months Ended

Nine Months Ended

September 30,

September 30,

**2008**

**2007**

**2008**

**2007**

United States

\$ 9,412 \$ 5,333 \$ 24,723 \$ 24,418

Asia



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21,254 18,808 67,843 76,925

Europe

8,320 7,320 22,046 26,204

Total

\$ 38,986 \$ 31,461 \$ 114,612 \$ 127,547

One customer represented 12.7% of revenue for the nine months ended September 30, 2007. No other customer was above 10% of revenue for the nine months ended September 30, 2008 or 2007.

NOTE 17. Recent Accounting Pronouncements

In March 2008, the Financial Accounting Standards Board ("FASB") issued SFAS No. 161, "Disclosure about Derivatives Instruments and Hedging Activities-an amendment of FASB Statement No. 133" ("SFAS 161"), which requires enhanced disclosures about an entity's derivative and hedging activities and thereby improves the transparency of financial reporting. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008 with early application encouraged. The Company is currently evaluating the potential impact of adopting SFAS 161.

In February 2008, the FASB adopted FASB Staff Position SFAS No. 157-2 - "Effective Date of FASB Statement No. 157" delaying the effective date of SFAS No. 157 for one year for all non financial assets and non financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The Company is currently evaluating the impact of the implementation of SFAS No. 157-2 on its consolidated financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141R, Business Combinations ( SFAS 141R ), which establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in an acquiree, and the recognition and measurement of goodwill acquired in a business combination or a gain from a bargain purchase. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

In November 2007, the Emerging Issues Task Force ( EITF ) issued EITF Issue No. 07-1 ( EITF 07-1 ), Accounting for Collaborative Arrangements, which defines collaborative arrangements and establishes reporting and disclosure requirements for such arrangements. EITF 07-1 is effective for fiscal years beginning after December 15, 2008. The Company is continuing to evaluate the impact of adopting the provisions EITF 07-1; however, it does not anticipate that adoption will have a material effect on its financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159 ( SFAS 159 ), The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115. SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reporting earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS 159 is effective for fiscal years that begin after November 15, 2007. The Company adopted SFAS 159 on January 1, 2008 and did not elect the fair value option for its financial instruments.

NOTE 18. Share Repurchase Program

In July 2008, the Board of Directors authorized a share repurchase program of up to 3 million shares of the Company's stock. The Company did not purchase any shares to date under this program.

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

Certain statements in this quarterly report on Form 10-Q are forward looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. In addition, we may, from time to time, make oral forward looking statements. Forward looking statements may be identified by the words "anticipate", "believe", "expect", "intend", "will" and similar expressions, as they relate to us or our management. These statements include, without limitation, the statement that we believe that our existing cash and cash equivalents will be sufficient to meet our anticipated cash requirements for working capital and capital expenditures for the foreseeable future.

The forward looking statements contained herein reflect our current views with respect to future events and are subject to certain risks, uncertainties and assumptions. Actual results may differ materially from those projected in such forward looking statements due to a number of factors, risks and uncertainties, including the risk factors set forth in this Current Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2007. We disclaim any obligation to update any forward looking statements as a result of developments occurring after the date of this quarterly report.

### **Critical Accounting Policies**

The preparation of consolidated financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make judgments, assumptions and estimates that affect the amounts reported. Certain of these significant accounting policies are considered to be critical accounting policies, as defined below.

A critical accounting policy is defined as one that is both material to the presentation of our consolidated financial statements and requires management to make difficult, subjective or complex judgments that could have a material effect on our financial condition or results of operations. Specifically, these policies have the following attributes: (1) we are required to make judgments and assumptions about matters that are highly uncertain at the time of the estimate; and (2) different estimates we could reasonably have used, or changes in the estimate that are reasonably likely to occur, could have a material effect on our financial position and results of operations.

Estimates and assumptions about future events and their effects cannot be determined with certainty. We base our estimates on historical experience and on various other assumptions believed to be applicable and reasonable under the circumstances. These estimates may change as new events occur, as additional information is obtained and as our operating environment changes. These changes have been included in the consolidated financial statements as soon as they became known. In addition, management is periodically faced with uncertainties, the outcomes of which are not within its control and will not be known for prolonged periods of time. These uncertainties are discussed in this report and in our Annual Report on Form 10-K for the year ended December 31, 2007 in the section entitled "Risk Factors." Based on a critical assessment of our accounting policies and the underlying judgments and uncertainties affecting the application of those policies, management believes that our consolidated financial statements are fairly stated in accordance with accounting principles generally accepted in the United States of America, and provide a fair presentation of our financial position and results of operations.

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Recently, the credit markets and the financial services industry have been experiencing a period of unprecedented turmoil and upheaval characterized by the bankruptcy, failure, collapse or sale of various financial institutions and an unprecedented level of intervention from the United States federal government. While the ultimate outcome of these events cannot be predicted, they may have a material adverse effect on our liquidity, financial condition and results of operations. In October 2008, our stock price has significantly declined to levels which may negatively impact our annual goodwill impairment test and our review of amortizable intangible assets during the fourth quarter of 2008. Our critical accounting policies regarding goodwill and long-lived assets and acquired intangible assets are as follows:

*Goodwill.* Our formal annual impairment testing date for goodwill is October 31st or prior to the next annual testing date if an event occurs or circumstances change that would make it more likely than not that the fair value of a reporting unit is below its carrying amount. In fiscal 2007, we changed our annual impairment testing date from December 31 to October 31. This change was made to allow us additional time to complete the impairment test by the end of the financial statement reporting deadline. The goodwill impairment test is a two-step process which requires us to make judgmental assumptions regarding fair value. The initial first step consists of estimating the fair value of our aggregated reporting unit using the market value of our common stock at October 31, multiplied by the number of outstanding common shares (market capitalization) and an implied control premium as if it were to be acquired by a single stockholder. We obtain information on completed sales of similar companies in a comparable industry to estimate an implied control premium for us. We compare the estimated fair value of the reporting unit to its carrying value which includes goodwill. If the results of the initial market capitalization test produce results which are below the reporting unit carrying value, we will also consider if, the market capitalization is temporarily low and, if so, we may also perform a discounted cash flow test. If the estimated fair value is less than the carrying value, the second step is completed to compute the impairment amount by determining the "implied fair value" of goodwill. This determination requires the allocation of the estimated fair value of the reporting unit to the assets and liabilities of the reporting unit. Any remaining unallocated fair value represents the "implied fair value" of goodwill which is compared to the corresponding carrying value to compute the goodwill impairment amount. We believe our estimates of the underlying components of fair value are reasonable. As of December 31, 2007, a one dollar per share increase or decrease in our common stock would have a \$30.5 million effect on our market capitalization before adding a control premium. Testing is required between annual tests if events occur or circumstances change that would, more likely than not, reduce the fair value of the reporting unit below its carrying value. Such an event may occur if, for an extended period of time, the market value of our common stock plus the implied control premium were less than the carrying value. Should actual results not meet our expectations or assumptions change in future years, our impairment assessment could result in a lower fair value estimate which could result in an impairment charge that may materially affect the carrying value of our assets and results from operations.

*Long-Lived Assets and Acquired Intangible Assets.* We periodically review long-lived assets, other than goodwill, for impairment whenever changes in events or circumstances indicate that the carrying amount of an asset may not be recoverable. Assumptions and estimates used in the determination of impairment losses, such as future cash flows and disposition costs, may affect the carrying value of long-lived assets and the impairment of such long-lived assets, if any, could have a material effect on our consolidated financial statements.

For more information, please see our critical accounting policies as previously disclosed in our 2007 Annual Report on Form 10-K.

See Note 17 to the condensed consolidated financial statements included elsewhere in this quarterly report on Form 10-Q regarding the impact of recent accounting pronouncements on the Company's financial position and results of operations.

### **Results of Operations for the Three and Nine Month Periods Ended September 30, 2008 and 2007**

We are a worldwide leader in the design, development, manufacture and support of high-performance process control metrology, defect inspection, and data analysis systems used by semiconductor device manufacturers. We

provide yield management solutions used in both wafer processing and final manufacturing through a family of standalone systems and integrated modules for both transparent and opaque thin film measurements and macro-defect inspection. All of these systems feature production-worthy automation and are backed by worldwide customer support.

On December 18, 2007, Rudolph, along with our wholly-owned subsidiary, Mariner Acquisition Company LLC, entered into, and consummated the transactions contemplated by, an agreement with Applied Precision Holdings, LLC and Applied Precision, LLC (collectively, Applied ), pursuant to which we purchased substantially all of the assets and assumed certain liabilities of the semiconductor division of Applied to be known as the Probe Card Test and Analysis division ( PCTA ). PCTA is engaged in the business of designing, developing, manufacturing, marketing, selling and supporting advanced probe card metrology and wafer probe process monitoring equipment and is complementary to our existing business.

The closing occurred on December 18, 2007 and we paid \$59.1 million in cash and issued 1.3 million shares of common stock for a total purchase price of \$73.2 million. Under the terms of the purchase agreement, we agreed to assume the following liabilities of Applied relating to the PCTA: accounts payable, assigned contracts, licenses and leases, warranty claims and employee liabilities. The measurement date was determined to be the date the acquisition was consummated since the number of shares to be distributed was not determinable until that date. The market price used to value the Rudolph shares issued as consideration for PCTA was \$10.73, which represents the average closing market price of Rudolph's common stock for the three day period ended December 18, 2007. In addition, we agreed to assume the defense of and all obligations relating to certain litigation. The cash portion of the purchase price is subject to further post-closing adjustment based on the final closing net asset balance. The purchase price has been preliminarily allocated based on estimates of the fair values of assets acquired and liabilities assumed. The final valuation of net assets is expected to be completed during 2008.

On January 22, 2008, we announced that we had acquired all intellectual property and selected assets from privately-held RVSI Inspection, LLC, headquartered in Hauppauge, New York. The acquired business is currently known as the Rudolph Technologies Wafers Scanner Product Group. We account for this acquisition as a business combination. The impact of the acquisition was not material to our consolidated financial position or results of operations.

Rudolph's business is affected by the annual spending patterns of our customers on semiconductor capital equipment. The amount that our customers devote to capital equipment spending depends on a number of factors, including general worldwide economic conditions as well as other economic drivers such as personal computer, cell phone and personal electronic device sales. Current forecasts by industry analysts for the semiconductor device manufacturing industry project a year-over-year decrease in capital spending of 10-20% for 2009. We monitor capital equipment spending through announced capital spending plans by our customers and monthly-published industry data such as the book-to-bill ratio. The book-to-bill ratio is a 3-month running statistic that compares bookings or orders placed with capital equipment suppliers to billings or shipments. A book-to-bill above one shows that semiconductor device equipment manufacturers are ordering equipment at a pace that exceeds the equipment suppliers' shipments for the period. The three month rolling average North American semiconductor equipment book-to-bill ratio was 0.8 for the month of September 2008, decreasing from the December 2007 book-to-bill ratio of 0.9.

Historically, a significant portion of our revenues in each quarter and year has been derived from sales to relatively few customers, and we expect this trend to continue. For the nine month period ended September 30, 2008 and for the years ended December 31, 2007, 2006 and 2005, sales to customers that individually represented at least five percent of our revenues accounted for 37.6%, 37.1%, 40.9%, and 62.6% of our revenues, respectively.

We do not have purchase contracts with any of our customers that obligate them to continue to purchase our products, and they could cease purchasing products from us at any time. A delay in purchase or cancellation by any of our large customers could cause quarterly revenues to vary significantly. In addition, during a given quarter, a significant portion of our revenues may be derived from the sale of a relatively small number of systems. Our

transparent film measurement systems range in average selling price from approximately \$250,000 to \$1.0 million per system, our opaque film measurement systems range in average selling price from approximately \$900,000 to \$2.0 million per system and our macro-defect inspection and probe card and test analysis systems range in average selling price from approximately \$250,000 to \$1.4 million per system. Accordingly, a small change in the number of systems we sell may also cause significant changes in our operating results. Because fluctuations in the timing of orders from our major customers or in the number of our individual systems we sell could cause our revenues to fluctuate significantly in any given quarter or year, we do not believe that period-to-period comparisons of our financial results are necessarily meaningful, and they should not be relied upon exclusively as an indication of our future performance.

A significant portion of our revenues has been derived from customers outside of the United States. In the nine months period ended September 30, 2008, approximately 78.4% of our revenues were derived from customers outside of the United States, of which 59.2% were derived from customers in Asia and 19.2% were derived from customers in Europe. In 2007, approximately 77.1% of our revenues were derived from customers outside of the United States, of which 58.5% were derived from customers in Asia and 18.6% were derived from customers in Europe. In 2006, approximately 70.6% of our revenues were derived from customers outside of the United States, of which 59.9% were derived from customers in Asia and 10.7% were derived from customers in Europe. In 2005, approximately 77.5% of our revenues were derived from customers outside of the United States, of which 56.3% were derived from customers in Asia and 21.2% were derived from customers in Europe. We expect that revenues generated from customers outside of the United States will continue to account for a significant percentage of our revenues.

The sales cycle for our systems typically ranges from six to 15 months, and can be longer when our customers are evaluating new technology. Due to the length of these cycles, we invest significantly in research and development and sales and marketing in advance of generating revenues related to these investments. Additionally, the rate and timing of customer orders may vary significantly from month to month. Accordingly, if sales of our products do not occur when we expect, our expenses and inventory levels may increase relative to revenues and total assets.

*Revenues.* Our revenues are primarily derived from the sale of our systems, services, spare parts and software licensing. Our revenues were \$39.0 million and \$114.6 million for the three and nine month periods ended September 30, 2008, compared to \$31.5 million and \$127.5 million for the three and nine month periods ended September 30, 2007, representing an increase for the three month period of 23.9% and a decrease for the nine month period of 10.1% in the respective year-over-year periods.

The following table lists the different sources of our revenue (in thousands):

**Three Months Ended**

**Nine Months Ended**

September 30,

**September 30,**

**2008**

**2007**

2008

2007

Revenue Type

Systems:

Metrology \$ 3,886 10%

\$ 6,754

22% \$ 19,944 17%

\$ 30,467

24%	Inspection	23,569	60%	15,963	50%	64,659	56%	66,207	52%	Parts	6,568	17%	3,282	10%	15,493	14%	9,537	7%
	Services	3,824	10%	3,540	11%	10,529	9%	10,530	8%	Software licensing	1,139	3%	1,922	7%	3,987	4%	10,806	9%

Total

\$ 38,986 100%

\$ 31,461

100% \$ 114,612 100%

\$ 127,547

100%

The year-over-year decrease in systems revenue for the nine month periods ended September 30, 2008 and 2007 is due to continued weakness in the overall semiconductor industry and reflects a decrease in inspection systems revenues of \$1.5 million and a decrease in metrology systems revenue of \$10.5 million. Systems revenue generated by our latest product releases and major enhancements in each of our product families amounted to 42% of total revenues for both the three and nine month periods ended September 30, 2008 compared to 26% and 29% of total revenues for the three and nine month periods ended September 30, 2007. The year-over-year increase in total parts and services revenue for the nine month periods ended September 30, 2008 and 2007 is primarily due to customers continuing to spend more on repair and maintenance of their existing equipment as well as parts revenues related to the our recent acquisitions. Parts and services revenues are generated from part sales, maintenance service contracts, system upgrades, as well as time and material billable service calls. The year-over-year decrease in software licensing revenues for the nine month periods ended September 30, 2008 and 2007 is primarily due to the sale of certain technology rights to Tokyo Electron in 2007.

Deferred revenues of \$7.5 million are recorded in other current liabilities at September 30, 2008 and primarily consist of \$5.1 million for deferred maintenance agreements and \$2.4 million for systems awaiting acceptance and outstanding deliverables.

*Gross Profit.* Our gross profit has been and will continue to be affected by a variety of factors, including inventory step-up from purchase accounting, manufacturing efficiencies, excess and obsolete inventory write-offs, pricing by competitors or suppliers, new product introductions, product sales mix, production volume, customization and reconfiguration of systems, international and domestic sales mix, and parts and service margins. Our gross profit

was \$16.8 million and \$49.6 million for the three and nine month periods ended September 30, 2008, compared to \$15.5 million and \$66.6 million for the three and nine month periods ended September 30, 2007. Our gross profit represented 43.1% and 43.3% of our revenues for the three and nine month periods ended September 30, 2008 and 49.4% and 52.2% of our revenues for the same periods in the prior year. The decrease in gross profit as a percentage of revenue for the nine month period ended September 30, 2008, compared to the nine month period ended September 30, 2007 is primarily due to integration costs for the two recent acquisitions resulting in the write-off of obsolete inventory and inventory write-up charges on sold systems, product mix which contained lower software sales, and fixed manufacturing costs representing a larger component of cost of goods sold on a lower revenue base.

*Research and Development.* Our research and development expense was \$8.3 million and \$24.6 million for the three and nine month periods ended September 30, 2008, compared to \$6.5 million and \$23.3 million for the same periods in the prior year. Research and development expense represented 21.4% of our revenues for the both the three and nine month periods ended September 30, 2008, compared to 20.7% and 18.3% of revenues for the same periods in the prior year. The year-over-year dollar increase for the nine month periods ended September 30, 2008 and 2007 in research and development expenses primarily reflects inclusion of the engineering teams acquired in our recent acquisitions and a write-off of abandoned software projects eliminated as part of our cost reduction efforts, partially offset by cost control initiatives and reprioritization of development programs. We anticipate research and development expense will be approximately \$6.7 to \$7.0 million for the three month period ending December 31, 2008.

*Selling, General and Administrative.* Our selling, general and administrative expense was \$7.9 million and \$27.5 million for the three and nine month periods ended September 30, 2008, compared to \$7.8 million and \$25.3 million for the same periods in the prior year. Selling, general and administrative expense represented 20.3% and 24.0% of our revenues for the three and nine month periods ended September 30, 2008 compared to 24.8% and 19.9% of our revenues for the same periods in the prior year. The year-over-year dollar increase for the nine month periods ended September 30, 2008 and 2007 in selling, general and administrative expense was primarily due to administrative costs associated with the recent acquisitions, partially offset by foreign currency exchange gains from international operations. We currently anticipate that selling, general and administrative expenses will represent approximately \$8.4 to \$8.6 million for the three month period ending December 31, 2008.

*Interest income and other, net.* Interest income and other, net was \$0.3 million and \$0.8 million for the three and nine month periods ended September 30, 2008, compared to \$1.1 million and \$3.0 million for the same periods in the prior year. The year-over-year decrease in interest income and other, net was primarily attributable to a lower average cash and marketable securities balance and lower interest rates.

*Income Taxes.* Income tax benefit was \$0.4 million and \$2.7 million for the three and nine month periods ended September 30, 2008 compared to income tax benefit of \$0.2 million for the three month period ended September 30, 2007 and income tax expense of \$5.3 million for the nine month period ended September 30, 2007. Our effective tax rate for the nine month period ended September 30, 2008 is 39.6%, compared to 29.8% in the prior year period. Our effective tax rate differs from the statutory rate of 35% primarily as a function of state and foreign income taxes offset by benefits from tax exempt interest.

## **Liquidity and Capital Resources**

At September 30, 2008, we had \$74.2 million of cash, cash equivalents and marketable securities and \$176.4 million in working capital. At December 31, 2007, we had \$73.9 million of cash, cash equivalents and marketable securities and \$176.3 million in working capital.

Typically during periods of revenue growth, changes in accounts receivable and inventories represent a use of cash as we incur costs and expend cash in advance of receiving cash from our customers. Similarly, during periods of

declining revenue, changes in accounts receivable and inventories represent a source of cash as inventory purchases decline and revenue from prior periods is collected. However, for the nine months ended September 30, 2008, as our revenues declined our change in inventories represented a use of cash. This was primarily due to increasing inventory related to new products, the slow down in the back-end of the inspection business and system shipments awaiting acceptance.

Operating activities provided \$11.3 million in cash and cash equivalents for the nine month period ended September 30, 2008. The net cash and cash equivalents provided by operating activities during the nine month period ended September 30, 2008 was primarily a result of net loss, adjusted to exclude the effect of non-cash charges, of \$8.7 million and decreases in accounts receivable of \$13.5 million, partially offset by increases in prepaid expenses and other assets of \$6.4 million, inventories of \$3.3 million and a decrease in accounts payable and accrued liabilities of \$1.6 million. Operating activities provided \$14.4 million in cash and cash equivalents for the nine month period ended September 30, 2007. The net cash and cash equivalents provided by operating activities during the nine month period ended September 30, 2007 was primarily a result of net income, adjusted to exclude the effect of non-cash charges, of \$22.9 million and a decrease in accounts receivable of \$14.1 million, partially offset by a decrease in accounts payable and accrued liabilities of \$8.0 million, an increase in inventories of \$7.6 million, a decrease in other current and non-current liabilities of \$6.3 million, and prepaid expenses and other assets of \$0.7 million.

Net cash and cash equivalents provided by investing activities during the nine month period ended September 30, 2008 of \$1.3 million was due to proceeds from sales of marketable securities of \$20.5 million, partially offset by acquisition costs for business combinations of \$8.5 million, purchases of marketable securities of \$8.2 million, and capital expenditures of \$2.5 million. Net cash and cash equivalents provided by investing activities during the nine month period ended September 30, 2007 of \$10.3 million was due to proceeds from sales of marketable securities of \$74.4 million, offset by purchases of marketable securities of \$62.8 million, capital expenditures of \$0.7 million and costs incurred for capitalized software of \$0.6 million.

Net cash and cash equivalents provided by financing activities for the nine month periods ended September 30, 2008 of \$0.1 million was due to proceeds received for sales of shares through share-based compensation plans. Net cash and cash equivalents provided by financing activities for the nine month periods ended September 30, 2007 of \$1.4 million was due to proceeds received and tax benefit for sales of shares through share-based compensation plans.

From time to time we evaluate whether to acquire new or complementary businesses, products and/or technologies. We may fund all or a portion of the purchase price of these acquisitions in cash. On December 18, 2007, we announced that our acquisition of the semiconductor division of Applied Precision Holdings, LLC had been completed. Under the terms of the agreement, we paid an aggregate of \$59.1 million in cash and issued an aggregate of 1.3 million shares of our common stock to Applied Precision Holdings, LLC. On January 22, 2008, we announced that we had acquired all intellectual property and selected assets from privately-held RVSI Inspection, LLC, headquartered in Hauppauge, New York. We will account for this acquisition as a business combination.

In July 2008, our Board of Directors approved a stock repurchase program of up to 3 million shares. We did not purchase any shares to date under this program.

Our future capital requirements will depend on many factors, including the timing and amount of our revenues and our investment decisions, which will affect our ability to generate additional cash. We believe that our existing cash, cash equivalents and marketable securities will be sufficient to meet our anticipated cash requirements for working capital and capital expenditures for the foreseeable future. Thereafter, if cash generated from operations and financing activities is insufficient to satisfy our working capital requirements, we may seek additional funding through bank borrowings, sales of securities or other means. There can be no assurance that we will be able to raise any such capital on terms acceptable to us or at all.

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

#### *Interest Rate and Credit Market Risk*



We are exposed to changes in interest rates and market liquidity primarily from our investments in certain available-for-sale securities. Our available-for-sale securities consist primarily of fixed income and variable rate income investments (U.S. Treasury and Agency securities asset-backed securities, mortgage-backed securities, auction rate securities, and corporate bonds). We continually monitor our exposure to changes in interest rates, market liquidity and credit ratings of issuers from our available-for-sale securities. It is possible that we are at risk if interest rates, market liquidity or credit ratings of issuers change in an unfavorable direction. The magnitude of any gain or loss will be a function of the difference between the fixed rate of the financial instrument and the market rate and our financial condition and results of operations could be materially affected. Based on sensitivity analysis performed on our financial investments held as of September 30, 2008, an immediate adverse change of 10% in interest rates (e.g. 3.00% to 3.30%) would result in an immaterial decrease in the fair value of our available for sale securities. As of September 30, 2008 we held \$0.7 million in municipal auction rate securities. We do not believe these securities are impaired currently and also believe we will sell them within the next twelve months.

#### *Foreign Currency Risk*

We have branch operations in Taiwan, Singapore, China and Korea and wholly-owned subsidiaries in Europe and Japan. Our international subsidiaries and branches operate primarily using local functional currencies. These foreign branches and subsidiaries are limited in their operations and level of investment so that the risk of currency fluctuations is not material. A substantial portion of our international sales are denominated in U.S. dollars with the exception of Japan and, as a result, we have relatively little exposure to foreign currency exchange risk with respect to these sales. Substantially all our sales in Japan are denominated in Japanese yen. From time to time, we may enter into forward exchange contracts to economically hedge a portion of, but not all, existing and anticipated foreign currency denominated transactions expected to occur within 12 months. The change in fair value of the forward contracts is recognized in the Consolidated Statements of Operations each reporting period. As of September 30, 2008, we had twelve forward contracts outstanding with a total notional contract value of \$3.5 million. We do not use derivative financial instruments for trading or speculative purposes.

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#### Item 4. Controls and Procedures

We conducted an evaluation of the effectiveness of the design and operation of our "disclosure controls and procedures," as defined in Rule 13a-15(e) or Rule 15d-15(e) under the Exchange Act, ("Disclosure Controls") as of the end of the period covered by this Quarterly Report. The controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO").

#### *Scope of the Controls Evaluation*

The evaluation of our Disclosure Controls included a review of the controls' objectives and design, our implementation of the controls and the effect of the controls on the information generated for use in this Quarterly Report. In the course of the controls evaluation, we sought to identify data errors, control problems or acts of fraud and confirm that appropriate corrective actions, including process improvements, were being undertaken. This type of evaluation is performed on a quarterly basis so that the conclusions of management, including the CEO and CFO, concerning the effectiveness of the controls can be reported in our Quarterly Reports on Form 10-Q and in our Annual Reports on Form 10-K. Many of the components of our Disclosure Controls are also evaluated on an ongoing basis by other personnel in our accounting, finance and legal functions. The overall goals of these various evaluation activities are to monitor our Disclosure Controls and to modify them on an ongoing basis as necessary. A control system can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of inherent limitations in a cost effective control system, misstatements due to error or fraud may occur and not be detected.

#### *Conclusions*

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As described in detail in Item 9A of our 2007 Form 10-K, our management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2007. Management's assessment identified one material weakness in internal control over financial reporting as of that date. This material weakness was identified in the process and procedures surrounding the preparation and review of the income tax provision. Because the remediation of the material weakness was not complete, our management, including our principal executive and principal financial officers, has concluded that our disclosure controls and procedures were not effective as of September 30, 2008.

We have implemented the following measures to address the material weakness and to enhance our internal control over financial reporting:

1. Obtain an understanding of the tax provision preparation and review procedures performed by our outside tax advisors.
2. Establish tax review meetings each quarter and at year-end with the external tax advisors and Company management.
3. Complete quarterly and annual tax compliance checklist to ensure all relevant tax items are considered in the preparation of the tax provision.

Management believes that we have made substantial progress towards remediating the material weakness in our internal controls over financial reporting. Our testing and evaluation of the operating effectiveness and sustainability of these changes to our internal controls over financial reporting have not yet been completed as the above-referenced remediation actions are still in the implementation process. Therefore, the material weakness identified in the year ended December 31, 2007 still exists as of September 30, 2008 and has caused our management to conclude that we did not maintain effective internal controls over financial reporting as of September 30, 2008. Notwithstanding the material weakness in our internal control over financial reporting that existed as of September 30, 2008, management believes that (i) the Quarterly Report on Form 10Q does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statement made, in light of the circumstances under which they were made, not misleading with respect to the periods covered by this Report and (ii) the financial statements, and other financial information included in this Report, fairly present in all material respects our financial condition, results of operations and cash flows as of, and for, the dates and periods presented in this Quarterly Report.

### *Changes in Internal Control over Financial Reporting*

There has been no change in our internal control over financial reporting that occurred during the period covered by this Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting, except for the activities described above.

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## PART II OTHER INFORMATION

### **Item 1. Legal Proceedings**

A discussion regarding pending legal proceedings is included in Part 1, Item 3, "Legal Proceedings," included in our Annual Report on Form 10-K for the year ended December 31, 2007.

In July 2008, the Company announced a favorable ruling in its ongoing patent infringement dispute with Camtek, Ltd., of Migdal Hamek, Israel. An 11-page decision issued by Judge Michael Davis of the US Federal District Court in Minneapolis, Minnesota, ruled in favor of Rudolph, denying Camtek's Motion for Summary

Judgment and upholding the validity of the patent claims Rudolph asserted against Camtek. This lawsuit was initially brought in 2005 by August Technology prior to its merger with Rudolph. The Company's suit against Camtek alleges that Camtek's line of Falcon semiconductor inspection systems infringe Rudolph's US patent No. 6,826,298. Rudolph is seeking monetary damages and an injunction barring sales of the Falcon line of inspection systems.

## **Item 1A. Risk Factors**

Other than those set forth below, there are no material changes from the risk factors as previously disclosed in our Annual Report on Form 10-K for the year 2007.

### ***Recent turmoil in the credit markets and the financial services industry may negatively impact our business, results of operations, financial condition or liquidity.***

Recently, the credit markets and the financial services industry have been experiencing a period of unprecedented turmoil and upheaval characterized by the bankruptcy, failure, collapse or sale of various financial institutions and an unprecedented level of intervention from the United States federal government. While the ultimate outcome of these events cannot be predicted, they may have a material adverse effect on our liquidity and financial condition if our ability to obtain credit from trade creditors were to be impaired. In addition, the recent economic crisis could also adversely impact our customers' ability to finance the purchase of systems from us or our suppliers' ability to provide us with product, either of which may negatively impact our business and results of operations.

*We may be required to record a significant charge to earnings if our goodwill or amortizable intangible assets become impaired.*

We are required under generally accepted accounting principles to review our amortizable intangible assets and investments in equity interests for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Goodwill is required to be tested for impairment at least annually. Factors that may be considered a change in circumstances indicating that the carrying value of our amortizable intangible assets or goodwill may not be recoverable include a decline in stock price and market capitalization and slower growth rates in our industry. We may be required to record a significant charge to earnings in our consolidated financial statements during the period in which any impairment of our amortizable intangible assets or goodwill is determined to exist. This could adversely impact our results of operations. Consistent with past years, we will be testing our goodwill and other identifiable intangible assets for impairment as of October 31, 2008.

Through September 30, 2008, we have concluded that there were no indicators of impairment that would cause us to accelerate our testing. In October 2008, our stock price has significantly declined to levels which may negatively impact our goodwill impairment test and our review of amortizable intangible assets during the fourth quarter of 2008. Please see Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations for our critical accounting policies related to goodwill and long-lived assets and acquired intangible assets.

## **Item 6. Exhibits**

<u>Exhibit No.</u>	<u>Description</u>
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**2.1 Agreement and Plan of Merger, dated as of June 27, 2005, by and among the Registrant, NS Merger Sub, Inc. and August Technology Corporation (incorporated by reference to Exhibit 99.2 to the Company's Schedule 13D filed with the SEC on July 7, 2005).**

**2.2 Amendment No. 1, dated as of December 8, 2005, by and among the Registrant, NS Merger Sub, Inc. and August Technology Corporation, to the Agreement and Plan of Merger, dated as of June 27, 2005, by and among the Registrant, NS Merger Sub, Inc. and August Technology Corporation (incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with**

the SEC on December 9, 2005).

- 2.3 Asset Purchase Agreement dated as of December 18, 2007, by and among the Registrant, Mariner Acquisition Company LLC, Applied Precision Holding, LLC and Applied Precision, LLC (incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with the SEC on December 21, 2007).
- 3.1 Restated Certificate of Incorporation of Registrant (incorporated herein by reference to Exhibit (3.1(b)) to the Registrant's Registration Statement on Form S-1, as amended (SEC File No. 333-86821 filed on September 9, 1999).
- 3.2 Amended and Restated Bylaws of Registrant (incorporated herein by reference to Exhibit (3.2(b) to the Registrant's Registration Statement on Form S-1, as amended (SEC File No. 333-86821), filed on September 9, 1999).
- 3.3 Amendment to Restated Bylaws of Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed with the Commission on February 15, 2006, No. 000-27965).
- 3.4 Amendment to Restated Bylaws of Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed with the Commission on August 1, 2007, No. 000-27965).
- 4.1 Rights Agreement (incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form 8-A, filed with the Commission on June 28, 2005, No 000-27965).
- 4.2 August Technology Corporation 1997 Stock Incentive Plan (incorporated by reference to the Appendix to August Technology Corporation's Proxy Statement for its 2004 Annual Shareholders Meeting, filed with the Commission on March 11, 2004, No. 000-30637).
- 31.1 Certification of Paul F. McLaughlin, Chief Executive Officer, pursuant to Securities Exchange Act Rule 13a-14(a).
- 31.2 Certification of Steven R. Roth, Chief Financial Officer, pursuant to Securities Exchange Act Rule 13a-14(a).
- 32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Paul F. McLaughlin, Chief Executive Officer of Rudolph Technologies, Inc.
- 32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Steven R. Roth, Chief Financial Officer of Rudolph Technologies, Inc.

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## SIGNATURES

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

Rudolph Technologies, Inc.

Date: October 31, 2008

By: /s/ Paul F. McLaughlin  
Paul F. McLaughlin  
Chairman and Chief Executive Officer

Date: October 31, 2008

By: /s/ Steven R. Roth

\_\_\_\_\_  
Officer

Steven R. Roth  
Senior Vice President, Chief Financial  
and Principal Accounting Officer

EXHIBIT INDEX

Exhibit No.    Description **2.1**

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2.2 Amendment No. 1, dated as of December 8, 2005, by and among the Registrant, NS Merger Sub, Inc. and August Technology Corporation, to the Agreement and Plan of Merger, dated as of June 27, 2005, by and among the Registrant, NS Merger Sub, Inc. and August Technology Corporation (incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with the SEC on December 9, 2005).

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31.1 Certification of Paul F. McLaughlin, Chief Executive Officer, pursuant to Securities Exchange Act Rule 13a-14(a).

31.2 Certification of Steven R. Roth, Chief Financial Officer, pursuant to Securities Exchange Act Rule 13a-14(a).

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Paul F. McLaughlin, Chief Executive Officer of Rudolph Technologies, Inc.

32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Steven R. Roth, Chief Financial Officer of Rudolph Technologies, Inc.

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EXHIBIT 31.1

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

I, Paul F. McLaughlin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rudolph Technologies, Inc.;

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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: October 31, 2008

By:  
/s/  
Paul  
E.  
McLaughlin

\_\_\_\_\_  
Paul  
F.  
McLaughlin  
Chairman  
and  
Chief  
Executive  
Officer

EXHIBIT 31.2

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

I, Steven R. Roth, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rudolph 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: October 31, 2008

By:

/s/

Steven

R.

Roth

\_\_\_\_\_  
Steven

R.

Roth

Senior

Vice

President,

Chief

Financial

Officer

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EXHIBIT 32.1

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

I, Paul F. McLaughlin, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Rudolph Technologies, Inc. on Form 10-Q for the quarter ended September 30, 2008 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Rudolph Technologies, Inc.

Date: October 31, 2008

By: /s/ Paul F. McLaughlin

Paul F. McLaughlin

Chairman and Chief Executive Officer



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A signed original of this written statement required by Section 906 has been provided to Rudolph Technologies, Inc. and will be retained by Rudolph Technologies, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

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**EXHIBIT 32.2**

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

I, Steven R. Roth, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Rudolph Technologies, Inc. on Form 10-Q for the quarter ended September 30, 2008 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Rudolph Technologies, Inc.

Date: October 31, 2008

By: /s/ Steven R. Roth  
Steven R. Roth  
Senior Vice President, Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Rudolph Technologies, Inc. and will be retained by Rudolph Technologies, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.